CHAPTER IV

4 TRANSACTION AUDIT OBSERVATIONS

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

GOVERNMENT COMPANIES

The Kerala State Cashew Development Corporation Limited

4.1 Avoidable loss

Hasty decision to import raw cashew nuts at exorbitant cost resulted in loss of Rs.9.76 crore.

Based on the report of the Managing Director that the pending supplies of raw cashew nuts would be sufficient to meet the processing requirement only up to May 2005, the Company invited (April 2005) tenders for import of 5000 MT of raw nuts of new crops from various origins except Nigeria. Agreement for supply of 6000 MT (± 10 *per cent*) of raw cashew nuts of Guinea Bissau origin was entered into (29 April 2005) with the authorised representative of Nomanbhoy & Sons Pte Limited, Singapore at the rate of US $1220 per MT (Rs.53314 at the exchange rate of Rs.43.70 per US dollar). The ordered quantity was to be supplied at port by 15 July 2005.

It was noticed by Audit that the estimated break-even cost[*] for the raw cashew nuts as worked out (April 2005) by the Company prior to acceptance of tender was US $ 1042.65 per MT (equivalent to Rs.45563). Thus, the Company resorted to import even after knowing that there would be a projected cash loss of Rs.4.65 crore (Rs.53314 – Rs.45563 = Rs.7751 x 6000MT) in the transaction. Even the above loss was wrongly computed by reckoning commission payable on sales as revenue leading to further under estimation of loss by Rs.33.48 lakh (US $ 1042.65 – 1029.88 x Rs.43.70 x 6000 MT).

The cargo intended for processing in July 2005 as per import decision, arrived (July 2005) at the port and was cleared on 09 August 2005. A quantity of 6349.855 MT was received and payment of Rs.33.66 crore was made (August to October 2005). The landed cost of raw cashew nuts was Rs.34.25 crore including C&F charges, interest levied, etc. The raw nuts hastily imported at exorbitant cost on the ground of projected non-availability of raw nuts for processing after May 2005, could actually be processed during the period August to October 2005. For processing the raw nuts and production of kernels, the Company incurred further expenditure of Rs.7.94 crore raising the total cost of the final product to Rs.42.19 crore against which the value realised on sale was Rs.32.43 crore. Thus, the total loss including processing cost amounted to Rs.9.76 crore as against

[*] Worked out on the basis of estimated sales realisation.

Rs.4.65 crore initially estimated. The sales realisation was less than even the raw material cost.

Thus, the hasty decision to import raw cashew nuts at exorbitant cost resulted in loss of Rs.9.76 crore.

The Management stated (April 2006) that the deal was made with the bonafide intention to restart the closed factories and to give employment to the workers, and if the management had not entered into the contract, closure of factories would have continued and the Government would not allow such a situation. The reply is not tenable since this aspect was not considered, as seen from the records, at the time of taking decision for procurement and the purchase was made even after estimating huge processing loss and the import of raw nuts prior to and after the contract in April 2005 were also made at much lower prices*. The processing of raw nuts hastily imported by indicating the requirement for May 2005 which were only processed in August 2005 defeated the purpose of the import.

The Government stated (July 2006) that the Company would not get raw nuts at the 'workability' rates and it could only purchase raw nuts at minimum rates offered by the parties in tender/negotiation. The sale of kernels at reduced rate subsequently was attributed to fall in price of kernel from 2.55/lb to 1.89/lb in the international market. The reply is not acceptable since the Company resorted to procurement even after projecting a loss of Rs.4.65 crore in the workability statement and incurred a heavy loss of Rs.9.76 crore due to sale of kernels at reduced rates. The fall in selling price and resultant reduction in export realization was due to delay in processing of raw nuts.

Oil Palm India Limited

4.2 Loss of Revenue

Non-incorporation of suitable provision in the tender to safeguard the Company's interest in respect of delayed payment and lifting of goods by customers resulted in revenue loss of Rs.43.06 lakh.

The Company had been engaged in the production and sale of crude palm oil and other palm oil products, the prices of which were subject to periodical revision. The tender conditions for sale of products provided that the successful bidder selected on the basis of tenders shall be issued a sale letter/confirmation of tender specifying the quantity to be sold and price applicable. The successful bidder had to pay in advance the full price of materials with other levies immediately on receipt of the confirmation from the Company and arrange to lift the tendered quantity within 7 days of receipt of the confirmation.

It was noticed in audit that neither the tender document nor the letter of confirmation of tender contained any provision to make good the probable revenue loss due to price fluctuation in the event of unreasonable delay on the part of customers in making the payment and lifting of materials. Even though

* prevalent rate for import in July 2005 was US $ 970 per MT

the payment was to be made in advance as stipulated in the tender, it was observed that in actual practice it was made only at the time of lifting the goods from the Company. In 34 out of 88 tenders during the period 2002-2005 the customers took time ranging from two weeks to six months for lifting the goods and making payment. The Company was also not charging the revised prices in respect of bidders who delayed the lifting of materials. In 16 out of the 34 cases mentioned above the revenue loss due to non-application of revised prices to customers who delayed lifting of materials during the three years ended 31 March 2006 worked out to Rs.43.06 lakh.

The Management stated (June 2006) that for receiving confirmation and arranging for advance payment and transport, the customers required more than ten days. Hence removal of stock cannot be enforced within seven days of confirmation.

The reply is not tenable since customers should not be allowed undue benefit at the cost of the Company by taking delivery of materials during periods when the Company could have made higher realisation. Further, in Plantation Corporation of Kerala Limited, another State PSU, where the market price was under wide fluctuations, a protective clause to add increase in lot price had been included in the contracts.

Thus, non-incorporation of suitable provision in the tender to safeguard the interest of the Company in respect of delayed payment and lifting of goods by customers resulted in revenue loss of Rs.43.06 lakh.

The matter was reported to the Government/Company in June 2006; their reply is awaited (August 2006).

The Travancore Cochin Chemicals Limited

4.3 Wasteful expenditure

Decision of the Company to entrust the recoating of cathode meshes to a firm having no experience in the work resulted in wasteful expenditure of Rs.38.60 lakh

The Company had been engaged in the production of caustic soda and chlorine in their Membrane Cell Plant since May 1997. The anode and cathode meshes used in the membrane cells had a life of six years and were due (June 2003) for replacement. In this regard, the Company had the option of either replacing or recoating the meshes. The original supplier of the plant, however, recommended (November 2002) for replacement only. In spite of the recommendation of the supplier, the Company considered the recoating as more economical. Instead of inviting tenders the Company made enquiries (October 2002) with an Italian firm Denora Elettrodi Spa (Denora) for recoating of cathodes and awarded (February 2003) the work for recoating of 516 cathodes at $917 per mesh. It was noticed that Denora did not have previous experience in recoating of cathodes. One cathode handed over to the firm on a trial basis was also not received back and tested at Company's plant before issuing the final work order. The first lot of 65 meshes was received back (June 2003) after recoating and payment of Rs.28.07 lakh was made.

As per the terms of the work order, the recoated meshes shall be guaranteed for satisfactory performance for a minimum period of six years and in the event of failure within the guarantee period, the firm shall provide compensation in the form of free recoating of deactivated meshes. The recoated meshes, however, did not yield the desired result after installation (August 2003) and recoating was declared (August 2003) as failure.

The Company returned (October 2003) two numbers of cathode meshes to Denora for analysing the causes of failure. Since no response was received the Company cancelled (December 2004) the work order without any financial obligation on the part of Denora. The bank guarantee provided by Denora for Rs.2.80 lakh was also not invoked. The total wasteful expenditure incurred by the Company on recoating worked out to Rs.38.60 lakh including freight, duties, etc.

Thus, the decision of the Company to entrust the recoating of cathode meshes to a firm having no experience in the work resulted in wasteful expenditure of Rs.38.60 lakh.

The Management stated (April 2006) that they made a trial with Denora to develop an alternate source of supply and these type of trials were advantageous to the Company in the long run eventhough every trial does not meet with immediate savings. The reply is not acceptable since development of alternate sources should have been made only through experienced firms in the work and by allowing the product development trial by the firm on Company's plant, no useful purpose was served. The Company also did not wait for the results of the trial by installing the mesh in Company's plant, before awarding the final contract.

The matter was reported to the Government (June 2006); their reply is awaited (August 2006).

The Kerala Minerals and Metals Limited

4.4 Avoidable expenditure

Decision of the Company to continue the purchase of bags at higher rates from a supplier who had defaulted resulted in avoidable expenditure of Rs.76.73 lakh.

The Company placed orders (December 2002) with Haver & Boecker, Germany (H&B) for the supply and erection of one automatic product packaging machine named "INTEGRA 2W". The machine was procured in August 2003 and was commissioned in November 2003. With a view to meet the requirement of special type of bags used in the machine, the Company, instead of inviting open tenders, made enquiries (9 June 2003) with two German firms viz., Bischof Sklein (Bischof) and Dy-pack Verpackungen (Dy-pack) on the ground that they were the suppliers recommended by H&B.

The offer of the firm M/s. Dy-pack at Rs.31.53 and Rs.28.81 for RC 813 grade and other grades respectively was found technically acceptable and a "one year" contract (July 2003) was concluded for 60,000 bags of RC 813 grade and 16,00,000 bags of other grades. As per the contract, the delivery was to be made in four quarters with an approximate quantity of 4,15,000 bags in each quarter commencing from second week of September 2003. In case the supplier failed to supply the bags as per the delivery schedule, the Company reserved the right to cancel the contract and make alternate purchase at the risk and cost (clause 2) of the supplier. Dy-pack, however, defaulted on the delivery schedule from second quarter onwards and supplied only 57,990 numbers of RC 813 grade and 8,27,060 numbers of other grades (comprising RC 822, RC 808 and RC 800 PG) by the end of the stipulated delivery period (August 2004).

The Company thereupon floated tenders in August 2004 and the lowest quoted rates per bag were Rs.18.77 (RC 808/822 grade), Rs.18.47 (RC 800 PG grade) and Rs.19.92 (RC 813 grade) respectively. Ignoring this significant fall in the rates by Rs.10.04, Rs.10.34 and Rs.11.62 per bag when compared to the procurement prices of July 2003, the Company, instead of invoking the provision of short closing the contract and cancelling the orders with Dy-pack, continued to procure bags at the higher rates till February 2005. The additional expenditure incurred on 7.12 lakh bags procured from Dy-pack during September 2004 to February 2005 worked out to Rs.76.73 lakh.

Thus, the decision of the Company to continue the purchase of bags at higher rates from a supplier who had defaulted resulted in avoidable expenditure of Rs.76.73 lakh.

The Management stated (July 2006) that the price bids of tender floated in August 2004 was opened in November 2004 and after opening the price bid only they could make out the difference in prices and the technical suitability of the bags was to be confirmed. It was also stated that the Company could not cancel the order issued to Dy-Pack unilaterally as it would have given rise to claim for damages.

The reply is not tenable since the tenders received in August 2004 and scheduled for opening in September 2004 were actually opened by the Company only in November 2004. The tenders, on opening, were found to be technically and commercially suitable. Hence the undue delay caused in opening the tenders cannot be a justifiable reason for not ascertaining the difference in prices in time. In terms of condition of the purchase order with Dy-Pack the order could have been cancelled without any claim for damages against the Company since they defaulted on supplies from the second scheduled quarter (October - December) onwards.

The matter was reported to the Government in May 2006; their reply is awaited (August 2006).

4.5 Avoidable extra expenditure

Unjustified decision to procure spare parts at exorbitant rates resulted in avoidable extra expenditure of Rs.27.74 lakh.

The Company engaged in the production of Rutile grade Titanium Dioxide Pigment had been procuring sealing rings (a spare part for Khosla air compressors) from Oriental Enterprises (OE) since 1999, at a basic rate of Rs.467 per unit. The Company made enquiries (April 2003) for the purchase of sealing rings and received two offers, one of which was from the regular supplier OE at Rs.467 per unit and the other one from Geekay Pneumatics (P) limited (GP) at Rs.10411 per unit. Both the firms were assessed as technically suitable; but the orders were placed (June 2003) on OE considering the substantial difference in price. In order to meet further requirements of sealing rings, the Company made (October 2003/March 2004) enquiries with the same firms and received (June 2004) per unit offer of Rs.467 and Rs.10411 from OE and GP respectively. The Company, however, placed (December 2003/September 2004) orders on GP at the exorbitant rate of Rs.10411 for 264 numbers on the ground that the firm was the authorised dealers of Khosla make air compressors. The entire material was delivered (February 2004 to March 2005) at a total cost of Rs.29.06 lakh.

In response to another enquiry made by the Company in February 2005, OE and GP quoted Rs.571 per unit and Rs.9426 per unit respectively for the sealing rings. Both the offers were found technically suitable and the committee recommended to purchase from either of the parties. Accordingly the Company placed orders with OE for 132 rings. On this occasion also OE had quoted for their own make 'orienta' spare part for which the technical approval was given.

It was observed in audit that OE had been the regular supplier of sealing rings for Company's Khosla compressors since 1999 and the technical acceptability of this material was reiterated by the purchase committee in June 2003. Disregarding the advantage in cost and without any valid reasons on record, the same purchase committee declared the spares offered by OE as technically not acceptable and approved the offer of GP which was 22 times higher. It was also noticed that subsequently (February 2005) the Company evaluated the offer of OE as technically acceptable and purchased (September 2005) 132 rings indicating that earlier technical evaluations made for rejection of their offer were not based on merit. The total avoidable extra expenditure on the purchase of 264 sealing rings, at the differential rate of Rs.10510 (Rs.11010 – Rs.500) amounted to Rs.27.74 lakh (including taxes, etc.,).

Thus, the unjustifiable decision to procure spare parts at exorbitant rates resulted in incurring of avoidable extra expenditure of Rs.27.74 lakh.

The matter was reported to the Government/Company in April 2006; their reply is awaited (August 2006).

Transformers and Electricals Kerala Limited

4.6 Avoidable extra expenditure

The Company had to procure materials at enhanced rates due to delay in intimating confirmation resulting in avoidable extra expenditure of Rs.24.54 lakh.

The Company, engaged in the manufacture of transformers and electrical equipments, received (July 2000) a work order from Kerala State Electricity Board (Board) for execution of a transmission project on turnkey basis. The work was to be completed in all respects by July 2001.

In order to meet the requirement of the above project the Company placed orders (November 2003) for purchase of 332.5 MT of GI structures with Ferro Galva Industries, Nagpur (FGI) at an ex-works rate of Rs.31000 per MT. As per terms of delivery, the supply of 148 MT of tower structure was to be completed on or before 15 March 2004 and for the balance quantity the Company was to inform the delivery date later. Before the issue of purchase order FGI had intimated (November 2003) the Company that the balance quantity of 183 MTs would be supplied at the contract rates subject to written confirmation before the end of February 2004 and agreement to take supply in April/May 2004.

The Company, however, did not intimate the delivery schedule for the balance quantity to FGI by February 2004 as stipulated. Consequently FGI expressed its inability to supply the balance quantity at the agreed rate of Rs.31000 per MT.

Subsequently, for completion of the work of KSEB, the Company made (July 2004) direct negotiation with FGI and placed orders (July 2004) for 641 MTs at an enhanced price of Rs.42000 per MT. The entire quantity (including the balance 183 MT as per earlier orders) was supplied at the revised rate. The extra expenditure on procurement of 183 MT worked out to Rs.24.54 lakh [183 MT (Rs.50807 – 37398)] including taxes and duties.

Thus, due to delay in intimating the delivery schedule for the balance quantity as per the firm's offer, the Company had to procure materials at enhanced rates resulting in avoidable extra expenditure of Rs.24.54 lakh.

The Management stated (March 2006) that due to the financial difficulty faced by the Company, the first priority of available funds was given to current factory production with intention to meet the delivery commitments for avoiding the incidence of liquidated damages. It was also stated that as there was less pressure from KSEB to complete the work, it was considered prudent to slow down the project work. The reply is not acceptable since the KSEB project work, awarded in July 2000, was due for completion by July 2001 and KSEB had withheld an amount of Rs.92.24 lakh towards liquidated damages. The Company could have intimated a staggered delivery schedule in February 2004 itself as agreed to by the supplier and avoided payment of enhanced rates.

The matter was reported to Government in May 2006; their reply is awaited (August 2006).

4.7 Avoidable extra expenditure

Failure of the Company to submit tenders after careful scrutiny of technical specifications resulted in avoidable additional expenditure of Rs.18.53 lakh.

The Company, engaged in the manufacture of transformers, obtained (August 2000) a work order from Kerala State Electricity Board (Board) for the construction of 33/11 KV substations at Varappuzha and Vadakkekara for a total contract price of Rs.4 crore. The scope of work included supply, installation and commissioning of autorecloser with sectionalisers. The technical specifications which formed part of the bid and contract stipulated that the number of units required was 27 autoreclosers and 81 sectionalisers, though the quantity to be supplied as per the price schedule mentioned "8 sets of 11 KV autorecloser with sectionaliser complete set as per specification".

The Company, however, wrongly presumed that one set comprised of one autorecloser and one sectionaliser and accordingly quoted Rs.41.56 lakh for eight sets as against one autorecloser and three sectionalisers mentioned in the technical specification. The mistake was noticed only when the Board clarified (October 2001) the position. The Board thereupon insisted on the supply of eight autoreclosers and 24 sectionalisers at the rates initially quoted by the Company. Consequently the Company had to procure (August 2005) 16 additional sectionalisers valuing Rs.18.53 lakh at its own cost.

Thus, the Company's failure to submit tenders after careful scrutiny of technical specifications resulted in avoidable additional expenditure of Rs.18.53 lakh.

The Management stated (June 2006) that technical specification is only a guidance for specification of equipment and the quantity of items to be supplied was as per the price schedule in which the actual requirement was for eight sets. It was also stated that from technical point of view, the autorecloser could have any number of sectionalisers or no sectionaliser at all, which varies from case to case. The reply is not tenable in view of the fact that 27 Autoreclosers and 81 sectionalisers mentioned in the technical specification indicated a ratio of 1:3 per set and also the Company did not seek any clarification from the Board before submission of quotations.

The matter was reported to Government in June 2006; their reply is awaited (August 2006).

Kerala Feeds Limited

4.8 Avoidable extra expenditure

Injudicious decision to purchase wheat at a higher price despite availability of its substitute maize at cheaper rates resulted in avoidable extra expenditure of Rs.15.56 lakh.

The Company, which is engaged in the production of cattle feed, uses Maize, Jowar or Wheat as raw material considering the cost factor. The Company had been following the practice of procuring live stock grade wheat, which was acceptable to the Company as per their quality parameters, from Food Corporation of India (FCI), whenever it was available. In the case of wheat the price of good quality wheat was normally higher than that of its substitute ingredients.

During the year 2004-05 the Company purchased 1902.675 MT of C&D grade wheat from FCI at a landed cost of Rs.7317.77 per MT. This grade of wheat was actually intended for human consumption as per FCI norms. It was noticed that at the time of deciding (13 April 2004) on purchase of higher quality wheat, the substitute material, 'maize', was available at Rs.6500 per MT. There was also a stock of 178.434 MT of maize in hand and thereafter the daily stock ranged between 173.195 MT and 906.522 MT during the month of April 2004 against the average daily requirement of 51.05 MT. Supply of 1205 MT of maize was also pending against earlier orders on that date. In view of the very high level of stock of maize, the purchase of good quality wheat at a higher price was not justifiable since there was no intention to make any value addition to fetch enhanced prices from the market.

Thus, the injudicious decision of the Company to purchase high quality wheat at a higher price even when substitute maize was available at cheaper rates, resulted in avoidable extra expenditure of Rs.15.56 lakh* .

The Government stated (July 2006) that the Company was in continuous efforts to improve the quality of the output by using wheat, with the only difference that the quality used in this purchase was a better one involving higher cost. The reply is not acceptable since the Company required only live stock grade wheat and the same was being purchased from FCI. The Company by purchasing good quality wheat intended for human consumption at exorbitant price as a one time measure, could only add to the cost without any increase in selling price. Since the Company had not purchased any further quantity of higher grade wheat the contention regarding improvement in quality of out put cannot be accepted.

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* 1902.67 MT X Rs.817.77 per MT (Rs.7317.77-Rs.6500)

Kerala State Industrial Enterprises Limited

4.9 Wrong fixation of tariff

Due to wrong fixation of tariff in respect of a particular category of customers, the Company suffered a loss of Rs.16.43 lakh.

As a part of its Air cargo operations the Company has been collecting and warehousing import/export cargo. The tariff applicable for warehousing import cargo (U/B)* was being revised from time to time and the latest revision was effective from July 2001. The revised (July 2001) tariff prescribed minimum charge of Rs.100 per package up to 50 Kg and Rs.40 for every additional 50 Kg or part thereof for the first week (one to seven days). For storage beyond seven days the tariff orders specified levy of warehousing charges from the date of arrival of the cargo, except in the case of customers warehousing cargo for the period from seven to 14 days, in which case the charges were specified only from the seventh day of arrival of the cargo.

It was noticed in audit that due to the above anomaly in tariff fixation, the Company had not been levying the prescribed tariff of 40 paise per kg. per day for the first seven days in the case of customers who warehoused the cargo for the second week of eight to 14 days. Due to wrong fixation of tariff by the Company, customers of this particular category were enjoying undue benefit of free storage facility for the first week of storage since the charges were limited to the second week alone. In respect of 7433 invoices raised against the above category of customers during the period from January 2004 to March 2006 the benefit allowed worked out to Rs.16.43 lakh.

Thus, wrong fixation of tariff by the Company in respect of a particular category of customers resulted in avoidable loss of Rs.16.43 lakh.

The Government stated (July 2006) that the rates were applicable to U/B which were predominantly personal in nature and the Company's intention was only to have expeditious clearance and not to make huge profit. The reply is not tenable since the tariff fixed is not equitable and allowed concessional minimum tariff for periods beyond seven days whereby the objective of expeditious clearance of cargo would also not be achieved. The anomaly is a result of defective tariff structuring.

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* Unaccompanied baggage

Kerala Police Housing and Construction Corporation Limited

4.10 Avoidable financing cost

Delay in taking decision on the offer of HUDCO for taking over existing loans at reduced interest rates resulted in avoidable financing cost of Rs.15.60 lakh.

The Company undertakes construction of buildings for Government of Kerala on ‘no profit no loss basis’. It had been availing loans from Housing and Urban Development Corporation (HUDCO) and other financial institutions. Such loans were guaranteed by the State Government and the Company was exempted (May 1993) from payment of guarantee commission until the exemption was revoked (October 2004) in pursuance of the Kerala Ceiling on Government Guarantees Act, 2003. The Company availed loans (1999) of Rs.6.82 crore and Rs.50 lakh from LIC Housing Finance Limited (LHFL) bearing an interest rate of 11 *per cent* per annum.

The Company received (April 2004) an offer from HUDCO stating their willingness to take over other loans of the Company at a reduced interest rate of 8.75 *per cent* per annum. The Board of Directors of the Company, however, took nearly a year to decide (March 2005) to permit HUDCO to take over the two loans. The Government approval for transferring the Government guarantee in favour of HUDCO was sought for in April 2005. The approval was not granted since the company had to remit the outstanding guarantee commission consequent to the revocation (October 2004) of exemption. If the company had acted upon HUDCO’s offer in time when the exemption from payment of guarantee commission was available (April to October 2004) necessary transfer of guarantee would have materialised and financing cost would have reduced by 2.25 *per cent* per annum during September 2004 (being the quarter immediately succeeding the one in which the offer was received) to March 2006.

Thus, delay on the part of the Company in acting upon the offer of HUDCO for taking over existing loans at reduced interest rates resulted in avoidable financing cost of Rs.15.60 lakh (up to March 2006).

The matter was reported to the Government/Company in April 2006; their reply is awaited (August 2006).

Kerala Garments Limited

4.11 Avoidable loss

Injudicious decision of the Company to produce readymade garments without confirmed orders resulted in avoidable loss of Rs.24.38 lakh.

The Company, engaged in the manufacture of readymade garments and having an accumulated loss of Rs.2.45 crore as on 31 March 1999, was implementing a revival-cum modernisation project at a cost of Rs.1.67 crore with funds from Kerala Industrial Revitalisation Fund Board (KIRFB). As per the revival package, the Company intended to produce readymade garments on its own. The Company simultaneously entered (August 1999) into a Memorandum of Understanding (MOU) with Eagle Stationery Est., UAE (ESE) under which the former had to manufacture 'Hanstyle' readymade shirts for marketing by ESE in the Gulf countries. The MOU was for a period of one year from the date of execution (August 1999) and renewal was to be decided on mutual consent. Stipulations as to the quantity to be produced, price, schedules of delivery, etc., were neither incorporated in the MOU nor confirmed through a valid contract. Audit noticed that the MOU itself did not contain the official seal of the firm and the document also did not bear the signatures of witnesses. Thus, the MOU would not serve the purpose of a legally binding document.

Relying on the MOU, the Company utilised the spare capacity and produced 29,129 shirts during the period from December 1999 to March 2001. The stock of the shirts was kept ready expecting that ESE would lift atleast 5000 shirts per month. The Company, however, did not receive any order from ESE.

Subsequently ESE backed out from the MOU on account of the marketing difficulties in the Gulf region. As a result, the Company had no option but to sell the shirts in the domestic market. The Company, however, could not dispose of the entire quantity and stock worth Rs.48.76 lakh was lying unsold until September 2006. Considering the degree of deterioration in stock the value was discounted by 50 *per cent* and the net value worked out to Rs.24.38 lakh.

Thus, the injudicious decision of the Company to produce readymade garments without confirmed orders resulted in avoidable loss of Rs.24.38 lakh.

The Government admitted (August 2006) that ESE, which backed out from the MOU, did not purchase a single shirt and they could not be sued as no formal agreement was entered into with them. It was further stated that if the stock of shirts after providing for 50 *per cent* discount could be sold for Rs.24.38 lakh there would be marginal profit. The reply is not tenable since the Company took the imprudent decision to manufacture ready made shirts without any formal agreement with ESE and the realisability of any amount for readymade garments manufactured six years back, is doubtful.

Malabar Cements Limited

4.12 Avoidable payment

Acceptance of raw-material not conforming to prescribed quality parameters resulted in avoidable payment of Rs.10.90 lakh.

The Company, engaged in the manufacture of Cement, has been using Cement Grade Lime Stone (CGLS) as a raw material. To meet the requirement of CGLS, the Company placed (July 2002) orders on five parties for supply of a total quantity of 1,20,000 MT during 2002-03 at an aggregate cost of Rs.2.55 crore. As per Clause 1 (b) of Annexure to purchase orders, if Silica content in CGLS exceeded 16 *per cent*, the material was to be rejected outright and no payment to be made towards the cost of material and transportation. The rejected material was not required to be returned to the suppliers. The quality of the material was to be determined by drawing truck-wise samples on daily average basis and the quality determined by the Company was binding on the suppliers.

It was noticed by Audit that out of 34,673.62 MT of the material delivered (May 2003) against the order, 2383.93 MT was received with Silica content exceeding 16 *per cent*. In contravention of the terms of the purchase order, the Company accepted the materials and paid an amount of Rs.10.90 lakh worked out on the basis of landed cost of Rs.457.33 per MT.

The Company stated (July 2006) that eventhough the quality of materials supplied was tested truck-wise on daily average basis at the Company's laboratory, weighted average of 15 days supply has been considered for the purpose of making payment. The contention of the Company is not acceptable since the purchase order conditions specifically mentioned that the quality of material was to be determined on daily average basis and not on fortnightly basis as applied by the Company.

Thus, the acceptance of raw-material not conforming to prescribed quality parameters resulted in avoidable payment of Rs.10.90 lakh.

The matter was reported to the Government in July 2006; their reply has not been received (August 2006).

STATUTORY CORPORATIONS

Kerala State Electricity Board

4.13 Undue tariff concessions

Failure of the Board to apply the correct tariff classification resulted in allowing undue tariff concessions amounting to Rs.20.49 crore to a private consumer.

Under Section 46 of the Electricity (Supply) Act 1948, the Board had been permitting licensees to distribute power to the General Public and separate Grid tariff was being fixed for such licensees. Tata Tea Limited (TATA) was one such distributor licensee in the Munnar area. As per separate Grid Tariff orders issued (May 1999 and August 2001) as approved by the Government, the 11 KV licensees/sanction holders who consume more than 50 *per cent* of the total energy themselves would not have the advantage of grid tariff. Normal HT I industrial (HT I) rates would be applied in such cases for the entire consumption as well as the maximum demand.

The Board further modified (April 2003) the tariff classifying the licensees in two categories i.e. G1 and G2. The licensees consuming less than 50 *per cent* of total energy themselves fall under G1 category and others under G2 category. The G1 and G2 category licensees were allowed concession of 30 and 10 *per cent* respectively over the normal tariff applicable to HTI consumers. This concessional rate was effective from October 2002.

Audit scrutiny revealed that TATA was a licensee having own consumption of energy above 50 *per cent* of that delivered by the Board and hence to be charged at the then prevailing HT I rate upto the introduction of separate Grid tariff rates in October 2002 and as per tariff applicable for G2 category with effect from October 2002. ***The Special Officer (Revenue) of the Board, however, ignored this fact and the licensee was billed at concessional grid tariff rates, reckoning own consumption of energy below 50 per cent for the period from September 1999 to November 2005.*** The actual billing amounted to Rs.53.46 crore against the aggregate amount of Rs.73.95 crore to be billed on the basis of HT I tariff classification.

Thus, the failure of the Board to apply the correct tariff classification resulted in allowing undue tariff concessions amounting to Rs.20.49 crore to a consumer.

The matter was reported to the Government/Board in May 2006; their reply is awaited (August 2006).

4.14 Undue benefit

Granting of rebate in contravention of the provisions of the agreement and in violation of the formula prescribed for maximum demand relief resulted in extending undue benefit of Rs.1.12 crore to a private party.

As a part of the Government decision (December 1989) to allow private captive hydel generation of power, the Board entered into (December 1994) an agreement with Indsil Electrosmelts Limited (IEL), a private entrepreneur, for the generation of power at Kuthungal hydro Project in Idukki district. The project was commissioned by IEL in June 2001. The monthly energy generated from the project and fed into the Board's grid was to be metered and the Board had to deliver this energy less 12 *per cent* towards wheeling charges and transmission and distribution loss, free of cost to IEL and its nominated associate. By virtue of the contribution of the power into the Board's grid, the Board should grant relief in maximum demand to IEL as per the prescribed formula under clause 14(a) of the agreement.

As per the formula the relief had to be worked out by taking 30 days as base for all the months and the number of days to be reckoned for granting relief should not include the days on which generation of power could not be made by IEL due to unavoidable reasons. Further, if there was no generation continuously for a period exceeding 15 days, no relief in maximum demand should be granted.

It was noticed in audit that IEL had not generated power continuously for 27 days each in March and April 2005 and the actual production was for four days and three days respectively. ***The Special Officer (Revenue) of the Board, however, deviated from the above contractual provisions relating to continuous non-generation for a period exceeding 15 days and extended ineligible maximum demand relief for 5368 and 5355 KVA respectively during these months.*** The undue benefit extended to IEL on this account worked out to Rs.27.88 lakh.

It was further noticed that relief was extended to the generating Company on maximum demand of 0.32 lakh KVA due to reckoning the maximum number of days in the month as actual generating days instead of 30 days prescribed as base in the formula included under the agreement. The excessive relief granted on account of this for non-generating days at Rs.260 per KVA (as per latest tariff revision of October 2002) for the period from December 2002 to June 2005 worked out to Rs.83.90 lakh.

Thus, granting of rebate in contravention of the provisions of the agreement and in violation of the formula prescribed for maximum demand relief resulted in extending of undue benefit of Rs.1.12 crore to a private party.

The matter was reported to the Government/Board in May 2006; their reply is awaited (August 2006).

4.15 Undue benefit

The Board failed to invoke reduction in prices on belated supplies and also refunded the liquidated damages levied in terms of the contract which resulted in undue benefit of Rs.1.06 crore to the supplier.

In order to meet the urgent requirement of energy meters to be used in distribution of power, the Board placed (31 March 2003) four purchase orders for supply of five lakh single phase static energy meters on four suppliers including Omni Agate Systems (P) Limited (OAS), Chennai, who was to supply 1.5 lakh meters at the rate of Rs.342.41 (all inclusive) for Central Region of the Board. Fifty *per cent* quantity was to be supplied within 30 days (i.e., by 29 April 2003) and the balance within 60 days (29 May 2003) from the date of purchase order. All the firms except OAS completed the supply within the delivery period. OAS supplied 1.10 lakh meters in July 2003 and 40,000 meters in August 2003 after the expiry of the scheduled delivery period. The terms of purchase provided (Clause 28) that the price of materials supplied after the scheduled delivery period would be adjusted taking into account the market price on the date of actual supply or the order price, whichever was lower.

It was observed by Audit that in response to the subsequent tenders invited in July 2003, the offer received (1 August 2003) for the supply of meters to the Central Region was Rs.256 per meter (all inclusive). Hence 40,000 meters received during August 2003 should have been paid at the revised rate of Rs.256 per meter in terms of the contract. The Board, however, did not invoke the above provision to adjust Rs.34.56 lakh towards price variation (Rs.342.41 – Rs.256) for 40,000 meters thereby making avoidable payment to the contractor.

Further, as per clause 15 of the purchase order, non-adherence to delivery schedule attracted liquidated damages at the penal rate of five *per cent* on the value of meters supplied belatedly for every week of delay.

Despite two weeks' extension of delivery period granted by invoking the *force majeure* clause on account of a transporters' strike, the entire quantity of 1.5 lakh meters was supplied after delays ranging from 40 to 67 days. Consequently, the Board deducted (August to October 2003) an amount of Rs.1.10 crore from the supply bills towards liquidated damages.

It was noticed that one and a half years after the recovery of liquidated damages, the firm made a request (April 2005) to the Government to condone the delay on the ground that the transporters' strike had affected production even beyond the period of the strike. The Board considered the firm's request and decided (May 2005) to restrict the liquidated damages to a maximum of 10 *per cent* and refunded (July 2005) an amount of Rs.71.25 lakh out of Rs.1.10 crore already deducted.

The Board's decision lacked justification, since the other three firms on whom orders for supply of 3.50 lakh meters were placed on the same date with the same terms and conditions, had supplied the entire quantity within the delivery schedule, without any extension on account of the transporters' strike.

Thus, failure of the Board to invoke reduction in prices on belated supplies and refund of the liquidated damages levied in terms of the contract resulted in undue benefit of Rs.1.06* crore to the supplier.

The Government stated (June 2006) that the price in the subsequent fresh tender was known to the Board only after completion of the supply and therefore the meters supplied after delivery period were accepted at the ordered rate. As regards non-levy of liquidated damages without ceiling, it was stated that no loss had been noticed due to the delay in supply of meters and that there was sufficient stock of meters during the period March to August 2003.

The reply is not acceptable since the rate applicable on the date of submission of the bid on 01 August 2003 was known to the Board before making final payment against invoices, yet the prices were not re-fixed as envisaged under the contract. In the case of liquidated damages the action of the Board in re-opening the case and accepting the request of the firm and releasing LD

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* Rs.34.56 lakh + Rs.71.25 lakh

amount recovered after 1½ years of the supply contract, does not appear to be justifiable. If the Board had sufficient stock, the procurement at the higher rate of Rs.342 per meter itself could have been avoided since the subsequent rate was only Rs.256 per meter.

4.16 Misutilisation of funds

Incentive funds released by the Government of India for development of Power Sector was misutilised for payment of donation and gift resulting in non-productive expenditure of Rs.2.50 crore.

Accelerated Power Development and Reforms Programme (APDRP) of Government of India envisaged upgradation of sub-transmission and distribution system in densely electrified zones in the urban and industrial areas and improvement in commercial viability of State Electricity Boards. The guidelines issued (June 2003) by the Government of India (GOI), Ministry of Power, in this regard provided for incentive component to encourage/motivate utilities to reduce cash losses.

According to the 'Incentives Scheme', the State Government would be given incentive in the form of grant upto 50 *per cent* of the actual total loss reduction by State Electricity Boards (SEBs)/Utilities and the State Government would release the funds to the State Power utility within a week of the said amount being credited to the Government account. The year 2000-01 was stipulated to be taken as the base year for calculation of loss reduction. The grant released under incentive component was to be utilised for improvement of power sector only.

The Government of India sanctioned (2005-06) Rs.64.94 crore to the State Government under APDRP towards incentive grant for the period up to 2002-03 and the amount was received in October 2005 and March 2006.

Ignoring the specific directions contained in paragraph 7 of the guidelines for utilisation of incentive amount for improvement in power sector only, the Board accorded sanction (June 2005) to donate Rs.one crore to Malabar Cancer Society, Kannur and to give a gift of Rs.400 each to all the employees of the Board who were in service during 01 April 2002 to 30 June 2005. Payment of Rs.one crore to Malabar Cancer Society, Kannur was made (November 2005) and an aggregate amount of Rs.1.50 crore was disbursed, (September 2005) as 'gift to employees'. As per Paragraph 10 (v) of the guidelines, diverted funds would be adjusted with 10 *per cent* penal interest, against the next instalment of Central Plan assistance to be released to the State Government in that year or in the subsequent year. Based on this the diverted amount of Rs.2.50 crore was recoverable and interest payable thereon for the period from July 2005 to July 2006 worked out to Rs.27 lakh (at the rate of 10 *per cent* for 13 months on Rs.2.50 crore).

Thus, incentive funds released by the Government of India for development of power sector was misutilised for payment of donation and gift resulting in non-productive expenditure of Rs.2.50 crore.

The Government stated (May 2006) that there was no diversion of funds as the donation was to an organ under the control of the Department and the gift was given to the employees of the Board within the power sector only. The reply is not acceptable since as per the programme approved by the Government of India the grant under incentive component shall be utilised for improvement in power sector only. Neither the donation to a society nor the gift to Board employees could be considered as a utilisation for improvement of power sector.

4.17 Loss of revenue

Wrong classification of consumers as non-industrial/non-commercial under HT II category instead of as commercial consumers under HT IV, resulted in loss of revenue of Rs.2.30 crore.

The Board has been collecting electricity charges from its consumers as per tariff notification issued from time to time. As per the tariff revision orders (October 2002), the tariff applicable to commercial establishments and business houses shall be High Tension (HT- IV) Commercial.

In the above tariff orders Airports which were undertaking commercial activities were, however, classified under High Tension II (HT II) tariff applicable to non-industrial/non-commercial category. Being commercial organisations airports should have been billed under High Tension IV (HT IV) Commercial, a tariff higher than HT II. As per the tariff revision orders (October 2002) issued by the Board, the monthly contract demand charge and the unit energy charge for HT IV consumers was Rs.350 per KVA and Rs.3.20 respectively as against Rs.300 and Rs.3 respectively under HT II. The short billing in respect of the three airports in Kerala at Thiruvananthapuram, Kochi and Kozhikode, due to wrong classification under lower tariff during the period from October 2002 to June 2006 worked out to Rs.95 lakh, Rs.97.37 lakh and Rs.37.78 lakh respectively.

Thus, the wrong classification of airports as non-industrial/non-commercial under HT II category instead of as commercial consumer under HT IV, resulted in loss of revenue of Rs.2.30 crore to the Board for the period October 2002 to June 2006.

The matter was reported to the Board/Government in October 2006; their replies are awaited (October 2006).

4.18 Avoidable loss

Failure of the Board to mention the escalation cost of the Project in the schedule to the insurance policy resulted in under assessment of claim by the valuers and consequent loss of Rs.80.78 lakh.

The Board had insured (July 1988) its assets at Kakkad Hydro Electric Project (KHEP) with Kerala State Insurance Department (KSID) for Rs.18.85 crore and the policy was effective up to November 1999. A fire accident occurred (October 1992) at KHEP in which the stator bars of Unit II generator and the insulating materials were destroyed. In order to finalise the claim, the reinsurers demanded (March 2000) the completed value of the project/estimated value of the insured items at the time of the accident or on a date very close to it. The Board reported (June 2000) the equipment's original cost as Rs.1.77 crore and estimated cost as Rs.5.10 crore (in December 1992). KSID restricted the payment of total assessed loss of Rs.1.24 crore in the ratio of the original cost (Rs.1.77 crore) to the estimated cost of Rs.5.10 crore on the ground that the original cost of the equipment was under-insured by 65.39 *per cent*. The net claim assessed (November 2003) was for Rs.38.48 lakh disallowing Rs.80.78 lakh for under-insurance.

As per the general conditions of the policy (Memo No.1) any increase or decrease in the insured amount would take effect only after the same had been recorded on the policy. The sum insured actually included escalation in cost. This fact was, however, omitted to be recorded in the schedule to the policy and the amount of Rs.18.85 crore was shown as the invoice cost (including freight and erection cost) without mentioning specifically the escalation in cost eventhough this was included in the above insured sum.

The Board decided (July 2003) to accept the payment of Rs.38.48 lakh in settlement of the claim under protest and received (July 2004) the amount.

As per Clause 7 of the General conditions of the Insurance Policy the disputed claim could have been taken up with the arbitrator. The Board, however, did not take advantage of this clause.

Thus, the failure of the Board to specifically mention the escalation cost of KHEP in the schedule to the insurance policy resulted in under assessment of claim by the valuers and consequent loss of Rs.80.78 lakh.

The Government stated (August 2006) that the Board's officials were not familiar with the intricate provisions of insuring the assets as it was outside their routine work. The fact, however, remains that the ignorance of provisions of insurance of assets by employees resulted in huge loss to the Board.

4.19 Avoidable expenditure

Failure of the Board to terminate the order in time and recover the additional cost on alternate procurement of meters at the risk and cost of HPL resulted in avoidable expenditure of Rs.68.60 lakh.

The Board placed an order (11 March 2004) on HPL Socomec (P) Limited (HPL), New Delhi for the supply of 2,000 numbers of LT, CT operated 3 phase 4 wire static watt hour meter at the rate of Rs.1,874.02 per meter for a total cost of Rs.37.48 lakh. As per the terms of the Order (Clause 7), delivery of the meters was to be completed within 60 days (09 May 2004) from the date of purchase order. Clause 12 of the purchase order further provided for the Board's right to inspect and approve the meters before despatch. The Board waived (July 2004) the pre-despatch inspection and the meters supplied (10 July 2004) after two months from the stipulated date of delivery did not pass the acceptance test. There were no reason on record for waiver of the pre-despatch inspection.

It was noticed in audit that eventhough HPL did not make supply within the scheduled time, the Board did not cancel the contract for failure to supply materials in time. Further, the opportunity for procuring the meters at risk and cost from the 2nd lowest tenderer (Elektron Energy Equipments (P) Limited) at Rs.2692.36 per meter was also not availed of within the validity period (04 June 2004) of the tender. The Board finally rejected (September 2004) the entire lot. As the firm did not replace the rejected meters, the purchase order was terminated (October 2004) at the risk and cost of the firm as per clause 4 and 13 of the agreement.

The Board re-tendered (October 2004) for procurement of meters of same specification and order was placed (January 2005) on Larsen and Toubro Limited, Chennai for the supply of 3500 meters to the Distribution (Central) region at the lowest negotiated rate of Rs.5397.47 per meter for a total value of Rs.1.89 crore. The additional expenditure incurred by the Board on procurement of 2000 meters worked out to Rs.68.60 lakh after adjusting Rs.1.87 lakh recovered through bank guarantee.

The purchase order placed on HPL was cancelled on 04 October 2004 after a delay of three months from the date of supply. Only after this was pointed out (October 2005) by Audit, the claim for additional expenditure of Rs.70.47 lakh from HPL on account of the risk and cost clause was preferred (28 November 2005). HPL refused (January 2006) to bear the risk and cost on the ground that the meters rejected by the Board were perfectly alright when taken back and the Board had not intimated how the meters were defective. No legal action was initiated (April 2006) by the Board as per the terms and conditions of the contract.

Thus, the failure of the Board to terminate the order in time and recover the additional cost on alternate procurement of meters at the risk and cost of HPL resulted in avoidable expenditure of Rs.68.60 lakh.

The Government stated (August 2006) that the District Collector had been requested to initiate revenue recovery action against the firm to realise the amount of Rs.68.60 lakh.

4.20 Undue benefit

Improper decision of the Board to deviate from contractual provisions resulted in undue benefit of Rs.20.55 lakh to the supplier.

The Board placed orders (February 2004) on Capital Power Systems Limited, Noida (CPS) for supply of three lakh single phase static meters at an all inclusive rate of Rs.204 per meter. The meters were intended to meet the urgent requirement for the replacement of mechanical meters under Accelerated Power Development and Reforms Programme (APDRP). As per clause 3 of the purchase order, the price was firm and statutory variation in taxes and duties during the scheduled delivery period was to be borne by the supplier. The scheduled date of completion of delivery was 06 May 2004.

The Government of Kerala increased the entry tax from 8 *per cent* to 13.8 *per cent* with effect from 01 April 2004. Despite the contractual stipulation the Board decided (April 2004) to bear the statutory variations in taxes and levies in respect of tenders/purchase orders already issued by the Board. While issuing this order, the Board ignored the fact that the tenderers had quoted for meters taking into account the future enhancement in taxes and levies. Based on the above orders CPS was allowed the benefit of enhanced rate of entry taxes in respect of quantities supplied in April/May 2004.

It was observed in audit that the Board rejected two offers at the time of tender evaluation on the ground that the quotes mentioned variations in taxes and duties to the Board's account. Further, in May 2004, orders were placed on two Delhi based firms at Rs.204 per meter all inclusive. Ignoring this, the Board, deviating from the contractual provisions, allowed the enhancement of 5.8 *per cent* in entry tax to CPS with effect from 06 April 2004. The actual additional payment so made for 1,87,500 meters purchased during April/May 2004, worked out to Rs.20.55 lakh.

Thus, the injudicious decision of the Board to deviate from the contractual provisions and allow enhancement in taxes resulted in undue benefit of Rs.20.55 lakh to the supplier.

The Government stated (August 2006) that the clause regarding firm price with statutory variations to be borne by the supplier was included in the purchase order as a then existing common condition. Most of the suppliers had expressed their reluctance to accept the clause; the Board decided to amend the clause in April 2004. The payment of entry tax was stated to be made to CPS in accordance with the provision of this order. The reply is not acceptable since general provision of purchase amended in April 2004 was made applicable to the purchase order issued to CPS in February 2004 whereby the suppliers who had already loaded their quoted price for statutory variations were given undue benefit by way of re-imbursement of entry tax.

4.21 Avoidable expenditure

Failure of the Board to terminate the purchase order placed on NLE and negotiate with the second lowest tenderer within the validity period for procurement of the material at risk and cost resulted in avoidable expenditure of Rs.18.35 lakh.

The Board invited (November 2003) tenders for the purchase of 102.8 MT of Hot Dip Galvanised Hexagonal Heads Bolts and Nuts of various size. The validity of the offers received was four months (11 April 2004) from the date of opening (12 December 2003) of tender. Out of the six offers received the contract price of Rs.45.84 lakh offered by NL Engineers (P) Limited, Mohali (NLE) was accepted and orders were placed (17 March 2004) for 102.8 MT. The second lowest tender was that of India Steel Corporation, Kolkatta at Rs.50.01 lakh.

As per clause 12 of the general conditions of tender (March 2004) NLE had to furnish security deposit (SD) amounting to Rs.2.29 lakh and execute the agreement within 15 days from the date of receipt of purchase order. NLE neither executed the agreement nor paid the requisite deposit. Ignoring this the Board proceeded with the procurement. The materials were scheduled for supply within three months (16 June 2004) from the date of purchase order.

NLE supplied (May 2004) 36 MT of Bolt and Nuts which were rejected by the Board as the threaded portion of the Nuts was found rusted. Since the materials were neither replaced nor further supplies were made, the order was terminated (29 July 2004) at the risk and cost of NLE.

In order to supplement the requirement arising from non-supply of the material, the Board procured 37.5 MT of the material from Alsteel Industrials, Kollam for Rs.26.25 lakh in March 2005 and 65.3 MT from Spring Lock Industries, Vadodara at Rs.43.12 lakh in May 2006 at the risk and cost of NLE.

Thus, the total additional expenditure on procurement of material with reference to the price of NLE worked out to Rs.23.53 lakh. After adjusting the EMD of Rs.1.01 lakh given by NLE the actual loss worked out to Rs.22.52 lakh. As these purchases were at the risk and cost of NLE the Board lodged (December 2005) a claim for Rs.22.52 lakh on the firm. The firm refused to make payment and filed a legal suit against the Board advancing counter claim for Rs.4.77 lakh. The recovery of the claim of Rs.22.52 lakh is doubtful.

Since NLE failed to comply with the contractual provisions regarding SD and execution of agreement the procurement should have been made from the second lowest tenderer – India Steel Corporation, Kolkata, who quoted a total contract price of Rs.50.01 lakh and thereby saved Rs.19.36 lakh.

Thus, the failure of the Board to terminate the purchase order placed on NLE and procure the material from the second lowest tenderer within the validity period resulted in avoidable expenditure of Rs. 18.35 lakh (net of SD forfeited Rs.1.01 lakh)

The Government stated (August 2006) that as per orders issued (November 2001) by the Board no further negotiation with other tenderers to match with the price of the lowest tenderer should be made after opening of tenders. It was also stated that even though the firm had not executed the agreement they offered (April 2004) the first lot for inspection and hence there was no reason to believe that the firm would not execute the agreement before expiry of the firm period. The reply is not tenable since the audit observation is on the failure of the Board to procure the material from the second lowest tenderer at the quoted price of Rs.50.01 lakh invoking paragraph 23 (a) of the general conditions of tender as the NLE failed to execute the agreement; and not on negotiation and reduction in price in violation of existing orders of the Board. The offer stated to have been made by the lowest tenderer for inspection of first lot by April 2004 could not be considered as a substitute for formal agreement to be executed under the contract and furnishing of security deposit.

4.22 Short realisation of revenue

Omission on the part of the Board in applying the correct revised tariff in assessing the energy consumption of HT consumers resulted in short realisation of revenue by Rs.16.08 lakh.

As per the general tariff revision notified (May 1999) by the Board and applicable from May 1999, High Tension consumers falling under the category of cold storage and freezing units were classified under 'HT IV–Commercial'. The tariff prescribed for such consumers consisted of demand charges at the rate of Rs.230/KVA per month plus energy charges of 215 paise per unit. The tariff was revised (August 2001) to Rs.290/KVA and 265 paise per unit and further (October 2002) to Rs.350/KVA and 320 paise per unit respectively.

Audit noticed that Royal Overseas Private Limited (ROL), Aroor and Euro Marine Products Limited (EMP), Puthenthope (HT consumers) were engaged in processing/cold storage of marine products and accordingly should have been assessed under 'HT IV – Commercial'. The Board, however, while issuing the invoices for the period from May 1999 onwards to ROL omitted to apply the HT IV commercial tariffs and the billing was done on the basis of the HT I Industrial tariff. In respect of EMP, eventhough the billing was initially made (May 1999) under HT IV commercial, it was changed (September 1999) to HT I category as the consumer complained against the changes and excess billed under HT IV was adjusted against subsequent bills. The billing was later (April 2005) recommenced under HT IV from EMP. Due to short billing arising from incorrect application of tariff, there was under realisation of revenue aggregating Rs.16.08 lakh (ROL Rs.5.27 lakh and EMP Rs.10.81 lakh).

Thus, the omission on the part of the Special Officer (Revenue) in applying the correct revised tariff in assessing the energy consumption of two HT consumers resulted in short realisation of revenue of Rs.16.08 lakh.

The Government stated (June 2006) that tariff of the consumers had been changed to HT IV and revised bills were under issue.

The Board further issued (May 2006) bills for Rs.16.24 lakh (EMP – Rs.10.20 lakh and ROL – Rs.6.04 lakh). ROL has filed writ petition in the Honourable Court and based on court orders Rs.1 lakh has been remitted. EMP has not remitted the amount (September 2006).

Kerala State Road Transport Corporation

4.23 Avoidable extra expenditure

Decision to procure high value Low Floor buses without conducting any cost benefit analysis and ignoring the lower efficiency levels during trial runs resulted in avoidable extra expenditure of Rs.53.20 lakh.

The Corporation decided (March 2004) to procure Low Floor buses with a view to give a new look and added efficiency in city operation. No cost benefit analysis or performance evaluation was conducted prior to taking the decision. Accordingly, orders were placed (April 2004) with Ashok Leyland Limited (ALL) for the purchase of four Low Floor Buses at a cost of Rs.26.30 lakh per bus. The Corporation had also purchased (November 2003) chassis for ordinary Leyland buses the total cost of which including body building charges was Rs.13 lakh per bus.

At the time of deciding the procurement of Low Floor buses the Corporation did not have a definite idea regarding 'added efficiency' as the efficiency level was not assessed with reference to that of the ordinary Leyland Buses in the operating fleet. During the trial run conducted (March/April 2003) the Low Floor buses recorded a mileage of 3.05 km per litre only which was lower than that (3.62 km/litre) of ordinary Leyland buses. While the average mileage obtained for ordinary buses was 3.70 km per litre, Low floor buses could obtain only 3.42 km (August 2005). Actual performance recorded for Low Floor buses during the months of December 2005, February 2006, March 2006 and April 2006 was 3.52 km, 3.64 km, 3.56 km and 3.54 km respectively indicating the dismal performance when compared to the cost involved. In view of the heavy loss (accumulated losses were Rs.1139.93 crore as on 31 March 2003) and working capital constraints, the Corporation should have avoided procurement of high value Low Floor buses involving additional expenditure of Rs.53.20 lakh {(Rs.26.30 lakh–13 lakh) x 4}.

Thus, the Corporation's decision to procure high value Low Floor buses without conducting any cost benefit analysis and ignoring the lower efficiency level during trial runs resulted in avoidable extra expenditure of Rs.53.20 lakh.

The matter was reported to the Government/Corporation in July 2006; their replies have not been received (August 2006).

4.24 Avoidable expenditure

The decision of the Corporation to purchase bus body kits at higher rates despite availability of full bus body of same specification at a lesser cost resulted in avoidable expenditure of Rs.22 lakh.

The Corporation placed (November 2003) orders with Hi Tech Auto Craft, Alapuzha (HTA) for the purchase of 50 bus body kits for assembly and mounting on "TATA 232"wheel base chassis at a landed cost of Rs.5.54 lakh per unit. The delivery was to be effected from January 2004 to July 2005. Simultaneously, the Corporation finalised (December 2003) another contract with the same firm (HTA) for construction and supply of 50 numbers "full bus body" for the same type of chassis (TATA 232) at the unit price of Rs.5.10 lakh. Eventhough the Corporation was aware of the additional expenditure of Rs.0.44 lakh per bus body kit involved in the first purchase order it was decided (June 2004) to continue with the procurement of bus body kits from HTA on the plea of utilising the labour in their Bus body building workshop at Pappanamcode. Fifty numbers of the bus body kits were supplied (January to November 2004) and payments made at higher rates (January 2004 to July 2005). The additional expenditure on purchase of 50 bus body kits worked out to Rs.22 lakh.

Thus, the decision of the Corporation to purchase bus body kits at higher rates when the construction of bus body itself was possible at a lesser cost resulted in avoidable expenditure of Rs.22 lakh.

The Management while admitting the loss on account of the decision of the Board stated (February 2006) that unless the labourers in the workshop were deployed for bus body construction, the result would have been mass idling of labour. It was also stated that there would have been labour unrest and consequent losses. The reply is not acceptable since the Corporation had been procuring full bus body for their chassis on earlier occasions also and it may not be a prudent decision to incur significant additional expenditure to avoid idling of labour.

The matter was reported to the Government in May 2006; their reply is awaited (August 2006).

4.25 Undue benefit

Decision of the Corporation to allow short supply of tyres and tubes by a supplier and purchase of the remaining quantity from the same supplier at enhanced rates resulted in undue benefit of Rs.17.92 lakh.

The Corporation invited (May 2004) tenders for the purchase of 24,000 tyres and 36,000 tubes for the year 2004-05. Out of eight quotations received, Birla Tyres (Birla) was rated as most economical with reference to cost per kilometer based on earlier performance, eventhough they were the second lowest considering the quoted price of Rs.5,120 per tyre and Rs.532 per tube. The Corporation placed (August 2004) orders on Birla for the purchase of 14,400 tyres and 21,600 tubes as against 24,000 tyres and 36,000 tubes offered. The delivery was scheduled to be completed during the period from September 2004 to July 2005.

Subsequently Birla intimated (September 2004) that they would be able to supply only 5,500 tyres and 8,250 tubes as against the order quantity of 14,400 and 21,600 respectively which was accepted (January 2005) by the Corporation. Birla supplied (September 2004 to April 2005) 5,120 tyres and 7,475 tubes at the purchase order rates and the balance quantity at the reduced rate of Rs.4,785 and Rs.498 respectively taking into account the reduction in rate of excise duty effective from 01 March 2005.

The Corporation without inviting tenders, placed (June 2005) another order on Birla for an additional quantity of 3000 tyres and 4500 tubes at an enhanced rate of Rs.5,300 per tyre and Rs.553 per tube. The entire quantity was delivered during the period July to August 2005 at a total cost of Rs.2.06 crore. The additional expenditure incurred with reference to the rates revised on account of reduction in excise duty worked out to Rs.17.92 lakh.

Thus, the decision of the Corporation to allow reduction in quantity of tyres and tubes ordered for from Birla and subsequent purchase of the remaining quantity from them at enhanced rates resulted in extending undue benefit to Birla to the extent of Rs.17.92 lakh.

The matter was reported to Government/Corporation in July 2006; their replies have not been received (August 2006).

Kerala State Warehousing Corporation

4.26 Extra expenditure

The decision of the Corporation to reject the economical offer of quality material and purchase of the same at higher rates from other firms resulted in extra expenditure of Rs.18.33 lakh.

The Corporation engaged in warehousing activity, was entrusted (November 2003) by the State Government the work of spraying of organic pesticides under the Centrally Sponsored Scheme for control of coconut mites for the year 2003-04. Accordingly, the Corporation invited (March 2004) tenders and purchased (March 2004) 1,600 litres of 'Econeem plus' from Margo Bio-Controls Private Limited (Margo) and 2,400 litres of 'Neemasal T/S' from EID Parry India Limited at the rate of Rs.590 per litre. Both the products contained the principal ingredient "Azadirachtin 1 *per cent*".

Subsequently, the State Government (October 2004) allotted implementation of the scheme in five districts to the Kerala Agro Industries Corporation Limited (KAICO), another State PSU and the remaining districts to the Corporation. Working instructions for the implementation of the scheme were issued (October 2004) to both the undertakings by the Directorate of Agriculture in pursuance of the Government's directions.

KAICO offered (December 2004) the Corporation for supply of Azadex 10000 containing Azadirachtin 1 *per cent*, which the Company had been using in its spraying activities, at the rate of Rs.540 per litre. The Corporation kept the matter in abeyance on the ground that KAICO's offer was belated one and suppliers had already been identified in March 2004 itself.

In response to the tender notice issued (January 2005) by the Corporation, KAICO again offered to supply 'Azadex 10000' at a reduced rate of Rs.525 per litre. The Corporation, however, did not consider the offer on the plea that manufacturers of 'Azadex 10000' offered by KAICO did not have ISI certification. Even though KAICO had produced (December 2004) before the Corporation the analytical report of Directorate of Agriculture that the product conformed to IS specifications, the Corporation continued to purchase from Margo 10,100 litres at Rs.590 per litre up to January 2005 and 23,300 litres at Rs.582 per litre thereafter.

It was noticed in audit that the Corporation ignored the fact that KAICO was also undertaking the same activity as assigned to them by the State Government using the same material. The working instructions issued by the Directorate of Agriculture in October 2004 did not contain any specific stipulation that the pesticide should conform to ISI specifications. The Coconut Development Board (CDB), the authority releasing funds for the scheme, had also clarified (February 2005) that those products which were chemically analysed by State Agricultural Universities could be used for spraying and the efficacy of Azadex offered for supply by KAICO had been certified by Bangalore Agricultural University. The decision to reject economical offer from KAICO on unjustifiable ground of quality was not convincing since the product was complying with necessary quality parameters and KAICO was using this material in their area of operation.

Thus, the decision of the Corporation to reject the economical offer of quality material and purchase of the same at higher rates from other firms during January to March 2005 resulted in extra expenditure of Rs.18.33 lakh.

The matter was reported to the Government/Corporation in July 2006; their replies have not been received (August 2006).

GENERAL

4.27 Wasteful expenditure

Abnormal delay in commencing commercial activities by the Government Companies rendered the establishment expenditure of Rs.1.22 crore wasteful and preoperative expenditure of Rs.3.03 crore as non-productive.

After incorporation under Section 34 of the Companies Act 1956, a newly formed company has to commence commercial operations at the earliest with a view to generate income by pursuing the objectives laid down in its Memorandum of Association. In the case of Public Sector Undertakings, the Government assumes the role of chief promoter in its formation.

A review of the incorporation and commencement of commercial activities by the Government companies in the State as of March 2005 revealed that three companies failed to commence the commercial activities within a reasonable period after incorporation and had been incurring huge establishment expenditure without any return from business. The names of these companies, their date of incorporation, objectives, Government investment, establishment expenditure incurred up to 31 March 2005, etc., are as given below:

Sl. No	Name of Company	Date of incorpora-tion	Objectives	Govern-ment invest-ment	Prelimi-nary/ preoper-ative expenses	Establish-ment expendi-ture	Reasons for not commencing operation
				Rs. in lakh			
1.	Kerala Special Refractories Limited	November 1985	Manufacture of and trading in refractories and special refractories items	398.23	223.56	64.52	For want of finance
2.	Kerala State Mineral Development Corporation Limited	June 1992	Development of exploration and exploitation of the mineral wealth	125.67	58.47	53.82	For want of finance, environmental clearance of projects, lack of space for rehabilitation of the public living in the proposed area, defective techno economic feasibility/market study, faulty project reports, inferior quality of the natural resources, etc.
3.	Kerala Irrigation Infrastructure Development Corporation Limited	August 2000	Construct a regulator cum-bridge and incidental infrastructure at Chamravattom.	21.14	20.51	3.55	Necessary personnel not recruited and construction not started even after five years of existence.
	Total			**545.04**	**302.54**	**121.89**	

In all the above cases, the delay in commencing commercial operations was due to lack of adequate pre-incorporation planning by the State Government and absence of preliminary/detailed study of the proposed business before the incorporation of the companies. No time frame had been fixed by the Government for starting commercial activities by these companies even after investing an amount of Rs.5.45 crore by way of share capital (Rs.4.38 crore) and borrowings (Rs.1.07 crore).

The newly formed companies had been incurring establishment expenses without undertaking any commercial activities for a period ranging from five to 20 years since their formation. The capital contribution received from the State Government was mainly utilised for meeting establishment expenditure. The reasons for the abnormal delay in the commencement of business operations were not analysed by the Government and remedial action taken.

Thus, the abnormal delay in commencing commercial activities by these companies and absence of close monitoring of their functions by the State Government, rendered the entire establishment expenditure of Rs.1.22 crore for the period up to 31 March 2005 wasteful. Besides, the pre-operative expenditure of Rs.3.03 crore also proved to be non-productive.

The matter was reported to the Government/Companies in July 2006; their replies have not been received (August 2006).

4.28 Avoidable payment

Failure of nine sick companies to avail of the concessional rate of employers' contribution under the Employees' Provident Fund Scheme resulted in avoidable extra payment of Rs.1.47 crore.

As per Section 6 of the Employees' Provident Funds and Miscellaneous provisions Act, 1952 (Act) the employers were under obligation to contribute to the fund at the rate of 12 *per cent* of the wages of employees per month with effect from 22 September 1997. The rate of employer's contribution was only 10 *per cent* in the case of companies which satisfied any of the following conditions:

- sick industrial company as defined in Clause (O) of sub-section (1) of Section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985 and which had been declared as such by the Board for Industrial and Financial Reconstruction (BIFR)
- an establishment which at the end of any financial year had accumulated losses equal to or exceeding its entire net worth and also sufferd cash losses; and
- an establishment in Jute, Beedi, Brick, Coir and Guar Gum industries/factories.

A test review of nine companies which satisfied the above criteria as provided under the Act revealed that the benefit of concessional rate of contribution was not being availed of by them. The contribution was continued to be made at the rate of 12 *per cent* instead of the permissible 10 *per cent* even after the companies were declared sick. The total avoidable additional employers' contribution remitted by these companies during the three years period up to 2004-05 worked out to Rs.1.47 crore (**Annexure 21**).

Thus, the failure of nine sick companies to avail of the concessional rate of employers' contribution under the Employees' Provident Fund Scheme resulted in avoidable extra payment of Rs.1.47 crore.

The Management of four Companies (Sl.No.1, 2, 5 and 8 of **Annexure 21**) stated (July/August 2006) that the remittance of employer's contribution at 12 *per cent* was being made as envisaged in the revival package. This contention is not acceptable since remittance at reduced rates was envisaged in respect of sick companies to reduce their liabilities. Non-availing of this benefit is therefore not justifiable. Three companies stated (July 2006) that they were effecting remittances at 10 *per cent* effective from July 2004 (Sl.No.3)/July 2006 (Sl.No.6 and 7). The fact, however, remained that the past excess contribution made could not be received back. The contention of the Company (August 2006) at Sl.No.4 of Annexure that it was bound to make employees' contribution at 12 *per cent* as per orders (October 1997) of the Assistant Provident Fund Commissioner is not tenable since the orders could not override the provisions of the Act.

4.29 Follow-up action on Audit Reports

Explanatory Notes* outstanding

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

The Audit Reports for the years up to 2004-05 have been presented to the State Legislature but six out of ten departments did not furnish explanatory notes on 31 out of 50 paragraphs/reviews relating to the Audit Reports for the year 2003-04 and 2004-05 as on September 2006.

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

4.29.2 As per the Handbook of Instructions for Speedy Settlement of Audit Objections, the replies to paragraphs are required to be furnished within one month from the presentation of the Reports by COPU to the State Legislature. Action Taken Notes (ATNs) to 212 paragraphs pertaining to 52 Reports of the COPU presented to the State Legislature between July 2000 and September 2006 had not been received as of September 2006 as shown below:

Year of the COPU Report	Total number of Reports involved	No. of paragraphs where ATNs not received
1998-2000	5	30
2001	3	8
2001-2004	20	98
2004-2006	24	76
Total	**52**	**212**

Response to inspection reports, draft paragraphs and reviews

4.29.3 Audit observations made during audit and not settled on the spot are communicated to the heads of the PSUs and the concerned departments of the State Government through inspection reports. The heads of PSUs are required to furnish replies to the inspection reports through the respective heads of departments within a period of six weeks. Inspection reports issued up to March 2006 pertaining to 94 PSUs disclosed that 4,645 paragraphs relating to 901 inspection reports remained outstanding at the end of September 2006; of these, 302 inspection reports containing 2,028 paragraphs had not been replied to for one to five years. Department-wise break-up of inspection reports and paragraphs outstanding as on 30 September 2006 is given in **Annexure 22**.

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

Similarly draft paragraphs and reviews on the working of PSUs are forwarded to the Principal Secretary/Secretary of the administrative department concerned demi-officially seeking confirmation of facts and figures and their comments thereon within a period of six weeks. It was, however, observed that sixteen draft paragraphs and three draft reviews forwarded to the various departments during April to August 2006, as detailed in **Annexure 23**, had not been replied to so far (September 2006).

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

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The

Countersigned

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