Overview

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1. Overview of Government Companies and Statutory Corporations

Audit of Government Companies is governed by Sections 139 and 143 of the Companies Act, 2013 (Act). The accounts of Government Companies are audited by Statutory Auditors appointed by the Comptroller and Auditor General of India (CAG). These accounts are also subject to supplementary audit by the CAG. Audit of Statutory Corporations is governed by their respective legislations. As on 31 March 2017, the State of Karnataka had 90 working Public Sector Undertakings-PSUs (84 Companies and 6 Statutory Corporations) and 12 non-working PSUs (all Companies), which employed 1.76 lakh employees. The State PSUs registered a turnover of ₹ 56,478 crore during the year 2016-17 as per their latest finalised accounts. This turnover was equal to 5.05 *per cent* of the State Gross Domestic Product indicating the important role played by the PSUs in the economy. The PSUs had accumulated profit of ₹ 299.26 crore as per their latest finalised accounts.

Investments in PSUs

As on 31 March 2017, the investment (capital and long-term loans) in 102 PSUs was ₹ 1,03,717.40 crore. Infrastructure Sector accounted for about 51.64 *per cent* of the total investment and Power Sector about 40.68 *per cent* in 2016-17. The Government contributed ₹ 23,115.41 crore towards equity, loans and grants/subsidies in 2016-17.

Performance of PSUs

The Return on Capital Employed of the PSUs, for 2016-17, worked out to 4.92 *per cent* and the Return on Equity, however, was (-) 0.08 *per cent*.

The working State PSUs earned a profit of ₹ 1,420.49 crore in the aggregate and incurred loss of ₹ 1,265.37 crore as per their latest finalised accounts at the end of September 2017. The major contributor to profit was Karnataka Rural Infrastructure Development Corporation Limited (₹ 109.88 crore). Huge losses were incurred by Karnataka Neeravari Nigam Limited (₹ 476.88 crore), Hubli Electricity Supply Company Limited (₹ 372.73 crore) and Gulbarga Electricity Supply Company Limited (₹ 131.25 crore).

Audit observed various deficiencies in the functioning of the PSUs. Cases discussed in the subsequent Chapters of this Report indicate that there was a financial effect of ₹ 1,685.38 crore. The losses could have been minimised or profits enhanced substantially with better management. There is a need for greater professionalism and accountability in the functioning of the PSUs.

Quality of accounts

The quality of accounts of working Government companies needs improvement. During the year, out of 66 accounts finalised, the Statutory Auditors gave unqualified reports on 19 accounts, qualified reports on 45 accounts, adverse reports (which means that the accounts did not reflect a true and fair view) for one accounts and disclaimer report (which means that auditor could not form an opinion on the accounts) on one accounts. The compliance with the Accounting Standards by companies remained poor as there were 79 instances of non-compliance in 27 accounts during the year.

Arrears in accounts and winding up

Fifty nine working PSUs had arrears of 75 accounts at the end of September 2017. The arrears pertained to the years 2013-14, 2014-15, 2015-16 and 2016-17. There were 12 non-working PSUs including five under liquidation. The Government may take a decision on the revival or closure of these non-working Companies.

2. Performance Audits relating to Government Companies

The Report includes observations emanating from the Performance Audits on the **'The Performance of Raichur Thermal Power Station Unit-8 of Karnataka Power Corporation Limited'** and **'Implementation of Projects by Cauvery Neeravari Nigama Limited'.** The Executive summaries of the audit findings are given below:

- **Performance Audit on 'The Performance of Raichur Thermal Power Station Unit-8 of Karnataka Power Corporation Limited'.**

Introduction

Karnataka Power Corporation Limited (KPCL; hereinafter referred to as the Company) was incorporated (July 1970) as a wholly owned State Government Company, with the main objective of planning, promoting and organising development of power including construction, generation and maintenance of power stations in the State. In pursuit of these objectives, the Company commissioned (1985-2002), a coal based thermal power station at Raichur with seven units of 210 Mega Watt (MW) each. Besides, Hydel, Solar and Wind generating stations were also commissioned by the Company over the years.

Raichur Thermal Power Station: Unit-8

The Company informed (October 2002) the Government of Karnataka (GoK) that the annual demand for power was showing an increasing trend of 9 *per cent* to 12 *per cent* and in order to meet the increasing demand, the 210 MW was to be expanded. In this backdrop, establishment of a new unit with 210 MW was approved (June 2003) by GoK for implementation by the Company at an estimated cost of ₹ 673.49 crore. Subsequently, the Board of Directors of the Company decided (August 2006) to go in for the more efficient upgraded version of 250 MW plant, considering the phasing out of 210 MW class of Turbine and Generator by the manufacturers and the continued need for technical support, spares and maintenance support during the life of the plant. The Estimated Project Cost was revised to ₹ 925 crore (August 2006), comprising mainly of Boiler, Turbine and Generator (BTG) Package, Mechanical Package, Electrical Package, Civil Package and others, including finance cost. The BTG Package was awarded (March 2007) to M/s. Bharat Heavy Electricals Limited based on approval of GoK (April 2006). The Unit was to be commissioned by September 2009. Though the Unit was synchronised in April 2010 at a cost of ₹ 1,044.57 crore, it was commissioned only in December 2010, *i.e.* after a delay of 15 months. The Company got an assurance (July 2006) from Mahanadi Coalfields Limited for supply of 10.11 lakh tonnes per annum of 'F' grade coal starting supply from 2010 and entered into an agreement for the same in March 2013.

Audit Objectives

The objectives of the Performance Audit were to assess whether:

- Operational efficiency of the Unit-8 of Raichur Thermal Power Station (RTPS) was achieved, leading to optimal output; and
- The Unit was able to keep associated environmental pollution levels within permissible limits through appropriate remedial steps.

Audit Findings

- The performance was sub-optimal during the first four years upto 2014-15 and the shortfall in generation during this period was 4,077.71 MU. (*Paragraphs 2.1.9.3, 2.1.10.1 and 2.1.10.4*)
- The loss of generation due to failure of equipment was 3,856.784 MU during the said period. (*Paragraphs 2.1.10.1 to 2.1.10.4*)
- The Management could have avoided much of the loss of generation due to failure of equipments (*viz.,* Electrostatic Precipitator, Coal Handling Plant and Air Pre-Heater) and ensured that the Unit lived upto the expectation of the State, which was reeling under severe power crisis. (*Paragraphs 2.1.10.1 to 2.1.10.4*)
- The auxiliary consumption of the Unit was above nine *per cent* till 2014-15 as against the norm of 8.5 *per cent* prescribed by Karnataka Electricity Regulatory Commission. (*Paragraph 2.1.11.1*)
- Heavy Fuel Oil (HFO), a start-up fuel, recorded very high consumption owing to repeated failure of equipment in the initial four years. (*Paragraph 2.1.11.3*)
- Consumption of coal was a big concern for the Unit as not only was the consumption very high, but there were concerns about the system of recording coal consumption, as it was not accurate. (*Paragraphs 2.1.11.4 and 2.1.11.5*)
- Consumption beyond limit not only resulted in financial loss but also impacted the environment as HFO and coal have a direct negative

effect on the environment. The excess water consumption also adversely affects water conservation policy of the Government. (*Paragraphs 2.1.11.2, 2.1.11.3 and 2.1.11.4*)

- The Unit could not achieve 100 *per cent* disposal of fly ash and did not comply with the guidelines issued by MoEF in the interest of protecting the environment. (*Paragraph 2.1.12.1*)

- The Ash Pond, meant for only bottom ash (20 *per cent* of total ash), was filled with fly ash too (in the form of slurry). That, as well as the fact that slurry from neighbouring plant (YTPS) was also proposed for disposal in the same Ash Pond, was liable to cause it to be full before its envisaged life-span, thereby endangering the neighbourhood and threating premature closure of the plant. There was no Action Plan in place to handle this crisis on a timely basis. (*Paragraph 2.1.12.1*)

- The Unit was responsible for higher Heat Rate and thus, prevented the Station from achieving Perform Achieve and Trade norms, thereby causing extra expenditure owing to purchase of Energy Saving Certificates (ESCerts) worth ₹ 107.39 crore. (*Paragraph 2.1.12.2*)

- The Stack Emission, though within the limits prescribed by KSPCB, was beyond the design of ESP. (*Paragraphs 2.1.12.3 and 2.1.12.4*)

Recommendations

The Company may consider:

1. ensuring strict compliance to operation and maintenance requirements, as recommended by the manufacturers, through a robust internal control mechanism, so that any defect noticed can be brought to the notice of the manufacturers immediately;

2. strengthening the Efficiency Section of the Unit-8, which was responsible to monitor the performance parameters;

3. reducing blow-downs to achieve the envisaged norm to reduce consumption of water;

4. ensuring that all avenues for use of ash like in building construction, road works, paint industry, *etc.* are tapped to make sure that 100 *per cent* disposal of fly ash is achieved;

5. enforcing the conditions in the ash disposal contract to ensure 100 *per cent* disposal of fly ash. This would enable the Company to overcome the crisis of Ash Pond being filled up much earlier than planned and avoid stoppage of generation in the near future; and

6. regularly monitoring the emission to ensure that emission is within the design parameters of Electrostatic Precipitator.

(Chapter 2.1)

➢ Performance Audit on 'Implementation of Projects by Cauvery Neeravari Nigama Limited'.

Introduction

The Cauvery river originates at Talakaveri in Kodagu district of Karnataka and finally flows into the Bay of Bengal. The Cauvery river basin extends over the States of Karnataka, Kerala, Tamil Nadu and the Union Territory of Puducherry. The Cauvery water-sharing dispute existed amongst these States since the 19^{th} century. The Inter-State Water Disputes Tribunal on the directions of the Hon'ble Supreme Court, in its Award (February 2007) allocated 270 tmc of water to Karnataka in a year and also specified quantum of water to each project. It also specified the area to be cultivated under each project, which totalled to 18.85 lakh acres (approx. 7,628 sq. km.). As the States did not agree to the Award of the Tribunal, they filed appeals before the Hon'ble Supreme Court, on which the final judgement was awaited (November 2017).

State Water Policy

The Government of Karnataka (GoK) formulated the State Water Policy, 2002 (SWP), for creation of irrigation potential by 2005 (target year) and construction of Field Irrigation Channels (FICs) by 2006 to achieve the ultimate irrigation potential of 45 lakh hectares (ha) in the State. The State Water Policy also emphasised Participatory Irrigation Management.

Cauvery Neeravari Nigama Limited (*CNNL*)

The Cauvery Neeravari Nigama Limited (Company) was incorporated in June 2003 under the Companies Act, 1956, to complete the works of and to maintain, operate, improve or modernise on-going Major and Medium Irrigation Projects including Lift Irrigation Works and Minor Irrigation and such works entrusted to the Command Area Development Authority (CADA) in the Cauvery basin.

The Company, under its jurisdiction, executes and maintains four Major Irrigation Projects, 19 Medium Irrigation Projects and 25 *Anicut* canals. It also executes works of Lift Irrigation Schemes, Drinking Water Schemes (DWS) and Restoration and Rejuvenation of rivers and tanks, and other works, which fall in the command area of the irrigation projects. Of the 18.85 lakh acres of land allowed to be cultivated under various projects, as per the Award of the Inter-State Water Disputes Tribunal, an area of 15.55 lakh acres fell in the jurisdiction of projects of the Company and the remaining 3.30 lakh acres (of the 18.85 lakh acres) fell under the jurisdiction of the Minor Irrigation Department of the Government of Karnataka.

Audit Objectives

The Audit Objectives were to assess whether:

- Proper planning was in place while taking up the projects; and

- The works were executed within the stipulated time frame and the implementation was effective in achieving the objectives set out in the Project Reports.

Out of the 19 projects selected for review, the works in respect of:

- Three projects were completed in time;
- Seven projects were completed after delays ranging from three months to four years from their scheduled date of completion;
- Seven projects are delayed upto four years from their scheduled date of completion and are yet to be completed; and
- One project, though delayed, its date of completion was yet to be due (as of November 2017) and another project was yet to be taken up.

Audit Findings

- Lacunae in planning as the Company was not preparing Zone-wise Annual Works Programmes, not having a database for selection of projects and carrying over 3,427 number of spillover works (57 *per cent* of total works) in its Annual Works Programmes. (*Paragraphs 2.2.11.2, 2.2.11.3 and 2.2.11.4*)
- Lack of priority in planning for potential oriented works and creation of Field Irrigation Channels (FICs) resulted in a total of 5,968 ha of potential oriented work and 42,400.68 ha of FICs remaining incomplete even after a lapse of more than 12 years, which should have been completed by 2005 and 2006 respectively as per State Water Policy. (*Paragraphs 2.2.11.6 and 2.2.11.7*)
- Deficiencies were noticed while preparing the estimates of the projects due to non-compliance with Karnataka Public Works Department Code. (*Paragraph 2.2.11.10*)
- Implementation of the projects suffered due to land acquisition problems, delays in approval of designs, non-synchronisation of associated works with main works and other administrative reasons, all of which were avoidable factors. (*Paragraph 2.2.12.1 to 2.2.12.4*)
- Adequate attention was not given to Inspection Reports of the Quality Control Divisions. (*Paragraph 2.2.12.6*)
- Monitoring of projects was inadequate due to lack of proper reporting system to the Board of Directors. (*Paragraph 2.2.12.7*)
- Benefits envisaged in the Project Reports of filling up of 81 tanks for providing drinking water to 310 villages, providing water to *suffering achkat* of 3,200 acres and efforts to restore and rejuvenate the Arkavathy river, were delayed and the objectives were not realised in

time. A total expenditure of ₹ 560.32 crore was incurred on this. (*Paragraph 2.2.12 and Appendix-4*)

Recommendations

1. The Company may prepare the comprehensive Annual Works Programme for effective water utilisation of Cauvery water.
2. Before taking up fresh works, the Company may prioritise completion of all the spillover works pending since many years.
3. The Company may accord greater priority in its plan documents for potential creation and Field Irrigation Canals (FIC), acquisition of land in advance and sharing information with Command Area Development Authority, so that the irrigation potential and FIC are created at the earliest.
4. The Company may take action for making payment towards land compensation, which were overdue since many years.
5. The Company may fix timeline for approval at various levels for clearance/approval of drawings, so that the process time for granting approvals is regulated.
6. The Company may ensure that the associated works are awarded in synchronisation with the main work.
7. The Company may monitor Action Taken Reports in the meetings and act upon them promptly.

(Chapter 2.2)

3. Compliance Audit Observations

The observations included in this Report highlight deficiencies in planning, investment and other activities in the management of PSUs, which resulted in financial irregularities. The observations are broadly of the following nature:

Undue favour to contractors amounting to ₹ 21.95 crore.

(Paragraph 3.1, 3.3)

Avoidable expenses amounting to ₹ 46.74 crore.

(Paragraphs 3.2, 3.4, 3.5, 3.7, 3.9, 3.11)

Unproductive investment amounting to ₹ 0.76 crore.

(Paragraph 3.10)

Miscellaneous cases amounting to ₹ 141.22 crore.

(Paragraphs 3.6, 3.8, 3.12)

Gist of some of the important audit observations are given below:

- Karnataka Neeravari Nigam Limited paid weightage of 25 *per cent* as incentive to the contractors contravening the tender conditions, unduly benefitting the contractor by ₹ 11.11 crore.

  (Paragraph 3.1)

- Karnataka Neeravari Nigam Limited did not utilise the relevant provisions of the conditions of Supply of Electricity of Distribution Licensees to reduce the contract demand during off-season and incurred additional contract demand charges of ₹ 2.11 crore. Besides, it did not monitor Power Factor and paid ₹ 1.24 crore as penalty, in addition to penalty of ₹ 0.45 crore towards delayed payment.

  (Paragraph 3.2)

- Krishna Bhagya Jala Nigam Limited paid ₹ 51.58 crore as weightage in the penultimate RA Bill instead of Final Bill and benefitted the contractor by ₹ 6.02 crore towards interest apart from making excess payment of ₹ 4.82 crore contrary to tender conditions.

  (Paragraph 3.3)

- Karnataka Road Development Corporation Limited did not hand over the land for construction of road from Kudalagi-Sandur to Torangal and from Honnali town to Honnali Taluk border and paid avoidable compensation of ₹ 35.20 crore to the contractor.

  (Paragraph 3.4)

- Karnataka Power Corporation Limited procured spares for its DG plants though it was aware that it was to switch over to Gas Plant and that environmental norms were not complied with. These spares worth ₹ 5.04 crore had to be written off.

  (Paragraph 3.5)

- The Mysore Paper Mills Limited, in view of it being referred to BIFR, shifted its operations to its Registered Office at Bhadravathi, but injudiciously retained its big office premises in Bengaluru for six of its officers/officials. This resulted in avoidable expenditure of ₹ 1.28 crore.

  (Paragraph 3.7)

- Cauvery Neeravari Nigama Limited did not avail auto-sweep facility from its bank for the funds in its current account and suffered loss of interest of ₹ 1.16 crore.

  (Paragraph 3.8)

- Karnataka State Financial Corporation did not adequately monitor implementation of its Lending Policy. There were procedural lapses exposing lack of internal control, risk of default and limitations to invoke legal recourse. The Corporation did not liquidate securities obtained as guarantee against default. The Company failed to initiate action under Section 29 and 31 of the SFC Act, 1951, and helped the borrowers escape recovery of loans.

  (Paragraph 3.12)