

## CHAPTER III

### 3. Transaction Audit Observations

Important audit findings emerging from test check of transactions made by the State Government companies are included in this Chapter.

#### Government companies

#### Karnataka Power Corporation Limited, Karnataka Power Transmission Corporation Limited and Electricity Supply Companies

##### 3.1 Irregular payment of ex-gratia

#### Companies made irregular payments of ₹ 40.38 crore as ex-gratia to their employees in contravention of the guidelines issued by the Department of Public Enterprises.

The Department of Disinvestment and State Public Sector Enterprises Reforms (DDPER) modified and issued (February 2005) detailed guidelines for payment of bonus and ex-gratia to the employees of the Public Sector Enterprises (PSEs). These guidelines *inter alia* stipulated that

- if any PSE wanted to pay ex-gratia to its employees, then the allocable surplus must be arrived at duly providing for uncovered accumulated losses, pending Statutory payments, arrears of depreciation of previous years and any other statutory provisions.
- the PSEs should have paid dividend as per the Government order of May 2003.
- the PSEs should not have raised loans from Banks and other financial institutions on the strength of Government Guarantee.

The PSEs are to submit their proposals for payment of ex-gratia to the Administrative Department along with a duly filled format "A" prescribed in the Payment of Bonus Act 1965. Approval of DDPER and Finance Department has to be obtained invariably before making payment. In no case, *ex-post facto* sanction should be sought from DDPER/Finance Department/Administrative Department. If any PSE made ex-gratia payment without prior concurrence or approval and sends the file for ratification, that shall not be agreed to and, in that eventuality, the Chief Executive Officer and Financial Advisor of the PSE shall be held personally responsible and necessary disciplinary proceeding shall be initiated against the erring official. It is the Administrative Departments' responsibility to initiate the disciplinary proceedings *suo motu* wherever payment of ex-gratia is made without following the above procedures/guidelines/norms.

During test check of three PSE's<sup>99</sup> viz., KPCL, KPTCL and ESCOMs, we observed (December 2009) that even though the PSEs had not met the criteria stipulated in the DDPER guidelines, the PSEs released ex-gratia to its employees. These releases were made during the last three years without obtaining prior approval of DDPER and Finance Department as detailed below.

- Though KPCL had allocable surplus of ₹ 58.58 crore during 2006-07, the PSE had raised loans on the guarantee of the Government and hence did not satisfy the criteria stipulated in the DDPER guidelines. The Board of Directors of KPCL, however, approved and paid ex-gratia to its employees for the year 2006-07 and sought (July 2008) ratification from the Government. The Government refused<sup>100</sup> to grant *ex-post facto* sanction. KPCL paid (August 2008 /July 2009) ex-gratia for the years 2007-08 and 2008-09 without adhering to the conditions stipulated in the DDPER guidelines. KPCL requested for *ex-post facto* approval to the Government during August 2008 (for 2007-08) and August 2009 (for 2008-09). The Government, however, communicated non-approval of the same during August 2008 and August 2009. The ex-gratia payments were made by the company inspite of non-approval by the Government year-after-year. The aggregate amount of ex-gratia paid for the period 2006-07 to 2008-09 was ₹ 6.16 crore.

In reply, Government forwarded (March 2010) the KPCL's contention that non-release of ex-gratia would have had an adverse effect on the industrial relations and the company had requested the Government again in January 2010 to ratify the ex-gratia payments. Government, however, is yet to communicate the approval for ex-gratia paid (September 2010).

- It respect of KPTCL and ESCOMs, the companies were dependent on Government for subsidy<sup>101</sup>. KPTCL had made profits in all the years from 2006-07 to 2008-09. All the ESCOMs too made profit in 2006-07 and 2007-08, but incurred losses during 2008-09. The profits made by KPTCL and ESCOMs were after considering the subsidy received from Government. KPTCL and ESCOMs had not declared dividend in any of the years during 2006-09.

Though KPTCL and ESCOMs had not met the criteria laid down under DDPER guidelines, these companies also made payments year-after-year. The Government did not approve<sup>102</sup> the payments of ex-gratia for any of the years. The Government stated (April 2008) that disbursal of

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<sup>99</sup> Karnataka Power Corporation Limited (KPCL), Karnataka Power Transmission Corporation Limited (KPTCL) and Electricity Supply Companies –ESCOMs, viz., Bangalore Electricity Supply Company Limited, Gulbarga Electricity Supply Company Limited, Hubli Electricity Supply Company Limited, Mangalore Electricity Supply Company Limited and Chamundeshwari Electricity Supply Corporation Limited.

<sup>100</sup> Government had been refusing to give *post facto* approvals for ex-gratia payments from the year 2003-04.

<sup>101</sup> between 2006-09 subsidy was given to all the ESCOMs in all the years and the total subsidy given was ₹ 4,934 crore.

<sup>102</sup> the Government had not approved ex-gratia payments from the year 2000-01.

ex-gratia was in total disregard of the guidelines and repetition of such acts in future would attract reduction in release of funds. KPTCL and ESCOMS, however, continued making payment towards ex-gratia for the years 2007-08 (August 2008) and 2008-09 (August 2009). The aggregate amount of ex-gratia paid for the period 2006-07 to 2008-09 by KPTCL and ESCOMs was ₹ 34.22 crore.

In reply the KPTCL stated (June 2010) that payment of ex-gratia was made as a custom for the last several years and to maintain industrial peace.

Payment of ex-gratia by these PSEs disregarding the criteria laid down under DDPER guidelines and without prior approval of the Government resulted in irregular expenditure of ₹ 40.38 crore during 2006-09.

The matter was reported to the Government (May 2010); its reply in respect of KPTCL is awaited (September 2010).

### **Karnataka Power Transmission Corporation Limited**

#### **3.2 Idle investment**

#### **Failure to complete transmission lines as planned resulted in extra expenditure of ₹ 15.12 crore and unfruitful expenditure of ₹ 17.12 crore.**

The Karnataka Power Transmission Corporation Limited (the erstwhile Karnataka Electricity Board) had approved (December 1994) a project for establishing a 220/66 KV Sub-station at Malur, which included construction of Double Circuit (DC) line from Somanahalli to the Malur Sub-station at a cost of ₹ 12.66 crore and construction of 220 KV DC line from Malur to Kolar at a cost of ₹ 6.60 crore. The work was to be completed by March 1999.

An Expert Committee of the erstwhile Karnataka Electricity Board (March 1997) noted that connecting the proposed Malur Station to the line between Hoody and Kolar, which was already overloaded, might further worsen the already low voltage situation. Since delay was foreseen in establishment of the Station at Chintamani / Kolar (400 KV), construction of a Single Circuit (SC) line between Somanahalli and Malur was recommended. The Committee stated that once the Station at Chintamani / Kolar was commissioned, this SC line itself would be a standby.

Disregarding this recommendation, the company took up (1998) construction of the DC line from Somanahalli to Malur. The construction was stopped in October 2001 because of way leave problems, after incurring expenditure of ₹ 11.55 crore. Similarly, the construction of the DC line from Malur to Kolar, taken up in May 1999, was stopped in August 2002 after investing ₹ 5.57 crore.

Many thefts were reported as the completed portions of the lines were not charged and remained without protection. The company accorded approval (February 2004), for completion of the balance work of Somanahalli – Malur line, on turnkey basis, 29 months after the work was stopped, to avoid further

theft and loss of property. Against the tendered (April 2004) amount of ₹ 7.52 crore, the offer of M/s Deepak Cables (India) Limited at ₹ 8 crore, 6.41 *per cent* in excess over the amount put to tender, was the lowest. The offer was valid up to December 2004. The quotation had factored in the materials available in stores at the time of tender notification, which were to be supplied to the turnkey contractor. As the materials valued at ₹ 1.84 crore were diverted (November 2004) the quoted price of M/s Deepak Cables for completion of the Somanahalli – Malur line was revised to ₹ 10.97 crore.

Recurring thefts on Malur – Kolar line forced the company to include the re-erection of the damaged towers and re-stringing of the stolen portion of this line as well in the turnkey contract. Incorporating this work the tender price of M/s Deepak Cables was raised to ₹ 12.27 crore (November 2005).

In between, the Central Purchase Committee (CPC) constituted (February 2005) a Fact Finding Committee to ascertain the actual quantities available in the stores. The CPC also decided to award the work to M/s Deepak Cables, subject to the condition that additional quantities would be ascertained based on the report of the Committee, which was ratified by the Board. The CPC authorised (November 2005) the Chief Engineer, Bangalore Zone to reassess the quoted price based on the report of the Fact Finding Committee and the price was revised (January 2006) again to ₹ 16.04 crore and issued the Letter of Award (LOA) to M/s Deepak Cables. This work was rejected by the contractor stating that the validity of the offer had expired.

The company then floated short term tender (March 2006), against which only an offer of M/s Deepak Cables was received, which was approved by the Board of Directors (August 2006). The quoted price of ₹ 27.39 crore of M/s Deepak Cables was 42.36 *per cent* above the revised estimate of ₹ 19.24 crore and 70.76 *per cent* above the price of ₹ 16.04 crore in the LOA of January 2006. The LOA was issued in August 2006 and the Detailed Work Award in October 2006. The work, which was to be completed in seven months *i.e.*, by May 2007, is yet to be completed (September 2010).

We observed that :

- the expenditure of ₹ 17.12 crore incurred on the above works till the works were stopped in October 2001 / August 2002, remained unutilised till date (August 2010).
- against the tender floated in April 2004, the LOA for ₹ 12.27 crore was issued only in January 2006, 21 months after receipt of the offer, which was rejected by M/s Deepak Cables. After calling for fresh tenders, the work was again awarded to M/s Deepak Cables, who was the lone bidder, for ₹ 27.39 crore. Owing to non-firming up of the quantities and delay in awarding work, the company had to bear extra expenditure of ₹ 15.12 crore<sup>103</sup>.

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<sup>103</sup> (₹ 27.39 crore - ₹ 12.27 crore).

- Disregarding the recommendation of the Expert Committee, Malur Station was commissioned (1999) by construction of another line to the Hoody-Kolar line. Malur Station is now connected permanently to the newly constructed 400 KV Station at Kolar.
- the company stated (April 2005) that two more 220 KV Stations at Bangarapet and Hoskote had been planned and therefore, construction of the Somanahalli – Malur DC line would become essential. The Station at Bangarapet has since been commissioned and is connected to the Kolar Station. The Hoskote Station does not require power from the line.

The Malur-Somanahalli line work which was supposed to be completed by 1999 is yet to be completed (September 2010) even after ten years of its original planned completion date. Delay at every stage, non-firming up of quantities and failure to issue LOA within validity period resulted in extra expenditure of ₹ 15.12 crore and unfruitful expenditure of ₹ 17.12 crore.

The matter was reported to the Government (May 2010); its reply is awaited (September 2010).

### 3.3 Avoidable loss

**Acceptance of bank guarantee without verification resulted in loss of ₹ 48.50 lakh.**

The Karnataka Power Transmission Corporation Limited (company) is involved in the transmission of power in the State. The company undertakes works of construction of stations and transmission lines. Clause 39 under contract performance guarantee in section ITB, Volume I (commercial requirements) of Standard Bidding Documents stipulate that the successful bidder to whom the work is awarded shall be required to furnish a performance guarantee from a Public Sector Indian Bank / Scheduled Commercial Bank in favour of the owner. The guarantee amount was to be 10 *per cent* of the contract price and it shall guarantee the faithful performance of the contract, in accordance with the terms and conditions specified in the bid documents.

In accordance with the above requirements, M/s Samala Marappa & Sons (contractor) furnished bank guarantees valued at ₹ 48.50 lakh<sup>104</sup> in respect of three works<sup>105</sup> awarded between May 2003 and January 2005 and were scheduled to be completed between November 2003 and June 2006. The bank guarantees were furnished from Tungabhadra Krushi Sahakara Bank (N), Bellary, a Co-operative Bank.

<sup>104</sup> one bank guarantee valued ₹ 8.76 lakh was furnished by M/s MVR Electricals.

<sup>105</sup> construction of single circuit line from RAACL to Bellary (₹ 1.36 crore), establishing sub-station at Kudithini (₹ 2.53 crore) and construction of line from the Munirabad-Bellary single circuit line to sub-station at Kudithini (₹ 0.97 crore).

As the contractor could not complete the work despite repeated extensions of time, the contracts were terminated and the contractor was blacklisted (August 2007). The company approached the co-operative bank for encashment of bank guarantee. The bank refused (August 2007) to honour the same stating that the bank guarantees were not issued by it. The company filed (September 2007) a First Information Report at Rural Police Station, Bellary.

We observed (March 2009) that the company accepted bank guarantees issued by Co-operative Bank in violation of the stipulations in the bidding documents. The company had not independently verified the guarantees from the issuing bank. Though the company lodged a complaint with the police, no departmental action was taken against the officials who had accepted the bank guarantees without verification, thereby failing to safeguard the financial interest of the company. This resulted in a loss of ₹ 48.50 lakh. It may be mentioned here that the State Government had issued (August 1981) instructions to ensure that guarantee documents were to be received directly from the Bankers and not through parties and confirmation of the fact of issue of such guarantee was to be obtained from issuing banks so that risks of forgeries are eliminated.

The company stated (November 2009) that it had framed guidelines in October 2005 according to which only bank guarantees issued by Public Sector Indian Bank/Scheduled Commercial Bank were to be accepted. The company also stated that to avoid such instances of fake bank guarantees, strict measures would be taken to get such documents verified by the issuing bank.

It is recommended that the company put in place strict procedures and guidelines for acceptance, verification and monitoring of bank guarantees.

The matter was reported to the Government (May 2010); its reply is awaited (September 2010).

**Karnataka Road Development Corporation Limited and Bangalore Electricity Supply Company Limited**

***3.4 Failure to recover labour welfare cess***

**The companies failed to recover labour welfare cess of ₹ 67.04 lakh from the payments made to contractors.**

Under Section 3(1) of the Building and Other Construction Workers' Welfare Cess Act, 1996 (Act), the Ministry of Labour, Government of India specified (September 1996) that the State Government should levy welfare cess at the rate of one *per cent* of the cost of construction incurred by an employer. Government of Karnataka (GOK) also formulated (November 2006) Building and Other Construction Workers' (Regulation of Employment and Conditions of Service) Rules, 2006 to enforce the provisions of the Act. The Government Order issued in January 2007 stipulated *inter-alia* that Public Sector

Undertakings carrying out building or other construction works<sup>106</sup> should deduct one *per cent* of the amount of cost approved as per the tender notification from the bill at the time of making payment to the contractor and remit the same to the Karnataka State Building and Other Construction Workers' Welfare Board (Welfare Board) within 30 days of making such payment. This was applicable to all the tenders submitted or finalised and works entrusted to contractors on or after 1 November 2006.

Test check in six companies<sup>107</sup> showed that Karnataka Road Development Corporation Limited (KRDCCL) and Bangalore Electricity Supply Company Limited did not levy the prescribed labour welfare cess of ₹ 67.04 lakh from the contractors during the period from March 2007 to May 2010. As the amount is not recovered from the contractors, the company was liable for payment of ₹ 67.04 lakh to the Welfare Board.

KRDCL stated (August 2010) that in respect of tenders notified before the issue (January 2007) of Government Order, letters were addressed to the contractors intimating the facts and in respect of other cases, recovery process had been initiated. BESCOM stated (September 2010) that the amount would be recovered from the pending bills of the contractors.

The matter was reported to the Government (July 2010); its reply is awaited (September 2010).

### **Karnataka Neeravari Nigam Limited**

#### **3.5 Extra expenditure**

**The company paid re-handling charges in addition to excavation and transportation charges resulting in inadmissible benefit to the contractor amounting to ₹ 9.93 crore.**

As per the Schedule of Rates (SOR) of Water Resources Department (WRD) 2007-08, the basic rates for '*excavation in all kinds of soil*', '*excavation in soft rock without blasting*' and '*excavation in soft rock requiring blasting*' included cost of all materials, machinery, labour, placing the excavated soil neatly in dump area with lead up to 1 km and lift up to 18 metre<sup>108</sup>.

The Karnataka Neeravari Nigam Limited (company) prepares estimates before awarding a work, based on the SOR and the works alongwith such estimated amounts are put to tender. In a 'percentage tender', the tenderer has to submit

<sup>106</sup> building or other construction works includes construction, alteration, repairs, maintenance and demolition in relation to works relating to generation, transmission and distribution of power.

<sup>107</sup> Karnataka Rural Infrastructure Development Limited, Bangalore Metro Rail Corporation Limited, Karnataka State Police Housing Corporation Limited, Mysore Sales International Limited, Bangalore Electricity Supply Company Limited and Karnataka Road Development Corporation Limited.

<sup>108</sup> for lead beyond 1 km, rate as defined in SOR was payable and for lift beyond 18 metre the basic rate was to be increased by 5 *per cent*.

his bid (Schedule-B to contract) duly stating at what percentage to the amount put to tender he is willing to execute the work.

The company floated (March 2008) percentage tender for construction of a canal from Kalasa Reservoir to Malaprabha River. The contractor, who quoted the lowest at ₹ 37.29 crore (31.45 *per cent* below amount put to tender based on SOR of WRD 2007-08) against the recast<sup>109</sup> tender amount (₹ 54.39 crore) was awarded the work. The rates for excavation as per agreement ranged from ₹ 49.60 per cum to ₹ 98.62 per cum for different items of excavation work and were inclusive of excavation, transportation and placing the excavated soil in dumping yard situated about 5 kilometres away. Further, rule 3 and 22 of Schedule B to contract stipulated that the rates quoted should be inclusive of the dewatering, desilting charges, pumping out water at all stages and no extra payment on any account should be made. Also, as per rule 27 of Schedule B to contract the quoted rates included all the leads and lifts and if any extra work was to be done by the contractor for his convenience no separate payment would be made and no claims would be entertained.

The Technical Subcommittee (TSC) of the company, which inspected the site of work in April 2009, reported that due to slushy and treacherous nature of soil in deep cut reaches it was not possible to transport the excavated muck by the tippers from the bottom. So, an additional excavator was stationed by the contractor at mid-level to collect the excavated soil from the bottom level excavator and dispose of through tippers. The TSC also reported that the contractor who was present at the site had requested for a suitable rate for the additional work.

The company worked out a data rate<sup>110</sup> of ₹ 100 *per cum* based on hire charges of excavator and cost of labour as there was no similar item in the SR for the additional work of re-handling the excavated muck and a supplementary agreement was entered into in July 2009.

As per the latest running account bill paid till the end of March 2010, the contractor was paid ₹ 6.31 crore for excavation of 9.93 lakh cum (soil and soft rock). In addition, for having re-handled this 9.93 lakh cum, an amount of ₹ 9.93 crore was also paid. The work was under progress as at the end of September 2010.

We observed that as per the contract the entire process of excavation, transportation and placing the excavated soil neatly in dump area, including all leads and lifts was covered in the initial scope of work. Making additional payments under the nomenclature of 're-handling' for items of work, which were already included in scope of work, resulted in extension of inadmissible benefit to the contractor amounting to ₹ 9.93 crore. We also noticed that the

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<sup>109</sup> the original amount put to tender for ₹ 49.64 crore was recast (July 2008) to ₹ 54.39 crore due to change in design. The contractor had quoted ₹ 37.29 crore for the initial tender also.

<sup>110</sup> Data Rates : Rates worked out when similar items are not available in Schedule of Rates.



additional excavator was placed at mid-level but re-handling charges were paid for the entire quantity of 9.93 lakh cum excavated from top to bottom.

The Management stated (July 2010) that the data rate was worked out due to obstacles encountered on account of physical, geological and engineering properties of the excavated strata and these parameters were entirely different from standard excavation. The strata were sub-charged with ground water and the soil slid down immediately on execution. The movement of tippers was difficult as it was not possible to form ramps causing difficulty and excavation was to be done by multi-level excavators. The reply is not in consonance with the scope of work mentioned in the contract / Schedule of rates. Further, in a percentage tender, the tenderer is liable to bear all risks, including difficulties encountered in executing the work.

The matter was reported to the Government (May 2010); its reply is awaited (September 2010).

### **Mysore Minerals Limited**

#### **3.6 Avoidable expenditure**

**The company failed to deduct tax at source from payments made to contractors, as required under the provisions of the Income Tax Act 1961 resulting in avoidable tax burden of ₹ 1.40 crore.**

Section 194C of the Income Tax Act 1961 (Act) stipulates that any person responsible for paying any sum to a resident contractor in pursuance of a contract shall, at the time of credit of such sum to the account of the contractor or at the time of payment thereof, deduct tax at source and under Section 200, the tax so deducted shall be credited to Central Government within the prescribed time. In case tax is deductible but has not been deducted, such payments are not allowed as deduction from profits in computing the income chargeable to tax as per Section 40(a)(ia).

We observed that the company did not have an effective system of deducting tax at source (TDS) before making payments to contractors. Failure to deduct tax rendered deduction of these expenses as inadmissible in arriving at taxable income. The amounts were therefore added back to the profits for computing taxable income resulting in avoidable payment of excess income tax. The company, in the subsequent years effected TDS from the contractors and claimed the benefits foregone. We, however, observed that as at the end of August 2010, payments valued at ₹ 1.40 crore were still pending for deduction of TDS in respect of 77 cases as detailed below:

(Rupees in lakh)

Financial Year	Assessment Year	Payments on which tax was not deducted at source	Deductions claimed during the subsequent year on the basis of payment of tax	Balance	Income Taxborne by the company
2004-05	2005-06	1,834.97	1,695.66	139.31	50.98
2005-06	2006-07	151.83	14.29	137.54	46.30
2006-07	2007-08	228.32	114.40	113.92	38.35
2007-08	2008-09	215.43	215.43	0	0.00
2008-09	2009-10	17.53	4.60	12.93	4.39
<b>Total</b>		<b>2,448.08</b>	<b>2,044.38</b>	<b>403.70</b>	<b>140.02</b>

The Government, while accepting the non-adherence to the provisions of the Income Tax Act, stated (August 2010) that action would be initiated to recover the applicable amount of TDS from the contractors / professionals or raise debit notes which would be allowed during assessments year 2011-12.

### **Karnataka Rural Infrastructure Development Limited**

#### **3.7 Avoidable loss**

**Deficiencies in preparation of quotations without including the relevant costs coupled with slow progress of works resulted in loss of ₹ 2.05 crore.**

Karnataka Rural Infrastructure Development Limited (company) participated in the tenders floated (November 2005) by Karnataka Urban Infrastructure Development and Finance Corporation (KUIDFC), another Government Company, for Urban Transport (improvements) of Karwar and Bhatkal. The company quoted ₹ 8.07 crore (2.08 per cent below the tender amount) and ₹ 3.34 crore (3.11 per cent below the tender amount) for Karwar and Bhatkal, respectively. KUIDFC issued (July 2006) work orders to the company for both the works with schedule of completion at 12 months for works at Karwar and 9 months for works at Bhatkal. The company furnished (July 2006) performance bank guarantee of ₹ 1.46 crore. KUIDFC released (August 2006) mobilization advance of ₹ 1.14 crore against which the company furnished a bank guarantee of matching amount.

During September 2006, October 2006 and November 2006, KUIDFC intimated the company of the slow progress and poor quality of work. As the company failed in fulfilling the contractual obligation, KUIDFC terminated (December 2006) the contracts, encashed the bank guarantees and adjusted mobilization advance. KUIDFC admitted bills of only ₹ 30.89 lakh out of the ₹ 89.79 lakh submitted by the company. The company approached (December 2006) the Hon'ble High Court of Karnataka and obtained a stay order on further proceedings by KUIDFC. The High Power Committee (HPC) for settlement of disputes between Public Sector Undertakings discussed the matter in March 2007 and directed the company to withdraw the writ petition unconditionally and facilitate re-tendering by KUIDFC. It also directed

KUIDFC and the company to work out the amount to be refunded to the company to the extent of work executed including performance guarantee. It further decided (May 2007) that the Company would withdraw the writ petition and issues relating to payment for work done and return of bank guarantee would be resolved. In July 2009, HPC resolved that KUIDFC would not return the bank guarantee and the company would accept this and not raise the matter again. Both the parties mutually agreed not to resort to any further legal proceedings.

We observed (February 2008) that the main reason for failure to execute the works were the failure of the company in preparation of workable bid amounts before participating in tenders and the slow progress in the execution of work. The company did not consider taxes, hire charges of machinery and anticipated escalation charges while quoting the rates for the works. As per company's own estimation in November 2006, considering the then prevailing rates, the loss was estimated at ₹ 2.20 crore. In respect of works at Karwar and Bhatkal, against the required financial progress of ₹ 1.35 crore and ₹ 1.67 crore as at October / November 2006, the company could achieve inordinately low financial progress of only ₹ 0.24 crore and ₹ 0.18 crore, respectively.

The deficiencies in preparation of bids without including the relevant costs coupled with slow progress of works resulted in loss of ₹ 2.05 crore<sup>111</sup>.

The company accepted (June 2010) that it had no experience in participating in tender works and items such as taxes and hire charges were also not considered for quotation. The company further stated that the hike in rates of cement, steel and asphalt could not be judged. The company should have exercised due care in preparing quotations especially when it had no experience in such works.

The matter was reported to the Government (July 2010); its reply is awaited (September 2010).

### **Chamundeswari Electricity Supply Corporation Limited**

#### **3.8 Extra expenditure**

#### **Non-signing of supplementary Power Purchase Agreement resulted in extra expenditure of ₹ 1.18 crore.**

Karnataka Power Transmission Corporation Limited (KPTCL) entered (March 2001) into a Power Purchase Agreement (PPA) with Vijayalakshmi Hydro Power Pvt. Ltd (VHPPL). The PPA was approved by the Karnataka Electricity Regulatory Commission (KERC). As per the PPA, for the energy delivered, KPTCL was to pay VHPPL ₹ 2.25 per unit with base year as 1994-95 with 5 per cent escalation per annum over the tariff applicable for the first 10 years from the date of signing of the agreement. KPTCL froze the tariff at ₹ 3.32 per unit with effect from April 2003 because of the high cost of power and due to various initiatives contemplated in the Electricity Act 2003.

<sup>111</sup> Bank guarantee : ₹ 1.46 crore plus bills not admitted: ₹ 0.59 crore (Bank guarantee of ₹ 1.14 crore is not considered as it was in lieu of the mobilization advance already drawn by the company).

In accordance with conditions in Electricity Act 2003, KPTCL was barred from trading in electricity with effect from June 2003 and to tide over the situation, State Power Procurement Co-ordination Centre (SPPCC) was established to co-ordinate the procurement of power from different sources.

In May 2005 the Government of Karnataka transferred (with effect from June 2005), the rights relating to trading of electricity from KPTCL to five Electricity Supply Companies<sup>112</sup> of which one was MESCOM. In March 2006, certain jurisdictional areas from MESCOM were transferred to Chamundeswari Electricity Supply Corporation Limited (CESC). In March 2006, Government assigned the PPA to CESC with effect from financial year 2006-07.

SPPCC invited (March / September 2006) VHPPL for re-negotiation of the tariff which was frozen at ₹ 3.32 per unit from 1 April 2003. The tripartite agreement (supplementary PPA) was to be signed by KPTCL, VHPPL and CESC. The draft supplementary PPA (February 2007) envisaged purchase of power at ₹ 3.32 per unit with escalation of 2 *per cent* per annum on the base tariff<sup>113</sup> retrospectively from April 2003. VHPPL concurred (February 2007) with the revised tariff and requested SPPCC to take further steps for the joint signature of respective parties along with release of its outstanding dues.<sup>114</sup>

We observed that though VHPPL concurred with the supplementary PPA in February 2007 and SPPCC had requested CESC to intimate a convenient date in June 2007, CESC did not sign the supplementary PPA. Since signing of supplementary PPA was kept long pending and substantial amount due to VHPPL remained unpaid, VHPPL revoked (July 2008) the consent given in January 2007 for reduced tariff and affirmed that only the PPA of March 2001 subsisted.

Based on an appeal (2008) by VHPPL, KERC ordered (April 2009) that the parties were bound by the PPA of March 2001 as no supplementary agreement was signed.

Thus, inordinate delay (February 2007 to July 2008) in finalising the proposal and failure of CESC to initial the supplementary PPA resulted in extra expenditure on purchase of power amounting to ₹ 1.18 crore<sup>115</sup>.

The Government while accepting the delay stated (September 2010) that the Company was newly formed and the concept of PPA was new to the Company. Government further stated that agreement could not be signed by the Company due to administrative reasons like change of management and officials.

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<sup>112</sup>Bangalore Electricity Supply Company Limited (BESCOM), Hubli Electricity Supply Company Limited (HESCOM), Mangalore Electricity Supply Company Limited (MESCOM), Gulbarga Electricity Supply Company Limited (GESCOM), and Chamundeswari Electricity Supply Corporation Limited (CESC).

<sup>113</sup> Base tariff means ₹ 3.32 per unit applicable for the year 2002-03.

<sup>114</sup> the outstanding dues was ₹ 35 lakh as at August 2006.

<sup>115</sup> the extra expenditure is for purchase of power between June 2005 (date of formation of MESCOM) to July 2010.

**The Mysore Electrical Industries Limited****3.9 Avoidable loss**

**The decision of the company to venture into an area of work in which it had no expertise resulted in a loss of ₹ 0.95 crore.**

The Mysore Electrical Industries Limited (company) is engaged in the manufacture of switchgears and motor control equipment. Karnataka Power Transmission Corporation Limited (KPTCL), another Government company in Karnataka, floated (December 2002) tenders for construction of transmission line from Chikkodi to substation at Kudachi (35.06 km) on total turnkey basis. The project envisaged construction of 120 towers and stringing of the lines with 'Drake' conductor. As the company did not satisfy the pre-qualification requirements, it identified M/s Theji Constructions Private Limited (TCPL) as a collaborator to participate in the tender. While the supply portion was to be executed by the company, civil and erection portions were to be executed by the collaborator. TCPL submitted (December 2002) their quotation for civil and erection portion to the company. The company participated (December 2002) in the tender and emerged as the lowest bidder with a bid of ₹ 7.48 crore which was 15.56 *per cent* above the amount put to tender and was awarded (July 2003) the project, which was to be completed by August 2004. The company furnished (June 2003) bank guarantee of 10 *per cent* (₹ 74.79 lakh) of the contract award cost. The award cost was revised to ₹ 7.99 crore<sup>116</sup> in April 2004.

A Memorandum of Understanding (MOU) was entered into (June 2003) between the company and TCPL according to which the rates quoted by TCPL for the civil and erection work were to be at firm quoted price and payment was to be on 'back-to-back basis'. Any loss to the company due to delay in erection and civil works was to be borne by TCPL. The company issued (January 2004) Letters of Award to TCPL for civil works and erection. The work was to be completed within six months (July 2004).

The company supplied (October 2003 to July 2005) materials valued at ₹ 4.63 crore to the site. TCPL completed (August 2004) the civil works but failed to complete the erection work. TCPL demanded advance payments as well as upward price revision<sup>117</sup> for erection and stringing of conductor. The company rejected the demand for increase in prices but released (January 2004 to January 2006) advances of ₹ 11.50 lakh to TCPL, even though the MOU did not provide for such advance payments. As only 90 out of 120 towers were erected even as of January 2007, the company terminated the contract in January 2007. The company encashed (January 2007) bank guarantee of ₹ 5.65 lakh furnished by TCPL. Retention money of ₹ 9.10 lakh of TCPL was retained by KPTCL. Then the company identified (February 2007) M/s RDS Constructions, Bellary as alternate contractor to complete the balance works. After erecting 15 out of the balance 30 towers, M/s RDS Constructions also expressed their inability to proceed further, citing various reasons. Thereafter,

<sup>116</sup> supply of materials: ₹ 6.65 crore; erection: ₹ 0.23 crore and civil works: ₹ 1.11 crore.

<sup>117</sup> erection of towers: ₹ 2,500 *per* MT as against the quoted rates of ₹ 1,350 *per* MT and stringing of conductor: ₹ 65,000 *per* km as against the quoted rates of ₹ 40,000 *per* km.

the company stopped (December 2007) the work and intimated KPTCL accordingly. A joint inventory of materials at the store yard of the company was conducted (May / June 2009) by KPTCL and the company. KPTCL decided (January 2010) to short-close the work and float fresh tenders for the balance work at the risk and cost of the company. The decision on encashment of bank guarantee furnished by the company, which was valid up to 30 September 2010, has not been taken by the Board of Directors of KPTCL (September 2010).

We observed (December 2009) that

- though the company was to execute only the supply portion of the contract erection and civil works were also an integral part of the turnkey contract and successful completion depended on the performance of the collaborator. Venturing into a turnkey project of constructing a power line depending largely on the collaborator exposed the company to the risk of breach of contract. No action was taken against the collaborator to recover the amounts lost.
- the rates of galvanised towers and Drake conductor, which constituted 77 *per cent* of the contract value of supplies, were more than the rates quoted in the turnkey contract. This was due to incorrect assessment of prevailing market prices and also as the rates quoted by the company were not reviewed by the pricing committee of the company. Out of the total requirement of 214 km of Drake Conductor, 115 km were not purchased as the difference between the rates quoted in the turnkey contract and the prevailing rates as on September 2007 had reached ₹ 1 crore.
- due to the short closure of the contract, the company lost ₹ 0.95 crore<sup>118</sup> and in addition may lose an additional ₹ 2.63 crore<sup>119</sup>. Further, the company would also be liable to pay additional expenditure for getting the project completed at its risk and cost through a different source by KPTCL as a penalty.

The company stated (June 2010) that the project could not be completed due to circumstances beyond its control and KPTCL had been requested to short close the project without insisting encashment of bank guarantee. The decision of the company to venture into an area of work in which it had no expertise, that too without satisfying the credibility of collaborator and also without properly evaluating the rates to be quoted, resulted in loss of ₹ 0.95 crore up to September 2010.

The matter was reported to the Government (June 2010); its reply is awaited (September 2010).

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<sup>118</sup> bills not accepted: ₹ 51.56 lakh; liquidated damages: ₹ 25.94 lakh and difference between purchase cost and rates quoted in turnkey contract: ₹ 20.57 lakh less net amount due to TCPL : ₹ 3.25 lakh (₹ 14.75 lakh minus ₹ 11.50 lakh).

<sup>119</sup> encashment of bank guarantee of ₹ 74.79 lakh and forfeiture of retention money of ₹ 187.73 lakh for which decision of Board of Directors of KPTCL is yet to be taken.

**Food Karnataka Limited****3.10 Avoidable payment**

**The decision to treat the interest earned on Government grants parked in fixed deposits as its income rather than adding it to the grants, resulted in avoidable payment of income tax of ₹ 65.10 lakh.**

The company was incorporated in April 2003 as a Special Purpose Vehicle (SPV) to promote and implement the objective of the Government of India (GoI) in the X<sup>th</sup> Plan Scheme, which included promotion of Food Parks. Each of the Agro Food Parks was eligible for a Central Grant of ₹ 4 crore and a matching development aid of ₹ 4 crore from the State. The Government of Karnataka (GoK) had vested the company with the responsibility of facilitating and developing six Agro Food Parks, one each at Malur, Hiriyur, Bagalkot, Jewargi, Maddur and Belgaum in Joint Venture through Public-Private Partnership. The Governments released grants from 2001-02 onwards.

The Ministry of Food Processing Industry (MFPI), GoI, released (July 2001) ₹4 crore and the GoK released ₹17 crore (between March 2002 and March 2010) to the company. The company, in turn released ₹17.86 crore between August 2006 and March 2010 to the different JV companies as per periodical demands. The balances remaining were parked in Fixed Deposits regularly. The details of receipt and utilization of funds provided by the Governments are tabulated below:

Year	Grants remaining unutilized at the beginning of the year	Grants received from Central/ State Governments	Grants released to JV Partners	Grants remaining unutilized at the end of the year
	(Rupees in lakh)			
2003-04	(KIADB <sup>120</sup> received the Grants)	750.00	-	750.00
2004-05	750.00	350.00	-	1,100.00
2005-06	1,100.00	200.00	-	1,300.00
2006-07	1,300.00	-	200.00	1,100.00
2007-08	1,100.00	-	400.00	700.00
2008-09	700.00	200.00	500.00	400.00
2009-10	400.00	600.00	686.45	313.55
		<b>2,100.00</b>	<b>1,786.45</b>	<b>313.55</b>

We observed that the Joint Venture partner selected to set up the Food Park at Maddur had not identified the land for the project and means of finance by obtaining term loan from bank. The Joint Venture Agreement for Agro Food Park at Belgaum was also cancelled as the JV partner had neither paid the land cost nor tied up means of finance. The company cancelled both the JVs in April 2007. The X<sup>th</sup> Five Year Plan under which the food park scheme was proposed for implementation lapsed in March 2007 and the State lost the possibility of Central financial aid of ₹ 8 crore for establishment of two parks. None of the

<sup>120</sup> Karnataka Industrial Area Development Board.

other four parks (under implementation) have commenced commercial operation till date (September 2010).

We further observed that the company had earned interest of ₹ 2.96 crore on grants kept in fixed deposits and treated the interest as its income. Income tax amounted to ₹ 65.10 lakh was paid on such income<sup>121</sup>. Since the interest earned from fixed deposits were from investment of unspent grants, it should have been added back to the principal amount of grants instead of accounting it as its income. The company could have avoided the tax of ₹ 65.10 lakh on interest income, besides the financial irregularity.

The company replied (October 2004 / October 2007) that the Government had not specified any conditions for utilisation of funds. The company also invited reference to the opinion of the Institute of Chartered Accountants of India, which stated that where the terms of agreement were silent as to utilisation of interest earned on funds placed in fixed deposits during the interim period, the funds should be added to ear-marked fund by routing it through income and expenditure account as the entire fund was to be utilised for a specific purpose. It stated that the interest was treated as revenue in the Profit and Loss Account accordingly. The company also stated (February 2010) that action would be initiated with the IT department for refund of tax collected.

The company's reply was not correct as the interest routed through Profit and Loss Account was not added back to grant fund as per the opinion of Institute of Chartered Accountants. The MFPI, GoI had also directed (August 2008) the Corporation Bank (where the fixed deposits were parked) to return the unspent balances along with interest as any unspent balance relating to a plan scheme was required to be deposited back to Exchequer. The Ministry further viewed (October 2008) the matter regarding payment of income tax on grant released as a financial irregularity. MFPI, GOI, in reply to the request of company (November 2008) not to treat it as a financial irregularity, stated (February 2009) that utilization of interest earned on grants to meet administrative expenditure was not admissible.

The Government in its reply (June 2010) stated that as the company had no other source of revenue, the interest on deposits was utilized for administrative expenditure. The contention of the company and the Government was not in line with observations of MFPI, GoI, which had already expressed that utilization of grants and interest earned on it, for administrative expenditure was not admissible and the payment of income tax was a financial irregularity.

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<sup>121</sup> interest earned during the period 2003-04 to 2008-09.



**Karnataka Agro Industries Corporation Limited**

**3.11 Inadequate arrangements for safeguarding movable and immovable assets**

**The company suffered a loss of ₹ 0.57 crore in the value of its assets during the last six years and assets remained exposed to encroachment due to inadequate safety arrangements.**

The company (Karnataka Agro Industries Corporation Limited) was incorporated in September 1967 with the main objective of manufacturing agricultural equipment, chemicals, manures, fertilizers and pesticides. The company became non-functional since September 2003 on account of non-competitiveness of the products of the company due to globalization, privatization and deregulation of the fertilizer market. The accounts of the company have been finalized and audited up to the year 2008-09, which were adopted in the Annual General Meeting held in December 2009. The latest certified accounts for the year ended 31 March 2009 depicted that the company had total assets of ₹ 18.47 crore (including immovable assets: ₹ 14.69 crore and movable assets: ₹ 3.78 crore).

In order to have better control over assets, the company should maintain complete and up-to-date records of each asset, besides making essential arrangements, such as, periodic physical verification, arrangements for watch and ward of the assets, and adequate insurance cover against the risk of floods, earthquake, *etc.* Further, in respect of the land, the company needs to construct a boundary wall and engage watch and ward on land lying vacant so as to prevent encroachments. In case of illegal encroachments on land, prompt legal measures should be taken by the company for making the land encroachment free. The deficiencies noticed in maintenance of proper records and taking adequate measures in safeguarding the movable and immovable properties by the company are summarized below:

**Inadequate maintenance of asset records**

In order to have a scientific and effective internal control system in force, the company needs to maintain 'asset records' for each asset with all important particulars of the assets such as location, original cost, accumulated depreciation, technical and engineering specifications of machineries, identification number, *etc.* We observed that the company did not maintain adequate and up-to-date records depicting all vital information. The 'asset records' maintained by the company were last updated up to 31 March 2004 and no updation was made thereafter.

**Physical verification of assets**

The system of physical verification of assets at regular time intervals is an essential tool of internal control as it helps in ensuring the availability of assets in the possession of the company at stated location. An effective system of periodic physical verification of assets minimizes the risks of loss / theft of

movable assets and encroachments in case of immovable properties and at the same time, enables the Management to take timely remedial action against the detected cases of theft / encroachments of assets. The company had no laid down policy for physical verification of assets.

The company has not carried out physical verification of assets since 2006-07. Though physical verification was conducted up to 2005-06, the company did not furnish a copy of the physical verification report and hence the discrepancy between physical count and book records could not be ascertained. Thus, the assets of the company remained exposed to the risks of theft / encroachment. The company replied (March 2010) that as all their employees had been relieved under 'Voluntary Retirement Scheme-2003' physical verification could not be conducted.

### **Encroachments due to inadequate security arrangements**

Proper arrangement for security and watch and ward of the immovable properties (*viz.*, land and buildings) is very essential as it ensures encroachment free availability of the land and buildings for company's own use as well as sale, as and when needed. As the physical verification of assets was not conducted, the position of encroachment, if any, on the land/buildings was not known. The company did not have khata<sup>122</sup> in respect of 48.41 acres of land out of the total area of 70.84 acres of land owned by the company in different parts of the State. The company replied (March 2010) that necessary action was being taken to get the khata transferred.

### **Non-use of assets**

The company needs to make adequate arrangements for proper maintenance and upkeep of the plant and machinery not in use. As the company has been non-functional since September 2003, periodical review of the position of these assets taking into account the reports of the physical verification is essential so as to avoid deterioration of assets due to efflux of time. The assets not in use for long also need to be considered for sale.

It was, however, observed that there were no proper arrangements for maintenance and upkeep of the assets not in use. Further, there was no system in the company for conducting a need-based review of the assets so as to decide on possible utility of these assets in future or their timely disposal. As a result, inventories valued at ₹ 0.57 crore considered obsolete, held by the company, are no longer useful and the remaining assets (valued at ₹ 3.78 crore) which are no longer required may be disposed of to the best advantage of the company. The company replied (March 2010) that major portion of assets have been disposed of and action was being taken to dispose of the remaining assets.

### **Insurance cover**

The insurance for the properties is a cover that guards the assets of the company against the probable losses due to natural calamities and other reasons

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<sup>122</sup> **Khata is a property document that includes details of the land or property *viz.*, name of the owner, size, location and built-up area of property *etc.***

such as fire, floods, riots, theft, *etc.*. Regular and adequate coverage of insurance at a nominal cost (premium) minimizes the risks against these losses. The company had not renewed the insurance since May 2007.

The company is exposed to risk of encroachments on its land/building in the absence of adequate watch and ward. There is also a risk of assets becoming obsolete due to non-use/lack of maintenance. In view of this, it is recommended that the company may:

- Maintain complete and up-to-date records giving all vital information of all movable and immovable assets;
- Periodically reconcile the discrepancies in the figures of the assets;
- Conduct physical verification of assets at regular time intervals;
- Make adequate security arrangements for watch and ward of immovable properties, either internally or outsourced, so as to prevent possibilities of encroachments;
- Make adequate arrangement for upkeep/maintenance of non-used assets and periodically review the position for their future utility; and
- Obtain regular and adequate insurance cover for all the assets against risks.

The matter was reported to the Government (June 2010); its reply is awaited (September 2010).

### **Karnataka Power Corporation Limited**

#### **3.12 Avoidable extra expenditure**

**The decision of the company to avail of two permanent High Tension connections instead of one temporary power supply and one permanent connection resulted in avoidable extra payment of ₹ 42.01 lakh on power charges.**

Karnataka Power Corporation Limited (company) proposed (January 2002) to construct Bellary Thermal Power Station (BTPS) in Bellary District. As per the agreement entered (December 2003) with M/s Bharat Heavy Electricals Limited (BHEL), construction power supply of 4 MVA was to be provided free of cost. In the meeting held (January 2004) between the company and BHEL, the company agreed to make available initially construction power supply of 500 KVA by February 2004 and 4 MVA by April 2004.

The company had approached Gulbarga Electricity Supply Company Limited (GESCOM), for sanction of 4 MVA in May 2003 itself. The company decided (September 2003) to avail of the construction power supply by tapping the 66 KV line passing adjacent to BTPS compound and floated (September 2003) tenders for establishing a sub-station. During the initial assessment of offers, as the lowest offer of ₹ 3.32 crore was very high compared to the estimated cost of ₹ 1.70 crore, the company re-floated (November 2003)<sup>123</sup> fresh tenders. The works were awarded in January / February 2004 to various agencies and

<sup>123</sup> GESCOM sanctioned (November 2003) a HT installation (EHT 4) of 4 MVA to the company.

was to be completed by April 2004. The sub-station was completed at a cost of ₹ 2.04 crore and serviced in July 2004.

The company, in addition to the above connection, had requested (December 2003) GESCO to provide High Tension (HT) connection of 500 KVA, which was accorded sanction in January 2004. The power supply was required to meet the initial start up operations between February 2004 and April 2004. The work of HT connection was completed in March 2004.

The company, thus, had two permanent HT connections of which 500KVA was to meet requirement from February 2004 onwards and 4MVA to meet the requirement from April 2004 onwards.

We observed (November 2009) that the decision to obtain a permanent connection of 500KVA for initial requirement (February 2004 to April / July 2004) was not justified. By obtaining permanent power supply, the company was liable to pay monthly minimum fixed charges for 500 KVA installation for a minimum period of five years as per Section 32.04 of Electricity & Distribution Code of GESCO. We further noticed that power was drawn from the 500 KVA line only in September 2004, by which time, power from 4 MVA line was already available (July 2004). In all, between the date of installation (February 2004) to date of disconnection (October 2009), power was drawn only for nine months<sup>124</sup> from 500 KVA line which could be met from 4 MVA line available.

Thus, the decision of the company to obtain permanent HT connection of 500 KVA instead of temporary power supply for temporary requirement resulted in payment of avoidable monthly minimum charges for five years totalling ₹ 42.01 lakh<sup>125</sup>.

The Government stated (August 2010) that the decision was taken to obtain permanent HT power supply from GESCO instead of temporary power supply considering the same as a standby source for BTPS construction activities. The fact that the company approached GESCO for disconnection of 500 KVA line in November 2006 which could not be disconnected as the initial agreement period for installation of HT power supply with GESCO was five years from the date of service indicated that there was no actual requirement of the supply. Moreover, the company had made standby arrangements by providing DG sets in July 2009, which could have been done in 2004 itself after availing of temporary connection.

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<sup>124</sup> September 2004 (65 KVA), November 2004 (171 KVA), December 2004 (210 KVA), February 2005 (1 KVA), November 2005 (375 KVA), November 2007 (12 KVA), December 2007 (17 KVA), January 2009 (50 KVA) and April 2009 (152 KVA).

<sup>125</sup> net of charges which would have been payable if temporary connection had been availed ₹ 48.91 lakh less ₹ 6.90 lakh (₹ 1.15 lakh x 6 months).

**Karnataka Renewable Energy Development Limited**

**3.13 Avoidable loss**

**Non-adherence to the provisions of Income Tax Act resulted in avoidable loss of ₹ 26.56 lakh.**

The provisions of Income Tax (IT) Act 1961 (Section 208) stipulate that Corporate Assesseees have to pay advance tax on estimated income in four instalments on the due dates prescribed<sup>126</sup>. As per Section 139 (1) of IT Act, the assesseees are required to file the returns before 31<sup>st</sup> October of relevant assessment year and any failure in payment of advance tax or filing of returns attracted penal interest (Section 234).

We observed (November 2009) that Karnataka Renewable Energy Development Limited (company) did not pay advance tax in any of the assessment years from 2002-03 to 2008-09 within due dates<sup>127</sup>. The company appointed (February 2008) a Tax Auditor for taking up tax audit for the years 2002 to 2006<sup>128</sup>. The company filed its returns and paid the tax along with interest. Tax returns were filed for the assessment years 2007-08 and 2008-09 only in December 2008 and January 2009 as against October 2007 and October 2008 respectively. The total interest paid due to non-payment of advance tax and delay in filing returns for the financial years from 2001-2008 was ₹ 74.03 lakh.

The company replied (January 2010) that it had backlog in Statutory Audit since 1996-97 and thus the IT returns could not be filed in time. The company further stated that Income Tax amounts were kept in fixed deposits which earned interest of ₹ 56.93 lakh.

The reply of the company does not justify non-adherence to the provisions of Income Tax Act, as payment of advance tax and filing of tax return were not connected to statutory audit. The non-compliance with provision of IT Act was not financially prudent and resulted in loss of ₹ 26.56 lakh<sup>129</sup>.

The matter was reported to the Government (May 2010); its reply is awaited (September 2010).

<sup>126</sup> up to 15 per cent before 15 June, up to 45 per cent before 15 September, up to 75 per cent before 15 December and up to 100 per cent before 15 March of the tax payable every year.

<sup>127</sup> for assessment years 2004-05, there was no tax liability and for assessment year 2005-06, tax deducted at source exceeded the tax payable for the year.

<sup>128</sup> Tax Auditor for 2006-07 and 2007-08 was appointed in February 2009.

<sup>129</sup> interest earned on Fixed Deposit was also liable to income tax of ₹ 9.46 lakh. Therefore the overall loss was ₹ 74.03 lakh less (₹ 56.93 lakh – ₹ 9.46 lakh).

**Karnataka State Police Housing Corporation Limited**

**3.14 IT Audit of Web based Project Management System software**

**Delay in complete implementation of Web based Project Management System software resulted in non fruition of investment made and non achievement of objectives.**

The Karnataka State Police Housing Corporation Limited (Company) was incorporated in 1985 under Companies Act 1956 and undertakes construction of residential and office buildings for Police, Prisons, Home Guards and Fire services departments.

The Company implemented a Web based Project Management System (WPMS) in 2001 for remote monitoring of the execution of projects by customising the Microsoft Project Server software and creating a web based network for connectivity between the divisions and head office. The Company has invested till date ₹ 2.80 crore in IT assets. The investment was meant to result in creation of IT infrastructure and capability required for effective and timely monitoring of projects remotely, the software has not been fully implemented so far (September 2010). We attempted a general review of the information technology policy and strategy of the Company and a detailed review of the development and performance of the WPMS to evaluate the overall achievement of objectives, which are discussed below:

***IT policy, planning and strategy***

**3.14.1** The Company had adopted IT based project monitoring tools from 2003 and made substantial investments in IT, it has not formulated any IT policy or strategy for implementation of computerisation in a planned manner. The Company had outsourced the maintenance of the WPMS software, hardware / servers, networking, database administration and change management functions. But, it had not formulated any policy for controlling the activities of the contractors to ensure the protection of IT assets and confidentiality of data. It had also not defined the recruitment policies to ensure that competent personnel were always available to support IT functions.

**Non-integration of the WPMS with TALLY accounting software**

The Company could not dispense with the practice of processing manual bills as it was not able to fully integrate the software with the TALLY accounting software used in Accounts Department. The efforts made for integration which would enable passing of Bills in a seamless manner and obviate data entry at different levels to ensure accuracy were not successful due to technical problems and deficiencies in implementation like non-incorporation of essential features, incomplete data capture *etc.*, which affected the accuracy / reliability of the database.

**e-Measurement book (e-MB)**

An e-MB was planned to be designed into WPMS to automate the monitoring process further. The plan was for WPMS to pick up the work details directly

from e-MB, avoid duplication of data entry and facilitate correct and timely generation of e-bills. We observed that the e-MB as envisaged to be implemented had design deficiencies – If the rates of items in the works contracts were to be amended, the full file had to be downloaded every time for amendments and uploaded again; there was no check against uploading any other text file giving room for manipulation; there was no log or record of the changes effected by the Company in respect of the rates or quantities of the works contracts, etc. We are of the opinion that unless the e-MB is automatically linked to the bills and controls and exceptions are built into the system it will be no better than the existing manual measurement book in terms of speed, efficiency and accountability. The Company stated (July 2010) that the necessary changes would be proposed after stabilization of the system.

### ***Ineffective monitoring of projects***

**3.14.2** Deficiencies arising out of lack of input and processing controls made the system incapable of generation of meaningful data for monitoring. Non-standardisation of time allotted for various tasks, improper / incorrect usage of the system, delay / failure in updating data and non-utilisation of monitoring tools and failure to input vital parameters which could serve as benchmarks for control, seriously affected the utility of the system leading to ineffective monitoring.

We observed that the Company has not formulated any guidelines or a framework based on which the time designated to the various tasks in the projects could be estimated and accordingly fed into the database for monitoring against timelines. Instances where the time fixed for ‘Supplying and Fixing LT cast iron pot heads’ ranged from 9 days to 252 days, the time allotted to complete the task of water supply and sewerage ranged between 0 and 2,576 days were noticed in analysis of the records. We are of the opinion that in the absence of a laid down framework by the Company based on time tested standardized task completion norms it would be difficult to enforce and monitor projects overshooting time frame allotted and secure Company’s financial interests.

### **Grant of extension of time and calculation of time overrun**

A review of the projects of the Company implemented by Bangalore Urban and Bangalore Rural Divisions revealed that extension of time (EOT) was sought by contractors after completion of projects and granted by the Company. In some cases, though the contractor had sought extension while the project was in progress, extension was given by the Company only after the completion of the project. It was seen that EOT of more than 100 days had been granted in many cases after completion of work and in one case it was 1,262 days. EOT was not handled through the system. As a result, the WBPMS could not be utilised for controlling delays. In the absence of reports to list projects where EOT had been granted, levy of penalties were watched offline. It was stated (August 2010) that Site Engineers have now been instructed to use WBPMS for monitoring EOT.

A report on time overrun is available in the system. Time overrun is to be calculated as the difference between the estimated end date and the actual end

date for completed projects where the actual end date is beyond the estimated end date. For ongoing projects, time overrun should be displayed only where the current date is beyond the estimated end date. Time overrun should be calculated as the period between current date and the estimated end date in such cases.

It was however seen that time overrun was calculated in all cases as the difference between the estimated end date and current date. Such mistakes made monitoring unrealistic and also affected the correctness of the project database.

These details when submitted for managerial information would affect the monitoring of works on a continuous basis which was essential to control time and cost overruns.

### ***Ineffective monitoring of payments***

**3.14.3** Absence of input and validation controls resulted in incomplete / incorrect data capture. Again, failure to streamline procedure for processing of bills and incorrect incorporation of parameters resulted in lack of validation controls. As a result, the WBPMS could not be utilised efficiently for monitoring of payments.

#### **Payments / issue of cheques**

We observed that the details of payments made by cheques were not captured properly in the system to ensure integrity and accuracy of the database. It was found that input and validation controls were totally absent making the payment database incomplete and unreliable. In instances even the basic detail of cheque numbers for payment to contractors bills were not captured. Also, the system did not capture the RA bill numbers for which payments had been released against the cheques issued thereby making it difficult for monitoring.

Incorrect generation of e-bills and consequent inability to use the facility for making payments in a transparent manner defeated one of the major objectives of the WBPMS.

### ***Defective database***

**3.14.4** There were inconsistencies in the data captured in various databases relating to projects, payments and contractors due to lack of validation controls. The databases were incomplete, contained incorrect data and the corrections made in the manual bills and records were not incorporated. The incorrect and unreliable databases seriously affected the utility of the WBPMS and resulted in perpetuation of the manual systems and records. It also indicated that the users at different levels did not have the capacity to use the WBPMS properly.

#### **Incomplete Project database**

The status of the projects (proposed, ongoing or completed) formed a very important data component in the WBPMS. Instead of obtaining the status automatically through the system, based on the completion dates, the Engineers in divisions manually entered the status. If the Engineers failed to change the



status to “completed”, the project continued to be shown as an ‘ongoing’ project. Even where projects have been completed, the actual date of completion and time taken for execution was not available in several cases as some of the engineers did not update the status promptly.

The failure in prompt updating of progress data would curtail the ability of the WBPMS to generate alerts which were required for controlling the projects.

#### *e-commerce*

**3.14.5** The Company created a e-commerce facility for the contractors to procure construction material through internet directly from the producers to be delivered to the work sites, ‘mystore.kspnc.org’ in July 2007. The portal linked the Company, the vendors and the contractors with the intention of simplifying procurement and reducing cost. It was seen that the portal had not found favour with the vendors as well as the contractors as only 35 registered vendors and about 50-60 contractors out of about 140 who executed works for the Company had used the portal since inception.

#### *Under-utilisation of the WBPMS*

**3.14.6** One of the major reasons for the inability of the Management to replace the manual systems even after seven years of implementation of the WBPMS was the lack of knowledge and unwillingness on the part of the users to use the system. It was seen that even the existing features of the WBPMS were not utilised to have better control over processes. We noticed the existing facility of Payment and recovery of mobilization advance, receipt and refund of security deposits were not used.

These matters were reported to the Government / Management (September 2010); their replies were awaited.

### **Follow-up action on Audit Reports**

#### *3.15 Explanatory notes outstanding*

**3.15.1** The Comptroller and Auditor General of India’s Audit Reports represent culmination of the process of scrutiny starting with initial inspection of accounts and records maintained in various offices and departments of the Government. It is, therefore, necessary that they elicit appropriate and timely response from the executive. Finance Department, Government of Karnataka issued instructions (January 1974) to all Administrative Departments to submit explanatory notes indicating a corrective / remedial action taken or proposed to be taken on paragraphs and reviews included in the Audit Reports within three months of their presentation to the Legislature, without waiting for any notice or call from the Committee on Public Undertakings (COPU).

Audit Reports for the years 2004-05 to 2008-09 were presented to the State Legislature between March 2006 and March 2010. Fifteen departments, which were commented upon, did not submit explanatory notes on 66 out of 145 paragraphs / reviews as on September 2010, as indicated below:

Year of the Audit Report (Commercial)	Total paragraphs and reviews in Audit Report	No. of paragraphs and reviews for which explanatory notes were not received
2004-05	25	5
2005-06	31	10
2006-07	36	15
2007-08	27	15
2008-09	26	21
<b>Total</b>	<b>145</b>	<b>66</b>

Department wise analysis is given below:

Name of the department	2004-05	2005-06	2006-07	2007-08	2008-09
Commerce and Industries	4	1	6	3	5
Energy		5	6	7	6
Water Resources			1		1
Forest					
Home					
Social Welfare	1			1	
Finance				2	
Co-operation		2			1
Information technology		2			
Public works			2	2	
Animal Husbandry					
Transport					2
Woman and Child Development					2
Rural Development and Panchayat Raj					1
Urban Development					1
General					2
<b>Total</b>	<b>5</b>	<b>10</b>	<b>15</b>	<b>15</b>	<b>21</b>

***Outstanding compliance with reports of Committee on Public Undertakings (COPU)***

**3.15.2** As per the instructions, the compliance (Action Taken Notes-ATN / Action Taken Report - ATR) with recommendations of COPU was required to be furnished within six months of placement of the Report in the Legislature. Replies to Eleven Reports of the COPU containing recommendations to 88 paragraphs, presented to the State Legislature between February 2004 and March 2010, had not been received as on September 2010, as indicated below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where replies not received
2003-04	1	2
2005-06	4	27
2006-07	2	4
2007-08	1	20
2009-10	3	35
<b>Total</b>	<b>11</b>	<b>88</b>

**3.16 Response to Inspection reports, Draft paragraphs and Reviews**

Audit observations noticed during audit and not settled on the spot are communicated to the head of PSUs and concerned departments of State

Government through Inspection reports. The heads of PSUs are required to furnish replies to the Inspection reports through respective heads of departments within a period of one month. Department wise break-up of Inspection reports and audit observations outstanding as on 31 March 2010 is given in **Annexure 14**.

Similarly, draft paragraphs and reviews on the working of Public Sector Undertakings are forwarded to the Principal Secretary / Secretary of the Administrative Department concerned demi-officially, seeking confirmation of facts and figures and their comments thereon within a period of six weeks. All the reviews have been discussed in the exit conference with the Government. It was, however, observed that one review and 11 paragraphs forwarded to the various departments during May 2010 to September 2010 as detailed in **Annexure 15**, had not been replied so far (September 2010). The views of Government / Department have been taken into consideration while finalising the reviews / paragraphs wherever replies have been received.

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

**BANGALORE**  
The

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Principal Accountant General  
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**COUNTERSIGNED**

**NEW DELHI**  
The

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Comptroller and Auditor General of India