



Chapter 1
Introduction

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1.1 About this Report

This Report of the Comptroller and Auditor General of India (C&AG) relates to matters arising from the Performance Audit of selected programmes and activities and Compliance Audit of Government Departments and Autonomous Bodies under Economic Sector.

Compliance Audit refers to examination of the transactions of the audited entities to ascertain whether the provisions of the Constitution of India, applicable laws, rules, regulations and various orders and instructions issued by competent authorities are being complied with.

The primary purpose of the Report is to bring to the notice of the State Legislature, important results of audit. Auditing Standards require that the materiality level for reporting should be commensurate with the nature, volume and magnitude of transactions. The findings of audit are expected to enable the Executive to take corrective actions as also to frame policies and directives that will lead to improved financial management of the organisations, thus, contributing to better governance.

This chapter, in addition to explaining the planning and extent of audit, provides a synopsis of the significant deficiencies and achievements in implementation of selected schemes, significant audit observations made during the Compliance Audit and follow-up on previous Audit Reports. Chapter-2 of this Report contains findings arising out of Performance Audits of 'Implementation of Textile Policy 2013-18' and 'Agricultural Marketing Reforms in Karnataka'. Chapter-3 contains observations of a Thematic Audit on 'Diversion of forestlands and Functioning of Karnataka State Compensatory Afforestation Fund Management and Planning Authority' and Compliance Audit in the Government Departments and Autonomous Bodies.

1.2 Auditee Profile

The Accountant General (Economic & Revenue Sector Audit), Karnataka, Bengaluru, conducts audit of 12 Departments and 25 Autonomous Bodies under the Economic Sector in the State. The Departments are headed by Additional Chief Secretaries/Principal Secretaries/Secretaries, who are assisted by Directors/Commissioners and subordinate officers under them.

The summary of fiscal transactions of the Government of Karnataka during the year 2016-17 and 2017-18 is given in **Table 1.1** below:

Table 1.1: Summary of fiscal transactions

(₹ in crore)

Receipts			Disbursements		
	2016-17	2017-18		2016-17	2017-18
Section A: Revenue					
Revenue receipts	1,33,213.79	1,46,999.65	Revenue expenditure	1,31,920.75	1,42,482.33
Tax revenue	82,956.13	87,130.38	General services	31,264.56	34,484.44
Non-tax revenue	5,794.53	6,476.53	Social services	54,549.24	58,652.35
Share of Union taxes/duties	28,759.94	31,751.96	Economic services	40,421.37	42,855.78
Grants-in-aid & contributions from GoI	15,703.19	21,640.78	Grants-in-aid & contributions	5,685.58	6,489.76
Section B: Capital and others					
Miscellaneous Capital receipts	26.96	3.70	Capital outlay	28,150.43	30,666.76
			General services	1,060.39	977.45
			Social services	6,896.84	8,676.76
			Economic services	20,193.20	21,012.55
Recoveries of loans & advances	99.84	136.93	Loans & advances disbursed	1,934.38	5,092.22
Public Debt receipts	31,155.92	25,121.86	Repayment of Public Debt	7,420.24	8,269.16
Contingency Fund	-	-	Contingency Fund	-	-
Public Account Receipts	1,79,318.45	2,00,615.43	Public Accounts disbursements	1,67,153.81	1,94,536.63
Opening Cash Balance	27,118.23	34,353.58	Closing cash balance	34,353.58	26,184.05
TOTAL	3,70,933.19	4,07,231.15	TOTAL	3,70,933.19	4,07,231.15

(Source: Finance Accounts 2017-18)

1.3 Authority for Audit

The authority for audit by the C&AG is derived from Articles 149 and 151 of the Constitution of India and the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971. C&AG conducts audit of expenditure of the Departments of the Government of Karnataka under Section 13¹ of the C&AG's (DPC) Act. C&AG is the sole auditor in respect of four Autonomous Bodies, which are audited under sections 19(2)², 19(3)³ and 20(1)⁴ of the C&AG's (DPC) Act. In addition, C&AG also conducts audit of 25 other Autonomous Bodies, under Section 14⁵ of C&AG's (DPC) Act, which

¹ Audit of (i) all transactions from the Consolidated Fund of the State, (ii) all transactions relating to the Contingency Fund and Public Accounts and (iii) all trading, manufacturing, profit and loss accounts, balance sheets and other subsidiary accounts.

² Audit of the accounts of Corporations (not being Companies) established by or under law made by the Parliament in accordance with the provisions of the respective legislations.

³ Audit of accounts of Corporations established by law made by the State Legislature on the request of the Governor.

⁴ Audit of accounts of any body or authority on the request of the Governor, on such terms and conditions as may be agreed upon between the C&AG and the Government.

⁵ Audit of all receipts and expenditure of a body/authority substantially financed by grants or loans from the Consolidated Fund of the State and with the previous approval of the Governor of the State and audit of all receipts and expenditure of any body or authority where the grants or loans to such body or authority from the Consolidated fund of the State in a financial year is not less than ₹ one crore.

are substantially funded by the Government. Principles and methodologies for various audits are prescribed in the Auditing Standards and the Regulations on Audit and Accounts, 2007 issued by the C&AG.

Under the directions of the C&AG, the Office of the Accountant General (E&RSA), Karnataka, conducts audit of Government Departments/Offices/Autonomous Bodies/Institutions under them which are spread all over the State.

1.4 Planning and conduct of Audit

Audit process starts with the assessment of risks faced by various Departments of the Government based on expenditure incurred, criticality/complexity of activities, level of delegated financial powers, assessment of overall internal controls and concerns of stakeholders. Previous audit findings are also considered in this exercise. Based on this risk assessment, the frequency and extent of audit are decided.

After completion of audit of units, Inspection Reports containing audit findings are issued to the heads of the Departments. The Departments are requested to furnish replies to the audit findings within one month of receipt of the Inspection Reports. Whenever replies are received, audit findings are either settled or further action for compliance is advised. The important audit observations arising out of these Inspection Reports are processed for inclusion in the Audit Reports, which are submitted to the Governor of the State under Article 151 (2) of the Constitution of India for submission before the State Legislature.

During 2017-18, in the Economic Sector Audit Wing, 1,311 party-days were utilised to carry out audit of 152 units.

1.5 Significant audit observations

In the last few years, Audit had reported on several significant deficiencies in implementation of various programmes/activities through performance audits, as well as on the quality of internal controls in selected Departments, which impacted the success of programmes and functioning of the Departments. Similarly, the deficiencies noticed during thematic and compliance audit of the Government Departments/organisations were also highlighted.

The present report contains two Performance Audits; one on 'Implementation of Textile Policy 2013-18' and another on 'Agricultural Marketing Reforms in Karnataka'. The report also contains one Thematic Audit on 'Diversion of forestlands and Functioning of Karnataka State Compensatory Afforestation Fund Management and Planning Authority' and six Compliance Audit paragraphs. The significant audit observations are summarised below:

1.5.1 Performance Audit on “Implementation of Textile Policy 2013-18”

The Department did not maintain a comprehensive and updated database on various value chain activities for framing appropriate interventions for growth of the Textile sector. The utopian investment and employment generation targets set in the Textile Policy 2013-18 were achieved only to an extent of 37 per cent and 24 per cent respectively. No evaluation was conducted to ascertain the reasons for poor performance in attracting investments and employment generation. The objectives of revival of Handloom sector and Spinning Mills in the Co-operative sector were also not achieved. The integrated Textile Parks were proposed for establishment at four locations without ensuring prospective investors and were mooted simply because land was available with KIADB. No information was available with the Department as to whether the approved projects were being implemented or were being withdrawn by the proponents.

Incentives/subsidies were also not released on time and the delay was beyond 12 months in 312 cases.

No norms were laid down for grant of incentives/subsidies to projects under ‘Special Package’. Moreover, incentives/subsidies worth ₹ 315 crore were sanctioned to a project on unjustifiable grounds.

The financial management was not robust as amounts were lying with the implementing agencies and penal interest was paid as bills were not discharged in time. Imparting of training to youth for employment in the Garment sector was curtailed to 1.09 lakh persons from the Textile Policy target of five lakhs ostensibly due to budgetary constraints. Monitoring was lacking though there were shortfalls in achievement in many areas.

Thus, the objectives of the Textile Policy of 2013-18 were not achieved by the Department though the Textile sector was touted as the biggest employment generator with low capital investment. Unless the aforesaid issues are suitably addressed, there is a high probability of subsequent Textile Policies too being plagued by these structural weaknesses in planning, implementation and achievement of targets.

(Paragraph 2.1)

1.5.2 Performance Audit on “Agricultural Marketing Reforms in Karnataka”

The term Agricultural marketing is referred to services involved in moving Agricultural produces from the farm to the consumer through trading at *mandis* and is primarily oriented to protect the interests of the farmers. The regulation of markets achieved only a limited success in providing an efficient marketing system, forcing the Government of India to undertake reforms and bring out a Model Act in 2003 for adoption by the State Governments. The reforms sought to liberalize licence conditions, open up the marketing sector for the private players, leverage on Information Technology for transparency

in market operations, enhance farmers' income through better price discovery due to wider markets, direct payment to farmers account, *etc.* The Government of Karnataka (GoK) amended the various provisions of the Karnataka Agricultural Produce Marketing Act, in line with the Model Act, 2003. To take the reforms forward, GoK constituted a Reforms Committee which recommended forming a Special Purpose Vehicle to provide a Unified Marketing Platform (UMP) in 162 *mandis* to facilitate e-trading and establishment of alternate markets.

Many of the Policy initiatives were either not implemented or were still under progress. Planning was deficient as no schedule was drawn to prioritise and implement the various reform initiatives. The UMP was rolled out in 160 main *mandis* but 352 sub-markets were left out.

Quality based trading, the unique selling proposition of the e-trading platform, which was to be provided in all *mandis* within two years was available in only 35 *mandis* while grading of the commodities was not available in any of the *mandis*. Another critical initiative, *i.e.* direct payment to the farmers account, commenced in six *mandis* on a pilot basis but was withdrawn due to farmers'/traders' opposition. The arrivals of commodity in the *mandis* had recorded only an incremental increase through e-trading in the five-year period and ranged between 7 and 12 *per cent*, despite the UMP being rolled out in 160 *mandis*. Price realisation by farmers continued to be governed by the market forces and trading data of eight major crops during 2017-18 indicated that price realisation was below the Minimum Support Price. The SPV was collecting transaction charges on the value of commodities sold through channels other than through e-platform. This was in violation of the rules/provisions of the Service Level Agreement and had resulted in enriching the SPV with an unintended benefit of ₹ 63.95 crore.

Broad basing of markets to enable the farmer sell his farm produce through alternate markets like Private Markets, Direct Purchase Centres, warehouse-based sales, Commodity Specific Parks, *etc.*, had not yielded the desired results. There were irregularities in the issue of licences to Private Market players and instances were noticed wherein the Private Markets players violated the licence conditions and resorted to unauthorised collection of fees from the farmers. The Regulatory Authority was not constituted though recommended by the Reforms Committee as segregation of functions was found essential due to opening the sector for private players. Besides, warehouse-based sales had not taken off yet.

The financial management was deficient as funds were released in excess of requirement and infrastructure projects were taken up without following due diligence. None of the Commodity Specific Parks fructified and amount released for the same remained with the *mandis*/KIADB. These deviations had resulted in idle expenditure on godowns (₹ 131.15 crore), auction platforms (₹ 171.52 crore), *etc.*

The Revolving Fund had not been recouped and unspent balance to the tune of ₹ 1,598.90 crore remained with the Procurement Agencies which were supposed to undertake market distress operations. Audit of Revolving Fund

accounts was in arrears and compliance to Audit Reports was not submitted to the Government by the Board. Huge losses were also reported by the Procurement Agencies, which should have got reflected in the accounts of the Revolving Fund. GoI had not reimbursed ₹ 656.06 crore towards MSP as the necessary documents were not furnished by the State Government.

The reforms undertaken were still at a nascent stage and thus to realise the intended benefits, sustained efforts and proper implementation by all concerned is essential.

(Paragraph 2.2)

1.5.3 Thematic Audit on “Diversion of forestlands and Functioning of Karnataka State Compensatory Afforestation Fund Management and Planning Authority”

‘Compensatory Afforestation’ is a mechanism to compensate for the loss of forests by planting trees elsewhere in lieu of diversion of forest for non-forest purposes approved under the provisions of Forest (Conservation) Act, 1980. The series of directives from the Supreme Court resulted in imposition of levies on the project proponent and culminated in the formation of a separate fund by the Central Government for carrying out Compensatory Afforestation and related activities in a systematic manner.

Our test-check of records showed deficiencies in the areas of approval or renewal of lease for diversion of forestlands (7,785.07 ha⁶) in contravention of provisions of the FC Act. Several projects were allowed to be executed by the Department, though prior approval of the Central Government was not taken in spite of that being mandatory. These projects were primarily undertaken by agencies belonging to the Government. Cases of short and non-levy of stipulated charges aggregating to ₹ 34.64 crore were also noticed. Due importance was not accorded for mutation and final notification of non-forestland as Reserved or Protected Forests.

As per MoEF guidelines, only lands suitable for afforestation should be accepted by the Department as compensation for the diverted forestland. But 997.28 ha of unsuitable lands were accepted and consequently Compensatory Afforestation in these lands could not be done. Success indicators of the plantations raised were not recorded in the Plantation Journals despite it being a mandatory stipulation and effectiveness of afforestation measures undertaken was not ensured by the Department. The absence of data made results unverifiable in Audit.

Annual Plan of Operations deduced from the Working Plan should be the basis for carrying out works but these were deviated in 10 cases without prior approval from the Competent Authority. Dwarf/medicinal species were required to be planted in the Windmill Project areas as per the APO but tree species were planted in violation of stipulations.

⁶ 320.88 ha+ 475.77 ha + 45.10 ha + 4,443.32 ha + 2,500 ha (Ref para Nos 3.2.2.2 to 3.2.2.4).

The Department did not engage any agency for independent concurrent monitoring and evaluation of Compensatory Afforestation works though CAMPA guidelines stipulate for compulsory evaluation study.

Though the Department complied with the rules and regulations, certain deviations/violations were noticed in the test-checked divisions, as shown in this report. The major areas of concern were those related to use of forest land for non-forest purposes without approval, acceptance of non-suitable lands for afforestation, not recording survival results in plantation journals, resorting to ratification of works executed in deviation and ignoring concurrent evaluation by third party consultants. These need closer attention and suitable corrective actions from the Departments to ensure that the spirit of the FC Act, as endeavoured to be upheld through CAMPA, is not completely lost.

(Paragraph 3.2)

1.5.4 Compliance Audit

Audit had reported on several significant deficiencies in critical areas which impacted the effective functioning of the Government Departments. These are as under:

Government in violation of financial rules released ₹ 19.89 crore to a Society for implementation of a Government of India Scheme of which a major portion of the amount remained unutilised. The Society kept funds in Savings Bank account instead of Flexi-Deposit account, resulting in loss of interest of ₹ 110.76lakh due to lower rate of interest.

(Paragraph 3.1)

The Minor Irrigation & Ground Water Development Department approved action plan for ₹ 90.95 crore towards repair to feeder canal and digging of boundary trenches in respect of 2,259 minor irrigation tanks in the State.

The expenditure of ₹ 25.40 crore spent in 10 test-checked Divisions towards repairs to feeder canals lacked justification, as the veracity of justification mentioned in the estimates were not cross-checked by the Controlling Officers. Excavation of boundary trenches for 2,259 tanks at ₹ 48.09 crore without clearance from the statutory authority was infructuous and was avoidable. The adoption of incorrect rates for excavation of boundary trenches not only boosted the estimates but also facilitated undue benefit to the contractors. Injudicious action of the EE in rejecting the lowest bids offered by Class-I contractors resulted in extra burden of ₹ two crore to the State Exchequer.

(Paragraph 3.3)

(i) Defective estimation, slippages in monitoring and unauthorised execution of works lead to inordinate delay in completion of four Lift Irrigation Schemes besides unproductive outlay of ₹ 17 crore. (ii) Failure to obtain Forestry

Clearance prior to entrustment of works and non-prioritisation of items of work resulted in unfinished projects, rendering an expenditure of ₹ 5.19 crore unfruitful.

(Paragraph 3.4.1 & 3.4.2)

(i) The Project Director paid ₹ 13.62 crore in contravention of Concession Agreement while making payment for first annuity installment in respect of State Highway Improvement Project.(ii) Incorrect adoption of date of completion of work resulted in short levy of ₹ 4.90 crore towards delay damages in a road construction contract.

(Paragraph 3.5.1 & 3.5.2)

Adoption of uneconomical rates in estimate and improper regulation of rates for excavation items coupled with short levy of liquidated damages had resulted in undue benefit of ₹ 11.14 crore to the contractor in a building construction contract.

(Paragraph 3.6)

(i) Overpayment of ₹1.29 crore was observed due to treatment of an item of work as variation item contrary to conditions of contract and also for undertaking excavation beyond the required depth.(ii) Ignoring the provisions of agreement, the Divisional Officer paid ₹ 98.97 lakh towards price adjustment for ineligible period and for items which were already included in the tender.

(Paragraph 3.7.1 & 3.7.2)

1.6 Lack of responsiveness of the Government to Audit

1.6.1 Response of departments to the Draft Paragraphs

Two Performance Audits, one Thematic Audit and six draft paragraphs were forwarded demi-officially to the Additional Chief Secretaries/Principal Secretaries/Secretaries of the Departments concerned between April and August 2018 to send their responses within four weeks. The Government replies for one Performance Audit and three draft paragraphs featured in this Report were received. The Government replies in respect of another Performance Audit, Thematic Audit and three draft paragraphs are awaited. The replies received are suitably incorporated in the Report.

1.6.2 Follow-up on Audit Reports

The Rules of Procedure (Internal Working), 1999, of the Public Accounts Committee provides that all the Departments of the Government should furnish detailed explanations in the form of Departmental Notes to the observations in Audit Reports, within four months of their being laid on the Table of Legislature to the Karnataka Legislature Secretariat with copies thereof to Audit Office.

The Administrative Departments did not comply with these instructions and 10 Departments (as detailed in **Appendix 1.1**) did not submit Departmental Notes for 19 paragraphs for the period from 2003-04 to 2016-17 (as of September 2018).

1.6.3 Paragraphs to be discussed by the Public Accounts Committee

Details of paragraphs pending discussion by the Public Accounts Committee as of September 2018 are given in **Appendix 1.2**. There are 188 paragraphs relating to the Audit Reports of various years from 1992-93 to 2016-17 pending for discussion in Public Accounts Committee. Delay in discussion or non-discussion of paragraphs may result in erosion of accountability of the Executive.
