Chapter IV

4. Transaction Audit Observations

Important audit findings emerging from test check of transactions made by the State Government Companies/Corporations have been included in this Chapter.

Government Companies

Kerala Automobiles Limited

4.1 Wasteful expenditure due to decision

The decision of the Company to purchase unauthorised prototype of four stroke engine from a local firm without undertaking any technical and financial feasibility study for its development resulted in wasteful expenditure of Rs. 1.15 crore.

The Company, engaged in the manufacture of various types of three wheelers, had been procuring two stroke engines from outside sources. New emission norms effective from April 2000 required the Company to switch over from two stroke to four stroke petrol engines. Hence the Board of Directors decided (May 2003) to go for the design and development of new four stroke engines. The Company entered (July 2003) into an agreement with the Supreme Enterprises (SE) for supply of already developed prototype of 'Yamaha' engine at the negotiated price of Rs. 55 lakh, without verifying the right of the local firm to supply the Yamaha engine prototype.

SE supplied the prototype and the Company made the payment in July 2003. The Company further incurred (July 2003 - June 2006) additional expenditure towards testing fee, consultation fee, tools, etc., to the tune of Rs. 60 lakh and the total expenditure for the prototype engine worked out to Rs. 1.15 crore.

Audit noticed (June 2007) that the Company could not proceed with further development of prototype and production of engines due to lack of technical infrastructure, poor financial position and possibility of legal action by the original equipment manufacturer for infringement of rights on the prototype supplied by SE. Thus, the expenditure of Rs. 1.15 crore incurred by the Company upto June 2006 remained wasteful.

Audit further noticed that no feasibility study on the project considering the then existing infrastructural facilities was conducted and the project was taken up by the Company, without arranging finance for implementation of the project which was later (June 2006) estimated at Rs. 5.15 crore. Moreover the technical expert who provided (February 2001) the assessment report on the 'Yamaha' engine design had warned the Company of infringement of patent right which was also not taken into consideration at the time of procurement of prototype and making payment.

Thus, the decision of the Company to purchase prototype of four stroke engine from a local firm who had no legal rights to sell it coupled with failure

to undertake any operational and financial feasibility study for its development, had resulted in wasteful expenditure of Rs. 1.15 crore.

The matter was reported to Government/ Management in March 2008; their reply was awaited (August 2008).

Kerala Feeds Limited

4.2 Avoidable revenue loss

Failure of the Company to revise the prices in consonance with its pricing policy so as to achieve the break even levels resulted in a loss of Rs. 3.68 crore.

The Company, engaged in the manufacture and sale of compounded cattle feed, follows cost plus pricing policy taking into account the prevailing market price. The Managing Director of the Company had the discretion to effect price adjustments up to five *per cent* of the maximum retail price based on variation in the formulation cost of raw materials.

The average raw material cost during the year 2005-06 was Rs. 5,280 per MT and the price charged by the Company during that period was Rs. 7,600 per MT which was covering both direct cost and overheads. From June 2006 onwards the cost of raw materials showed an increasing trend which reached Rs. 5,911 per MT in August 2006. Up to August 2006 the Company, however, did not initiate any action to revise the price while its competitors increased (August 2006) the price by Rs. 360 per MT. Even though the Company subsequently made (November 2006) a marginal increase in price by Rs. 200 per MT, it continued to incur losses. Until August 2007 the Company effected a total increase in price of Rs. 1,000 per MT when the raw material cost itself showed an increase of Rs. 1,178 per MT. The total price revision made by the competitors during the same period was Rs. 1,260 per MT. The total cash loss incurred by the Company on 1,54,616 MT feed sold from September 2006 to July 2007 was Rs. 3.68 crore as a result of its failure to revise the prices in consonance with its pricing policy so as to achieve the break even levels.

The Government stated (June 2008) that the Company had to fulfil the social responsibility and consequent to the Government policy of controlling the price of cattle feed, the Company could not increase the selling price in tune with the increase in the raw material cost. The fact remains that neither the action of the Company was in conformity with its pricing policy nor the Government made good the loss.

Travancore Cochin Chemicals Limited

4.3 Extra expenditure

Decision of the Company to discontinue the insurance of critical items of machinery under Machinery Breakdown Policy resulted in extra expenditure of Rs. 74.25 lakh.

The Company, engaged in the production and marketing of caustic soda, had been insuring (since 2000-01) its major electrical items with Kerala State Insurance Department under the Machinery Breakdown Policy (MBP). Under this policy, any loss or damage by fire arising from short circuit within the electrical appliance and installation had also been covered. The schedule of machinery insured under MBP for the period 2004-05 included an EMCO make Rectifier Transformer which had a critical function to power the electrolysers. The sum assured for this item was Rs. 1.38 crore.

Subsequently, the Company discontinued (March 2005) the insurance under MBP on the ground that it was not advantageous considering the ratio of claim amount received and the actual amount of premiums paid during the previous years. The Company failed to safeguard its interest as coverage of risk under insurance was much more important than the expenditure incurred on premium since the cost of damage would be left uncovered in the case of non-insurance.

In April 2007, the rectifier transformer was damaged due to short circuit and was repaired at a cost of Rs. 90 lakh. Later, in the light of accident and breakdown of the transformer, the Company insured (January 2008) all critical equipments under MBP with the Oriental Insurance Company Limited.

Thus the decision of the Company to discontinue the insurance of critical items of machinery under MBP resulted in extra expenditure of Rs. 74.25 lakh after excluding saving towards premium payable for two years.

The matter was reported to the Government/ Management in April 2008; their reply was awaited (August 2008).

Kerala Tourism Development Corporation Limited

4.4 Avoidable extra expenditure

Failure of the Company to regulate payments in accordance with the contractual provisions resulted in avoidable extra expenditure of Rs. 55.53 lakh.

The Company had been outsourcing the cleaning works of its hotel units since March 2001. The work was entrusted to Flowrence Nightingale Professional Service Agencies (March 2001) at Rs. 1,200 per 1,000 sq. ft per month for premium properties. In the case of other properties, the work was entrusted to Safe Security Services (November 2001-March 2007) @ Rs. 574 per 1,000 sq. ft. per month and Omega Security Agencies (June 2007) @ Rs. 670 per 1,000 sq. ft. per month. Agreements were also executed (March/ November 2001/

June 2007). As per the terms of agreement, the rates fixed for all the three firms were all inclusive.

Audit observed (February 2008) that the Company paid service tax as claimed by the contractors even though the rates were all inclusive, which led to excess payment. The total excess payment made by the Company towards service tax to the above three firms for the period April 2004 to January 2008 worked out to Rs. 55.53 lakh. Thus the failure of the Company to regulate payments in accordance with the contractual provisions resulted in avoidable extra expenditure of Rs. 55.53 lakh.

Government stated (May 2008) that in the notification released for selecting manpower supply agencies and in the agreement the Company had not envisaged that the rate was inclusive of service tax, and EPF, ESI and other statutory labour welfare measures only was meant by the term "all inclusive". The term "all inclusive" includes all and the Company cannot interpret it at its discretion later. If the taxes were not to be covered, the same should have been clearly specified in the agreements.

United Electrical Industries Limited

4.5 Wasteful expenditure

Decision of the Company to commence the construction activities of pole casting project without Government approval and acceptance of order before creating infrastructural facilities resulted in a wasteful expenditure of Rs. 29.60 lakh as well as a committed liability of Rs. 37.85 lakh.

The Company participated (January 2005) in a tender floated by Kerala State Electricity Board (KSEB) for supply of Pre Structured Concrete (PSC) poles, the manufacturing facilities for which were yet to be set up. The total cost of the project for setting up the pole casting yard and other infrastructural facility as per project report was Rs. 2.50 crore consisting of rupees one crore for fixed investment and Rs. 1.50 crore towards working capital. The sources of financing considered were bank loan (Rs. 1.50 crore) and Company's own contribution (Rupees one crore).

The Company submitted (March 2005) the proposal to the Government for approval and sought for one time financial assistance. In the meanwhile, the Company received (April 2005) an order from KSEB for supply of 3.13 lakh poles to be delivered from September 2005 to August 2010. While the Government approval was pending, the Company commenced the construction work of yard and incurred expenditure of Rs. 42.61 lakh up to January 2006. Eventually, the Government rejected (January 2007) the proposal of the Company on the grounds of low margin of profit, requirement of additional manpower, lack of requisite technology, etc.

Thereupon, the Company abandoned (March 2007) the project and the expenditure liability incurred as on that date amounted to Rs. 67.45 lakh against which payment was made to the extent of Rs. 29.60 lakh (March 2007). Further, due to non-supply of poles, KSEB terminated (September

2007) the supply order at the risk and cost of the Company. The risk and cost claim by KSEB remains to be received (May 2008). There was no justification on record for making financial investment in the project before getting the approval of Government and for accepting supply orders before creating infrastructural facilities. Thus the decision of the Company to commence the construction activities of pole casting project without Government approval resulted in wasteful expenditure of Rs. 29.60 lakh as well as a committed liability of Rs. 37.85 lakh.

Management stated (June 2008) that they were taking up the matter with KSEB to implement the project further on a joint venture basis and if KSEB agreed for the proposal, they would approach the Government for the permission for the project. The fact remains that the action of the Company in making huge financial investment without obtaining approval from Government lacked justification.

The matter was reported to Government in May 2008; their reply was awaited (August 2008).

Kerala State Industrial Development Corporation Limited

4.6 Undue favour

Decision of the Company to waive the upfront fee ignoring the offer of the loanee to make the payment, if insisted, resulted in undue benefit of Rs. 25 lakh to a society for acquisition of land on behalf of a private entity.

The Company sanctioned (February 2006) a term loan of Rs. 50 crore to Infopark, Kochi (society owned by Government of Kerala) for acquiring 136 acres of land to be transferred to Dubai Internet City (DIC) in connection with their Smart City Project in Kochi for Information Technology development in the State. A loan agreement was entered into (May 2006) with Infopark.

The letter of sanction (February 2006) and clause 2.3 of the agreement prescribed payment of an upfront fee equal to 0.5 *per cent* of the loan amount by the loanee to the Company on the date of signing of the loan agreement or by way of adjustment from the initial disbursement of the loan amount. Infopark, however, requested (August 2006) the Company to release the loan amount in full without deducting the upfront fee in view of urgent requirement of funds and requested for waiver of the upfront fee. Infopark further agreed to pay upfront fee by a separate cheque subsequently, if insisted, by the Company.

Audit noticed (April 2007) that at the time of approval of waiver of upfront fee by the Board of directors, the matter regarding waiver of upfront fee of Rs. 25 lakh was placed before the Board (249th meeting dated 22 September 2006) without presenting the fact that Infopark had agreed to pay the fee by a separate cheque if insisted. The Board had not recorded any specific reasons for waiver of upfront fee indicating that the decision for waiver was taken by the Board without considering an alternate option beneficial to the Company. Thus, decision of the Company to waive the upfront fee ignoring the offer of

the loanee to make the payment subsequently resulted in extension of undue benefit to Infopark for acquisition of land on behalf of a private entity.

The matter was reported to Government/ Management in May 2008; their reply was awaited (August 2008).

Kerala Electrical and Allied Engineering Company Limited

4.7 Avoidable cash loss

Decision of the Company to accept orders for supply of additional quantity of alternators at a rate lesser than the variable cost resulted in cash loss of Rs. 25.38 lakh as well as payment of liquidated damages of Rs. 5.59 lakh.

The Company accepted (November 2003) an offer from Integral Coach Factory (ICF), Chennai for supply of 194 alternators of 4.5 KW to ICF at a basic price of Rs. 39,926 each plus duties and taxes. The basic price did not fully cover the direct expenses. The delivery was to be completed by August 2004.

As per the terms of the purchase order, ICF reserved the right to increase or decrease the order quantity by 30 *per cent* on the same price and other terms and conditions during the currency of the contract and the Company was bound to supply the quantity so ordered according to the revised delivery schedule fixed by ICF. As such the Company was under obligation to supply a maximum additional quantity of 58 numbers only. The Company, however, accepted (January/ February/ August 2004) orders from ICF for supply of additional quantity of 282 alternators at originally agreed basic rate of Rs. 39,926 each on the same terms and conditions and delivery schedule was extended upto 24 December 2004. The Company completed the supply of entire quantity by December 2006 and borne liquidated damages (LD) of Rs. 5.59 lakh.

Audit noticed (September 2007) that during the period from 2003-04 to 2006-07, the cost of the alternator ranged between Rs. 41,930 and Rs. 53,137 as against the accepted basic rate of Rs. 39,926. Since the Company had the option to accept only 58 numbers as additional order quantity, there was no justification for accepting the order for supply of the remaining 224 numbers of alternators at a cash loss of Rs. 25.38 lakh as the Company was having (December 2003) orders worth Rs. 3.81 crore. Further, the Company had lost Rs. 5.59 lakh as LD levied by ICF for delay in supply. Thus, the decision of the Company to accept orders for supply of additional quantity of alternators at a rate lesser than the variable cost resulted in cash loss of Rs. 25.38 lakh as well as payment of liquidated damages of Rs. 5.59 lakh.

The Government stated (July 2008) that even as the said contract was under execution, ICF awarded a number of other contracts all of which contributed generously to the Company's bottom line. They also stated that it was the management's view at that time to look at the standing and antecedents of the customer and not to consider the order in isolation. The fact however remained that the Company, which has been suffering continuous heavy losses, incurred additional cash loss to satisfy a customer, which resulted in impacting its bottom line rather than contributing to it. The action of the Company to sell at a cash loss did not safeguard its financial interests.

Kerala Small Industries Development Corporation Limited

4.8 Undue advantage

The Company, which had the objective of developing small scale industries in the State, overburdened the SSI units with Rs. 53 lakh.

The Company, engaged in the promotion of Small Scale Industrial (SSI) units in the State, had been distributing paraffin wax to all the candle manufacturing SSI units and tiny units for the last 30 years. In view of possible exploitation by private traders, the Company submitted (January 2005) a proposal to Government of India (GoI) for import of 1,000 MT of wax under the Japanese Debt Relief Grant Assistance Scheme for distributing the material at affordable price to members of the weaker sections of the society (beneficiaries) engaged in candle manufacturing. Under the Scheme, GoI sanctioned (October 2005) a grant of rupees two crore for the import of wax and the Company utilised (June 2007) Rs. 1.93 crore for the import of 450 MT availing full exemption of customs duty amounting to Rs. 68.96 lakh after execution of bond with customs authorities. During the period from June 2007 to January 2008 the Company distributed 450 MT of wax to SSI units at a price of Rs. 59,000 per MT. In connection with the distribution of wax the Company incurred Rs. 13.60 lakh as additional expenditure.

Audit noticed (December 2007) that in respect of indigenous procurement and distribution of wax, the Company adopted the practice of distributing wax to SSI units at purchase cost plus Rs. 1,200 per MT as service charges. In the instant case, the Company, however, added the exempted customs duty also to arrive at the selling price of Rs. 59,000 thereby overburdening SSI units with the expenditure of Rs. 68.96 lakh not actually incurred. The net gain accrued to the Company by overcharging the SSI units with exempted customs duty, after providing for margin of Rs. 1,200 per MT towards service charges, worked out to Rs. 53 lakh [*]. Thus, under a scheme for distribution of wax, the Company which had the objective of developing small scale industries in the State overburdened the SSI units with exempted customs duty of Rs. 53 lakh.

Management stated (July 2008) that they executed a bond for Rs. 81.72 lakh for release of wax without payment of customs duty and if the customs department raised a claim on the Company for customs duty it was bound to pay the duty as per bond executed. However, the Company could have obtained a counter guarantee from the SSI units for liability towards customs duty.

[*] Rs. 59,000 x 450 MT minus (Rs. 1.93 crore + Rs. 13.60 lakh + [Rs. 1,200 x 450 MT]).

Statutory Corporations

Kerala State Electricity Board

4.9 Undue benefit to Tata Tea Limited

Decision of the Board to allow reduction in penal interest outside the scope of the licensing agreement resulted in undue benefit of Rs. 61.32 lakh to a private licensee.

Tata Tea Limited (TTL), a distribution licensee, executed (January 1990) an agreement with the Board for distribution of electricity in Munnar area at the grid tariff rate fixed by the Board. The agreement was for a period of five years and thereafter would be in force until terminated by either party with three months' notice. As per clause 8 (a) of the agreement the licensee had to make payment for power and energy supplied, within 15 days, failing which penal interest at the rate of 18 *per cent* per annum had to be paid on arrears due to the Board.

Audit observed that accumulated dues from TTL for the period upto November 2005 were Rs. 6.11 crore and the interest due thereon at 18 *per cent* was Rs. 1.84 crore. The Board held discussions with TTL and it was decided (November 2005) to reduce the penal interest from 18 *per cent* to 12 *per cent* as a package of one time settlement for payment of dues within 15 days from the date of communication of dues. The Board issued invoice on 3 May 2006 for arrears and TTL remitted the amount in full including interest on 17 May 2006. The undue favour, thus, extended to TTL by way of reduction in penal interest was to the tune of Rs. 61.32 lakh.

Since there was specific provision in the licence agreement for payment of penal interest at 18 *per cent* per annum on arrears due and the amount collected by the TTL from consumers by way of current charges was also being retained by them, there was no justification for the Board to allow the undue concession of reduction in rate of penal interest to 12 *per cent*. This was also not justifiable when the Board itself was paying interest ranging from 6.5 *per cent* to 17 *per cent* on loans taken from banks/ financial institutions. Thus the decision of the Board to allow reduction in penal interest outside the scope of the licensing agreement resulted in undue benefit of Rs. 61.32 lakh to a private licensee.

The matter was reported to Government/ Management in March 2008; their reply was awaited (August 2008).

4.10 Avoidable extra expenditure

The delay in conducting inspection of materials by the Board resulted in non-supply of materials and its alternate purchase at an additional cost of Rs. 1.32 crore.

The Board placed (14 February 2006) purchase order for procurement of 151 kilo metres (kms) of various sizes of 1,100 V grade Control Cables on Arun Manufacturing Company, Delhi (AMC), at a total firm price of Rs. 1.46 crore. As per the purchase order, AMC was to commence delivery within two months with a minimum quantity of 17 kms and complete it within six months (13 October 2006) thereafter. The materials had to be inspected and approved by the nominee of the Board before despatch and for this AMC was to give 20 days advance intimation.

AMC intimated (25 March 2006) the readiness of first batch of 20 kms of cables for inspection. The Board, however, conducted inspection only during 22 to 24 May 2006. Due to delay in inspection, AMC requested (7 June 2006) the Board for extension of delivery schedule by eight months and demanded (3 August 2006) enhancement of price by 50 *per cent* on the ground that raw material cost had increased more than 100 *per cent* from the offer date. The Board extended (4 August 2006) the delivery schedule upto 14 February 2007 without imposition of penalty. AMC, however, did not supply the material.

Consequently, the Board terminated (November 2006) the purchase order placed with AMC and arranged (March - May 2007) purchase of 151 kms of control cables through two other suppliers at an additional expenditure of Rs. 1.39 crore at the risk and cost of AMC, which was not accepted (27 July 2007) by AMC. Thus, the undue delay on the part of Board in conducting inspection of materials provided by AMC and subsequent termination of the purchase order resulted in procurement of material from alternate source at an additional cost of Rs. 1.32[*] crore.

The Management stated (April 2008) that delay in inspection was due to delay in execution of agreement by AMC and steps were in progress for recovery of Rs. 1.32 crore from AMC. The reply is not relevant to the point as the execution of agreement was a pre-condition for payment and not for conducting inspection of material. The delivery was to begin within two months from the date of purchase order and AMC had intimated readiness of materials in time for inspection. The Board also had the option of withholding payment in the event of non-execution of agreement.

[*] As reduced by Security deposit of Rs. 7.30 lakh.

4.11 Loss of capital subsidy

The decision of the Board to include departmentally executed rural electrification works under RGGVY scheme in violation of the REC guidelines and conditions of tripartite agreement rendered it ineligible for capital subsidy of Rs. 10.57 crore.

Government of India (GoI) introduced (March 2005) Rajiv Gandhi Grameen Vidyutikaran Yojna (RGGVY) for providing electricity to all households in five years. The scheme to be implemented through Rural Electrification Corporation Limited (REC) envisaged 90 *per cent* capital subsidy on overall cost of the project and 10 *per cent* loan by REC. The conditions associated with the project as prescribed in the REC guidelines and the tripartite agreement entered (July 2005) into between GoI, REC and the Board, stipulated execution of the project on turnkey basis only for the Board to be eligible for subsidy.

Under RGGVY, GoI sanctioned (April 2005) electrification of 3,578 hamlets in 930 villages with an outlay of Rs. 343 crore for VEI[∝] scheme and Rs. 94.57 crore for REDB[√] package for construction of seven 66/ 11KV substations and eighteen 33/ 11KV substations. REC thereupon sanctioned (June 2005/June 2007) the works for execution through the Board.

Audit noticed (May 2007) that though the Board was eligible for subsidy only for works executed under turnkey contracts, departmentally executed works valuing Rs. 11.74 crore were included under the scheme when there were sufficient other works which qualified for assistance to be proposed under the scheme. Due to this, ultimately the Board had to treat (December 2006) the above works under normal development plan thereby rendering it ineligible for *90 per cent* subsidy.

Thus the decision of the Board to include departmentally executed rural electrification works under the scheme circumventing the REC guidelines and conditions of tripartite agreement rendered it ineligible for capital subsidy of Rs. 10.57 crore.

Government stated (June 2008) that due to social obligation as well as certain other reasons such as to provide power supply to certain classes of prospective consumers the Board was forced to execute the work proposed under the scheme without waiting indefinitely for favouring the turnkey contractor. It was further stated that there arises no question of lapse of fund since the funds were being utilised for executing other works under RGGVY. The reply is not relevant to the point since the Board included departmentally executed works under the scheme for which subsidy was not available when other eligible works for subsidy were available for inclusion. The departmental works were also delayed till January to April 2007 and some of the works were not even completed indicating that no social purpose was served by foregoing the 90 *per cent* subsidy and soft loan of 10 *per cent*.

[∝] Village Electrification Infrastructure.

[√] Rural Electricity Distribution Backbone.

4.12 Loss of interest income

The omission on the part of the Board in prescribing compounded rate of interest in the quotations invited for short terms deposits from banks resulted in interest loss of Rs. 30.68 lakh.

During the second half of 2005-06 the financial position of the Board improved due to sale of power outside the State and adjustment of unscheduled interchange in transfer of inter-state power. Consequently the Board started (January 2006) parking temporary surplus funds in short term deposits with nationalised and scheduled banks. During the period April 2006 to January 2007 there were surplus funds ranging between Rs. 10 crore and Rs. 145 crore with the Board and these were deposited with 15 nationalised/ scheduled banks for periods of 7 days to 327 days fetching interest at rates ranging between 5.01 and 9.51 *per cent* per annum. The Board had been investing the surplus funds at the interest rates fixed after inviting quotations from nationalised/ scheduled banks from time to time. The banks allowed compounded rate of interest in respect of deposits for periods of two quarters or more when the quotations invited by the Board specifically mentioned that the interest rate should be on compounded basis.

Audit noticed that out of 33 instances of short term deposits for which quotations were invited, the Board, however, insisted on offers at compounded rates only in seven instances even though there were 13 more instances of deposits where the periods exceeded two quarters and involved 202 to 326 days. Thus, due to the failure in inviting offers from the Banks on compounded rates of interest, the banks allowed only simple rate of interest. The differential loss of interest in the above 13 instances relating to the period May to November 2006 worked out to Rs. 30.68 lakh.

Government stated (June 2008) that all the nationalised banks were quoting rates at simple interest which would invariably be more than the quarterly compounding rates and as such there was no loss to the Board. The reply is not correct since the simple interest rates quoted by banks were either the same or marginally lower than the compounded rates.

4.13 Loss due to undue favour

The decision of the Electricity Board to waive annual increase in pole rentals without justifiable grounds resulted in undue benefit to Asianet to the extent of Rs. 7.79 crore.

Asianet Satellite Communications Limited (Asianet) entered into (November 1992) an agreement with the Board for distribution of cable television network using Board's electric poles for a period of 10 years. The annual pole rental was fixed at rupee one per pole as a promotional offer. Clause 19 of the agreement provided for revision of terms and conditions including rate of pole rentals every three years, if necessary. Accordingly, the Board revised the pole rental to Rs. 17 per pole in December 1999. Following the request of new

cable operators to allow them also to use electric poles, the Board further revised (October 2002) the pole rental to Rs. 54 (rural areas) and Rs. 108 (urban areas) per pole per annum. As per the revised orders, contract for use of LT poles was to be for a period of ten years with a condition for increase of pole rental rates by *12.5 per cent* every year. The revised orders were to be effective from the date of expiry (November 2002) of the then existing agreement. A new agreement was to be executed with Asianet for a period which may extend up to a maximum of 10 years.

The revision was challenged (November 2002) by Asianet in the Hon'ble High Court of Kerala and the Court dismissed (June 2005) the petition and allowed the Board discretion to decide on the request of Asianet. Thereupon, the Board rejected (December 2005) the request (September 2005) of Asianet for reduction in rates and issued (December 2005) demand notice to Asianet for Rs. 22.99 crore towards pole rental dues at revised rates together with interest at 24 *per cent* per annum. Asianet filed a writ petition before the High Court and obtained stay order against the demand notice after payment (January/ February 2006) of Rs. 9 crore. The Board, however, did not initiate any action to get the stay vacated even though two years have elapsed. Without getting the stay vacated, based on the representation (February 2006) of Asianet, the Board waived (March 2006) annual increase of 12.5 *per cent* in pole rentals upto March 2006 and allowed a nominal increase of five *percent* thereafter, thereby extending undue benefit to Asianet to the extent of Rs. 7.79 crore.

Audit noticed (June 2007) that Board had taken the decision to revise the earlier demand and waive annual increase in pole rentals already effected merely on the basis of a representation from Asianet without adequate justification that too before vacating the stay pending before the Court. Thus the decision of the Board to waive annual increase in pole rentals without justifiable grounds resulted in undue benefit to Asianet to the extent of Rs. 7.79 crore.

The matter was reported to Government/ Management in May 2008; their reply was awaited (May 2008).

4.14 Loss of revenue

Failure of the Board to keep inventory of thyrister valuing Rs. 9,750 resulted in generation loss of 6.89 MUs of power valued at Rs. 2.02 crore.

Kallada Small Hydro Electric Project (KSHEP) of the Board having two generating units of 7.5 MW each, uses water from the reservoir of Kallada Irrigation Project. As the water discharge for power generation was being restricted during irrigation period (June to September), the Board had to generate power to the full extent when there was adequate water discharge.

On 1 December 2005 Unit I and II of KSHEP tripped due to problems in servomotors and thyrister respectively. Generation in Unit II resumed on

2 December 2005 after replacing the defective thyrister[ℵ] with that of Unit-I. The defective servomotors of Unit I was repaired on 10 December 2005 but generation could resume only on 10 January 2006 after installation of a new thyrister at a cost of Rs. 9,750. Due to delay in replacement of the defective thyrister in Unit I, the Board lost generation of 5.17 [♣] million units of power valued at Rs. 2.02 crore for 30 days (11 December 2005 to 10 January 2006) when there was sufficient discharge of water from the reservoir.

Audit noticed (April 2006) that the thyrister had developed defects in 2002 also and the same was replaced through purchase from BHEL. Yet, the Board did not keep adequate spares of this low value item to avert generation loss in emergent situations. Thus failure of the Board to keep inventory of thyrister having meagre cost resulted in generation loss of 5.17 MU of power valued at Rs. 2.02 crore.

Government stated (July 2008) that the interruption in Unit I was not due to non-availability of thyrister alone but with the problem of servomotor also and even if a spare thyrister was available, Unit I could not have been put into service immediately because of its faulty servomotor. It was also stated that the thyrister was not readily available in the market and a compatible one was not easily obtainable. The fact remains that the defect in servomotor was rectified on 10 December 2005 and non-availability of thyrister was the main reason for the forced outage of Unit I and the Board should have kept a spare thyrister (value Rs. 9,750 only) to avoid forced outage.

4.15 Avoidable liability due to violation of statutory provision

The Board's failure to deduct tax at source on interest payment in conformity with provisions of Income Tax Act, 1961 may result in liability to the extent of Rs. 1.59 crore.

As per Kerala Electricity Supply Code 2005, consumers of the Board had to maintain as security deposit an amount equivalent to three months' electricity bills (two months' bill in the case of consumers having bi-monthly billing) for availing power. Consumers were eligible for interest on such security deposit with effect from 1 April 2005 at bank rate or at rates fixed by Kerala State Electricity Regulatory Commission (KSERC). In conformity with the direction of KSERC, the Board had been crediting interest at the rate of 6 *per cent* per annum to the consumers' account during the first quarter of the subsequent financial year for adjustment against electricity bill.

As per provisions of the Income Tax Act, 1961 (Section 194 A) the Board was responsible for deduction of tax at source on interest exceeding Rs. 5,000 at the rate of 10 *per cent* (individuals) and 20 *per cent* (companies). Failure to

[ℵ] A thyrister, also known as silicon controlled rectifier, is a special type of diode that only allows current to flow when a control voltage is applied to its gate terminal. It is used as a switch in the power circuit as it can only be turned on by providing a pulse at its one of the sandwitched layer called gate, and the pulse is also called fixing pulse or triggering pulse.

[♣] Based on the average generation of power in Unit I during September 2005 (5.2505 MU), October 2005 (5.25 MU) and November 2005 (5.02 MU).

deduct tax at source attracted penalty equivalent to a sum equal to the amount of tax deductible at source. Interest at the rate of 12 *per cent* per annum was also payable on the defaulted tax payment.

During the first quarter of 2006-07, the Board credited Rs. 37.44 crore to the consumers' account as interest on security deposit for the financial year 2005-06. Out of this, income tax of Rs. 1.28 crore was deductible at source on interest amounts credited to 1,524 High Tension and Extra High Tension consumers since the interest payment exceeded Rs. 5,000. The Board, however, did not deduct the tax at source. As per provisions of the Act the Board was liable to pay penalty of Rs. 1.28 crore and interest of Rs. 31 lakh (upto May 2008) on the amount of tax not deducted at source. Thus the Board's failure to deduct tax at source on interest payment may result in additional liability to the extent of Rs. 1.59 crore.

The matter was reported to Government/ Board in June 2008; their reply was awaited (June 2008).

4.16 Idle investment of borrowed Funds and interest payments

Decision of the Board to purchase CMRI without connected accessories (RF module) resulted in blocking up of funds amounting to Rs. 75.53 lakh and avoidable interest liability of Rs. 10.66 lakh.

For downloading of data from static meters, the Board assessed the requirement of common meter reading instrument (CMRI[#]) at one CMRI for every 40 distribution transformers. Accordingly, the Board issued (January 2005/ 2006) two purchase orders to Signals and Systems Private Limited (SSPL), Chennai, the lowest bidder, for procurement of an aggregate quantity of 258 CMRIs under the Accelerated Power Development and Reforms Programme (APDRP) at a total price of Rs. 75.53 lakh. As per terms of the purchase order, supply was to commence within 45 days from the date of order and completed within 60 days. In order to transfer data between the meter and the CMRI, the Board was to purchase the Radio Frequency (RF) modules separately from the meter manufacturers. SSPL supplied all the CMRIs during the period February 2005 to October 2006. These CMRIs were subsequently issued to various electrical sections of the Board.

Audit noticed (June 2008) that the CMRIs issued to electrical sections had been lying unutilised as of June 2008 since the RF module had not been procured by the Board from the meter manufacturer. As a result, Rs. 75.53 lakh had been blocked up since October 2006. Since 75 *per cent* of the cost of the APDRP scheme was funded through loan from Rural Electrification Corporation Limited/GoI at interest rates varying between 9 to 12.50 *per cent* per annum, the Board would pay avoidable interest of Rs. 10.66 lakh[Θ] on the

[#] CMRI is a two way communication interface between various static energy meters and a base computer station for the purpose of exchange of data.

[Θ] Calculated at 10.75 per cent per annum, being the average rate of interest charged by REC/GoI on loans given under APDRP scheme.

idle investment. Thus, the decision of the Board to purchase CMRI without connected accessories (RF module) resulted in blocking up of funds amounting to Rs. 75.53 lakh and avoidable interest liability of Rs. 10.66 lakh.

The matter was reported to Government/ Board in June 2008; their reply was awaited (August 2008).

Kerala State Road Transport Corporation

4.17 Avoidable financial commitment

Decision of the Corporation to accept the tenders submitted in violation of tender conditions led to award of work at higher amount leading to extra financial commitment of Rs. 18 lakh.

The Corporation invited tenders (June 2005) for construction of an Office-cum-shopping Complex at Kasargode at an estimated cost of Rs. 4.32 crore as the Probable amount of contract (PAC). As per the conditions of tender, copies of price bid should be submitted only in a sealed cover by Registered post/Speed post/courier service. Tenders submitted otherwise would be rejected. Of the seven tenders received, two tenderers (L-1 - Moideen Kutty Haji and L-3 - M. Sreekantan Nair) submitted the bids by hand and the Corporation accepted the tenders in violation of the above tender conditions. These two tenderers were qualified as L1 and L3. The Concord Constructions (CC), (the L-2 Tenderer), who quoted Rs. 4.27 crore, would have been the lowest. The fourth lowest tenderer (T.K. Rajan) thereupon approached (December 2005) the High Court of Kerala citing the violation of tender conditions by the Corporation. In the meanwhile the eligible lowest tenderer (CC) withdrew the offer on expiry of the validity period (March 2006). The Court directed (June 2006) the Corporation to consider the tender submitted by Shri T.K. Rajan. Thereupon the Corporation awarded the work (January 2007) to Shri T.K. Rajan at Rs. 4.45 crore at an additional financial commitment of Rs. 18 lakh (Rs. 4.45 crore – Rs. 4.27 crore). The work was in progress (April 2008).

Audit noticed (August 2007) that instead of considering the offer of the two tenderers who violated the tender conditions, the Corporation could have awarded the work to CC (L-2) at Rs. 4.27 crore and avoided the additional liability. Thus the decision of the Corporation to accept the tenders submitted in violation of tender conditions led to the award of work at higher amount leading to extra financial commitment of Rs. 18 lakh.

The Management stated (April 2008) that there was delay in getting additional tender forms printed and on finding it difficult to receive the tenders by post within the prescribed time, the tenderers were asked to submit the tenders by hand. The Management, however, should have made necessary arrangements in time to ensure compliance with the tender conditions.

The matter was reported to the Government (April 2008); their reply was awaited (August 2008).

4.18 Avoidable extra expenditure

The decision of the Corporation to ignore a valid lowest offer and procure material at higher rate resulted in avoidable extra expenditure of Rs. 2.13 crore.

The Corporation invited tenders (July 2006) for purchase of 25,000 nylon tyres, 40,000 tubes and 50,000 flaps. Out of six offers received, the rates quoted by Michigan Rubber (India) Limited (MR) were the lowest at all inclusive rate of Rs. 6,975 per tyre, Rs. 695 per tube and Rs. 155 per flap. The Corporation, however, decided (September 2006) to re-tender on the ground that MR was a new firm having no previous experience with the Corporation and that the price of natural rubber was likely to come down.

Thereupon the Corporation invited tenders (September 2006) for supply of 20,000 nylon tyres, 30,000 tubes and 40,000 flaps under two part bid system. Out of six offers received, the technical bid of MR was rejected on the ground that they had not supplied a minimum of 500 tyres to the Corporation during the last five years and that their quality had not been assessed. The higher rates offered by Birla Tyres (Rs. 6,930 per tyre, Rs. 650 per tube and Rs. 230 per flap exclusive of VAT) and J K Industries Limited (Rs. 7,000 per tyre, Rs.600 per tube and Rs. 200 per flap exclusive of VAT) were accepted. Orders were placed on Birla Tyres (November 2006) for 15,000 tyres, 22,500 tubes and 30,000 flaps and J K Industries Limited (November 2006) for 9,000 tyres, 13,500 tubes and 18,000 flaps and the supplies were completed by 31 March 2008.

Audit noticed (April 2008) that the Corporation had purchased (January 2002) 4,800 tyres and 7,200 tubes from Betul Tyre and Tube Industries Limited which was subsequently renamed and registered (January 2005) as Michigan Rubber (India) Limited. MR had also submitted copies of fresh certificate of incorporation consequent on change of name, factory licence, certificate issued by Bureau of Indian Standards, test report issued by Central Institute of Road Transport along with their bid in August 2006 as well as the subsequent tender in September 2006 and also the details of supply made by them to the Corporation during the year 2002. The Corporation, however, ignored these records submitted by MR and rejected their offer on the untenable ground that MR had not supplied a minimum of 500 tyres during the previous five years. Further, laying down a condition of a minimum supply of 500 tyres to the Corporation amounted to restricting the number of suppliers and hence the competition which was not in the interest of better price discovery.

Thus the decision of the Corporation to ignore a valid lowest offer and procurement of material at higher rates resulted in avoidable extra expenditure of Rs. 2.13 crore[*].

The Government stated (June 2008) that even though the Corporation had purchased more than 500 tyres from Betul Tyre and Tube Industries Limited during the previous five years, the tender opening committee had not

[*] Rs. 14.12 crore + Rs. 4.67 crore – Rs. 16.66 crore.

considered the certificate produced by the firm to this effect without specifying any reason. The fact remained that the Corporation had incurred huge extra expenditure due to the lapse on the part of the tender committee.

4.19 Avoidable extra expenditure

The failure of the Corporation to make prompt payment to a supplier as per contract and subsequent purchase of material at higher rates from alternate sources resulted in avoidable extra expenditure of Rs. 67.77 lakh.

To meet the requirement of 1,200 MT of Pre-cured Tread Rubber (PCTR) for the year 2005-06, the Corporation decided (July 2005) to procure 50 *per cent* of the material from Association of State Road Transport Undertakings (ASRTU) approved rate contract suppliers and balance 50 *per cent* from SSI units. Accordingly, orders were placed in August 2005 for 600 MT of PCTR with Hill Top Rubbers Pvt. Ltd. (HTR), New Delhi (an ASRTU rate contract supplier) at Rs. 88.49 per kg. For the balance 600 MT, tenders were invited in July 2005 and orders placed in October 2005 with four SSI units at Rs. 94.36 per kg.

The Corporation, however, did not insist for entering into an agreement with HTR on the ground that there was no need for execution of a separate agreement with ASRTU contractors. On the request of HTR the Corporation agreed to make (September 2005) 100 *per cent* payment immediately after inspection of materials. However, there was delay ranging between 2 to 35 days on the part of the Corporation in making payments for the material supplied by HTR between October 2005 and February 2006.

Since the Corporation could not adhere to the terms of payment, HTR supplied only 96.64 MT of PCTR up to March 2006 as against the ordered quantity of 600 MT. On the ground that the failure to supply PCTR hampered production, the Corporation cancelled (April 2006) the unexecuted portion of 503.36 MT of the material and procured 376.567 MT (May 2006 to March 2007) from three SSI units at rates varying between Rs. 99 per Kg and Rs. 116.84 per Kg. When compared to the procurement rate of Rs. 88.49 per kg of HTR, the Corporation incurred extra expenditure of Rs. 67.77 lakh on the purchase of 376.567 MT of PCTR from SSI units at higher rate. Thus, the failure of the Corporation to make prompt payment to a supplier as per contract and subsequent purchase of material at higher rate from alternate sources after cancellation of existing contract resulted in avoidable extra expenditure of Rs. 67.77 lakh.

The Management stated (July 2008) that due to financial crisis there was some delay in making payment in time. However, the Corporation had sufficient funds available from Kerala Transport Development Finance Corporation Limited for making payment for purchases in time.

General

4.20 Follow-up action on Audit Reports

Explanatory notes[♣] outstanding

4.20.1 The Audit Reports of the CAG 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. Finance Department, Government of Kerala issued (April 2005) instructions to all Administrative Departments to submit explanatory notes indicating a corrective/remedial action taken or proposed to be taken on paragraphs and reviews included in the Audit Reports within two months of their presentation to the Legislature, without waiting for any notice or call from the Committee on Public Undertakings (COPU).

The Audit Reports for the years up to 2006-07 have been presented to the State Legislature but ten departments did not furnish explanatory notes on 54 out of 75 paragraphs/ reviews relating to the Audit Reports for the year 2004-05 to 2006-07 as of September 2008.

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

4.20.2 As per the Handbook of Instructions for Speedy Settlement of Audit Objections issued by the State Government the replies to paragraphs are required to be furnished within one month from the presentation of the Reports by COPU to the State Legislature. Action Taken Notes (ATNs) to 286 paragraphs pertaining to 72 Reports of the COPU presented to the State Legislature between July 2000 and July 2008 had not been received as of September 2008 as shown below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where ATNs not received
1998-2000	1	2
2001	4	13
2001-2004	13	49
2004-2006	25	87
2006-2008	29	135
Total	**72**	**286**

Response to inspection reports, draft paragraphs and reviews

4.20.3 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 (IRs). The heads of PSUs are required to furnish replies to the IRs through the respective heads of departments within a period of six weeks. IRs issued up to March 2008 pertaining to 81 PSUs disclosed that 4,112 paragraphs relating to 852 IRs

---

[♣] 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.

remained outstanding at the end of September 2008. Of these, 666 IRs containing 3,601 paragraphs had not been replied to for one to five years. Department-wise break-up of IRs and paragraphs outstanding as on 30 September 2008 is given in **Annexure 20**.

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 12 draft paragraphs and one draft review forwarded to various departments during May-July 2008 as detailed in **Annexure 21**, had not been replied to so far (September 2008).

It is recommended that the Government should ensure that (a) procedure exists for action against the officials who fail to send replies to IRs/ draft paragraphs/ reviews 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 **(S.NAGALSAMY)**
The **Principal Accountant General (Audit), Kerala**

Countersigned

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