



**Report of the
Comptroller and Auditor General of India
for the year ended March 2016**

Performance Audit on Sikkim State Lotteries



GOVERNMENT OF SIKKIM

Report No. 1 of 2017

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PREFACE

1. The Report of the Comptroller and Auditor General of India for the year ended March 2016 has been prepared for submission to the Governor of Sikkim under Article 151 (2) of the Constitution of India for being laid before the State Legislature.
2. The Report covering the period 2010-16 contains results of performance audit on Sikkim State Lotteries.
3. The Audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.

EXECUTIVE SUMMARY

In India, the States can organise lotteries subject to observance of provision of the Lotteries (Regulations) Act, 1998 and Lotteries (Regulations) Rules, 2010. The Lotteries (Regulation) Act, 1998 regulates the Lotteries and provides for matters connected therewith throughout the country. The Act empowered the Central Government as well as the State Governments to make Rules to implement the provisions of the Lotteries (Regulation) Act. The first Scheme for conduct of Sikkim Government Lotteries was notified in March 1972 more than 45 years ago when Sikkim was not a State of India. After merger with India, the first Lottery schemes by the State Government were introduced in 1978 and various schemes of Lotteries have been organised by the Government of Sikkim.

(Paragraph 1.1 & 1.2)

During 2010-16, the State of Sikkim organised 44,834 draws of various lottery schemes. Audit observed many lapses in the lottery operations of the State relating to monitoring, maintenance of records, deposit of revenues, failure to authenticate and ascertain prize payments by Marketing Agents (MAs), the draw process, failure to obtain details of prize winning tickets and unsold tickets from MAs and absence of checks and controls on operation of lottery schemes.

(Paragraph 2.1)

The MAs were appointed for marketing the State Lotteries. The appointment of MAs lacked transparency and consistency. The MAs were selected sometimes through the tender process, sometimes through negotiation after calling for offers individually and sometimes by extension of terms of contract with existing MAs without tendering which deprived the State to get the highest bid and optimum revenue.

(Paragraph 2.2)

Rule 3(2) of Rules, 2010 envisaged that the State Government should organise a lottery or lotteries only after issuing notification in the Official Gazette, outlining the purpose, scope, limitation and methods thereof. Failure to issue mandatory notification under Rule 3(2) of Rules, 2010 in time resulted in repeated litigations, delay in award of marketing contract and consequent financial loss of ₹ 13.52 crore.

(Paragraph 2.2.3)

Despite disqualification of the tender and contrary to recommendation of the tender selection committee, M/s Pan India Network Pvt Ltd. was awarded marketing contract of Online Lotteries in November 2012 for five years.

(Paragraph 2.2.5)

Rule 18 of the Sikkim Online Network Lottery Rules, 2001 inter alia envisaged that the State Government may after opening of tenders and on the recommendation of Tender Security Committee or any organisation authorised by the State Government appoint MA for selling computerised network lottery tickets. There was no provision in the Rules for appointment/re-appointment by extension of contract without calling for tenders. M/s Summit Online Trade Solutions Pvt. Ltd. was appointed MA for marketing eight on-line lottery schemes of

the State without calling for tenders. Further, the MA had not installed the Central Server within Sikkim as required under the agreement signed with the State.

(Paragraph 2.2.6)

Against the total sale proceeds of ₹ 44,834.87 crore during 2010-16, the MAs deposited ₹ 628.74 crore to the Government Account which comprised of Minimum Guaranteed Revenue (MGR), prize money above ₹ 10,000, draw expenses, printing charges (in respect of paper lotteries) and the unclaimed prizes. The sale proceeds deposited to Government Account constituted only 1.40 per cent of the total sale proceeds while 98.60 per cent of the proceeds were retained by the MAs. The net revenue (MGR) realised by the State after meeting the expenses on draw, printing costs of lottery tickets, prize money above ₹ 10,000 etc. constituted a mere 0.40 per cent of the sale proceeds. Thus, the MAs appeared to be the de facto beneficiaries of the State's Lotteries while the State received a meagre revenue from its Lotteries' business.

(Paragraph 2.3.1)

During 2010-16, in the three online weekly games with large prize money, the Directorate allowed the MA to retain prize money amounts ranging from ₹ 1.00 crore to ₹ 11.58 crore for periods ranging from one week (7 days) to 80 weeks (560 days). No penalty was imposed on the MA for retention of the undrawn prize money. Allowing the MA to regularly retain the prize money against the above games for prolonged periods till the jackpot was hit resulted in undue favour to the MA of ₹ 3.50 crore towards interest (calculated @ 8 per cent per annum) due to non-insistence for deposit of undisbursed prizes.

(Paragraph 2.3.5)

It was noticed that during 2010-16, paper lottery tickets were printed mainly from four security printers, without call of tenders. The printing presses were instructed by the Directorate of Sikkim State Lotteries (DSSL) to deliver the paper lottery tickets directly to the two area distributors appointed by the MA (located at Kolkata) without any check by any officer of the DSSL. Hence, there was no control over actual number of tickets printed and the delivery and distribution of lottery tickets to the MA. The MA provided details of sale of tickets to the Department from time to time. The Department had adopted a system of sale on "all sold" basis where all tickets handed over to the MA were considered as 'sold' and did not insist on the MA to return the unsold tickets.

The tickets in the case of Online Lotteries were printed instantly on demand of customers at the points of sale. The number of tickets printed depended upon the demand of the customers. The State had no means to independently verify the number of tickets printed and sold by the MAs against any draw. The State entirely depended on the statements submitted by the MAs regarding the number of tickets sold. There was no mechanism to regulate the printing, sale, cancellation and accounting of 'unsold' tickets in respect of Online Lotteries.

(Paragraph 2.4)

In contravention to the provision of the Lottery (Regulation) Rules, 2010 relating to conduct of draw of lots by operating draw machine or any other mechanical method visibly

transparent to the viewers, the State, for Online Lotteries, used electronic devices called Random Number Generators (RNGs) for drawing results of the lottery schemes. The RNGs were programmed to generate the results automatically exactly at the time of draw and such results were instantly transmitted to the central servers at Mumbai and from thereon to the various points of sale placed in different States. Thus, the draw of results for Online Lotteries was done by using a method which was non-mechanical, could not be easily understood and not visibly transparent to the viewers. Merely by looking at the draw of results through RNGs, it was not understood how the Department could ascertain that the system was free from manipulation.

(Paragraph 2.5)

The internal control system in the Department was weak as evidenced by absence of control system in preparation of the lottery game designs or schemes. All schemes were prepared by the MAs themselves while the Department approved the schemes without any vetting to verify if the lottery schemes conformed to the Act and Rules. The MAs were authorised to distribute prizes upto ₹ 10,000 but there was no system in the Department to verify the authenticity of distribution of such prizes by MAs indicating serious lapse of control. The MAs were never asked to submit audited statement of accounts, there was no system for proper verification of submitted accounts/records and for periodical inspection of accounts of distributor/area distributor etc. Monitoring of the activities of the distributors or their sub-agents to detect illegalities/irregularities was found lacking. Despite running Online Lotteries since August 2001 for more than 14 years, the Directorate of Sikkim State Lotteries did not have any expert on Information and Communication Technology (ICT) on its roll. The entire operation of Online Lotteries was run by the MAs using application software, computer programmes and internet networks of their own choice without prescription of any norms and standards by the State. The Central Servers were located in Mumbai in data centres of the MAs' own choice, in contravention of Lottery Rules, 2010 which provide that it should be located within the State. Annual finance and systems audit of the various lottery schemes organised by the MAs had not been conducted so far (July 2017) as necessitated by the Lottery Rules, 2010.

(Paragraph 2.7 & 2.8)

Chapter I: Introduction

1.1 Legal framework

In terms of the Lotteries (Regulation) Act, 1998 "lottery" means a scheme, in whatever form and by whatever name called for, distribution of prizes by lot or chance to those persons participating in the chances of a prize by purchasing tickets. Lotteries organised by Government of India (GoI) or the Government of a State is a Union subject, but the taxes on sale of such lotteries is a State subject. The policy of GoI relating to lotteries has been strictly against holding, authorising or extending support to any kind of lottery in any form and for any purpose howsoever laudable on the ground that they encourage the gambling spirit and disturb the normal economic equilibrium. However, States are allowed to organise lotteries subject to scrupulous observance of provision of the Lotteries (Regulations) Act, 1998 and Lotteries (Regulations) Rules, 2010.

The Lotteries (Regulation) Act, 1998 regulates the Lotteries and provides guidance for matters connected therewith throughout the country. The Act empowered the Central Government as well as the State Governments to make Rules to carry out the provisions of the Lotteries (Regulation) Act. While the Central Government has enacted the Lotteries (Regulation) Rules, 2010, State Governments have simultaneously enacted their own Rules, viz. Sikkim State Lottery Rules, 2003 and Sikkim Online Network Lottery Rules, 2001.

1.2 Evolution of the Sikkim State Lotteries

On the basis of records available with the Directorate of Sikkim State Lotteries (DSSL), the first Scheme of Sikkim Government Lotteries was notified in March 1972, i.e. more than 45 years ago when Sikkim was an independent kingdom. After merger with India (1975), the first Lottery Scheme was introduced in 1978 by the State Government. Various schemes of lotteries have been organised by Government of Sikkim continuously since commencement of lotteries in the State.

In the earliest stage of implementation of Lottery Schemes in Sikkim prior to 1978, a commission of 25 *per cent* of the value of tickets was allowed at source to the agents at the time of purchasing of tickets. The rate of commission, however, varied from time to time by the Government in the interest of sales/revenue. Bonus was also allowed on prize winning tickets to the agents/sellers.

The proceeds from the lotteries were aimed to be utilised for developmental activities and for the welfare of ex-armed Servicemen of Sikkim. The Authority to frame rules relating to the Lotteries was vested with the Government of Sikkim.

After 1978, however, the State Government began organising lotteries through Organising Agent (s) (*referred to as Marketing Agent at present*), selected from time to time through negotiation or by calling tenders and entering into agreements. All such lotteries were initially drawn through paper tickets printed in advance bearing the name of the lottery,

date of draw, ticket number, prizes, name of the State, price of ticket, terms and conditions for claim of prizes etc.

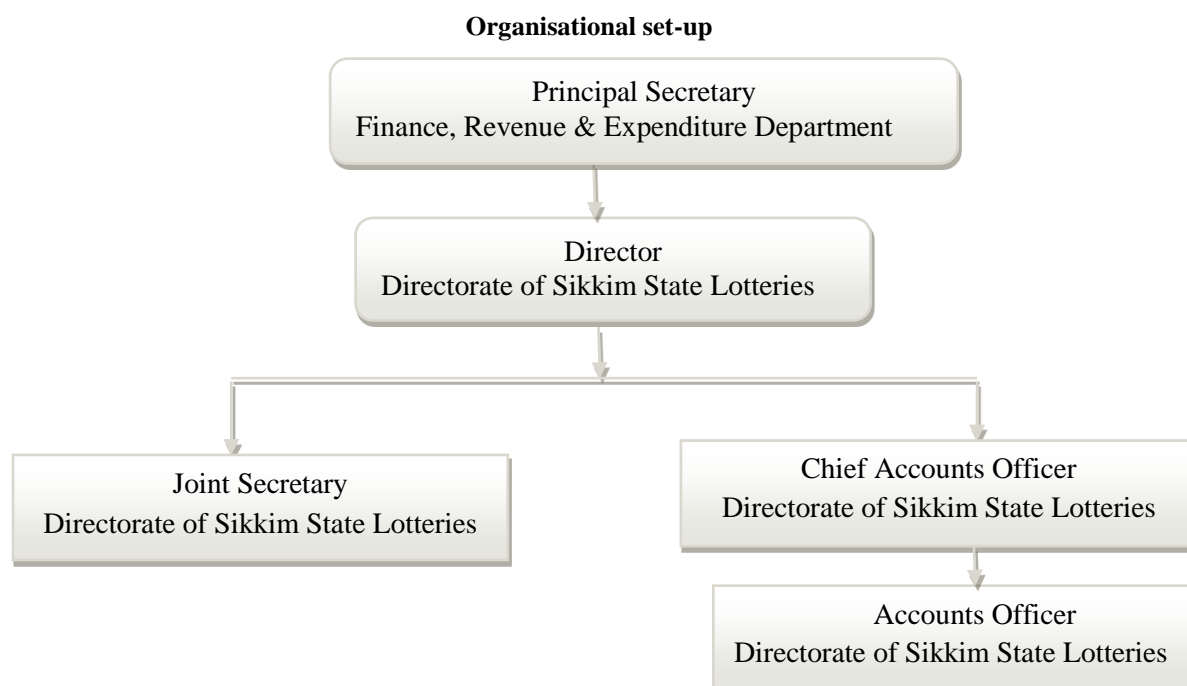
The State Government introduced 'Online Lotteries' in August 2001. Online lottery scheme is an internet based lottery established to facilitate players to purchase lottery tickets, generated by computers or instant ticket vending machines at lottery terminals. Information about the sale of tickets and the player's choice of any particular number or combination of numbers, are simultaneously registered with a central computer server.

Rule 3(20) of the Lotteries (Regulation) Rules, 2010 empowers the Comptroller and Auditor General of India (CAG) to conduct audit of any lottery or lottery scheme, organised by any State. In view of the said provision, audit of lotteries organised by the State of Sikkim, for the period 2010-16 has been conducted.

During the period 2010-16, the State was organising both conventional paper based Lottery as well as Online Lotteries. The State engaged three distributors for marketing its lotteries – two for online lotteries and one for paper lotteries. Total 44,834 lottery draws were conducted during the period.

Organisational set-up

Principal Secretary, Finance, Revenue and Expenditure Department (FRED), Government of Sikkim is the overall administrative head of Sikkim State Lotteries. The Director, Directorate of Sikkim State lotteries (DSSL) oversees the day to day functioning of the State Lotteries. The Director is supported by a Joint Secretary, a Chief Accounts Officer, an Accounts Officer and other accounts and administrative staff in the discharge of his functions. Organisational set-up is given in the diagram below.



1.3 Audit Objectives

The audit was conducted to assess whether:

- *procedures laid down in the Lottery (Regulation) Act, 1998/the Lotteries (Regulation) Rules, 2010 and the State specific Rules of Sikkim Government on Lotteries, were adhered to while organising lotteries;*
- *revenues accrued through operation of lotteries were properly assessed and remitted;*
- *all records relating to printing, sale of tickets and return of unsold tickets, were maintained;*
- *the internal control mechanism was adequate and effective; and*
- *the revenue generated was used for prescribed purposes.*

1.4 Audit Criteria

The audit findings were benchmarked against the following criteria:

- ❖ The Lotteries (Regulation) Act, 1998;
- ❖ The Lotteries (Regulation) Rules, 2010;
- ❖ Sikkim State Lottery Rules, 2003;
- ❖ Sikkim Online Network Lottery Rules, 2001;
- ❖ Notification/orders issued by the Central/State Government from time to time.

1.5 Scope and methodology of audit

The audit covered the period from 2010-11 to 2015-16. The audit methodology consisted of issue of questionnaires, examination of records/reports etc., available with DSSL and the Marketing Agents, joint site visits to Points of Sale, Central Servers etc.

The audit commenced with an Entry Conference with the Principal Secretary, FRED, Government of Sikkim and his team of officers on 15 January 2016 wherein, audit objectives, criteria and methodology were discussed. The Exit Conference was held on 9 December 2016 with the Principal Secretary, FRED and his team of officers wherein the audit findings were discussed. The Report, with modifications, was issued again to the Government and replies were received in July 2017. Replies furnished by the Department have been suitably incorporated in the Report.

1.6 Acknowledgement

The Indian Audit and Accounts Department acknowledges the co-operation of the State Government in providing all records and information during this audit.

Chapter II: Audit findings

2.1 Lottery schemes

The Lotteries (Regulation) Rules, 2010 envisaged that no lottery should have more than one draw in a week and total numbers of draws, from all lotteries put together should not be more than 24 per day. Thus the maximum numbers of draws that could be considered by the State in a week would be 168. The State of Sikkim organised to sell the lottery tickets by appointing selling agents or distributors called 'Marketing Agents' (MAs). Three different MAs had been engaged by the State during the period 2010-16 for selling its lotteries - one MA for paper lottery and two MAs for Online Lotteries. Each MA was allotted draws of eight lottery schemes per day totalling 24 draws in a day.

During 2010-16, the State of Sikkim organised 44,834 draws of various lottery schemes. The year-wise number of draws conducted during 2010-16 by the State is shown in the table below:

Table 2.1
Number of draws conducted

| Year | No. of draws of lotteries |
|--------------|---------------------------|
| 2010-11 | 7882 |
| 2011-12 | 8632 |
| 2012-13 | 7417 |
| 2013-14 | 7734 |
| 2014-15 | 7208 |
| 2015-16 | 5961 |
| Total | 44834 |

Source: Directorate of Sikkim State Lotteries

The number of draws conducted during 2010-16 ranged from 5,961 draws in 2015-16 to 8,632 draws in 2011-12. The less number of draws in 2015-16 as compared to other years was due to suspension of paper lottery schemes during the year.

While the Department conducted maximum number of draws during the period audited, serious lapses were noticed in the selection procedure of MAs, monitoring of functioning of the MAs, maintenance of proper records, timeliness of deposit of revenues, authentication and verification of prize payments by MAs, draw process, retrieval of prize winning tickets and unsold tickets from MAs, checks and controls in preventing illegal schemes, periodical audit of software systems and procedures adopted by the MAs for running online lotteries, etc. as brought out in the subsequent paragraphs in this Chapter.

2.2 Organising Lotteries by the State Government

2.2.1 Lack of transparency and consistency in appointment of MAs

The following methodology for organising lotteries was prescribed by the State from time to time:

- As per section 4(c) of the Lottery (Regulation) Act, 1998, the State Government shall sell the lottery tickets either itself or through distributors or selling agents.
- The State Government may after inviting tenders and on the recommendation of the Tender Security Committee or any Organisation authorised by the State Government in its behalf appoint Marketing Agent for selling computerised network lottery tickets. The State Government may specify the qualifications, experience and terms and condition for appointment of Marketing Agents and sub-agents¹.
- The Government may by floating open tenders or such other manner deemed appropriate appoint a person/persons or firm/firms having experience in running lotteries as Distributor for a period as determined by the Government².

The appointment of MAs lacked transparency and consistency. The MAs were selected sometimes through the tender process, sometimes through negotiation after calling for offers individually and sometimes by extension of terms of contract with existing MAs without tendering which deprived the State to get the highest bid and optimum revenue. These irregularities have been brought out in the subsequent paragraphs.

2.2.2 Irregularities in appointment of Marketing Agents

The period of agreements entered into with the MAs were not uniform. Agreements were drawn with the MAs for varying periods ranging from 3 years to 7 years with provision for extension of term of agreement for a further period of five years on mutually agreed terms. No reasons were recorded for adopting varying periods of agreements with the MAs.

The Marketing Agents (MAs) engaged by the State from time to time during 2010-16 is given in Table 2.2 below.

Table 2.2
Details of Marketing Agents engaged

| Sl. No. | Name of Marketing Agent | Type of Lottery | Initial Period of contract | Modality adopted for selection of MA | Extension through tendering/negotiation/nomination | Total No. of Years (as of March 2016) | Remarks |
|---------|--|-----------------|----------------------------|--|--|---------------------------------------|--|
| 1 | Future Gaming Services & Hotels Pvt. Ltd; 355-359, Daisy Plaza, 6 th Street, Gandhipuram, Coimbatore (known earlier as M/s Martin Lottery Agency Pvt. Ltd.) | Paper Lottery | 1999-2002 | Initially appointed for 3 years through tendering process. | 2002-2021 | 16 | Paper Lottery remained suspended during the period 13 July 2015 to 5 June 2016 due to court cases, delay in finalisation of tenders etc. |
| 2 | Tashi Delek Gaming Solutions Pvt. Ltd; 135 Continental Building, Dr. Annie Besant Road, Worli, Mumbai. | Online Lottery | 7 years from March 2002 | Appointed through tendering process | Till December 2012 | 10 | Different Online Lottery schemes conducted simultaneously. |

¹Sikkim Online Network Lotteries Rules, 2001

²Sikkim State Lotteries Rules, 2003

| Sl. No. | Name of Marketing Agent | Type of Lottery | Initial Period of contract | Modality adopted for selection of MA | Extension through tendering/negotiation/nomination | Total No. of Years (as of March 2016) | Remarks |
|---------|---|-----------------|----------------------------|--------------------------------------|--|---------------------------------------|---------|
| 3 | Summit Online Trade Solutions Pvt. Ltd, 6/35, W.E.A. Karol Bagh, New Delhi. | Online Lottery | 2005-2012 (7 years) | Through negotiation | 2012-2017 | 12 | |
| 4 | Pan India Network Pvt Ltd; 135 Continental Building, Dr. Annie Besant Road, Worli, Mumbai | Online Lottery | 2012-2017 | Through tendering | ----- | 05 | |

Source: Directorate of Sikkim State Lotteries

The MAs were initially appointed through tendering in three of the four cases. The initial appointment of the MAs was for varying periods. The MA, Tashi Delek Gaming Solutions Pvt. Ltd. was replaced by its sister concern Pan India Network Ltd. from 2012-13 onwards. The MAs were found running the State's Lotteries for 12 years or more taking recourse to the extension clause. It was further noticed in audit that the MAs were often given extension without competitive tendering. Hence, assessment of the best alternative for the State was not done. The extension of agreements without competitive bidding had a negative impact on the State's lottery business as it often led to litigations, cancellation of agreements and consequent financial loss to the State as detailed in the succeeding paragraph.

In reply, the DSSL, *inter alia*, stated (July 2017) that the litigation was only for non-issuance of notification under Rule 3(2) of Lotteries Regulation Act, 2010 and not for appointment of MA by extension of terms of agreement without tender. The reply was not tenable as the writ petition, in case of M/s Future Gaming Services and Hotels Pvt. Ltd. (FGSHPL), which came for hearing in September 2014 in the Honourable High Court of Sikkim was against extension of term of contract with the paper lottery MA without calling tenders and the High Court instructed the State Government to call for fresh tenders and the Department accordingly called for tenders and appointed FGHSPL on 24 January 2015. Further, this appointment was also challenged in the Honourable High Court in June 2015 for non-issuance of notification under Rule 3(2) of Lotteries Regulation Act, 2010. Thus, the fact remained that the litigation was primarily done for appointment of MA by extension of terms of agreement without tender.

2.2.3 Appointment of M/s Future Gaming Services and Hotels Pvt. Ltd. as MA

The marketing agency M/s Future Gaming Services and Hotels Pvt. Ltd. (FGSHPL) (formerly called M/s Martin Lottery Agencies Ltd.) was first allocated the work of marketing paper lottery schemes through call of tenders initially for a period of three years period from 6 August 1999 to 5 August 2002. Before termination of the above agreement period, the Agency was re-appointed in February 2001, after calling for tenders, through a new agreement for a five-year period upto April 2006. Before termination of the period of this agreement, the Agency was again appointed as MA on 6 October 2004 for another five years from 18 October 2004 to 17 October 2009, through call of tenders. The term of this

agreement was extended for further five years upto 17 October 2014 in August 2009 by drawing a renewed agreement with the MA. Again on 6 August 2013, a year before completion of term of this agreement, the agreement was again extended for five years from 18 October 2014 to 17 October 2019 without calling for tenders.

A writ petition was filed (September 2014) in the Honourable High Court of Sikkim challenging the extension of period of agreement upto 17 October 2019 without call of tenders. The Honourable High Court passed an order (24 September 2014) confining the agreement of 6 August 2013 for a period from 18 October 2014 to 31 January 2015 and instructed the State Government to call for fresh tenders and finalise all tender processes including opening of tenders by 7 January 2015. Agreement with the selected party/distributor was to be executed on or before 31 January 2015. The Department accordingly called for tenders and appointed FGHSPL on 24 January 2015 as distributor of paper Lotteries of Sikkim Government for a five years period. However, this appointment was again challenged in the Honourable High Court in June 2015 for non-adherence to Rule 3(2) of Rules, 2010 which envisaged that the State Government should organise a lottery or lotteries only after issuing notification in the Official Gazette, outlining the purpose, scope, limitation and methods thereof. In its judgement, the Honourable High Court instructed (22 June 2015) the State to undertake fresh tender proceedings by issuing the mandatory notification under Rule 3(2) of Rules, 2010. The DSSL issued the required Notification, as ordered by the Honourable High Court, only on 30 October 2015 – more than four months after the High Court Order. Thereafter, the DSSL undertook the tender process and appointed M/s FGHSPL as MA for paper lottery on 6 June 2016 for five years, from 18 July 2016 to 17 July 2021, after an inordinate delay of more than one year from the Honourable High Court Order.

The above sequence of events showed that the extension (August 2013) of agreement of the MA for further five years upto October 2019 without calling for tenders and failure to issue mandatory notification under Rule 3(2) of Rules, 2010 in time resulted in repeated litigations, delay in award of marketing contract and consequent financial loss of ₹ 13.52 crore³ to the State exchequer due to suspension of the paper lotteries for more than a year.

In reply, the DSSL stated (July 2017) that since the Honourable High Court of Sikkim had passed an order saying that the Rule 3 (2) of the Lotteries (Regulation) Rules, 2010 was mandatory and its non-compliance had vitiated the entire process of conducting lotteries of the State of Sikkim, the delay in issue of notification was due to time taken in examination of the matter by various authorities⁴ in the State Government.

The reply was not tenable as the Department had sufficient time for issue of the mandatory notification under Rule 3 (2) of the Lotteries (Regulation) Rules, 2010, which were published by GoI as early as April 2010 itself, much before the High Court order. Even after the High Court order, the delay in issue of the notification was more than four months.

³Calculated @ ₹15.00 crore MGR per annum offered by the MA in the earlier tender of 2014. MGR for 329 days from 13 July 2015 to 5 June 2016 comes to ₹13.52 crore.

⁴Finance Department, Law Department, Home Department, CMO etc.

Further, the DSSL did not furnish any justification for the extension of term of agreement and delay in completing the tender process in awarding the contract.

2.2.4 Appointment of M/s Tashi Delek Gaming Solutions Pvt. Ltd. as MA

The State Government published notice inviting tender (NIT) in a national newspaper⁵ for appointment of MA for Sikkim State Online lottery on 8th/ 9th July 2001. While five firms purchased the tender documents, only one firm, M/s Tashi Delek Gaming Solutions (TDGS) Pvt. Ltd., a Mumbai based agency submitted its offer on 28 July 2001. Although only the TDGS participated in the tender and even though it did not fulfil one important condition of the tender⁶, the State Government appointed the agency as MA for marketing the State's Online Lotteries on 24 August 2001. The term of the agreement was for a period of seven years with provision for further extension of five years thereafter. The MA agreed to pay 20 per cent of sale proceeds as Government share subject to Minimum Guaranteed Revenue (MGR⁷) of ₹ 35 crore, ₹ 45 crore, ₹ 65 crore, ₹ 85 crore, ₹ 135 crore, ₹ 195 crore and ₹ 220 crore in the first to seventh year respectively, totalling ₹ 780 crore⁸. The MA was also required to execute Bank Guarantee (BG) in favour of the Government for every quarter of the year by 10th day of the first month of the quarterly period for an amount proportionate to the quarterly period in relation to the MGR for the year.

After completing process of establishment of infrastructure for running the Online Lotteries by the MA, the State commenced draw and sale of the Online Lottery schemes through the MA from 29 March 2002 onwards.

In the meantime, the legality of the tender notice of July 2001 through which TDGS was appointed as MA was challenged before the Honourable High Court (HC) of Sikkim in 2002. The Honourable HC disposed of the case vide judgement dated 24 June 2003 quashing the entire tender process awarding contract to the TDGS as MA. The agreement of 24 August 2001 was also nullified. The Honourable HC, *inter alia*, directed the State to invite fresh tenders following norms, rules and procedures after adequate publicity and giving sufficient and reasonable time to the bidders. The whole exercise was to be completed within three months from the date of judgement i.e., from 24 June 2003. In the interim period, the State was instructed to: (i) appoint interim MA until new MA was appointed in pursuance of fresh tenders or (ii) allow the existing MA to continue for the stipulated period of three months only till new MA was appointed, that too, after clearing the outstanding dues or (iii) make any alternative arrangement for the said period under the wisdom of the State Government.

Two days after delivery of judgement by the Honourable HC, on 6 June 2003, the State requested TDGS to continue as MA for three months on the same terms and conditions stipulated in the original contract of 24 August 2001. The TDGS accordingly continued business of marketing the Online Lotteries of the State. On 27 June 2003, the TDGS

⁵The Statesman (Calcutta & Delhi editions).

⁶That the MA was required to be a registered Company to be eligible to take part in the tender process. TDGS was not registered at the time it participated in the tender.

⁷MGR referred to the minimum amount of revenue that the MA was required to pay to the State annually irrespective of the size of turnover from the sale of lottery tickets for the year.

⁸The revenue model was worked out by the MA on its own - no analysis for the same was available on records.

requested the State for reduction of State share from 20 *per cent* as envisaged in the agreement of 24 August 2001 to 10 *per cent*, which the State did not agree. On 8 September 2003, the State was informed by TDGS that the three months' time granted by the Honourable HC would expire on 24 September 2003 and since the State was unable to float new tender, TDGS desired to discontinue being MA for the State's Online Lotteries. Since the State was not in favour of reducing the State share and the MGR, the TDGS issued notice to the State (12 November 2003) for termination of the agreement dated 24 August 2001. This was, however, not accepted by the State and, on the contrary, a supplementary agreement was entered between TDGS and the State on 9 December 2003. The State reduced (December 2003) the State share from 20 *per cent* to 5 *per cent* while keeping the MGR unchanged. However, despite reduction in the State share, the MA had huge outstanding dues which kept increasing year after year. The MA while refusing to clear the dues gave notice to the State on 5 October 2004 for settlement through arbitration in terms of agreement dated 24 August 2001. On 1 March 2005, after a joint meeting between the State and TDGS, it was decided to initiate arbitration proceedings. However, during the pendency of the arbitration case, the two parties again entered into another agreement dated 18 November 2005 titled interim agreement introducing new games with revised terms.

The Sole Arbitrator, a retired High Court Judge, awarded (June 2011) recovery of ₹ 96.48 crore *plus* interest @ 12 *per cent* per annum to the State for the period 2002 to 2005-06. The MA, however, appealed to the District Court, East (Gangtok) against the arbitration. The District Court disposed of the case by setting aside the arbitral order in favour of the MA in July 2016. The State Government appealed to the Honourable HC, Sikkim in October 2016. As of May 2017, appeal of the State Government was pending with the Honourable HC of Sikkim.

It was observed in Audit that even while the legal proceedings continued, the MA was allowed to run the Online Lotteries till 15 December 2012, without calling for tenders, revising terms of the earlier agreement time and again. In terms of the revised agreements, sale proceeds were to be deposited in Government account within 15 days from the date of the draws. Failure to do so would attract penal interest at 12 *per cent* from 1 October 2010. While the MA failed to deposit entire sale proceeds, even deposit of prize money⁹ above ₹ 10,000 was delayed beyond the stipulated time leading to penal interest of ₹ 67.37 lakh which the Department failed to realise. From 16 December 2012 onwards, the marketing of Online Lottery schemes were awarded to Pan India Network Ltd., a sister concern of Tashi Delek Gaming Solutions, as highlighted in the succeeding paragraph.

The DSSL stated (July 2017) that the matter was *sub-judice* and still pending in the Honourable High Court of Sikkim.

2.2.5 Irregular appointment of Pan India Network Pvt. Ltd. as MA

The DSSL published Invitation of Expression of Interest (IEI) for marketing eight Online Lottery Schemes of the Government of Sikkim during the last week of April 2012. A six member Tender Opening Committee was constituted by the Government (May 2012)

⁹Super Lotto prizes totalling ₹14.91 crore, of draw no 273 & 548 held on 14.08.12 & 27.09.12 and Prize money ₹12.72 crore for the period from 11/2010 to 12/2012.

consisting of senior officers from various Departments¹⁰ with the purpose of evaluating the bids. Two companies submitted bids against the IEI – Pan India Network Pvt. Ltd. and Tashi Delek Gaming Solutions Pvt. Ltd. The bids were opened on 17 June 2012. After scrutiny of bid documents, the Committee, among other things, observed that the two companies appeared to belong to the same parent organisation as indicated by their identical office address and closeness of offers of MGRs of ₹ 10.05 crore and ₹ 10.00 crore per year respectively. The Committee, therefore, decided to reject the bids on the grounds that there could be implicit understanding between the two companies in offering the bids and recommended invitation of fresh IEI with the objective of exploring possibilities of increasing Government revenue to the maximum from prospective Marketing Agents, after thorough analysis of market situation of lottery business in the country. The Committee submitted its decision of rejecting the bids and recommendations for fresh tenders to the Commissioner-cum-Secretary (CCS), FRED on 15 September 2012. In terms of the conditions incorporated in the bid documents, the Tender Committee reserved the right to select/reject the bids. The Government would take a decision on the recommendations of the Tender Committee which would be final and binding.

The CCS after examining recommendations of the Tender Committee rejected the recommendations without recording any reasons and submitted a different proposal to the Chief Secretary (CS) – to call the two bidders M/s Tashi Delek Gaming Solutions and M/s Pan India Network (whose bids were rejected by the Tender Committee) for negotiation to enhance the bid amount. The proposal of the CCS, FRED was accepted by the CS in September 2012 and by the Chief Minister (CM) in October 2012.

Thereafter, the two companies were called for negotiation on 10 October 2012. While the Company Tashi Delek Gaming Solutions disagreed to raise the amount of MGR of ₹ 10.00 crore offered to the Government earlier, the other bidder M/s Pan India Network Pvt Ltd agreed to enhance its earlier offer of ₹ 10.05 crore to ₹ 10.50 crore. The CCS, FRED accordingly submitted the negotiated higher offer of Pan India Network Pvt Ltd to the CS for consideration on 18 October 2012.

The CS after examining the slightly enhanced MGR offered by Pan India Network Pvt. Ltd. proposed to the CM on 20 October 2012 for calling of open tenders to get best MAs and reasonable revenue to the Government. The CM approved the proposal of the CS on 1 November 2012. However, on the very next day (2 November 2012), the CCS, FRED recorded in his notes that the matter was discussed with the CS on 2 November 2012 and since tenders had already been invited earlier and the Government had approved calling of bidders for negotiation, FRED could go ahead with execution of agreement with Pan India Network Pvt. Ltd. The CCS, FRED thereafter instructed the Director, DSSL to execute the agreement with Pan India Network Pvt. Ltd. The agreement for marketing eight Online Lottery schemes of the Government of Sikkim was accordingly executed between Government of Sikkim and Pan India Network Ltd. on 7 November 2012 for a period of five years.

¹⁰Controller of Accounts; Pr. Director (Budget); Director, Commerce & Industries Department; Director, Sikkim State Lotteries; Additional Secretary, Law Department and Addl. Director, IT Department.

Audit scrutiny revealed the following:

- The two bidders, M/s Tashi Delek Gaming Solutions Pvt. Ltd. and M/s Pan India Network Pvt Ltd. whose bids were laid before the Committee for evaluation belonged to the same parent organisation and had the same office address. Hence, there was no real competition in the bidding and was a case of collusive bidding.
- One of the qualifying criteria/condition for the tender was that any MA having any outstanding liabilities towards sale proceeds on lottery, prize money or other dues to the Government of Sikkim would not be allowed to participate in the bid. The Company Tashi Delek Gaming Solutions was embroiled in a legal battle with the State Government due to default in payment of assured revenue to the State. Dues payable to the State Government as awarded in an arbitration case¹¹ amounted to over ₹ 96.48 crore. Despite this fact, the Company was allowed to participate in the bid, in violation of the bid conditions.
- The Tender Committee's rejection of the two bids and recommendation for invitation of fresh bids was not accepted by the CCS, FRED.
- Despite disqualification of the tender and contrary to recommendation of the tender selection committee, M/s Pan India Network Pvt Ltd. was awarded marketing contract of Online Lotteries in November 2012 for five years.
- Reasons for rejection of the recommendations were also not recorded in the files produced for Audit. The Department, *inter alia*, stated that the decision to award marketing contract of Online Lotteries to Pan India Network Pvt. Ltd. was taken in the best interest of the State as invitation of fresh bids would cause delay and loss of revenue to the State. The reply of the Department was not tenable as the Tender Committee had also recommended extension of agreement with the existing MA for a further one-year period for completing fresh tender process, to maintain continuity of flow of revenue to the State and thereby avoid loss to the State. The Department stated (July 2017) that the two companies were separate entities with distinct Corporate Identity Numbers (CIN)¹² and separate Directors. The reply was not tenable as the two companies had the same office address, telephone number, same trademark of games captioned 'playwin' and the same authorised signatory.

2.2.6 Irregular appointment of M/s Summit Online Traders Pvt. Ltd. as MA

The agency M/s Sugul & Damani (*later renamed M/s Summit Online Traders Pvt Ltd*) was first appointed MA (9 May 2005) for marketing Online Lotteries through a process of negotiation. In terms of the agreement signed with the MA, the MGR payable to the State was determined at one *per cent* of the turnover upto a turnover of ₹ 1,000 crore or ₹ 10 crore per annum, whichever was higher. On additional turnover over and above ₹ 1,000 crore the MA was required to pay 0.50 *per cent* of the additional turnover to the State.

¹¹ The Company had challenged the award of the Arbitrator and filed fresh petition in a District Court in the State. The matter was *sub judice* awaiting final disposal.

¹² CIN is a unique 21 digit alpha-numeric number given to all Private Limited companies. CIN is used to track all aspects of the company from incorporation by the Registrar of Companies.

There was nothing in the departmental records to indicate the basis/analysis for determining the MGR payable to the State by the MA at the above mentioned rates.

The MA commenced marketing of Online Lotteries from 27 August 2005. The term of the agreement for marketing computerised Online Lotteries was for seven years with provision for further extension of five years thereafter. The firm changed its name to M/s Summit Online Trade Solutions Pvt. Ltd. from December 2010 onwards. In February 2012, before termination of the above agreement, the MA wrote to the CM for extension of the term of agreement for a further period of five years invoking clause 9 of the agreement of May 2005, which, *inter alia*, provided for extension of the term of agreement for additional five years. The CM instructed Secretary FRED to examine the matter and put up for consideration. The CCS, FRED¹³ proposed extension for just one year so that scope for calling fresh tenders remained. The Secretary, FRED further proposed that in the subsequent agreement, provision for further extension should be done away with. The CM approved the proposal.

The MA agreed for a one-year extension but wrote that in such case it would not be able to adhere to the requirement of the Department to install the Central Computer Server at Gangtok just for one year after incurring ₹ 4 crore to ₹ 5 crore on establishment of the Central Server. Finally, the CM approved proposal of the Department to extend the initial agreement of 9 May 2005 for a further period of five years and 108 days¹⁴ upto 26 August 2017. Accordingly, a new agreement was drawn on 9 November 2012 extending the term of the earlier agreement upto 26 August 2017. In terms of the renewed agreement, the MGR payable to the State was determined at (i) 1 *per cent* of the turnover upto ₹ 1,000 crore or ₹ 10 crore per annum, whichever was higher and on additional turnover over and above ₹ 1,000 crore, 0.25 *per cent* of the additional turnover with effect from 9 May 2012 to 8 November 2013 and with effect from 9 November 2013 to 26 August 2017; 1.05 *per cent* of the turnover upto ₹ 1,000 crore or ₹ 10.50 crore per annum whichever was higher and on additional turnover over and above ₹ 1,000 crore, 0.25 *per cent* of the additional turnover. In this case also, no basis or analysis was revealed in the departmental records for determining the MGR payable to the State by the MA at the above mentioned rates.

The MA assured the Government that it would install the Central Server required for running the online lotteries preferably at Gangtok or within the geographical boundary of Sikkim.

Rule 18 of the Sikkim Online Network Lottery Rules, 2001 *inter alia* envisaged that the State Government may after opening of tenders and on the recommendation of Tender Security Committee or any organisation authorised by the State Government appoint MA for selling computerised network lottery tickets. There was no provision in the Rules for re-appointment by extension of contract without calling for tenders. Further, even after more than four years of signing the new agreement for re-appointment, the MA had not installed the central server in Sikkim, in terms of the agreement. Despite non-fulfilment of agreement, extension of five years was given. The MA continued to run the lottery

¹³Sh. K. N. Bhutia

¹⁴The extra 108 days was allowed on the ground that the MA actually commenced the draws from 17 August 2005.

operations through the central server set up by him in Mumbai with no presence of any State Government representative to monitor the transactions taking place in the central server.

The Department stated that the term of agreement of the MA was extended for further five years in the best interest of the State in compliance to the condition included in clause 9 of the agreement of May 2005. Regarding installation of Central Server, the Department stated it was pursuing the matter with the MA.

The reply of the Department was not tenable as (i) the Department did not call for tenders to ascertain the best deals for the State through competitive bidding despite there being a provision in the State's Rules for appointment/re-appointment of MA through tenders (ii) the Department fixed the MGR at around ₹ 10 crore per annum without recording any basis or analysis and, (iii) the Department had failed to get the MA install the central server in Sikkim as of July 2017, even after more than five years of signing the agreement.

The Department further stated (July 2017) that it has since stopped granting extension of contract or of awarding marketing contract through negotiations and was henceforth rigorously following tendering procedure in the selection process of MAs.

2.2.7 Penalty not imposed for delay in deposit of MGR

In terms of the agreement dated 9 May 2012 (clause 10.2), the MA agreed to deposit MGR into the consolidated fund of the State or into any other Account or Fund, as prescribed by the State Government, without any deduction etc. on or before 10th of every succeeding month. While the MA failed to deposit the entire sale proceeds, even the MGR of ₹ 4.46 crore for the period 1 July 2012 to 31 March 2013 was retained by the MA beyond due dates. No penal interest was imposed on the MA resulting in loss of ₹ 15.84 lakh to the Government.

The Department stated (July 2017) that it has since directed the MA to remit the penal interest.

2.3 Revenue Receipts

2.3.1 Sale Proceeds not realised from Marketing Agents

Clause 4 (d) of the Lotteries (Regulation) Act, 1998 envisaged that the proceeds of sale of lottery tickets shall be credited into the Public Account of the State. Further, clause 3 (17) of the Lottery (Regulation) Rules notified in April 2010 requires that the organising State shall ensure that proceeds of the sale of lottery tickets as received from the distributors or selling agents or any other source are deposited in the public ledger account or in the consolidated fund of the organising State. Sale proceeds is defined by the Lottery (Regulation) Rules, 2010 as the amount payable by the distributor to the organising State in respect of sale of tickets calculated at the face value printed on each ticket in respect of Lotteries of a particular draw or scheme or both. It was observed that despite clear instruction under the Central Acts and Rules for deposit of sale proceeds of lottery tickets into the consolidated fund of the State, the DSSL did not include any condition in the

agreements drawn with the MAs for deposit of the entire sale proceeds into the State's account, as elucidated in the subsequent paragraphs.

The year-wise position of sale proceeds of lottery tickets *vis-à-vis* the amounts deposited to Government Account during 2010-15 by the four Marketing Agents (MAs) engaged by the Department for running the State's Lotteries is shown in the following table:

Table 2.3
Details of sale proceeds of lottery tickets vis-à-vis amount deposited in Government Account

(₹ in crore)

| Year | Sale proceeds from State Lotteries | Portion of sale proceeds deposited to Government Account | | | | | | | Sale proceeds not deposited to Government |
|--------------|------------------------------------|--|----------------------------|---------------|------------------|------------------|---------------|-------------|---|
| | | Govt. Rev. (MGR) | Prize money above ₹ 10,000 | Draw expenses | Unclaimed Prizes | Printing charges | Total | Percentage | |
| 2010-11 | 5055.53 | 30.37 | 69.79 | 1.27 | 0.07 | 23.82 | 125.32 | 2.48 | 4930.21 |
| 2011-12 | 6012.57 | 28.63 | 18.87 | 1.21 | 0.12 | 35.74 | 84.57 | 1.41 | 5928.01 |
| 2012-13 | 7105.51 | 31.75 | 37.13 | 1.55 | 0.19 | 45.76 | 116.38 | 1.64 | 6989.13 |
| 2013-14 | 11171.56 | 32.82 | 29.56 | 2.16 | 0.16 | 75.78 | 140.48 | 1.26 | 11031.08 |
| 2014-15 | 11591.15 | 31.37 | 27.66 | 2.11 | 0.09 | 42.77 | 104.00 | 0.90 | 11487.14 |
| 2015-16* | 3898.55 | 24.81 | 20.32 | 1.67 | 0.08 | 11.11 | 57.99 | 1.49 | 3840.56 |
| Total | 44834.87 | 179.75 | 203.33 | 9.97 | 0.71 | 234.98 | 628.74 | 1.40 | 44206.13 |

Source: Directorate of Sikkim State Lotteries. *The sudden dip in sales & revenue in 2015-16 was due to suspension of paper lottery schemes during major portion of 2015-16 (August '15 to March '16).

Against the actual sale proceeds of ₹ 44,834.87 crore during 2010-16, the MAs deposited ₹ 628.74 crore to the Government which comprised of Minimum Guaranteed Revenue (MGR), prize money above ₹ 10,000, draw expenses, printing charges (*in respect of paper lotteries*) and the unclaimed prizes. The partial sale proceeds deposited to Government Account thus constituted only 1.40 per cent of the total sale proceeds while 98.60 per cent of the proceeds were retained by the MAs. The net revenue (MGR) realised by the State after meeting the expenses on draw, printing costs etc. constituted a mere 0.40 per cent¹⁵ of the sale proceeds. Thus, the MAs were getting the major share of revenue from the State's lotteries while the State received a meagre share of revenues. Even the sale proceeds indicated above were based on figures submitted by the MAs whose authenticity was not verified by the Department. The Department had not established any mechanism to independently verify and obtain the correct sales figures from MAs. It relied on the sales figures submitted by the MAs.

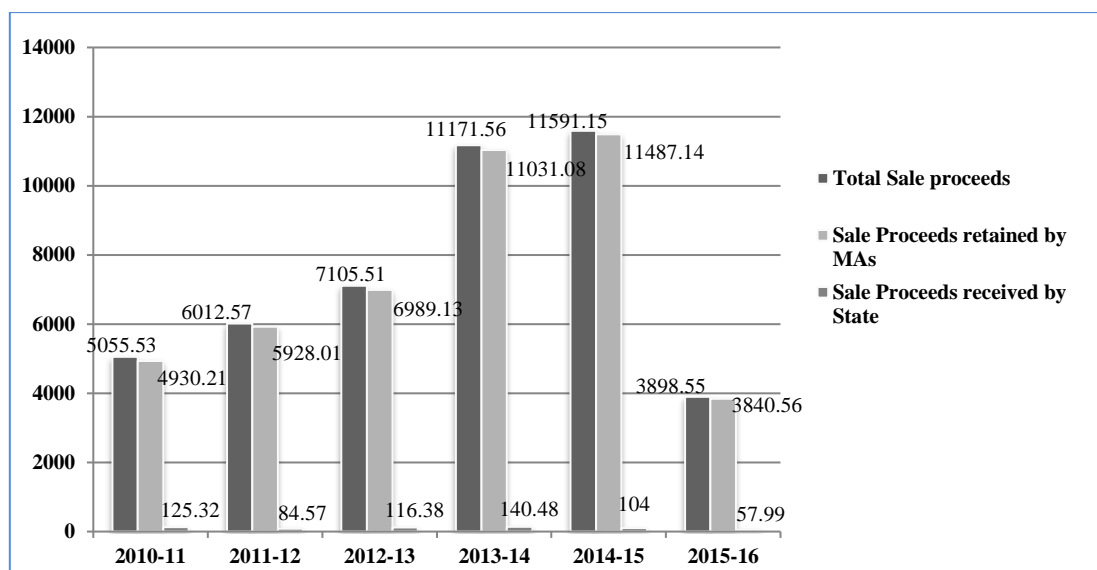
The revenue receivable by the Government was not linked to the sales turnover from the lotteries. While the sales turnover continuously and consistently increased from ₹ 5,055.53 crore in 2010-11 to ₹ 11,591.15 crore in 2014-15¹⁶, there was no corresponding increase in revenue shares paid to Government. Rather, the percentage of revenue paid to Government continuously and persistently declined from 0.60 per cent in 2010-11 to 0.27 per cent in 2014-15. Thus, while the volume of sales and the corresponding income of the MAs increased by over 129 per cent between 2010-11 and 2014-15, the Government share of revenues remained more or less static.

¹⁵ $179.75 (MGR) \times 100 / 44834.87 (\text{sale proceeds}) = 0.40 \%$

¹⁶ Period 2010-15 has been taken to determine trend of sales turnover, Govt. revenue etc. instead of 2010-16 to arrive at a reasonable conclusion due to suspension of paper lottery schemes during major part of year 2015-16.

A graphical representation of the total sale proceeds, sale proceeds retained by the MAs and the proceeds deposited to the State is as follows:

Chart 2.1
Details of sale proceeds, sale proceeds retained by the MAs and proceeds deposited



Clause 4 (d) of the Lotteries (Regulation) Act, 1998 envisaged that the proceeds of sale of lottery tickets shall be credited into the Public Account of the State. Further, clause 3 (17) of the Lottery (Regulation) Rules notified in April 2010 requires that the organising State shall ensure that proceeds of the sale of lottery tickets as received from the distributors or selling agents or any other source are deposited in the public ledger account or in the consolidated fund of the organising State. From the sale proceeds, payments like prize money to winners, printing charges, draw charges, taxes imposed by different States and the operational expenditure incurred by the MAs had to be met. From the balance amount the State needed to decide its share of revenue and the MA's commission. However, the State had not worked out any mechanism for determining optimum share of its revenue resulting from the lotteries. The State accepted the fixed MGR offered by the MAs without any analysis and irrespective of the volume of sales.

The Department stated that due to absence of detailed procedures for deposit of sales proceeds and making various payments out of it, the Department was unable to get the entire sales proceeds deposited into the State's account. The Department also stated (July 2017) that it was practically impossible for the State and the MAs to get the entire sale proceeds deposited into the State's account.

The reply of the Department was not acceptable considering the fact that the State has been continuously organising lotteries for more than four decades. The negligence in laying down appropriate procedures and modalities and thereby laxity in getting the entire sales proceeds deposited into the State's account amounted to undue favour to the lottery MAs besides continuously vitiating the provisions of the Act/Rules at the cost of the State's interest.

2.3.2 Irregular authorisation to the MAs for disbursement of prizes upto ₹ 10,000

Rule 4(4) of the Lottery Regulation Rules, 2010, *inter alia*, envisages that the organising State shall pay to the distributors or the selling agents the prize amount disbursed by the distributors or selling agents to the winners, if any, out of the sale proceeds deposited in the public ledger account or in the consolidated fund of the organising State. In violation of the above Rule, the MAs were allowed to disburse prizes upto ₹ 10,000 to the winners directly, in terms of the agreements, from the sale proceeds on behalf of the Government. It was observed in audit that sale proceeds to the tune of 87 per cent to 90 per cent of the total collection from the Lotteries was shown as disbursed directly by a MA (M/s Summit Online Trade Solutions). The other three MAs did not submit year-wise details of prizes disbursed by them. Such disbursement of prizes, by the MAs directly from the sale proceeds contravened Rule 4(4) of Lottery (Regulation) Rules, 2010.

The Department stated (July 2017) that the MAs were authorised to disburse prizes upto ₹ 10,000 to enable instant payment of prizes to the winners and thus win their confidence. The fact is that the Lottery Regulation Rules, 2010 did not permit payment of prizes by the MAs directly from the sale proceeds.

2.3.3 Absence of controls on disbursement of prizes by MAs

While on one hand, the Department violated Rules by authorising the MAs to directly disburse prize money upto ₹ 10,000 from sale proceeds, on the other hand it never conducted any scrutiny to verify the authenticity of disbursement of such prizes to the winners by the MAs. Thus, possibility of retention of prize (*upto ₹ 10,000*) money on unsold tickets/undisbursed prize money by the MAs could not be ruled out. The Department needed to lay down control systems and procedures to regularly monitor, verify and authenticate the payment of prizes to rule out chances of retention of undisbursed prize money.

2.3.4 Failure to keep records of prize winning tickets

Rule 3(16) of the Lottery (Regulation) Rules, 2010, *inter alia*, envisages that the organising States shall keep records of the prize winning tickets along with amount of prize or prizes in respect of each draw in a manner prescribed by the State. Further, in terms of Rule 13 (3) (a) of the Sikkim State Lottery Rules, 2003, the MAs were required to surrender to the Government all prize winning tickets under non-income tax bracket¹⁷ along-with account of prizes disbursed by them within 120 days from the date of each draw. The Department, however, did not insist on the Online Lottery MAs for production of prize winning tickets valuing upto ₹ 10,000 for subsequent verification.

In the case of paper Lotteries, however, the MA submitted periodical reports on prize winning tickets upto ₹ 10,000 which were reported as verified randomly by an office assistant posted at Kolkata before destruction of the tickets.

The Department stated that the MAs were authorised to disburse prizes upto ₹ 10,000 themselves to allow winners of small prizes to receive prizes easily from the points of sale

¹⁷i.e. prizes upto ₹ 10,000

itself. Regarding deposit of prize winning tickets upto ₹ 10,000, the Department stated that it was physically not possible to collect prize winning tickets from Punjab, Maharashtra and Goa where the Sikkim State Lotteries were sold. Reply of the Department is not tenable as action of the Department in (i) allowing the MAs to directly disburse prize money (*upto ₹10,000*) from the sale proceeds without any verification or check, and (ii) failure to obtain prize winning tickets, was contrary to the Rules governing the scheme of lotteries and was fraught with the risk of misappropriation of sale proceeds by the MAs terming such proceeds as prize moneys. Moreover, for online lotteries, there was no need for physical collection of prize winning tickets. Details could have been submitted electronically. However, no action had been initiated by the Department on the matter.

The Department stated (July 2017) that mirror server had been installed in the Lottery Directorate as the central servers were located in Mumbai. The reply was not tenable as details of individual prize winning tickets for prizes disbursed upto ₹ 10,000 could not be obtained from the mirror servers.

2.3.5 Retention of jackpot prizes by MA

The State organised three weekly Online Lottery schemes which offered large prize money as the first prize called jackpot amount. The three lottery schemes named Saturday Super Lotto, Tuesday Thunderball and Thursday Super Lotto carried jackpot prizes ranging from ₹ 1.00 crore to over ₹ 10 crore.

Although draws were conducted each week for each such super lottery mentioned above, the jackpot prizes were not hit every week. It was noticed in audit that the jackpot amount, when not hit, was rolled over to the draw for the next week with increase in prize money. It was further noticed that the jackpot was generally hit after prolonged periods of 3 weeks to more than one year. The initial prize money was gradually increased by small amount every week till the final hit. The jackpot prizes, whenever not hit, were retained by the MA. Section 4 (f) of the Lotteries (Regulation) Act, 1998 envisaged that prize money remaining unclaimed within such time as may be prescribed by the State Government or not otherwise distributed would become property of the State Government. However, the Department had not inserted any clause in the agreement with the MA that the jackpot amount remaining undisbursed with the MA should be deposited to the Government account immediately after the draw. There was no justification for the MA to retain the jackpot amount once the draws were concluded and results declared. The DSSL never insisted on the Online Lottery MA to deposit the prize amount not hit, after conclusion of each draw.

During 2010-16, in the three weekly games with large prize money, the Directorate allowed the MA to retain prize amount ranging from ₹ 1.00 crore to ₹ 11.58 crore for periods ranging from one week (7 days) to 80 weeks (560 days). No penal interest was imposed on the MA for retention of the undrawn prize money. Allowing the MA to regularly retain the prize money against the above games for prolonged periods till the jackpot was hit resulted in undue favour to the MA. In monetary terms, the undue favour to the MA has been worked out to ₹ 3.50 crore towards interest (calculated @8 per cent per annum) due to non-insistence for deposit of undisbursed prizes by the DSSL.

Based on the Audit observation, the Department asked the MA for depositing the roll over jackpot amount to the Government exchequer till it was hit. However, as of July 2017, the MA had not deposited the roll over amount into the Government account.

The Department stated (July 2017) that it would relook into the matter and take up necessary corrective steps.

2.3.6 Appropriate Revenue Model not formulated

To assess the revenue potential out of organising lotteries, it was necessary that the DSSL should have done a cost-benefit analysis of the lottery business from time to time, with a cost break-up of different expenditure components involved in running the lotteries and the ultimate revenue that was likely to be generated.

A detailed cost breakup was needed to ascertain the actual expenditure to be incurred on establishment of the Points of Sale (POS), commission to the agents/retailers, cost of paper, printing charges, prize money to be paid, expenditure on manpower, payments to be made to the Internet Service Providers (ISPs) and Data Centres, payment to other States where Sikkim State Lotteries were planned to be played, etc. Only after determining the proposed expenditure on each component, the Department could have determined the actual profitability. Audit noticed that no cost benefit analysis had ever been attempted. The Department had also not impressed upon the MAs to prepare separate and clear accounts of income and expenditure relating to operation of Lotteries and never asked the MAs to furnish details of actual expenditure incurred by them on running the lotteries.

The Department failed to prepare an appropriate Revenue Model based on actual Income and Expenditure relating to Lotteries to ensure an optimum revenue share. It entirely depended upon the MGR quoted by the MAs for marketing the State's lotteries. The MGRs receivable from each MA was not based upon any analysis, but was based on the rates offered by the MAs. The Department did no exercise to ascertain whether the MGR offered by the MAs was reasonable and optimum and linked to Sales turnover. It was noticed in audit that the MGR offered by each MA was around ₹ 10 crore per annum irrespective of whether the offers were called through tenders or fixed through negotiation by calling individual offers or through extension of agreement. The basis on which the MAs offered this rate and the reason for accepting this amount by the State Government was not on record. In terms of the Lottery (Regulation) Act, 1998 and Lottery (Regulation) Rules, 2010, the entire sale proceeds was to be deposited in the State account and all expenditure were to be incurred by the State. Instead of accepting fixed MGR, the State Government should have ensured deposit of the sale proceeds in Government account as per Lottery (Regulation) Act and Rules *ibid* and the Government should have incurred all expenditure from the same account and the MAs should have been paid commission after deducting expenditure incurred by it.

The Department stated that since the State's lotteries were sold in far off places like Maharashtra, Punjab, Goa, etc., it was not possible to conduct market study for ascertaining various costs and risks involved in running the lotteries to arrive at an appropriate revenue model. It, therefore, adopted the MGR model. The Department, however, assured to make

efforts to adhere to the Audit recommendation once it was fully equipped with adequate manpower to handle the task.

The MGR model adopted by the State was not only against the extant Act/Rule, but it also did not protect the financial interest of the State. As of June 2017, the Department had not initiated action to formulate appropriate revenue model for the State's lottery operations.

The Department stated (July 2017) that it would look into the matter in the light of new regulations likely to be notified by the MHA, GoI.

2.3.7 Year-wise sales vis-à-vis revenue paid

The Minimum Guaranteed Revenue (MGR) payable by the MAs formed the main revenue received by the Government besides other small amounts received on account of draw expenses, unclaimed prizes and printing charges. The year-wise position of sale proceeds of lotteries shown by the MAs vis-à-vis the revenue realised by the State is indicated in the following table:

Table 2.4
Position of sale proceeds of lotteries shown by the MAs vis-à-vis the revenue realised

| Year | Sale Proceeds from State Lotteries (in ₹ crore) | Govt. Rev. (in ₹ crore) | Percentage of MGR to Sales |
|---------|--|----------------------------|----------------------------|
| 2010-11 | 5055.53 | 30.37 | 0.60 |
| 2011-12 | 6012.57 | 28.63 | 0.48 |
| 2012-13 | 7105.51 | 31.75 | 0.45 |
| 2013-14 | 11171.56 | 32.82 | 0.29 |
| 2014-15 | 11591.15 | 31.37 | 0.27 |
| 2015-16 | 3898.55 | 24.81 | 0.64 |

Source: Departmental figures.

It may be seen that while the sales turnover continuously and consistently increased year after year from ₹ 5,055.53 crore in 2010-11 to ₹ 11,591.15 crore in 2014-15¹⁸, there was no corresponding increase in revenue of the Government. The percentage of revenue receipts to sales turnover declined from 0.60 per cent in 2010-11 to 0.27 per cent in 2014-15 although the sale proceeds doubled during the same period. The volume of sales and the corresponding income of the MAs increased by over 129 per cent between 2010-11 and 2014-15 but the Government revenues remained more or less static. Thus, the revenue receivable by the Government was not linked to the sales turnover of the Lotteries.

The Department stated (July 2017) that the revenue was not linked to the sales turnover presently as the State realised the committed revenue from the MAs through the State's existing process. However, the MHA, GoI is reviewing the situation and is likely to notify new regulations whereby revenue receivables are expected to be linked to sales turnover.

2.4 Printing of lottery tickets

The State of Sikkim organised two types of lotteries, paper lotteries with pre-printed tickets and Online Lotteries. Rule 3(5) of the Lottery (Regulation) Rules, 2010 envisage that the paper lottery tickets and the stationery on which the Online Lottery tickets are issued shall

¹⁸There was sudden dip in sales & revenue in 2015-16 due to suspension of paper lotteries. Hence, we have taken the period 2010-11 to 2014-15 to determine the usual trend of sales vis-à-vis revenues.

be printed by the organising States at a Government Press or any other High Security Press included in the panel of the RBI or the Indian Banks Association, Mumbai. Further, Rule 8 of the Sikkim State Lottery Rules, 2003 envisages that the Government through the Director (State Lotteries) shall appoint printers of good repute for the printing of lottery tickets at such terms agreed upon by both the parties in the printing of tickets. Moreover, the Government shall take all reasonable care to ensure the genuineness and authenticity of lottery tickets and to make the duplication and sale of fake lottery tickets impossible.

It was noticed that during 2010-16, paper lottery tickets were printed mainly from four security printers¹⁹, without call of tenders. During the period 2010-16, an amount of ₹ 234.98 crore was incurred on printing of paper Lottery tickets by the Department. The printing cost was paid into the Department's savings account by the MA appointed for marketing the paper lotteries. The printing cost was separately deposited by the MA and did not form part of MGR.

All four printers were found to be empanelled as security printers under the Indian Banks Association. These four printers were continuously engaged by the DSSL for printing paper lottery tickets for many years, exact date for which could not be ascertained as the old records relating to selection of these printers could not be provided to Audit. The modality adopted for selection of the security printers and justification of rate fixed for printing of lottery tickets, thus, could not be ascertained from the records produced to Audit.

2.4.1 Return of unsold tickets to the State by the Marketing Agents/Distributors

Rule 3(16) of the Lotteries (Regulation) Rules, 2010 envisaged that the organising State shall keep records of tickets printed, tickets issued for sale, tickets sold, tickets which remain unsold at the time of draw and the prize winning tickets along-with amount of prize(s) in respect of each draw in the manner prescribed by the organising State. Rule 4(5) of Rules, 2010 further envisages that the distributors or selling agents shall return the unsold tickets to the organising State with full accounts along-with challans of the money deposited in the public ledger account or in the consolidated fund of the organising State through the sale of tickets.

Records relating to printing of the tickets and handing over of such tickets to the Marketing Agent were maintained by the Department. The MA provided details of sale of tickets to the Department from time to time. The Department had adopted a system of sale on "all sold" basis where all tickets handed over to the MA were considered as 'sold' and did not insist on the MA to return the unsold tickets.

It may be mentioned that there was no provision in the State or Central Rules for treating all tickets handed over to the MA as sold on 'all sold' basis. The State Rules, 2003 and Central Rules, 2010 clearly emphasised return of unsold tickets by the MAs to the State. Hence, the Department's adoption of the system of 'all sold basis' requiring no return of the unsold tickets to the State was not in conformity with the State or Central Rules.

¹⁹ Printing Press empanelled under RBI or Indian Bank Association as security press. Two printers each at Hyderabad and Faridabad had been selected for the process of printing lottery tickets.

In terms of Rule 8(7) of the Sikkim State lottery Rules, 2003, the Director or any other officer authorised by him was required to deliver the printed tickets to the distributor(s) appointed by Government for sale. It was, however, seen that the printing presses were instructed by the DSSL to deliver the paper lottery tickets directly to the two area distributors appointed by the MA (located at Kolkata) without any intermediary check by any officer of the DSSL. Hence, there was no control over actual number of tickets printed and the delivery and distribution of lottery tickets to the MA.

The Department stated (July 2017) that it has since posted its own staff in Kolkata to supervise delivery of paper lottery tickets to the MA and would strengthen the office at Kolkata by posting additional staff to augment the control mechanism.

2.4.2 Maintenance of records of Online Lottery tickets by the State

The tickets in the case of Online Lotteries were printed instantly on demand of customers at the points of sale. The number of tickets printed depended upon the demand of the customers. The State had no means to independently verify the number of tickets printed and sold by the MAs against any draw. The State entirely depended on the statements submitted by the MAs regarding the number of tickets sold and printed. There was no mechanism to regulate the printing, sale, cancellation and accounting of tickets in respect of Online Lotteries.

2.4.3 Maintenance of records of printed tickets by Distributors/Selling Agents

In terms of Rule 4 (3) of the Lottery Regulation Rules, 2010, the distributors or selling agents were required to maintain records of tickets obtained from the State, tickets sold and those which remained unsold upto the date and time of draw along-with other details as may be specified by the State. Thus, in terms of Rules, 2010, the State was required to specify the manner in which the Distributor/Selling agents were required to maintain records of tickets obtained from the State, tickets sold and those which remained unsold upto the date and time of draw along-with other details. It was, however, seen that the State had not issued any notification or order specifying the manner in which the Distributor/Selling agents were required to maintain records of tickets obtained from the State, tickets sold and those which remained unsold upto the date and time of draw. Further, during the course of audit, the sale of paper lotteries was suspended and hence, Audit could not verify the manner in which the Distributors/Sub-Agents maintained the records of tickets received, sold and unsold.

2.4.4 Security features in tickets

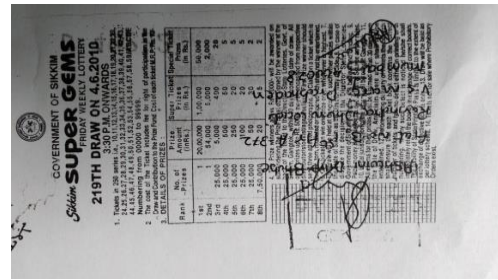
Rule 8 of the Sikkim State Lottery Rules, 2003 relating to printing of lottery tickets, *inter alia*, envisaged that the Government was required to take all reasonable care to ensure the genuineness and authenticity of lottery tickets and to make the duplication and unauthorised sale of lottery tickets impossible. All tickets were required to bear the State's logo, facsimile signature of the Director, all prizes offered, date of draw and terms and conditions on the back of the tickets conforming to the rules and agreement signed between the State and the MA. Rule 9 (4) of the Sikkim Online Network Lottery Rules, 2001, *inter alia*, envisaged that in addition to the above features, the tickets may have security marks or bar

codes to protect players as well as State's interest. It was seen that important factors like the quality of paper on which the tickets were to be printed, quality of print, dimension of the tickets and type and size of font to be applied for printing the tickets were nowhere specified. Even though paper ticket lottery was not in operation during the time the audit was conducted, an old ticket was examined and it was found that the font size and print quality used in printing the terms and conditions for claiming prizes at the back of the lottery tickets was small and barely legible as may be seen in the photographs of tickets given below.

Image 2.1



Image 2.2



Further, security features like bar codes were specified only for Online Lottery tickets and not for paper lottery tickets. The photographs of tickets indicate the print quality and layout of a prize winning paper lottery ticket drawn on 4 June 2010.

2.5 Draw process

Rule 11 of the Sikkim Lottery Rules, 2003 envisages that all draws of State Lottery shall be conducted within Gangtok, Sikkim only, shall be open to public and shall be held under the supervision of the Director or any other officer authorised by him in the presence of judges appointed by the Government. Draws would be conducted on the day and time prescribed by the Government from time to time. Further, in terms of Rule 10(6) of the Sikkim Online Network Lottery Rules, 2001, the State Government in consultation with the Marketing Agent would specify the time of draw-break at which sale of online tickets to the players and purchasers would be stopped. However, it was seen that no such specific time of draw break at which sale of online tickets to the purchasers had been determined by the State Government till date. It could not be ascertained in audit at what point of time before draw the online MAs actually stopped selling of the tickets. Regarding paper lottery tickets also, no time had been prescribed anywhere regarding the stoppage of sale of tickets by the agents/retailers before the draw.

Draw Machine: Clause 2(d) of the Lottery (Regulation) Rules, 2010 envisaged that the draw of prize winning numbers for each lottery or lottery scheme is conducted by operating the draw machine or any other mechanical method based on random technology visibly transparent to the viewers. The methods adopted for drawing results of paper and Online Lotteries are elucidated below.

Draw of paper lotteries

The draws of the paper lotteries were conducted in the draw hall located in the DSSL, Gangtok. All draws were conducted on the day and time prescribed by the State from time to time. The draws were conducted under the direct supervision of the Director or his authorised representative in presence of draw judges who watched over the draw process and validated the results of draw. Paper lotteries were drawn by operating a mechanical draw machine (shown alongside) based on random technology which was visible to the viewer.

Image 2.3

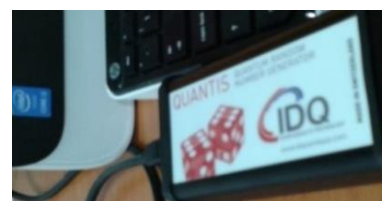


Draw machine of paper lotteries

Draw of Online Lotteries

The Lottery (Regulation) Rules, 2010 envisaged installation of central computer server consisting of a system of multiple computers at a central location under the direct control of the organising State that accepts, processes, stores and validates the Online Lottery transactions or otherwise manages, monitors and controls the entire system of Online Lottery. The State had notified the Sikkim Online Network Lottery Rules, 2001 in August 2001, in terms of which, the 'central computer system' was defined as a system of multiple computers installed for diverse functions of computing, data communication, ticket transactions, prize amount calculation, verification of prize amount, cancellation of tickets etc. The State Rules, 2001 further envisaged that the State may appoint computer engineers/experts to conduct audit and inspection of the computer system network installed by the MA. Such person would be responsible for checking and counting of tickets being sold, detect any computer related errors, mistakes, frauds, misuse of system, data manipulation and such other work assigned by the Director, DSSL.

Image 2.4



RNG Device used by Sumit Online Trade Solutions to generate draw results

It was, however, seen in audit that the central servers for the Online Lotteries were not located in Sikkim to enable the State to have direct control over the entire systems and processes of draw of Online Lotteries. The central servers were located in Mumbai in data centres of the MAs' own choice with no presence of any State Government authority. The entire operation of Online Lotteries was run by the MAs using application software, computer programmes and internet networks of their own choice without fixing of any norms and standards by the State. The State had also not appointed any computer engineer/expert to supervise and inspect the computer system networks for detecting any computer related errors, mistakes, frauds, misuse of system, data manipulation etc. In fact, the DSSL

Image 2.5



RNG & Computer Monitor of Pan India Network Ltd.

was not aware about the number of POS under each MA in different States (*Maharashtra, Punjab, etc.*) and the status of operation of a POS at any point of time.

Mirror Server: A server as a secondary server used for ready back-up of data required to be updated simultaneously with the central computer server. Audit noticed that the mirror server was installed in the DSSL office. However, the mirror server was used for only generating complied reports from time to time. Thus, the installation of mirror server did not serve the purpose as the data in central server was not reflecting in the mirror server on real-time basis.

Non-transparent process of on-line draw: In contravention to the provision of the Lottery (Regulation) Rules, 2010 relating to conduct of draw of lots by operating draw machine or any other mechanical method visibly transparent to the viewers, the State, for Online Lotteries, used electronic devices called Random Number Generators (RNG) for drawing results of the lottery schemes. The RNGs were programmed to generate the results automatically exactly at the time of draw and such results were instantly transmitted to the central servers at Mumbai and from there-on to the various points of sale placed in different States. Thus, the draw of results for Online Lotteries was done by using a method which was non-mechanical, could not be easily understood and not visibly transparent to the viewers. Merely by looking at the draw of results through RNGs, it was not understood how the department could ascertain that the system was free from manipulation.

There was nothing on record to show that the Government had conducted an IT audit of hardware and software used by the MA to draw an assurance that the system did not permit any manipulation or malpractice in draws.

2.5.1 Violation of provisions of the Lotteries (Regulation) Rules, 2010 in draws of Online Lottery scheme

Rule 3(14) of the Central Rules, 2010 emphasise that the organising State shall not offer a prize on a lottery ticket or in an Online Lottery on the basis of single, double or triple digit in any form or combination. The spirit of the above Rule was clearly that the draw of any lottery in any form or combination should be conducted at least with four digits from 0000 to 9999. The prize winning probability thus, at the most, should be 1:10000 and not higher than in terms of the Rule²⁰.

It was seen in audit that one Online Lottery MA, Summit Online Trade Solutions Pvt Ltd. conducted eight daily draws of different lottery schemes. Out of the eight daily draws, in case of 6 draws (Smart Online Lottery Scheme), the prize winning probability for 80 per cent of the prize money (2nd prize) in the schemes was designed to be as high as 1:120 as against 1:10000. This defeated the spirit of Rule 3 (14) of the Central Rules, 2010. For winning a minimum bet (2nd prize), a player was required to make the following choices:

- One letter from among 3 letters: J (Jack)/Q (Queen)/K (King)
- One symbol out of 4 card symbols: ♠ (Spade) ♣ (Club) ♥ (Heart) ♦ (Diamond).

²⁰Out of 10000 tickets purchased serially from 0000 to 9999, one would win just 1 prize, hence probability of winning = 1:10000.

- One alphabet out of 2 alphabets: A, B.
- One digit out of 5 digits: 1,2,3,4 & 5.

Thus, the winning probability of a bet in the above scheme was $1:3 \times 1:4 \times 1:2 \times 1:5 = 1:120$. In a two-digit lottery, the winning probability is 1:100 and in three-digit lottery 1:1000. Thus the above scheme marketed by the MA was akin to a two digit lottery and hence contravened Rule 3(14) of Lottery Regulation Rules, 2010.

The Department in its reply (July 2017) stated that it had discontinued the above Schemes from August 2016.

2.5.2 Publication of results

In terms of Rule 12(1) of the Sikkim State Lottery Rules, 2003, the list of prize winning ticket numbers in each draw would be published in the Official Gazette and such publication would be final and official announcement of the result of the draw. The result of each draw would be published in the national, regional and local newspapers for wide circulation and also in modern mass media.

The result of the draws were published by the Lottery MAs on behalf of the State Government at their own cost in one National and three State level newspapers in English, Hindi and Nepali languages – (i) Sikkim Mail (English), (ii) Anugamini (Hindi), (iii) Himali Bela (Nepali) and Dhankeshri & Lottery Sambad (English and Bengali Papers for paper Lotteries).

The results of the lottery draws were also published in local dailies of the States under whose jurisdiction Sikkim State Lotteries were played – (i) Viswa Darpan, Hindi (Punjab & Maharashtra), (ii) Vishwa Darpan, English (Punjab & Goa), Dainik Jagaran, Punjabi (Punjab), Echo of India, English (National). The results were hosted in the Departmental website and also published in the Official Gazette of the State Government.

2.6 Co-ordination with other States

The Ministry of Home Affairs (MHA), Government of India in August 2011, *inter alia*, instructed all the Principal Secretaries (Finance/Home) of State Governments to (i) keep the State Government in whose territory lottery tickets are sold duly informed of marketing arrangements established by the organising State and give them all details of persons/firms involved in selling/distribution/printing of lotteries; (ii) ensure that the persons/firms involved in selling/distribution/printing of lotteries do not violate any provision of the Act/Rules as the organising States shall be liable for any lapse/violation on their part; (iii) provide such other information to the State Government, in whose territory the tickets are sold, as required under the Act/Rules; (iv) keep in direct touch with the officers of the State Government in whose territories the tickets are being sold. The MHA further advised officers of both Governments should meet every few months so that any issues relating to lotteries are mutually resolved. Further, in terms of Rule 3 (5) of the Sikkim State Lottery Rules, 2003, the distributor (MA), could appoint stockists or selling agents to sell lottery tickets to the public at their own arrangements. The MA was, however, required to submit list of such stockist or selling agents with necessary particulars to the Director, DSSL. Paper

Lotteries of Sikkim were sold in Sikkim and West Bengal mainly. Online Lotteries were being sold in Punjab, Maharashtra, Sikkim (*Tashi Delek/Pan India*) and Goa.

Despite the above clear instructions by the MHA, the co-ordination of the State with other State Governments under whose jurisdiction Sikkim State Lotteries were being sold was found inadequate. Details of stockists/selling agents of MAs available with the Department did not match with selling agents involved²¹, as elucidated below.

Information obtained from the State of Punjab²² revealed that a number of agencies unknown to the State Government sold Sikkim State lotteries in the State of Punjab. In terms of records available with the DSSL, lotteries organised by Sikkim State were marketed in different States through the following four MAs engaged by the State Government during 2010-15.

Table 2.5
Details of lottery draws marketed in different states through different MAs

| Name of Marketing Agency | Year | Period for which draws were conducted for the year | Total number of draws conducted during the year |
|---------------------------------|---------|--|---|
| Tashi Delek Gaming Solutions | 2010-13 | 22.04.2010 to 15.12.2012 | 7648 |
| Pan India Network Ltd | 2012-15 | 16.12.12 to 31.03.2015 | 6569 |
| Summit Online Trade Solutions | 2010-15 | 01.04.2010 to 31.03.2015 | 13180 |
| Future Gaming Solutions Pvt Ltd | 2010-15 | 01.04.2010 to 31.03.2015 | 11476 |

Source: Departmental Records

During the period 26 July 2010 to 15 December 2012, the agency Pan India Network Ltd. sold Sikkim Lottery tickets in respect of 2,210 draws in Punjab. However, during this period, this Agency had not been authorised/engaged by the Government of Sikkim for marketing its lotteries, as can be seen from Table 2.5 above. Pan India Network Ltd. commenced marketing Sikkim Lotteries only from 16 December 2012 after the State Government appointed it as MA for marketing its Online Lotteries for a five-year period through an agreement signed on 7 November 2012. Thus, the sale of Sikkim State lottery tickets in respect of 2,210 draws by Pan India Network, without the knowledge of the State, during the period 26 July 2010 to 15 December 2012 in Punjab was not correct and showed complete lack of control by the State over activities relating to lottery.

Further, the Sikkim Government conducted 6,569 draws of lotteries Marketed by Pan India Ltd during 16 December 2012 to 31 March 2015, out of which, lottery sales of only 1,057 draws were shown in Punjab. Whether sale of tickets in respect of balance 5,512 draws of Sikkim Lotteries during 16 December 2012 to 31 March 2015 were effected in Punjab, was not known. The DSSL could not furnish any information in this regard to Audit.

a) Another agency 'S & Company' marketed lottery schemes in respect of 1,087 draws of Sikkim Lotteries in Punjab during the period 2010-12. Similarly, the agency 'Swastik Agencies' ran Lottery Schemes of the State of Sikkim in respect of 4,009 draws during 2010-14 and the agency 'Skill Lotto Solutions Pvt. Ltd.' ran such schemes in respect of

²¹In case of lotteries sold in Punjab.

²²Information provided by O/o Pr. AG (Audit), Punjab to O/o AG (Audit) Sikkim in April 2016.

510 draws in Punjab during 2014-15. None of the above three agencies were found appointed by the Sikkim Government to market its lotteries during that period.

b) The firm Summit Online Trade Solutions Pvt. Ltd. (*earlier called M/s Sugal & Damani*) has been continuously engaged by the State of Sikkim since May 2005 for marketing the State's Online Lotteries. During the period 2010-15, the number of draws of lottery schemes run by the Agency totalled 13,180 draws. The Agency is understood to be selling Sikkim Lotteries in Punjab and Maharashtra. Despite this fact, information obtained from Punjab did not reveal the Agency's name in marketing Sikkim State Lotteries in Punjab. In all likelihood, the MA marketed Sikkim Lotteries through some other Agency. The DSSL, however, could not furnish any reason for this.

The above facts indicated that there was no control by the State on sale of lottery tickets and no co-ordination done by the State Government with other State Governments under whose jurisdiction Sikkim Lotteries were sold.

The DSSL authorities stated during Exit Conference that the cases mentioned in the Audit para probably related to other States' Lotteries as the same MAs were found to market lotteries of various States under similar scheme names. The reply was not tenable as the fact remained that the State did not have list of sub agents, if any, appointed by MAs nor of all POSs and it indicated absence of coordination with other States.

2.7 Internal Control

In terms of the Lottery Regulation Rules, 2010, in cases where an organising State appoints or authorises distributors or selling agents, it shall be the responsibility of the organising State to ensure that the said distributors or selling agents act in conformity with the provisions of the Act and Rules. Every organising State shall conduct an annual financial and systems audit of the various lottery schemes organised by it including Online Lottery. The Organising State shall devise suitable means and procedures to effectively supervise the conduct of the lottery including the process of draws and all steps till publication of results to prevent any malpractices.

Despite the above stipulations by the GoI, it was seen that the internal controls, monitoring and supervision of the lottery operations were severely lacking as elucidated in the succeeding paragraphs.

- Although the State took up draw of 24 schemes per day authorised by GoI, there was no control over the process and the monitoring system was weak. All schemes were prepared by the MAs themselves and it appeared that the Department approved the schemes without any vetting.
- The MAs were authorised to distribute prizes upto ₹ 10,000 but there was no system in the Department to verify authenticity of distribution of such prizes by the MAs indicating serious lapse of control.
- The MAs were never asked to submit audited statement of accounts, there was no system for proper verification of submitted accounts/records and for periodical inspection of accounts of distributor/area distributor *etc.*

- Monitoring of the activities of the distributors and sub-agents appointed by the M.A. to detect illegalities/irregularities was found lacking as verification of records of distributors and printing agents were never carried out.
- The DSSL was not aware about the number of POS under each MA in different States (*Maharashtra, Punjab, etc.*) and the status of operation of a POS at any point of time. No returns and reports had been prescribed for furnishing regular information relating to opening of new POS; non-functioning/closure of existing POS; POS-wise transaction details; progressive balance of undisbursed prize money below ₹ 10,000 paid by the MAs from sale proceeds etc.
- The DSSL did not have a dedicated grievance redressal cell responsible for receiving/registering complaint relating to illegal/fake lottery via specific email address and toll free number. As a result, there was no system/well established procedure to deal with complaints from the general public in matters relating to illegal/fake lottery.
- Despite running Online Lotteries for more than 14 years, the DSSL did not have any expert on Information and Communication Technology (ICT) on its roll. The entire operation of Online Lotteries was run by the MAs using application software, computer programmes and internet networks of their own choice without fixing of any norms and standards by the State. The Central Servers were located in Mumbai in data centres of the MAs' own choice with no presence of any State Government authority whatsoever.
- The happenings in the Points of Sale (POS) of Online Lotteries on a real time basis was not streamed into the 'mirror server' placed in the Director's office. The 'mirror servers' only generated compiled reports from time to time.

2.8 Internal Audit & Annual Financial and Systems Audit

The Internal Audit wing of the FRED, responsible for conducting internal audit of State Government Departments, had not conducted any internal audit to evaluate the functioning of the lottery schemes. Further, in terms of Rule 3(19) of Lotteries (Regulation) Rules, 2010, every organising State was required to conduct annual financial and systems audit of the various lottery schemes organised by it including Online Lottery. However, annual finance and systems audit of the various lottery schemes organised by the State had not been conducted so far (July 2017).

2.9 Site visit of Central Servers at Mumbai

A site visit at the location of Central Servers of two MAs - M/s Pan India Network and M/s Summit Online Traders at Navi Mumbai (*Vashi & Koper Kherni*) was made during February 2016 by Audit along with an officer of the State Government. The State authorities had not visited the central servers for inspection of the system anytime in the past. Hence, the Department was not aware about the state of installation and functioning of the central servers. Some of the issues observed during the joint site visit were as under:

- The Central Servers of the MA Summit Online Traders Pvt Ltd were kept at two different seismic zones, one at Dhirubhai Ambani Knowledge Centre (*primary data*

centre), Navi Mumbai and the other at Hyderabad (*secondary data centre*). The MA (*Summit Online Traders Pvt Ltd*) informed audit that the data from the primary data centre was replicated to secondary data centre on real time basis so that in case of disaster in one location, the other centre would ensure continuity of business. However, the DSSL was unaware of this.

- The Central Servers of the MA Pan India Network Private Ltd. were, installed in the same floor of the same building at Vashi, Navi Mumbai. In case, any disaster struck the building, there was risk of disruption in continuity of business of the MA (Pan India Network Pvt. Ltd.).
- As stated by the State Government representative accompanying the audit team during the site visit, at the Point of Sale level, the system could be accessed only through a password. Each POS was granted access to the MA's main server after it cleared the authorisation and authentication process established by the MA. The hardware installed at the POS had unique terminal id built in the system hence only authorised terminal with matching terminal id was granted access to the main server. If the POS personnel changed any configuration or hardware in any POS, the access to the main server was barred. However, no IT Audit of the system had been done by the State Government to check this.
- During the site visit of central server located at Mumbai, it was explained to Audit that the draw machine including the RNG at Gangtok were kept in isolation and not connected to the outside digital world. This was done to remove any suspicion regarding remote manipulation of draw results. It was, however, revealed in the inspection of the draw machines including RNGs at Gangtok, used by the MAs that these were not kept in isolation but were connected with their respective Central Servers at Mumbai and hence were vulnerable to manipulation. There was no Government control over the entire process.
- Similarly, the lottery scheme applications needed to be audited to ensure that the programmes were free from malicious outputs before such schemes were rolled out to the public.
- It was found during examination of draw data furnished to Audit that a number of tickets were shown as 'cancelled'. The norm and method for cancellation of tickets had not been laid down by the State. Hence, the modality for cancellation of tickets was decided by the MAs themselves while the DSSL was not even aware of the fact.
- Following the site visit to Mumbai, one MA - M/s Summit Online Traders Pvt. Ltd. provided an external drive containing data dump from the Central Server for 2014-15 which had over 900 GB captured in Linux based OS. However, it was found that sizeable information contained was coded and many of the required fields like details of cancelled tickets, prize winning tickets, prize pay-outs, progressive balance of unclaimed prizes etc. were absent. Despite request to the Department to get the data, this was not furnished, as a result, analysis of data could not be done in audit.
- The MA Pan India Network Ltd. furnished a report which, *inter alia*, stated that all draws were audited through an external auditor Ernst & Young immediately after the draw closed *vis-à-vis* declared results. However, report of the external auditors was not provided

to Audit for verification. This report was neither demanded nor given to the Department. There was nothing on record to show that the MA took the permission of the State Government before appointing Ernst & Young for the audit.

2.10 Purpose of Organising Lotteries by the State

In the earliest stage of implementation of Lottery Schemes in Sikkim in 1972 before Sikkim became part of India, the proceeds from the Lotteries were aimed to be utilised for developmental activities of the Government and for the welfare of ex-armed Servicemen in Sikkim. Apart from the above general objective, the State Government had not prescribed any specific purpose for which revenue from lotteries was to be utilised. Rule 10 (5) of the Sikkim Online Network Lottery Rules, 2001 envisaged that the State Government may announce some schemes for public utility, humanitarian and benevolent causes or any such social development activity including infrastructural facilities in the State out of the net profits made under such scheme. However, no such announcement towards utilisation of revenue from any Online Lottery schemes for any humanitarian or benevolent cause etc. had been made by the Government till date. In the agreements entered with the Marketing Agents, it was mentioned that the Government intended to generate revenue with the objective of utilising such funds for good causes for health, education, infrastructure development, anti-poverty programmes and other developmental activities etc. In October 2015, the State Government brought out a Notification under Rule 3(2) of Lottery Regulation Rules, 2010 delineating the purpose for conducting and organising the lotteries which was for generating and raising additional revenues to promote various development activities of social importance like health, education, poverty alleviation, empowerment of women, welfare and upliftment of vulnerable groups of society like destitute children, differently-abled/handicapped persons, senior citizens etc. The purposes for which the State intended to utilise revenues from lotteries were, thus, very general in nature cutting across various sectors of Government functions. The revenues generated from lotteries was not kept separately with the objective of utilising it for specific purposes. It formed part of general revenues of the State which was utilised for myriad purposes.

The Department stated (July 2017) that the State Government conducted lotteries to generate revenues for taking up various developmental activities in the State. The Department, however, did not mention the specific developmental activities for which revenues from the lotteries were being utilised.

Chapter – III: Conclusion and Recommendations

3.1 Conclusion

The DSSL has not done a cost benefit analysis of Lottery Business nor prepared any appropriate Revenue Model. This has resulted in less revenue to the State and the optimum benefit has gone to the MAs. The Marketing Agents have cornered 98.60 *per cent* of sale proceeds of lotteries while the State could receive a meagre 1.40 *per cent* of sale proceeds, during the audit period 2010-2016. Despite clear provision in the Act and Rules, the entire sale proceeds were not deposited into the State's account. The State had not devised any modality to ascertain the quantum of sale proceeds, realisation and deposit of the entire sale proceeds of lottery tickets from the MAs in the Government Account in conformity to the Lotteries (Regulation) Act, 1998 and Lotteries (Regulation) Rules, 2010. Despite running lotteries for more than four decades continuously, the State had not devised appropriate revenue model to ensure realisation of a reasonable share of the sales turnovers as its share of revenue. The MGR model of revenue which pegged the revenue receivable by the State at about ₹ 10 crore per annum per MA, irrespective of significant increase in sales turnover, was not based on any analysis of receipt and expenditure incurred.

The authenticity of distribution of prizes upto ₹ 10,000 directly by the MAs, which constituted major chunk of the sale proceeds, was never verified by the DSSL. The award of marketing contract of the State's lotteries to various lottery MAs was characterised by lack of transparency, frequent extensions of contract without competitive bidding and considerable delay in finalisation of tenders led to huge loss of revenue to the State. The DSSL failed to get the Central Servers of Online Lottery MAs installed at Gangtok thereby making it extremely difficult for the State to monitor transactions of Online Lotteries besides violation of Lotteries (Regulation) Rules, 2010, which prescribed installation of server within State boundary. The application software, programmes, operating systems, hardware and all other devices used by the online MAs were neither prescribed nor standardised by the DSSL. Annual financial and systems audit of the Lottery Schemes run by the MAs had never been conducted. The game designs of the lottery schemes were not analysed by the DSSL to ascertain their legality in terms of Lottery (Regulation) Rules, 2010. The State's overall monitoring of lottery operations by the MAs, was virtually non-existent. The operations of lotteries business were fully controlled and conducted by the private operators called MAs. Even basic objectives of running lotteries business, viz. carry out development activities and welfare schemes in Sikkim, were not fulfilled as no such schemes were ever drawn by the Government, nor funded from the revenue earned from lotteries.

3.2 Recommendations

The Directorate of Sikkim State Lotteries (DSSL) may consider implementing the following recommendations:


- The State needs to lay down clear and workable modality to ascertain the quantum of sale proceeds and deposit thereof into Government account. Benchmarking of State revenue should be done with gross value of sale proceeds of lottery tickets. Commission of distributors should be fixed after deducting operating cost, prize money, printing cost, charges to the other State, etc.
- Uniformity may be brought in the process of award of marketing contracts, by following laid down procedure for selection of marketing agencies to make it more competitive and transparent.
- The application software, programmes, operating systems, hardware and all other devices may be prescribed and standardised. Uniformity, to the extent possible, in utilisation of hardware and software systems should be maintained for all Online Lottery MAs. Annual financial and systems audit of the Lottery Schemes must be conducted.
- Internal control system may be strengthened by appropriate measures, preferably by setting up an independent internal audit wing and compliance with the observations made by the wing may be ensured.
- Government should draw the scheme for utilisation of revenue generated out of operation of lotteries, as envisaged under Notification under Rule 3(2) of Lottery Regulation Rules, 2010, for development activities of social importance like health, education, poverty alleviation, etc. and it should be kept in a separate account earmarked for above purpose.

Gangtok
The 17 August 2017


(Rina Akoijam)
Accountant General (Audit), Sikkim

Countersigned

New Delhi
The 18 August 2017


(Shashi Kant Sharma)
Comptroller and Auditor General of India

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