

CHAPTER IV

4 TRANSACTION AUDIT OBSERVATIONS

Important audit findings as a result of test check of transactions made by the State Government Companies/Corporations are included in this Chapter.

GOVERNMENT COMPANIES

Transformers and Electricals Kerala Limited

4.1 Avoidable loss

Delay in furnishing bank guarantee deprived the Company of the benefit of advance payment with consequential interest loss of Rs.92.40 lakh.

The Company engaged in the production of heavy electrical equipment received (October 2002) orders for Rs 36.32 crore from BSES Limited (renamed as Reliance Energy Limited from March 2004) for the supply of generator power transformers and spares. As per the payment terms, the Company was to receive 10 *per cent* advance on the date of agreement and balance 90 *per cent* together with taxes and other levies by means of Letter of Credit (LC) prior to five months to the date of inspection of equipment.

The BSES sought (November 2002) reduction in prices for which the Company offered (December 2002) to reduce the package prices to Rs 32.82 crore subject to alteration in payment terms as interest free advance of 20 *per cent* of ex-works price of the main equipment on the date of agreement, 30 *per cent* on completion of six months from the date of order and balance payment against LC on pro-rata basis. The Company, however, had to provide necessary Bank Guarantee (BG) before release of advances by BSES. The alteration in payment terms was accepted by BSES. Purchase order was received in December 2002 from BSES and the agreement executed in March 2003.

In terms of the agreement the Company had to furnish BG in July 2003 towards release of 30 *per cent* advance amounting to Rs.7.70 crore. The BG was, however, furnished after a delay of 12 months (July 2004) and BSES released the payment in August 2004. The delay in furnishing the BG by the Company was caused on account of procedural delays involved in obtaining counter guarantee from Government to facilitate issue of BG by Company's bankers (State Bank of Travancore).

Thus, the failure of the Company to furnish bank guarantee for release of advance payment in terms of the agreement deprived the Company of the benefit of advance payment which entailed interest loss of Rs 92.40 lakh (at the rate of 12 *per cent* per annum).

The Government, while admitting the fact, stated (July 2005) that the real advantage of interest on advance payment finally accrued to the Company.

The reply is not acceptable since the package price quoted by the Company was reduced after taking into account the savings in interest charges that would arise from timely receipt of advance payments from BSES, the benefit of which did not accrue to the Company.

Kerala Transport Development Finance Corporation Limited

4.2 Avoidable expenditure

The Company procured thermal paper rolls without inviting tenders which resulted in extra expenditure of Rs. 21.82 lakh.

As a part of its advertisement campaign, the Company which is engaged in financing the Kerala State Road Transport Corporation (KSRTC), decided (July 2003) to advertise on the reverse side of the paper rolls used by KSRTC in their Electronic Ticketing Machines. As a consideration for allowing advertisement, the Company agreed (July 2003) to supply the thermal paper rolls with necessary advertisement free of cost for a period of six months up to November 2003. The period of free supply was further extended (November 2003) for another six months up to July 2004.

The Company appointed (August 2003), Panchami Systems, Thiruvananthapuram (PS) as the supplier of thermal paper rolls with advertisement on the reverse side, at Rs.19.50 per roll. The Company supplied two lakh paper rolls received from PS during the period August 2003 to July 2004 at a total cost of Rs.39 lakh to KSRTC.

It was noticed during audit that the Company did not give adequate publicity while selecting (August 2003) PS as the supplier; the rate of Rs.19.50 per roll was finalised without inviting formal tenders, relying on the quotations received through KSRTC. When compared to the rate of Rs.19.50 per roll at which orders were placed by the Company on PS, the rate offered by another firm (Gopsons papers, Noida) in response to the tenders invited (December 2003) by KSRTC was only Rs.8.59 per roll inclusive of cost of printing advertisement. With reference to this the additional expenditure incurred by the Company on two lakh paper rolls at the rate of Rs 10.91 per roll worked out to Rs 21.82 lakh.

Thus, due to procurement of thermal paper rolls without inviting open tenders, the Company incurred avoidable extra expenditure of Rs. 21.82 lakh.

The Government stated (July 2005) that an immediate decision on procurement was required by the Company since Electronic Ticketing Machine was inaugurated in August 2003 which necessitated the supply of thermal paper rolls with advertisement immediately. Therefore, a decision was taken with available quotations at that point of time. The reply is not tenable since KSRTC decided to implement Electronic Ticketing Machine in February 2003; the Company had enough time to invite tenders and avail of the advantage of reduced rates in the procurement of paper rolls.

Travancore Sugars and Chemicals Limited

4.3 Avoidable expenditure

Imprudent decision to reject the lowest offer for supply of ENA resulted in avoidable expenditure of Rs.59.51 lakh.

The Company engaged in the production of Indian Made Foreign Liquor (IMFL), invited (March 2004) tenders for the purchase of 10 lakh bulk litres (BL) of Extra Neutral Alcohol (ENA), a major raw material. As per conditions of the tender, the Company reserved the right to accept or reject or negotiate any tender without assigning any reasons. The lowest rate of Rs.30.50 per BL was offered by Anjana Traders and Agencies, Kochi (ATA). ATA being a transporter of molasses for the Company, had not furnished the security deposit on the ground that the amounts due to them from the Company should be considered as security. The Company rejected (16 April 2004) this lowest offer on the ground of insufficient security deposit. ATA had agreed (17 April 2004) to supplement the shortage, if any, in security deposit and to supply the entire quantity at the quoted rate of Rs.30.50 per BL. Before considering the request of ATA, the contract was awarded (30 April 2004) to Michael & Michael Chemicals, Goa (M&M) at Rs.34.70 per BL. The request of ATA was finally considered by the Board only on 12 May 2004 and the contract awarded to M&M was also cancelled (May 2004) on the ground that the rate quoted was very high and unprofitable.

On retender (May 2004), the contract was awarded to ATA itself at a higher rate of Rs.34.25 per BL restricting the quantity to 5 lakh BL. While accepting the higher offer, the Company agreed to adjust the dues outstanding against ATA as security deposit whereas the same option was not considered when the firm offered the lower rate of Rs 30.50 per BL in April 2004.

For the balance quantity of 5 lakh BL, orders were placed (November 2004) on Chandra Babu.C, Trivandrum at Rs.38.66 per BL. The quantity procured against the above two orders was 5 lakh BL and 4.995 lakh BL respectively.

It was noticed during audit that the Company was aware of the increasing trend in price of ENA from Rs.25.72 per BL in March 2004 to Rs.30.50 per BL in April 2004. Instead of availing the advantage of the lowest price offered (April 2004), by ATA, the Company awarded the contract to M&M at higher rates and took a decision (May 2004) to cancel this order and to reconsider the offer of ATA in May 2004, after a period of one month. Though the intention of cancelling the orders with M&M was to avail of the benefit of lowest rate of Rs.30.50 per BL offered by ATA in April 2004, this benefit could not be derived due to the decision of the Company to re-tender instead of accepting the offer of ATA. The order quantity of 10 lakh BL was also unnecessarily split and subsequent orders were placed at the enhanced rates. By not accepting the offer of ATA for 10 lakh BL at Rs.30.50 per BL in April 2004 itself, the Company had incurred avoidable expenditure of Rs.59.51 lakh on the procurement of 9.995 lakh BL of ENA.

The matter was reported to Management/ Government (June 2005); their replies have not been received (September 2005).

Kerala Automobiles Limited

4.4 Avoidable loss

Injudicious decision to procure poor quality Elgi engines resulted in avoidable loss of Rs 25.68 lakh.

The Company, engaged in the manufacture of three wheelers, had been purchasing rope-start as well as self-start diesel engines from Greaves Limited, Ranipat (GL). The Company identified (March 1999) Elgi Equipments Limited, Coimbatore (EEL) as an additional source for supply of three wheeler engines citing various advantages of their Elgi-Faryman engines when compared to the Greaves engines being used. The price of Elgi engines was also higher by 2.58 *per cent*.

After rolling out (July 1999) three wheelers fitted with Elgi engines, the Company started receiving regular complaints both from dealers and customers on the poor performance of the engines involving major problems like starting troubles, over-heating, high noise level, etc. The Company ignored the reports (November 1999) and continued to procure engines from EEL. Out of the total number of 464 engines valued at Rs.87.98 lakh purchased from EEL during the period 1998-99 to 2002-03, 432 engines related to purchases after November 1999.

In view of the poor performance of the vehicles fitted with Elgi engines and resultant complaints from the field, the Company finally decided (March 2004) to liquidate the stock by re-selling 110 engines costing Rs.18.66 lakh to EEL itself at a reduced value of Rs.11.33 lakh. The cash loss incurred on this account amounted to Rs.7.33 lakh. Out of 85 autorickshaws fitted with Elgi engines which remained unsold, 70 were sold by replacing the engines at 50 *per cent* cost to customers involving a loss of Rs 8.26 lakh. The balance 15 autorickshaws fitted with Elgi engines were remaining unsold (August 2005) since 2001-02. The value of this dead stock was Rs 10.09 lakh.

Thus, the injudicious decision to continue with the procurement of poor quality Elgi engines resulted in avoidable loss of Rs 25.68 lakh, besides spoiling the market reputation of the Company.

The Management stated (July 2005) that Elgi engines were purchased to develop a second source to counter the monopoly of Greaves engines. It was further stated that they dispensed with the idea of purchasing Elgi engines once it was certain that the engine was a failure. The reply is not acceptable since the price at the time of deciding for procurement of Elgi engine was 2.58 *per cent* more than that of Greaves engines and the Company failed to stop procurement of the engines even after receipt of adverse reports (November 1999) on their performance. Moreover, the continued sale of three wheelers with defective engines spoiled the name of the Company in the market.

The matter was reported to Government in June 2005; their reply has not been received (August 2005).

Kerala Livestock Development Board Limited

4.5 Incorrect classification of tariff

The Company failed to include the correct classification of tariff in the agreement with TATA for supply of power which resulted in avoidable payment of Rs.13.42 lakh.

The Company, engaged in cattle breeding, fodder production and allied activities, had a livestock farm at Mattupatty in Idukki District. The power supply for the above farm was being made by Tata Tea Limited (TATA), a sanction holder for supply of electricity under the Indian Electricity Act, 1910.

The categorisation of the consumer would be as per Kerala State Electricity Board (KSEB) tariff notification issued from time to time. As per the agreement entered into between the Company and TATA which was renewed (July 2002), the Company was classified under HT category.

The tariff made applicable by TATA for the purpose of billing was HT I Industrial category at Rs.270 per KVA for demand charges and Rs.2.50 per unit for energy charges which was further revised to Rs.3 per unit from October 2002. Since the Company was engaged in livestock development, the correct tariff applicable as per notification issued by the KSEB was that for HT III Agriculture at Rs.165 per KVA as demand charges and Rs.1.30 per unit towards energy charges from the date of agreement (July 2002).

The Company, however, did not ensure inclusion of correct classification having lower tariff in the agreement with TATA; an amount of Rs.13.42 lakh was paid in excess of the demand and energy charges during the period from July 2002 to March 2005. The efforts made (September 2004) by the Company to obtain refund of the excess amount from TATA was turned down (October 2004) since the classification HT Industrial was already included in the agreement.

Thus, the failure of the Company to include the correct eligible tariff in the agreement with TATA for supply of power resulted in avoidable payment of Rs.13.42 lakh.

The Government stated (July 2005) that efforts were being made by the Company to categorise the tariff under HT-III Agriculture. This confirms that the failure of the company, while entering into agreement, to ensure correct classification led to avoidable payment.

Malabar Cements Limited

4.6 Avoidable payment

Failure to exclude overlapping provisions in the work order of service agents with reference to the new fuel supply agreement resulted in avoidable payment of Rs.60.32 lakh towards bonus.

The Company entered into (April 2003) an annual Fuel Supply Agreement (FSA) with Singareni Collieries Company Limited (SCCL). As per the contract SCCL was to ensure the quality and grade of coal with reference to specified formula based on the ash and moisture content in the coal. For ensuring the grade and quality the FSA also provided for payment to SCCL guarantee charges at five *per cent* of the basic price of coal. For movement of coal from SCCL under the above contract, the Company appointed (March 2003) Naresh Kumar & Co Pvt. Limited (NKC), Secunderabad as the liaison/service agent. Ignoring the fact that SCCL had to ensure grade and quality of coal on payment of prescribed guarantee charges under the agreement, the Company included an overlapping provision for payment of bonus at Rs.23 per MT to the liaison agent, NKC, for every percentage decrease in ash content for the quantity of coal received. The liaison agent transported 89,903 MT of coal under the contract during the period April 2003 to April 2005 and was paid bonus aggregating Rs. 60.32 lakh.

Thus, the Company's failure to exclude overlapping provisions in the work order of service agents with reference to the FSA resulted in avoidable payment of Rs.60.32 lakh towards bonus for ensuring quality of coal.

Management stated (June 2005) that the FSA specified that the ash content in the coal would be in the range of 18 to 25 *per cent* and even one *per cent* reduction in ash content was very significant and hence bonus clause for ash reduction was included. The reply is not acceptable in view of the fact that agreement with SCCL for supply of coal had a provision for ensuring grade and quality at prescribed charges; the role of the transportation agent in this regard had, therefore, been rendered redundant.

The matter was reported to the Government in June 2005; their reply has not been received (September 2005).

STATUTORY CORPORATIONS

Kerala State Electricity Board

4.7 Implementation of Circle and Town schemes by Kerala State Electricity Board under Accelerated Power Development and Reforms Programme

Introduction

4.7.1 Government of India (GOI) approved (February 2001/June 2003) the Accelerated Power Development and Reforms Programme (APDRP) to

leverage reforms in the power sector through the State Governments and State Electricity Boards (SEBs) during the period from April 2000 to March 2012. The salient features of APDRP were upgradation of sub-transmission and distribution networks including energy audit and computerisation of billing with a view to reducing transmission and distribution (T&D) loss and cost of energy sold. The nodal agency for the implementation of APDRP was Power Finance Corporation Limited (PFC). Central Power Research Institute (CPRI) and National Thermal Power Corporation Limited (NTPC) were engaged as Advisor-cum-Consultants for the finalisation of detailed project reports (DPRs)/snap shots for the Circle/Town scheme. Three circles* and seven towns** were approved by GOI (August/November 2002) and the Kerala State Electricity Board (Board) (May/September 2003) for implementation of APDRP in Kerala by 2003-04 and 2004-05 respectively.

A Memorandum of Understanding (MOU) was signed (August 2001) between GOI and the State Government which was followed by two Memoranda of Agreement (MOA) in October 2002/July 2003 between GOI and the Board detailing the funding, administration, commercial and technical parameters under APDRP.

Deficiencies and irregularities noticed in audit on the basis of evaluation of the funding and implementation of the APDRP with reference to the parameters fixed in the MOA are discussed in the succeeding paragraphs.

Project cost and finance

4.7.2 The details of funds (excluding consultancy fee) received from GOI against the Circle and Town schemes by March 2005 were as given below.

(Rupees in crore)

Sl. No.	Scheme	Revised project cost excluding consultancy	Total share of GOI (25 per cent each as grant and loan)	Amount received/allocated	Eligible amount of re-imburement by March 2005	Excess amount allocated/received	Percentage of excess amount
i	ii	iii	iv	v	vi	vii (v-vi)	viii
1	Circle	148.24	74.12	90.79	74.12	16.67	22.49
2	Town	160.72	80.36	70.43	60.27	10.16	16.86
	Total	308.96	154.48	161.22	134.39	26.83	19.96

In this regard, following deserve mention :

4.7.3 Government of India released excess funds aggregating Rs.26.83 crore over and above the amounts due for release under the provisions of

* Kasargod, Manjeri and Pathanamthitta

** Alappuzha, Kollam, Kochi, Kozhikode, Kannur, Thalassery and Thiruvananthapuram

Memorandum of Agreement (MOA) Circle scheme (Rs.16.67 crore) and Town scheme (Rs.10.16 Crore) .

4.7.4 As per the MOA, the State Government should transfer GOI loan to the Board within a week of its receipt on the same terms and conditions. Audit analysis revealed that Rs.48.92 crore out of funds amounting to Rs.80.61 crore, were transferred (March 2003 - March 2005) to the Board after delay of up to 11 months. GOI loan carried interest rates ranging from 9 to 12 *per cent*. But the State Government transferred the funds to the Board at higher rates of interest in violation of the MOA which resulted in excessive burden of interest of Rs.1.15 crore to the Board.

4.7.5 The Board had been furnishing utilisation certificates at the DPR rates, which were at variance with the actual rates in respect of static meters, 11 KV lines, distribution transformers, etc. As the DPR rates were higher than the actual procurement rates, there was diversion of funds by Rs.17.70 crore and the penal interest payable during the two years ended 31 March 2005 worked out to Rs.1.64 crore (April 2005).

4.7.6 Rural Electrification Corporation (REC) which was providing counterpart funding for the schemes, released (March 2003 - March 2005) Rs.115.31 crore for the Circle (Rs.66.01 crore) and Town (Rs.49.30 crore) schemes and quarterly interest thereon was paid by the Board after allowing rebate for prompt payment for the period up to March 2005. Additional rebate of 0.5 *per cent* was available for providing the default escrow cover for the funds released by REC. Failure of the Board to create default escrow cover for counterpart funding by REC resulted in foregoing the additional rebate of 0.5 *per cent* during the period from March 2003 to March 2005 and consequent extra payment of interest of Rs.76.78 lakh.

4.7.7 The Board had incurred a total expenditure of Rs 224.16 crore for the Circle (Rs 140.96 crore) and Town (Rs 83.20 crore) schemes out of the amount of Rs 276.53 crore received up to March 2005 from GOI and REC for APDRP. In the Circle scheme, the Board has utilised Rs.24.65 crore towards single/three phase meters, distribution transformers, DTR meters, etc., in excess of the quantity projections made in the DPRs which has not been regularised (March 2005).

4.7.8 According to the Board (December 2002), allocation of Rs.15.45 crore towards consultancy fee for the finalisation of DPRs/snap shots against Circle (Rs.7.41 crore) and Town (Rs.8.04 crore) schemes was not justifiable in view of the limited scope of work. The Board has not taken up this matter with GOI even after a lapse of two years (March 2005).

Targets and achievements

4.7.9 APDRP was to be implemented by the Board during the period from 2002-03 to 2003-04 (Circle scheme) and 2003-04 to 2004-05 (Town scheme).

Physical target

4.7.10 The physical targets such as installation of meters, construction/reconductoring of 11 KV lines etc., in respect of Circle and Town schemes

was to be achieved by March 2005. A review of the physical targets vis-à-vis achievements revealed the following :

- Out of 13 physical parameters under the Circle scheme, the Board was able to achieve only eight till March 2005.
- The achievement against the remaining five parameters such as construction/reconductoring of 11 KV lines, installation of AB switches/feeder/border meters and repair & maintenance (R&M) of distribution transformers, ranged from 50 to 99 *per cent*.
- In the case of Town scheme, the Board could achieve only eight out of 27 physical parameters by March 2005.
- There was no physical achievement against seven items such as installation of new 33KV substations/lines, distribution transformer/feeder/border meters, 9 KVAR LT capacitors and computerised data logging at substations.
- The achievement against the remaining 12 factors ranged between 17 and 83 *per cent* (installation of single/three phase static meters/AB switches, 11 KV substations, construction/reconductoring of 11 KV lines/UG cables/LT lines, R&M of distribution transformers, etc.).

Financial target

4.7.11 The financial target achieved against the Circle scheme was 95 *per cent* and the scheme was closed (March 2005) after a time over run of one year. The Town scheme achieved a financial target of 52 *per cent* only till the targeted period of completion (March 2005) despite the release of funds by GOI in excess of the financial milestones as per the MOA.

Non-achievement of targets

4.7.12 Due to non-achievement of physical targets within the stipulated period, the Board could not achieve the committed benchmark parameters in respect of T&D loss under the Circle and Town schemes and the stipulated reduction in gap between the average rate of revenue realization and the average cost of sale of energy per unit under the Town scheme. The Board incurred an aggregate loss of Rs.185.03 crore for the years 2003-04 and 2004-05 for the Circle (Rs.13.76 crore) and Town (Rs.171.27 crore) schemes on these accounts.

Procurement of materials

4.7.13 The Board used to procure materials for the APDRP clubbing the requirements with that of similar materials for other schemes. Audit analysis revealed that a proper system was not being followed by the Board for procurement of materials, as shown in the succeeding paragraphs.

Failure to invite fresh tenders

4.7.14 The Board placed (November 2002) orders on Elymer Electrics (P) Limited, Delhi (EEL) for the supply of 60,000 three phase static meters at a

total cost of Rs.9.03 crore (unit cost Rs.1,504.80) against tenders invited in January 2002. Additional orders were also issued (February/March 2003) to EEL for 15,000 meters each for Rs.4.30 crore at Rs.1,446.16 and Rs.1,418.60 per meter respectively. The entire quantity was supplied by May 2003.

It was noticed in audit that EEL had supplied (January 2003) the same type of meters to Madhya Pradesh State Electricity Board at the unit rate of Rs.522. The lowest per unit rate quoted in response to the tender invited (April 2003) was also Rs.595.80 indicating the declining trend in price of meters. In the absence of a system to ascertain the rates prevalent in other SEBs for meters, the Board did not avail of the advantage of declining rates. Alternatively, the Board could have availed of the advantage in price by inviting fresh tenders in November 2002 instead of placing orders on EEL, after a delay of 10 months, at the higher rate. As the market rate for November 2002 was not available, the extra expenditure incurred in the purchase of 60,000 meters could not be quantified by Audit. The avoidable extra expenditure in the procurement of additional 30,000 meters with reference to the rate prevalent in January 2003 worked out to Rs.2.73 crore.

Undue benefit due to wrong refixation of prices

4.7.15 As per specific provisions included in the conditions of contract for procurement of meters, the Board was empowered to refix prices in respect of delayed deliveries based on the prevalent market price. It was, however, noticed in audit that even in cases where market rates based on subsequent bids were available, the Board followed the practice of refixing the prices at the lowest market rates only from the date of opening of tenders instead of from the date of bids. The undue benefit extended as a result to two suppliers in respect of 46,250 meters delivered (August 2003 and February 2004) after due dates against tenders invited (March and December 2003) worked out to Rs.46.82 lakh as detailed in **Annexure 19**.

Extra expenditure due to delay in procurement

4.7.16 As per projections made (August 2002), the Board required a total number of 900 distribution transformers for the APDRP circle scheme which was to be completed by March 2004. The Board, however, initiated action for procurement of transformers only in July 2003. Although the Board placed (March 2003) order for 400 transformers on Kerala Electrical and Allied Engineering Company Limited, Kochi (KEL) at the rate of Rs.44,354 per unit, on variable price basis, procurement for the APDRP was not made simultaneously ignoring the increasing trend in price. Subsequently (December 2003), order for 500 transformers was issued to The Unipower Systems, Kottayam at the rate of Rs.48,261 per unit and a further quantity of 450 to KEL (January 2004) at the rate of Rs.54,096 on variable price basis. The transformers were delivered by September 2003, December 2004 and May 2004 respectively. Non-placement of orders for distribution transformers despite increasing trend in prices resulted in non-availment of net benefit in price aggregating Rs.35.50 lakh after taking into account the interest savings in this respect.

Implementation of computerised billing

4.7.17 Deficiencies noticed in the procurement of computer systems are discussed below:

Loss due to defective tender evaluation

4.7.18 In connection with the procurement of system software for computerised LT billing in 560 sections and 10 data centres, the Board received (December 2002) three offers; out of this, the lowest two offers were that of Microsoft Corporation (India) Pvt. Limited (Microsoft) at Rs.3.32 crore and Oracle (India) Pvt. Limited (Oracle) for Rs.3.58 crore. The offer of Oracle included Rs.40 lakh for development of complete application software for billing whereas in the case of Microsoft the item was to be separately implemented by the Board with the assistance of Pricewaterhouse Coopers Pvt. Limited (PCL). While evaluating the tenders the rate for development of complete application software was, however, omitted to be excluded from the offer of Oracle. Due to this, the offer of Microsoft which was higher by Rs.14 lakh was finally accepted (January 2003). Thus, wrong evaluation of tenders resulted in a loss of Rs.14 lakh to the Board.

Non-implementation of computerisation

4.7.19 The application software developed by the Board for computerised billing developed errors leading to defective billing and resultant loss of revenue. The Board, however, has not assessed the extent of loss in this regard. Centre for Development of Advanced Computing, Thiruvananthapuram was engaged (January 2005) by the Board to assess the deficiencies and submit a report. Pending receipt of this, further computerisation in 383 billing units was kept in abeyance (March 2005).

Absence of technical evaluation in selection of servers

4.7.20 For the purpose of computerisation, the Board procured (March 2003) 80 servers for PC systems from CMC Limited, Thiruvananthapuram at Rs.80 lakh. Subsequently (December 2003), a further quantity of 97 servers was also procured from the same firm for Rs.2.22 crore. The first batch of servers was commissioned in July 2003 and second batch in February/March 2004.

Audit noticed that the Board conducted (September 2003) technical evaluation by an Expert Committee only in the case of the second batch and the first batch procured without any evaluation was found to be grossly inadequate for the Board's requirement due to insufficient CPU capability. Hence, the servers installed at a cost of Rs.80 lakh did not yield the desired benefit.

To sum up :

The Board was not able to reduce the T&D loss and cost of energy sold due to non-implementation of circle and town schemes in Kerala by March 2005 under APDRP despite the availability of funds. Utilisation certificates were furnished by the Board to GOI at DPR rates, which were at variance with the actual cost. The Board made extra payment of interest due to its failure to avail of the additional rebate of interest against REC loan. The Board incurred extra expenditure in the purchase of meters due to non-invitation of fresh tenders. Defective billing under computerisation has not been set right.

The matter was reported to Board/Government in June 2005; their replies have not been received (August 2005).

4.8 Avoidable loss

Failure of the Board to take follow up action for reimbursement of dues and omission to claim centage charges as per the terms of the MOU resulted in loss of Rs.65.91 lakh.

The Board entered into (March 1997) a Memorandum of Understanding (MOU) with Power Grid Corporation of India Limited (PGCIL) for the construction of 220 KV bay extension at Pallom substation at an estimated total cost Rs.5.20 crore on deposit work basis. The work was completed (October 2000) at a total cost of Rs.6.72 crore (including the value of material supplied by Power Grid: Rs.83.04 lakh).

Audit noticed that against the actual expenditure of Rs 5.76 crore incurred by the Board for the above work on behalf of PGCIL, the reimbursement made (May 2002) was to the extent of Rs.5.28 crore only. The Board did not take further follow-up action for re-imburement of balance amount of Rs.48.47 lakh due against expenditure incurred on behalf of PGCIL.

As per clause 6.1 of the MOU, the PGCIL was liable to pay the centage charges at the rate of 21 *per cent* on the cost of equipment/materials procured both by the Board/PGCIL, towards stores incidentals and supervision charges. Audit noticed that the Board, while computing the centage charges, failed to claim (January 2002) centage charges of Rs 17.44 lakh on value of material (Rs 83.04 lakh) supplied by PGCIL, in the total value of work.

The Government stated (June 2005) that the expenditure not reimbursed by the PGCIL related to diversion works and PGCIL was not liable to pay the same. Regarding centage charges, it was stated that action was being taken to recover the amounts from PGCIL. The reply is not acceptable as the expenditure amounting Rs. 12.35 lakh actually rejected by PGCIL on the grounds of diversion works, have already been excluded by Audit while arriving at unrecovered claim of Rs 48.47 lakh.

Further, since the final claim has already been settled the chances of recovery of Rs 65.91 lakh are remote. Thus, the failure of the Board to take follow up

action for reimbursement of dues and omission to claim centage charges as per the terms of the MOU resulted in loss of Rs.65.91 lakh.

4.9 Undue benefit to a supplier

Injudicious decision of the Board to allow enhancement in the firm rate resulted in an undue benefit of Rs.37.79 lakh to the supplier.

For procurement of 2000 Nos. of 12 m 'A' type poles required for 33 KV transmission lines in six Transmission circles, the Board placed (December 2003) orders on Shubham Comtech & Exports Pvt. Limited (SCE) at their lowest all inclusive rate of Rs.12,168 per pole. The price was stipulated (Clause 3) as firm. The Board did not incorporate the usual price variation formula in the contract with SCE even though the steel prices were subject to frequent revision.

The delivery of the material was to commence within 30 days (January 2004) and be completed within three months (March 2004). On the ground of increase in price of steel, SCE expressed (January 2004) their inability to supply the entire quantity at firm price and delivered (April 2004) only 646 poles at the agreed rate.

SCE, thereupon, requested (April 2004) for shortclosing of the purchase order. The Board finally accepted (September 2004) a revised price of Rs.14,959 per pole (all inclusive). The firm supplied (up to April 2005) 1354 poles at the enhanced rate involving additional cost of Rs.37.79 lakh (1354 x Rs. 2791).

Audit noticed that a local SSI unit (Auto Turns, Attingal) had offered (December 2003) to supply the poles at the lowest rate of Rs.12,168 per pole. The Board, however, did not accept this offer which was valid up to February 2004 though SCE in January 2004 had demanded enhancement in rate.

Thus, the injudicious decision of the Board to allow enhancement in the firm rate resulted in an undue benefit of Rs.37.79 lakh to the supplier.

The Government stated (July 2005) that the Board allowed reasonable escalation in the basic price to accommodate the steep hike in the price of steel and the post tender offer of Auto Turns was not considered since it would involve violation of rules and procedures. The reply is not acceptable as SCE would have quoted the firm rates taking into account the trend of rise in the price of steel. Considering the lower offer of Auto Turns when SCE demanded revision in rates in violation of the purchase order, would not be a violation of rules and procedures. Further, the delivery period of three months was also actually extended to 16 months affecting the targeted works.

4.10 Avoidable loss

Delay on the part of the Board in handing over of sites, making payments in time and failure to obtain insurance cover for materials resulted in avoidable loss of Rs 1.27 crore.

The Board entered into (April 2000) a turnkey contract with Andrew Yule & Company Limited, Calcutta (AYL) for the design, procurement, erection and commissioning of four 33/11 KV substations (Thiruvallloor, Orkattery, Melady, Ramanattukara) and bay extension at 110 KV substation, Vadakara at a total cost of Rs.9.52 crore. Financing of the project was out of loans provided by Rural Electrification Corporation Limited (REC) and Indian Overseas Bank (IOB) in the ratio 1:2 at the interest rate of 13.5 - 14 *per cent* per annum.

As per the contract, the work was to be completed within six months from the date of handing over of the land to the contractor. The Board, however, handed over the site to AYL during the period November 2000 to January 2002 only as against the start up date of April 2000. The works in all the five substations were not completed (April 2005) by AYL on the ground of delay in making payments against works executed. The total expenditure incurred on the project as of April 2005 was Rs 3.04 crore (Rs 2.61 crore on materials and Rs.0.43 crore on civil works).

Audit analysis revealed that there was a delay of 6 to 20 months on the part of the Board in handing over the sites for commencement of work by AYL. Though the funds were disbursed (March 1998 to March 2001) by REC and IOB to the extent of Rs 7.94 crore, the advance payment as well as stage payments against executed works were delayed by 1 ½ - 16 months. These delays arising from diversion of funds contributed to non-completion of the works. Funds to the extent of Rs.3.04 crore, invested in the Project, remained idle from August 2002 to April 2005 involving interest loss of Rs 1.12 crore at the borrowing rate of 13.5 *per cent* per annum.

The contract also provided (Clause 2) for joint insurance cover in the names of KSEB and AYL against damage to works and materials. The Board, however, failed to obtain the insurance cover in its name and materials worth Rs.15 lakh stored at site were destroyed (March 2004) by fire. In the absence of insurance cover the Board could not make good the loss.

Thus, the delay on the part of the Board in handing over of sites, making payments in time and failure to obtain insurance cover for materials resulted in avoidable loss of Rs 1.27 crore.

Government stated (August 2005) that the Board had taken all possible follow-up action for handing over the sites and they handed over all but one site in November 2000. Acute shortage of funds and delay in rectification of defective breakers were also attributed to reason for delay. The insurance coverage was stated to have been not revalidated by AYL even after repeated instruction. The reply is not tenable since the Board had a separate land acquisition wing; the acquisition and handing over of site should have been

done in time. As the project funds were provided by REC and Bank, finance cannot be considered as a constraint for delayed payments.

4.11 Non-realisation of dues

The Board could not recover Rs 1.23 crore towards energy consumption charges due to a faulty agreement with IOC for supply of fuel oils.

The Board had been using fuel oils (LSHS, HSD Oil) and lubricants for generation of power in its Brahmapuram Diesel Power Plant. For setting up fuel installation having storage and handling facility for fuel oils, the Board leased out land to Indian Oil Corporation Limited (IOC). As per clause 4 (c) of the lease agreement (July 1995) IOC had to pay the charges for consumption of water and electricity consumed on the premises.

For the supply of fuel oils and lubricants, the Board entered into (December 1995) a separate agreement with IOC. In this agreement the Board included clause 9 specifying maintenance of storage and allied facilities by the sellers (IOC) at their own cost. Under the same clause, a provision was also made stating that the maintenance and operation cost would be incurred by the buyers (Board), which was in contradiction to the earlier stated provision. Taking advantage of the ambiguity in the agreement IOC refused to make payment for electricity consumed during the period from July 1998 to July 2005 amounting to Rs.1.23 crore.

Audit noticed that in a similar agreement for supply of fuel oils, etc. with another company (BPCL), the Board was availing the benefit of concession at the rate of 3.5 *per cent* on the cost of the oils, etc., in consideration of the electricity and maintenance cost incurred by the Board on full storage establishments.

Thus, absence of due care in drafting the agreement for supply of fuel oil resulted in loss due to non-receipt of charges for energy consumption amounting to Rs.1.23 crore.

The matter was reported to Management/Government (May 2005); their replies have not been received (September 2005).

4.12 Locking up of funds

Construction of office-cum-commercial complexes without ensuring financial viability resulted in locking up of funds amounting to Rs.2.05 crore and interest loss of Rs.65.71 lakh.

As part of development of its own infrastructure, the Board approved (April 1999) a proposal for construction of office-cum-commercial complexes in 16 locations in the State on a self sustaining basis so as to avoid the drain on the Board's resources. The finance required for the scheme was tied up (May to August 2000) with Kerala Power Finance Corporation Limited (KPFL) at 1.5 *per cent* above State Bank of Travancore prime lending rate from time to time. At the time of entering into agreement the annual rate of interest so fixed was 13.5 *per cent*. The schemes were appraised as financially

viable and eight office-cum-commercial complexes involving a total area of 13,565.56 sq.m. were constructed during the period from July 2001 to July 2004 at a total cost of Rs.8.27 crore. This included 3,737.32 sq.m. of commercial area involving a proportionate cost of Rs. 2.20 crore.

Audit noticed that in five out of the eight complexes, constructed (July 2001 to June 2004), the entire commercial area aggregating 1,676.83 sq.m. valued at Rs.1.15 crore could not be leased out and remained vacant. In the remaining three complexes only 295.72 sq.m., out of 2,060.49 sq.m. area constructed could be used and the balance 1,764.77 sq.m. costing Rs.90.51 lakh could not be leased out. Altogether a commercial area of 3,441.60 sq.m., valued at Rs.2.05 crore remained un-occupied (August 2005) since construction for periods ranging between 13 and 49 months. The interest loss on the above investment worked out to Rs.65.71 lakh at 13.5 *per cent* per annum.

The non-occupancy of these complexes was due to their location in remote areas where leasing out the commercial complexes was difficult. The Board, while recommending all locations as financially viable (March 1999) had not noted this in respect of these areas.

Thus, the decision to construct office-cum-commercial complexes without ensuring financial viability resulted in locking up of borrowed funds amounting to Rs.2.05 crore leading to interest loss of Rs. 65.71 lakh.

The Government stated (August 2005) that the commercial complexes were constructed anticipating good response; but the actual response was not as expected. The reply indicates defective conceptualisation of the construction of buildings earmarking considerable areas for commercial purposes.

4.13 Non-recovery of claims

Inaction on the part of Government in taking decision in respect of claims recoverable by the Board from a private consumer firm, despite Court directions, resulted in non-realisation of Rs.14.27 crore and interest loss of Rs.6.39 crore.

Indsil Electrosmelts Limited, Palakkad, (IEL) an EHT consumer of the Board, was allowed (December 1994) to construct a 21 MW captive hydro electric power plant at Kuthungal in Idukki District. The construction of the project was in the final stages in August 2000.

IEL had been availing of the concessional rate of tariff for a period of five years from October 1994 based on the Industrial policy of the State Government. This concession was further extended till 20 August 2000 and IEL had to remit current charges at ruling tariff thereafter. The firm refused to remit the current charges at ruling tariff since August 2000 and approached the High Court contending that the captive project was completed in August 2000 and they could not draw power free of cost from the plant due to failure of the Board to construct allied transmission lines.

The Court issued (November 2000) directions to the Government to take immediate decision in the matter. The Government did not extend

concessional tariff beyond 20 August 2000. The Government, however, allowed IEL to remit the electricity charges initially at the concessional tariff up to February 2001 and the difference with reference to the ruling tariff in 48 monthly instalments commencing from March 2001. IEL declined to remit the dues of Rs.14.27 crore (billed as per ruling tariff) pertaining to the period up to May 2001 and petitioned Government against charging of ruling tariff. Due to inaction on the part of Government to decide the issue, IEL again approached the Court and the Court again directed (August 2001) the Government to dispose of the petition within a period of three months. The Government should have taken a decision in the matter by December 2001. Although the arrears of current charges due to the Board involved a significant amount (Rs.14.27 crore), Government had not taken a decision in the matter so far (May 2005). The Board also did not take any follow-up action for obtaining a decision from Government in the matter even though the private consumer had been retaining huge funds of the Board.

Thus, the inaction on the part of the Government in taking a decision in respect of claims recoverable by the Board from a private consumer firm, even after Court directions, and failure of the Board to follow-up the matter with Government resulted in non-realisation of Rs.14.27 crore and interest loss of Rs.6.39 crore (at the rate of 12.5 *per cent* per annum) for the period from November 2001 to May 2005.

The matter was reported to Management/Government (June 2005); their replies have not been received (September 2005).

4.14 Undue benefit to a Contractor

The Board failed to take into account the prevailing market prices of materials at the time of negotiation of contract rates which resulted in undue benefit of Rs.5.80 crore to a Contractor.

With a view to reduce line length loss by direct evacuation of power from the Kayamkulam power plant to 220 KV sub-station at Kundara, the Board awarded (May 2001) the 220 KV line construction work of 23 km length to Tata Projects Limited, Hyderabad (TATA) on turnkey basis at a cost of Rs.8.57 crore (excluding taxes). The work was to commence in May 2001 and to be completed by May 2002.

Owing to delays in completion of tree-cutting along line routes, approval of profile and tower schedules, foundation designs, etc., by the Board, the work was not started even after the scheduled completion date. The contractor, thereupon, demanded revision in scope of work for quantities not envisaged, revised schedule of unit prices and extension of completion period by 18 months. Since large variation in the quantity of work involved huge costs, the Board should have re-tendered the work. Instead, a revised price of Rs.36.69 crore was negotiated with the same party which was also accepted by a high level committee constituted (July 2003) by the Government. After exclusion of a few items the final contract price of Rs.31.64 crore was fixed and supplementary agreement executed (December 2003).

Audit analysis revealed that the work was originally awarded (May 2001) without properly estimating the quantities and the contract indicated the quantities as 'provisional' and subject to variation. Even though the Board had been contracting similar line works on a regular basis, the quantities in the work awarded to TATA were provisionally estimated. The increases provided at the time of supplementary agreement in respect of 16 items ranged between 4.35 and 395 *per cent* indicating that either the original estimation was wrong or the revised quantities estimated by TATA and accepted by the Board were exorbitant. The Board, however, had not investigated the matter.

As per the original contract the agreed rates were to be applied for quantity variations. The Board, however, revised the prices for quantity variations in the supplementary agreement and the increases granted ranged between 69 and 1686 *per cent*.

It was noticed in audit that the high level committee constituted by Government failed to take into account the prevailing market prices of materials while negotiating and finalising the revised contract price of Rs.31.64 crore. Due to this the rates allowed in respect of 11 items were higher than the market rates by 36 to 183 *per cent* and resulted in undue benefit of Rs.5.80 crore to the contractor.

The matter was reported to Board and Government in June 2005; their replies are awaited (September 2005).

4.15 Avoidable loss of interest

The Board failed to collect additional cash deposit aggregating Rs.2.17 crore from two Extra High Tension consumers resulting in loss of interest of Rs.82.46 lakh.

In order to ensure payment of monthly current charges and for safe custody of installation in the premises, the consumers of the Board had to deposit amounts with the Board. In the case of Extra High Tension (EHT) consumers such security deposit was stipulated in clause 14 (d) of the Condition of Supply of Electrical Energy as equal to two times the probable monthly current charges. The Board was also at liberty to enhance such deposit {Clause 14 (d)} and to review every year the deposits at the credit of the consumers.

Based on the above, the Board issued (August 2000) orders stipulating payment of additional security deposit by its EHT consumers, 50 *per cent* in cash and the balance in the form of Bank Guarantee. As per orders (January 2002) the amount of security deposit was to be based on the average of 12 months' maximum demand charges and energy charges immediately preceding the month in which the additional security deposit was demanded.

A review of the collection and adequacy of such cash deposit of 50 *per cent* from 32 non-seasonal consumers* was conducted in audit. It was noticed that

* Represents consumers who uses power supply during all seasons of the year.

due to absence of proper internal control, the Board did not raise demand for an aggregate amount of Rs.2.17 crore due from two consumers (Binani Zinc Limited and Travancore Rayons) since March 2002. In the case of five EHT consumers, though the bills were raised the deposit amount aggregating Rs.2.97 crore was collected after delays ranging between 19 and 30 months. Failure to raise the demand for the additional cash deposit of Rs.2.17 crore resulted in avoidable payment of interest of Rs.82.46 lakh for the period from March 2002 to April 2005 at the rate of 12 *per cent* per annum.

The matter was reported to the Board/Government in June 2005; their reply is awaited (September 2005).

Kerala State Road Transport Corporation

4.16 Avoidable extra expenditure

Failure of the Corporation to accept the offer for free supply of thermal paper and hasty decision to procure the material at own cost resulted in avoidable loss of Rs.1.08 crore and commitment for Rs.5.17 crore towards balance quantity of thermal paper to be procured.

The Corporation decided (February 2003) to introduce Electronic Ticketing Machine (ETM) at all its units in a phased manner. The supplier, Microfx, Thiruvananthapuram, who provided (February 2003) the thermal paper rolls for printing tickets in the initial stages, offered (May 2003) to supply the paper roll free of cost if they were allowed to print advertisement on the reverse side of the paper. The Corporation, without conducting any market enquiry/study decided (May 2003) to purchase required paper rolls at their own cost on the ground that permitting the supplier to canvass advertisement in lieu of the cost of paper was not profitable to the Corporation. Accordingly, decision was taken (June 2003) to invite tenders from interested parties for advertising on the reverse side of the paper.

Further, the Corporation in the same meeting (June 2003), based on the offer of Kerala Transport Development Finance Corporation Limited (KTDFC) for supply of paper free of cost with the right to print advertisement, decided to accept the offer of KTDFC, but for a restricted period of six months i.e, up to April 2004. The arrangements with KTDFC for supply of free paper rolls with advertisement rights were extended (November 2003) for further period of six months, i.e. up to July 2004.

In accordance with the decision taken (June 2003), the Corporation invited (November 2003) tenders for advertisement rights alone on the paper rolls for which no response was received. The Corporation should have further extended the period of KTDFC to avail of the benefit of supply of free paper rolls. Instead, the Corporation invited (December 2003) tenders for purchase of paper rolls and placed orders (February 2004) with Gopson Papers Limited, Noida (GPL) for 72 lakh rolls at Rs 8.68 per roll including CST. The Corporation received (upto September 2005) 12,40,680 paper rolls valued at

Rs 1.08 crore and balance quantity (59,59,320 rolls) was committed to be received in terms of purchase order.

Thus, the failure of the Corporation to accept the offer of KTDFC and other local firm (Microfx) for free supply of thermal paper and hasty decision to procure the material at own cost resulted in avoidable loss of Rs.1.08 crore and commitment for Rs.5.17 crore towards balance quantity of thermal paper to be procured.

The matter was reported to Management/Government (April 2005); their replies have not been received (August 2005).

4.17 Revenue loss

Failure of the Corporation to take follow-up action for display of advertisement resulted in revenue loss of Rs. one crore and avoidable interest payment of Rs.38.47 lakh.

The Corporation decided (March 2003) to implement Global Positioning System (GPS) for its Volvo and Fast passenger buses. The Financiers of the Corporation, Kerala Transport Development Finance Corporation Limited (KTDFC) were allowed (March 2003) to sponsor the system costing Rs.one crore with the right for advertisement. The sponsorship fee of Rs. one crore was received (March 2003).

The Corporation could not implement the GPS till March 2004 and alternatively proposed (March 2004) display of advertisement of KTDFC on the back of two Volvo buses and also in the bulk head partitions of all buses for a period of five years. In addition to the sponsorship fee already received the charges of advertisement material were also to be borne by KTDFC. The proposal was accepted (March 2004) by KTDFC.

Audit noticed that the Corporation did not initiate any follow-up action for display of advertisement. There were no reasons on record for not initiating action for display of advertisement. KTDFC converted (August 2004) the amount of Rs.one crore into a loan with interest rate of 9 *per cent* per annum. The Corporation was also directed (August 2004) to pay interest at the rate of 12 *per cent* per annum from the date of receipt (27 March 2003) of the amount to the date of conversion (15 August 2004). Payment of Rs.16.70 lakh was accordingly made (August 2004). The loan amount of Rs.one crore together with interest (Rs.23.27 lakh) was being repaid at an Equated Daily Instalment (EDI) of Rs.7,000 from the escrow account opened for the purpose.

Thus, the failure of the Corporation to take follow-up action for display of advertisement resulted in revenue loss of Rs. one crore and avoidable interest payment of Rs.38.47 lakh (net of interest saving of Rs.1.50 lakh).

The matter was reported to Management/Government (April 2005); their replies have not been received (September 2005).

4.18 Avoidable expenditure

Injudicious decision to enter into Annual Maintenance Contract for mini buses despite availability of its own facilities resulted in avoidable expenditure of Rs.1.23 crore.

The Corporation with a fleet strength of 4,338 buses as on 31 March 2003 had sufficient infrastructural facilities, technical expertise and man-power in all its 83 operating units and five workshops to carry out routine and preventive maintenance and repair works of the fleet. In fact these works were being attended to since inception (March 1965) by its own staff with the facilities created.

During the period from March 2002 to March 2005, the Corporation procured 289 mini buses. Deviating from the usual offer for price of vehicles alone, the suppliers had offered annual maintenance also at rates ranging from 50 paise per km to Rs.1.35 per km for the initial period of three years. The Corporation did not take into account its own extensive repair and maintenance facility available throughout the State and entered into Annual Maintenance Contract (AMC) for the first three years while placing orders in addition to the warranty provided by the supplier. The actual annual maintenance charges paid to the three suppliers (TATA, Ashok Leyland and Eicher) during the period of October 2002 to April 2005 amounted to Rs.1.23 crore.

It was noticed in audit that the AMC covered only routine items like periodical oil change, hub greasing, replacement of normal wear and tear items, servicing of alternators, etc., which the Corporation was also carrying out in respect of its regular fleet. The maintenance work involved in respect of the new vehicles during the first three years is generally very limited which could have been attended to by utilising the facilities available at its operating units and workshops.

Thus, the injudicious decision to enter into an AMC despite having its own facilities resulted in avoidable expenditure of Rs.1.23 crore. The Corporation which had an accumulated loss of Rs.1139.94 crore (as on 31 March 2003) and which was incurring huge annual loss should have adopted cost-conscious measures rather than incurring avoidable expenditure.

Management stated (August 2005) that they have decided to discontinue the AMC and impart necessary training to their staff in maintenance of mini buses.

The matter was reported to Government in May 2005; their reply is awaited (September 2005).

4.19 Avoidable extra expenditure

The Corporation procured mini buses at the highest rates which resulted in avoidable extra expenditure of Rs.47 lakh besides liability for additional operating expenditure of Rs 0.73 per Km for five years.

The Corporation had (May 2003) 40 TATA mini buses in its vehicle fleet for economic operation in sub-urban areas. The Corporation invited (May 2003) tenders for the purchase of 50 mini buses to augment its fleet strength. Of the three firms who quoted, the offer of Ashok Leyland Limited, Kochi (ALL) at Rs.7.83 lakh per bus was the lowest with advantages of sturdiness and inter-changeability of spare parts with the bigger buses in the fleet as well as suitability for operation in all ranges. The Corporation, however, evaluated the highest offer of Eicher Motors Limited, Kochi (Eicher) of Rs 8.30 lakh per bus as economical on the ground of low running and maintenance cost at Rs.7.25 per km as against Rs.7.37 per km worked out for the ALL mini buses. Accordingly, orders were placed (May 2003) on Eicher for 50 mini buses at the all inclusive price of Rs.8.30 lakh per bus. This was followed by another purchase order (July 2003) for 50 buses on Eicher at the same rate. All the 100 buses were supplied during the period from August 2003 to June 2004.

Audit analysis revealed that the Corporation had adopted 90,000 km as the annual operation for the five year life of mini buses for the purpose of evaluation of the offer of ALL and Eicher whereas the actual annual operational level quoted by them was 96,000 km and 90,000 km respectively. With reference to the higher operational level of ALL, the annual running and maintenance expenditure was Rs.7.15 per km as against Rs.7.25 per km computed for Eicher. The evaluation based on uniform methodology would have rendered the lowest price (Rs.7.83 lakh per bus) of ALL more economical with reference to performance as well. The resultant extra expenditure incurred was Rs.47 lakh (at the rate of Rs.0.47 lakh on 100 buses).

It was further noticed that the actual mileage obtained for Eicher buses during the year 2004 was only 5.23 km/litre as against 6.33km/litre adopted for purpose of evaluation which had the impact of additional expenditure of 73 paise per km per bus on their operational expenditure.

Thus, the decision of the Corporation to procure mini buses at the higher rates resulted in avoidable extra expenditure of Rs.47 lakh besides liability for additional operating expenditure of 73 paise per km for the five years up to 2007-08.

The Management stated (August 2005) that the decision to purchase Eicher mini buses was taken after evaluating the trial runs conducted. The reply is not tenable as the evaluation of tender was done with a higher performance level when compared to actuals.

The matter was reported to Government in June 2005; their reply is awaited (September 2005).

GENERAL

4.20 Corporate Governance in State Government Companies

Introduction

4.20.1 Corporate Governance is the system by which companies are directed and controlled by the management in the best interest of the shareholders and others ensuring greater transparency and better and timely financial reporting. The Board of Directors are responsible for governance in State Government Companies.

4.20.2 The Companies Act, 1956 was amended in December 2000 by providing, *inter alia*, for a Directors' Responsibility Statement (Section 217) to be attached to the Director's Report to the shareholders. According to Section 217(2AA) of the Act, the Board of Directors has to report to the shareholders that they have taken proper and sufficient care for the maintenance of the accounting records for safeguarding the assets of the company and for detecting and preventing fraud and other irregularities.

Further, in terms of Section 292A of the Companies Act, 1956, notified in December 2000, every public limited company having paid up capital of not less than rupees five crore shall constitute an Audit Committee, at the Board level. The Act also provides that the Statutory Auditors, Internal Auditors, if any, and the Director in charge of Finance should attend and participate in the meetings of the Audit Committee.

4.20.3 The main components of Corporate Governance are:

- matters relating to the Board of Directors;
- Director's Report;
- constitution of the Audit Committee.

4.20.4 Out of the 85 working State Government Companies, Audit reviewed 25 Companies (all unlisted) as detailed in **Annexure 20**. Audit findings are discussed in the succeeding paragraphs.

Board of Directors

4.20.5 The responsibility for good governance rests on the Corporate Board which has the primary duty of ensuring that principles of Corporate Governance both as imbibed in law and those expected by the stakeholders are scrupulously and voluntarily complied with and the stakeholders' interests are kept at the highest level. For this purpose, every company should hold meetings of the Board of Directors at regular intervals. Every Director should attend these meetings to share the expertise and knowledge and to guide the affairs of the company.

Meeting of the Board of Directors

Board meetings were not held as prescribed.

4.20.6 Section 285 of the Companies Act, 1956 requires that in the case of every company, a meeting of the Board of Directors should be held every three months and at least four such meeting should be held every year. Audit

scrutiny revealed that only three meetings of the Board of Directors were conducted by TCCL during the year 2002-03. In the case of KFDC only three meetings each of the Board were conducted during the years 2001-02 and 2003-04. Similarly the Board of Directors of KSCCL met only three times during the years 2001-02, 2003-04 and 2004-05. Thus, the managements of these Companies failed to comply with the legal provision.

Attendance of Directors in the Board meetings

Directors failed to attend the Board meetings regularly

4.20.7 Audit noticed that nine Directors of four companies (TELK, KTDC, KSCSC and KSCCL) did not attend any of the meetings conducted during the year 2001-02 while eight Directors of five companies (MCL, RBDCK, KTDFC, KSCSC and KSCCL) failed to attend any meeting during the year 2002-03. Similarly eight Directors of four companies (KAMCO, KSIDC, TCC and KSEDC) absented themselves from all the meetings conducted during the year 2003-04 while seven Directors of four companies (KTDC, KSCCL, KSIDC and KSEDC) did not attend any of the meetings conducted during 2004-05. This indicated that the Directors did not actively participate in the management of the affairs of the Companies and in the decision making process to safeguard the interest of the Companies.

Preparation of the Minutes of the meetings of the Board of Directors

4.20.8 Section 193 of the Companies Act, 1956, stipulates that every company shall prepare the minutes of proceedings of all general meetings and the meetings of the Board of Directors within thirty days of such meeting. The record of proceedings of a meeting is required to be recorded in the minutes book. It was observed that in two companies (TCCL and KAL), the minutes of the meeting of Board of Directors were not prepared within thirty days of the meeting.

Directors Report to shareholders

4.20.9 The Companies Act, 1956 {Section 217 (2 AA)} requires that a report of the Board of Directors including a Director's Responsibility Statement (DRS) is to be attached to every balance sheet laid before the shareholders at the Annual General Meeting. Audit scrutiny revealed that the Director's Report of KAL for the year 2002-03 did not include the DRS. The DRS regarding the application of Accounting Standards in the case of KTDFC had been given although the company had been consistently flouting the Accounting Standard-15, i.e., accounting for retirement benefits of employees in its financial Statements.

Addendum to the Director's Report

4.20.10 As per Section 217(3) of the Companies Act, 1956 the Board is bound to give the fullest information and explanations in an addendum to the Board's report on every reservation, qualification or adverse remark contained in the Auditor's report. Audit scrutiny disclosed that the Board of Directors of four companies (KTDC, KSBC, OPL and KTDFC) failed in complying with this statutory requirement. Even though the Statutory Auditors of KEL made a number of qualifications/ adverse remarks in their Audit Report on the accounts of the company for the financial year 2001-02, the Directors of the company replied only selectively to a few qualifications.

Audit Committee

Role and functions

4.20.11 The main functions of the Audit Committee are to assess and review the financial reporting system, to ensure that the financial statements are correct, sufficient and credible. It follows up on all issues and interacts with the Statutory Auditors before finalisation of the annual accounts. The Committee also reviews the adequacy of the Internal Control System and holds discussion with Internal Auditors on any significant finding and follow up action thereon. It also reviews the financial and risk management policies and evaluates the findings of internal investigation where there are any suspected frauds or irregularities or failure of the Internal Control System of a material nature and reports to the Board.

4.20.12 Nine public limited companies were selected by audit for review; of these in two companies (TTP and KAMCO) the paid up capital was less than Rupees five crore and hence they were not required to constitute the Audit Committees. In respect of the remaining seven companies, the position is given in the succeeding paragraphs.

Terms of reference

Terms of reference were not specified by board

4.20.13 The Board of three companies (MCL, KFL and TCCL) failed to specify the terms of reference of Audit Committees in writing. The terms of reference proposed by the Board of Directors of RBDCK did not give its Audit Committee the mandate to deal with fraud or fraud related risks.

Meetings of Audit Committees

4.20.14 The Following were noticed:

- The Audit Committee was constituted by TCCL only in March 2002 and hence no meeting was conducted during the year 2001-02. The Company did not hold even one meeting of the Audit Committee during the year 2004-05.
- Even though the Audit Committee was constituted (August 2001) no meeting was conducted by TELK during the years 2001-02 and 2002-03. Only one meeting was conducted during the year 2003-04.
- The Audit Committee of MCL met only once during the years 2002-03 and 2004-05.
- Only one Audit Committee meeting was conducted by KSHDC during the years 2001-02 and 2002-03.
- The Audit Committee of RBDCK has been meeting only once in a year since its formation in June 2001.
- KSHDC and TELK had not ensured the attendance of the Statutory Auditors and Internal Auditors in any of the meetings of the Audit Committee, in violation of subsection 5 of section 292 A of the Companies Act, 1956.

Frequency of Audit Committee Meetings was low

- As per orders (August 2001) of the Government, the Cost Auditors are required to attend the meetings of the Audit Committee. The Cost Auditors of TCCL, however, did not attend any of the meetings of the Audit Committee.

Discussion by the Audit Committees

4.20.15 Section 292A(6) of the Companies Act, 1956, requires that the Audit Committee should have discussions with the auditors periodically about the internal control systems, the scope of audit including the observations of the auditors and review the half-yearly and annual financial statements before submission to the Board and also ensure compliance of the internal control systems.

4.20.16 Audit scrutiny revealed the following:

Audit Committee did not discuss the Internal Control System

- The adequacy of the internal control measures and internal audit were not being reviewed by the Audit Committees of KFL, TCCL, MCL, KSHDC, RBDCK and TELK.
- Even though the terms of reference of the Audit Committee of RBDCK required half yearly review of seven items of internal control, the Audit Committee had only one discussion in respect of two items.
- The Government had asked (May 2004) KFL to take action against some of the officials found guilty by the Inspection Wing of the Government and report compliance. The matter was not discussed by the Audit Committee of the company.
- The Audit Committees of TCCL, MCL, KSHDC, RBDCK and TELK have not reviewed the financial and risk management policies of the company.
- The first Audit Committee meeting of KFL directed the Managing Director to convene a meeting of all divisional heads to discuss about the internal control techniques to be implemented in the company and also place the item for discussion during the next meeting of the Committee. The matter, however, was not discussed by the committee in any of the subsequent meetings.
- The Audit Committee of MCL had given a recommendation for the disposal of obsolete stores which was not implemented by the Board. No reasons were, however, communicated to the shareholders for non-implementation of the said recommendations by MCL as required under subsection- 9 of the section 292 A of the Companies Act, 1956.

Recommendation of Audit Committee was not considered by the Board

Attendance of Chairman of Audit Committee at the Annual General Meeting (AGM)

4.20.17 Sub section 10 of Section 292 A of the Companies Act, 1956, requires the Chairman of the Audit Committee to attend the AGM of the company and provide any clarification on matters relating to audit. The Chairmen of the Audit Committees of four companies (TCCL, KSHDC, RBDCK and TELK) had never attended any AGM during the period under review. The Chairman of MCL did not attend the AGMs for the years 2001-02 and 2002-03.

General

4.20.18 As per Section 383(A) of the Companies Act, 1956, all companies having paid up capital of not less than 2 crore shall have a whole time Company Secretary. Five companies (KFL, KAL, KTDFC, KSCSCL and KEL), however, did not comply with this provision.

Attendance of the Directors in the AGMs

4.20.19 In the absence of any compelling provision in the Companies Act, 1956, the attendance of directors in the AGMs was found to be minimal. Scrutiny in audit revealed that out of the twenty five companies selected by audit, in thirteen companies none of the Directors other than the Managing Directors and Chairmen of the Board of Directors attended any of the AGMs conducted during the period from April 2001 to March 2005.

To Sum up:

- **The attendance of Directors in the Board meetings as well as in the AGMs was found to be not regular.**
- **Some companies have violated provisions of the Companies Act, 1956, regarding the minimum number of Board meetings, preparation of Board minutes and Directors' Report.**
- **The frequency of Audit Committee Meetings was found to be low. The Audit Committees of most of the companies have not discussed the effectiveness of the internal control system. Further the Audit Committees of most of the companies did not have any meaningful discussions on matters having serious bearing on finance and audit.**

4.21 Delay in placement of Annual Reports of Government Companies before State Legislature

As per Section 619 A (3) of the Companies Act, 1956, where State Government is a member of a Company, the State Government shall cause an Annual Report on the working and affairs of the company along with audit report and comments or supplement of the Comptroller and Auditor General of India to be placed before State legislature within three months from the date of Annual General Meeting (AGM) in which the accounts have been adopted. The Annual Report consists of report by the Board of Directors on the working of company as required in Section 217 of the Companies Act, 1956, annual financial statements for the year and Auditors' Report thereon with the comments/ supplementary report of Comptroller and Auditor General of India. The placing of the Annual Report before the State Legislature gives it an opportunity to have important information regarding the performance of a Government company, in which the State Government is the major share holder.

Audit scrutiny of related records revealed that the Annual Reports of most of the companies have either not been placed or been placed belatedly, mainly due to delay in conducting AGMs. As a consequence it delayed finalisation of accounts and delay in placing the Report even after conducting the AGM. Out of 108 Government companies, 16 companies placed their Annual Reports for

2003-04 before the State Legislature during the period up to March 2005 and out of this only five* companies placed the Annual Reports within the prescribed time.

Audit further noticed that :

- there were delays ranging from three to eleven years in placing the Reports in respect of ten companies as shown in **Annexure 21** mainly on account of delay in finalisation of accounts. Even after holding the AGM, delay ranging from two to eight months was observed in placing these Reports before the legislature.
- Travancore Cements Limited and Pharmaceutical Corporation (IM) Kerala Limited have placed their Annual Report for the years 2001-02 and 2000-01 respectively after a delay of one year after conducting the AGM even though the accounts related to old periods.
- though the accounts of Kerala Minerals and Metals Limited (KMML), Malabar Cements Limited (MCL), Kerala Feeds Limited (KFL) and Transformers and Electricals Kerala Limited (TELK) were finalised up to 2003-04, Annual Reports for the period up to 1999-00 (TELK), 2000-01 (KMML) and 2001-02 (MCL, KFL) only had been placed.
- 57 companies as mentioned in **Annexure 22** had finalised accounts relating to different periods during 2004-05. The Annual Reports pertaining to these periods had not been placed in the Legislature till date (May 2005).
- the Committee on Papers Laid Before the Table (2001-04) in its Sixth Report dated 3 February 2004 noted that there was serious lapse on the part of administrative departments in ensuring timely presentation of Annual Reports to the Legislature.

The matter was reported to Government in July 2005; reply was awaited (September 2005).

4.22 Persistent non compliance with Accounting Standards in preparation of financial statements

Accounting Standards (AS) are the acceptable standards of accounting recommended by the Institute of Chartered Accountants of India and prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards. The purpose of introducing AS is to facilitate the adoption of standard accounting practices by companies so that the annual accounts prepared exhibit a true and fair view of the transactions and also to facilitate the comparability of the information contained in published financial statements of companies. Under Section 211 (3A) of the Companies Act 1956 it is obligatory for every company to

* Kerala State Industrial Enterprises Limited, Travancore Titanium Products Limited, Tourist Resorts Kerala Limited, Oil Palm India Limited and Kerala Agro Machinery Corporation Limited

prepare the financial statements (profit & loss account and balance sheet) in accordance with the AS. A review of the financial statements and the Statutory Auditors' report thereon in respect of 20 selected companies revealed non-compliance with one to four Accounting Standards as detailed in **Annexure 23**.

It would be seen from the **Annexure** that:

- out of the 20 companies which finalised their previous years' accounts as of March 2005, 12^{*} companies violated AS 15 which deals with accounting for retirement benefits to employees (viz., provident fund, pension, gratuity, leave encashment etc.) provides that the contribution payable by the employer towards retirement benefits be charged to statement of Profit and Loss for the year on accrual basis and the accruing liability calculated according to actuarial valuation.
- seven[#] companies did not comply with AS 2 relating to determination of the value at which inventories are carried in financial statements until the related revenues are realised and provides that inventories should be valued at the lower of cost or net realisable value.
- four[@] companies persistently flouted AS 12 which deals with method of accounting for Government grants as to whether it related to capital or revenue.
- two⁺ companies having distinguishable segments have not complied with AS 17 which deals with segment reporting and establishes principles for reporting financial information about the different types of products and services and also the different geographical areas in which it operates.
- out of the 20 Companies test checked in audit, 17 Companies continuously violated the Accounting Standards.

The matter was reported to Government in July 2005; reply is awaited (July 2005).

4.23 Follow-up action on Audit Reports

Explanatory Notes^{} outstanding*

4.23.1 The Audit Reports of The Comptroller and Auditor General of India represent the culmination of the process of scrutiny starting with initial inspection of accounts and records maintained in the various Government Companies and Statutory Corporations. It is, therefore, necessary that they elicit appropriate and timely response from the Executive.

* Serial No. 2, 3, 5, 7, 9, 14, 15, 16, 17, 18, 19 and 20 of **Annexure 23**

Serial No. 1, 2, 3, 4, 5, 6 and 7 of **Annexure 23**

@ Serial No. 4, 5, 11 and 12 of **Annexure 23**

+ serial No. 3 and 14 of **Annexure 23**

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

The Audit Reports for the years up to 2003-04 have been presented to the State Legislature but three out of ten departments did not furnish explanatory notes on seven out of 20 paragraphs/reviews relating to the Audit Report for the year 2002-03 as on September 2005.

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

4.23.2 As per the Handbook of Instructions for Speedy Settlement of Audit Objections, the replies to paragraphs are required to be furnished within one month from the presentation of the Reports by COPU to the State Legislature. Action Taken Notes (ATNs) to 322 paragraphs pertaining to 60 Reports of the COPU presented to the State Legislature between July 2000 and September 2005 had not been received as of September 2005 as shown below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where ATNs not received
1998-2000	6	39
2001	3	8
2001-2004	25	178
2004-2006	26	97
Total	60	322

Response to inspection reports, draft paragraphs and reviews

4.23.3 Audit observations made during audit and not settled on the spot are communicated to the heads of the PSUs and the concerned departments of the State Government through inspection reports. The heads of PSUs are required to furnish replies to the inspection reports through the respective heads of departments within a period of six weeks. Inspection reports issued up to March 2005 pertaining to 98 PSUs disclosed that 6,303 paragraphs relating to 1,157 inspection reports remained outstanding at the end of September 2005; of these, 341 inspection reports containing 2,458 paragraphs had not been replied to for one to five years. Department-wise break-up of inspection reports and paragraphs outstanding as on 30 September 2005 is given in **Annexure 24**.

Similarly draft paragraphs and reviews on the working of PSUs are forwarded to the Principal Secretary/Secretary of the administrative department concerned demi-officially seeking confirmation of facts and figures and their comments thereon within a period of six weeks. It was, however, observed that fifteen draft paragraphs and one draft review forwarded to the various departments during April to July 2005, as detailed in **Annexure 25**, had not been replied to so far (September 2005).

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

Thiruvananthapuram

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The

Countersigned

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(VIJAYENDRA N. KAUL)

Comptroller and Auditor General of India

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