CHAPTER V

INTERNAL CONTROL SYSTEM

PUBLIC HEALTH ENGINEERING DEPARTMENT

5.1 Internal Control System in the Public Health Engineering Department

Evaluation of the internal control system in the PHED revealed deficiencies in its budgetary, administrative and supervisory controls. Non-maintenance of basic records also affected the accuracy and completeness of the monthly accounts. Internal audit arrangements were also deficient and unable to provide assurance against possibilities of financial irregularities.

Highlights

Ineffective budgetary control resulted in overall savings of Rs.152.05 crore during 2001-06 affecting State's financial interest and hindering departmental activities.

(Paragraph 5.1.7)

Six Divisions had incurred 37 to 64 *per cent* of their total expenditure in March alone during 2003-04, 2004-05 and 2005-06 indicating non-existence of any departmental control over March rush.

(Paragraph 5.1.8)

Monthly Accounts were submitted late by 19 days to 200 days during 2004-06. No reconciliation of expenditure was carried out during the last five years.

(Paragraph 5.1.13)

Water tax amounting to Rs.5.76 crore was lying un-recovered at the end of March 2006.

(Paragraph 5.1.15)

CI fittings worth Rs.1.21 crore were lying idle in the Water Supply Store Division for two to 11 years due to excessive and unplanned purchase.

(Paragraph 5.1.17)

The Department failed to check quality of drinking water supplied to the consumers due to lack of proper infrastructure, causing risk to public health.

(Paragraph 5.1.18)

5.1.1 Introduction

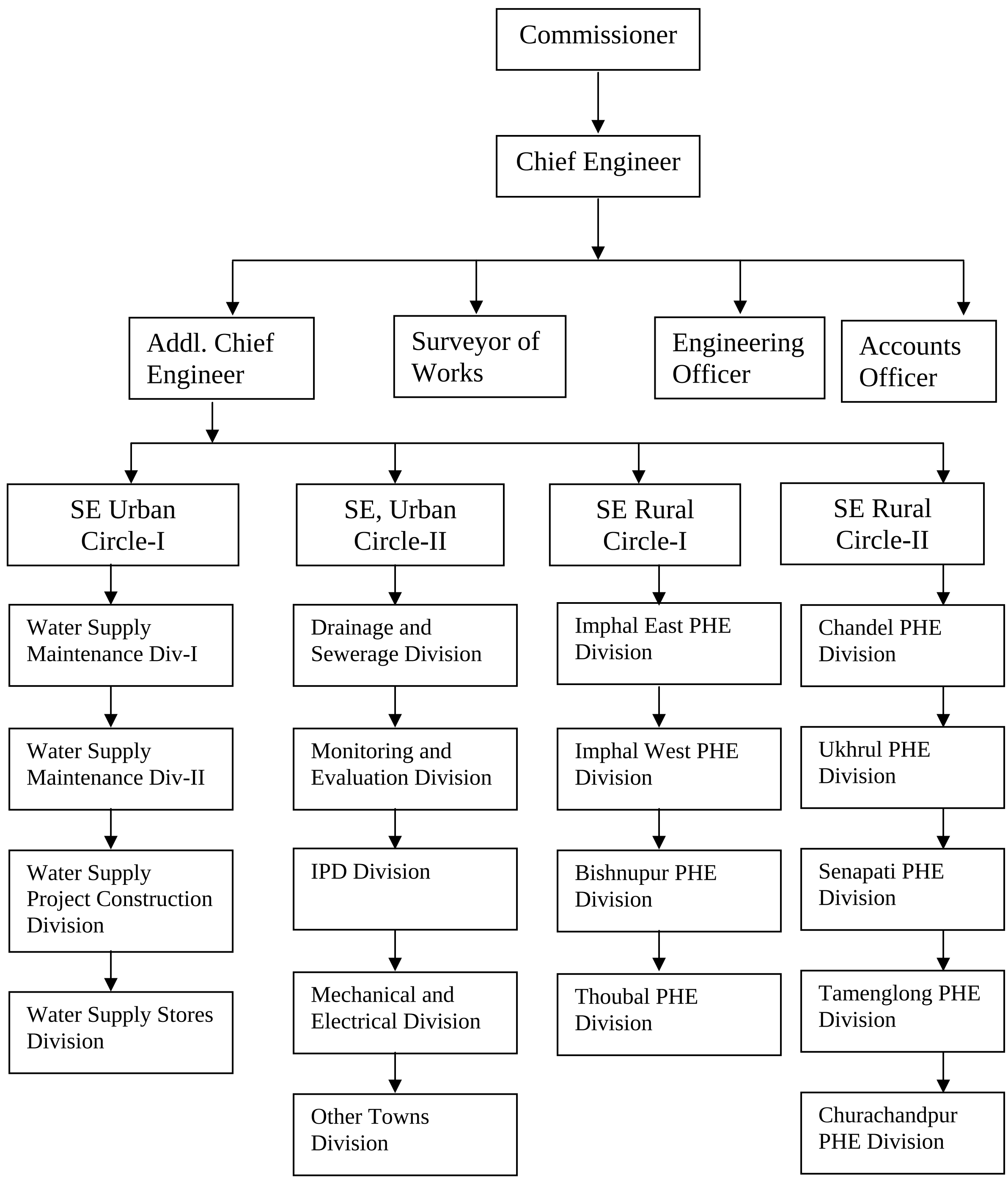
Internal control system is a management tool to provide reasonable assurance that organisational objectives are being achieved. A built-in internal control system and strict adherence to statutes, codes and manuals provide reasonable assurance to the management about compliance with applicable laws, norms and rules thus achieving reliability of financial reporting and effectiveness and efficiency in operations.

The Public Health Engineering Department (PHED) is responsible for planning, constructing and maintaining both urban and rural water supply schemes, distribution network for providing safe drinking water and proper sanitary conditions conserving water resources, and creating public awareness on public and personal hygiene.

5.1.2 Organisational set up

The Commissioner (PHED) is the Administrative Head of the Department. The Chief Engineer (CE), PHED is the executive and technical head. He is assisted by an Additional Chief Engineer; four Superintending Engineers (SE); one Surveyor of Works, one Engineering Officer looking after Administrative matters, and one Accounts Officer who is in charge of the accounts of the Department. There are 18 Divisions headed by Executive Engineers.

An organogram of the Department is given below:



5.1.3. Scope of Audit

To examine and evaluate the internal control system of the Department, records of 13[1] out of 18 Divisions and the Office of the Chief Engineer (CE) were test checked for the period 2001-06 during April-July 2006.

5.1.4. Audit objectives

The objectives of audit were to ascertain the adequacy of the following internal controls in the Department:

- Budgetary and Expenditure controls;
- Financial controls;
- Administrative controls;
- Operational controls; and
- Supervisory controls.

5.1.5. Audit criteria

Audit criteria adopted for assessing the effectiveness of internal controls of the Department were as under:

- The norms/procedures prescribed in the Central Public Works Department Manual
- Central Public Works Accounts Code
- Executive orders issued by the Government from time to time
- Delegation of Financial Powers Rule, 1995.

Audit findings

Budgetary and Expenditure Controls

5.1.6 Non-observance of prescribed procedure

General Financial Rules (GFRs) 49 to 53, 65 and 73 envisage adherence to budgetary controls, which provide for the Administrative Departments to prepare budget estimates based on inputs from lower formations, spend within the budgeted amounts, avoid rush of expenditure at the close of the year and surrender the anticipated savings in time. Supplementary provision for funds is to be made only in case the original allotment proves insufficient. This requires regular monitoring by the Department of monthly expenditure incurred by the Drawing and Disbursing Officers (DDOs) of subordinate offices.

[1] (i) Monitoring and Evaluation Division, (ii) Water Supply Store Division, (iii) Water Supply Maintenance Division-I, (iv) Water Supply Maintenance Division-II (v) Other Towns Division, (vi) Water Supply Project Construction Division, (vii) Chandel PHE Division, (viii) Churachandpur PHE Division, (ix) Imphal West PHE Division, (x) Bishnupur PHE Division, (xi) Ukhrul PHE Division, (xii) Tamenglong PHE Division and (xiii) Drainage and Sewerage Division.

The Department operates two types of budget *viz*., Plan and Non-plan Budget. Non-plan budget includes salary, travelling expenses and medical/office expenses.

The Plan budget is provided for original works, renovation/repairing of existing works and also for operation and maintenance works. The Department has to prepare annual plans and submit to the Government for approval.

Audit scrutiny revealed that no Plan budget proposals were received from various programme implementing officers for the years 2003-04, 2004-05 and 2005-06. The basis on which the Department framed plan budget estimates without reference to the basic information received from programme implementing officers was neither on record nor stated.

5.1.7 Ineffective Budgetary control

The CE is responsible for exercising budgetary control to ensure that no expenditure is incurred in excess of sanctioned grants and that savings are surrendered in advance before the end of the financial year. The actual expenditure vis-à-vis budget provisions during 2001-06 were as follows:

Table 5.1

(Rupees in crore)

Year	**Budget provision**				**Total expenditure**	**Savings (-)/ Excess (+)**
	Original	**Supplementary**	**Surrendered**	**Total**		
2001-02	64.08	25.93	2.42	87.59	53.02	34.57 (-)
2002-03	63.16	84.68	Nil	147.84	109.08	38.76 (-)
2003-04	71.03	64.11	Nil	135.14	65.32	69.82 (-)
2004-05	59.43	69.14	Nil	128.57	117.19	11.38 (-)
2005-06	91.02	44.34	Nil	135.36	137.84	2.48 (+)
Total:	**348.72**	**288.20**	**2.42**	**634.50**	**482.45**	**152.05** (-)

Source: Appropriation Accounts

From the above table it is clear that the Department failed to carry out prescribed regular monitoring of expenditure, resulting in unnecessary supplementary provisions of Rs.25.93 crore and Rs.64.11 crore during 2001-02 and 2003-04 respectively when the actual expenditure was even less than the original budget provisions. Further, there were overall savings of Rs.152.05 crore during 2001-06, which were not surrendered before the end of the financial year as per provisions of GFRs. Thus, the preparation of budget was not realistic. The unnecessary supplementary demands show lack of planning with its consequential effect on the allocation of scarce financial resources of the State to more needy areas and developmental activities.

5.1.8 Drawal of funds to avoid their lapse at the end of financial year

GFRs state that it is against the interests of the State to spend money hastily or in an ill-considered manner just to avoid lapse of budget grant at the end of the financial year (Note 2 under Rule 69). Rush in March has the risk of the Government not getting proper value for money as the expenditure is likely to take place without due diligence. The GFRs require the controlling officers to avoid rush of expenditure in the closing months (Note 3 under Rule 69) by keeping a close watch on the progressive expenditure of the DDOs on a month to month basis. However, it was noticed that six Divisions[2] had incurred 37 to 64 *per cent* of the total expenditure in March alone in 2003-04, 2004-05 and 2005-06, as detailed below:

Table 5.2

(Rupees in crore)

Year	Total expenditure incurred during the year	Expenditure incurred in March	Percentage of expenditure in March to that of the Year
2003-04	32.02	20.44	64
2004-05	25.74	11.70	45
2005-06	36.97	13.51	37

Source: Voucher level computerisation

This indicates that financial rules had been flouted and no internal control had been exercised in this respect.

Financial Controls

5.1.9 Poor Cash Management

Central Treasury Rules provide that money should not be drawn from the treasury when it is not required for immediate disbursement.

Scrutiny of cashbooks of Water Supply Store Division and Water Supply Maintenance Division–I, however, revealed that the Divisions retained heavy cash balances at the end of each month ranging from Rs.0.67 lakh to Rs.1.07 crore, and Rs.0.81 lakh to Rs.43.54 lakh respectively, during April 2005 to February 2006. The Divisions did not analyse the position of cash balances and as such, the periods of retention of cash balances could not be ascertained during Audit.

5.1.10 Fictitious cash transactions

There were instances of fictitious cash transactions in the cashbook only to show funds as spent at the close of the year. For example, the EE, Water Supply Stores Division drew two self cheques for Rs.2.73 crore (No. C-838996:Rs.200.00 lakh and C-838097: Rs.73.37 lakh) on 31 March 2005 and deposited the amount into his official bank account (Account No.01000/050545, SBI, Paona Bazar, Imphal) on 5 April 2005. However, on 31 March an expenditure of Rs.2.93 crore was booked in the cash book as disbursements to various contractors, despite the fact that on that date, the EE had only Rs.20.60 lakh as opening cash balance, inclusive of a bank balance of Rs.9.52 lakh as per his cashbook, and the self cheques were credited to his bank account only on 5 April 2005. Despite special requisition, the EE could not produce the actual payees' receipts for the said amount. The cash

[2] (i) Water Supply Maintenance Division-I (ii) Water Supply Maintenance Division-II (iii) Other Town Division (iv) Water Supply Project Construction Division (v) Chandel PBE Division and (vi) Churachandpur PHE Division.

transactions shown by him on 31 March 2005 were, thus, fictitious and need to be investigated.

Administrative Controls

5.1.11 Non-maintenance of records

One of the principal instruments of ensuring management control over the organisation's functioning is the system of maintaining various returns to watch the transactions.

Test-check of records of five Divisions, however, revealed that important records like register of works, works abstract, deposit register, and contractor's ledger, were not maintained by these Divisions. As a result, the Divisions were not in a position to know the actual expenditure on each work (sub-head wise), up-to-date payment to the contractors, and actual amount of security deposits of each contractor held in the Department. The detailed position is shown in *Appendix-5.1*.

5.1.12 Non-payment of electricity charges

Meeting known or anticipated contingencies is an indicator of the strength of administrative controls in an organisation. Test-check of three Divisions revealed that the Divisions had not paid electricity charges in time and had to pay surcharge amounting to Rs.45.39 lakh[3] due to delay in clearing them. This showed poor administrative controls and lack of anticipation of inevitable expenditure.

5.1.13 Delay in submission of monthly accounts and non-reconciliation of expenditure

Regularity in submission and reconciliation of accounts allows the Department to effect timely corrections in its expenditure pattern and adjust it to the availability of funds. Failure in this regard results in poor budgetary control and misdirected utilisation of resources. As per prevailing procedures the Divisional Officers are required to submit monthly accounts to the Office of the Sr. Deputy Accountant General (A&E), Manipur by the tenth of the following month. This system is an important mechanism through which monitoring and control over expenditure is exercised. Scrutiny of monthly accounts submitted to the Office of the Sr. Deputy Accountant General (A&E), however, revealed that during 2004-06, 17 Divisional Officers rendered their monthly accounts after considerable delays ranging from 19 to 200 days.

It was further noticed that during 2001-06, reconciliation of the actual expenditure incurred by the Department with the expenditure booked in the Office of the Sr. Deputy Accountant General (A&E) was not carried out, defeating the system of monitoring and control of expenditure.

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[3] Imphal West PHED (Rs.25.82 lakh), Water Supply Maintenance Division-I (Rs.8.14 lakh) and Other Town Division (Rs.11.43 lakh).

5.1.14 Non-reconciliation of treasury drawals and remittances

The actual cash flow into Government accounts has to be reconciled with the accrual of revenue. A proper and diligent reconciliation helps in identifying and plugging loopholes in loss of revenue. This assumes added importance in cash strapped States like Manipur.

Para 22.3.1 of CPWA-Code provides that all remittances made into accredited banks (through treasuries) as well as cheques drawn on them by Works Divisions are accounted for under Major Head 8782 – Cash Remittance. The accredited bank prepares and sends daily scrolls of remittances received and payments made to the concerned treasuries with a copy to the Divisional Officers concerned. On receipt of the copies of the daily scrolls, the Divisional Officers effect the reconciliation in Form 51 indicating therein the difference between the cheques issued and the remittances made by the Divisions on one hand and the cheques encashed and remittances accounted for by the bank on the other. The monthly Divisional Accounts are required to be supported by the above schedule of reconciliation of cheques drawn and remittances made to the accredited bank. This internal control prevents fraudulent manipulation of cheques and pilferage of Government revenue in transit.

Audit scrutiny revealed that no such reconciliation was carried out by the Divisions during the last three years. In the absence of reconciliation it is not possible to establish that money remitted into treasuries had actually been accounted for in Government account and cheques issued had actually been encashed for the amount written, and not for higher amounts; this is fraught with the risk of misappropriations and fraudulent payments, if any, remaining undetected and has serious implications for the actual cash balance of the State and its overall credit-worthiness.

5.1.15 Poor collection of water tax

In order to discharge its responsibilities, Government needs resources. An important component of resources is the service charges that Government receives for the services provided by it. Lack of diligence in collection of revenues reflects upon the Department's overall attitude towards ensuring compliance with its own operating principles.

As per the provisions of Manipur Water Supply Act, 1992 the consumers are required to pay water tax at the rate fixed by the Government from time to time, within 15 days from the date of receipt of the bill, failing which the Department is empowered to disconnect the water connection. In addition, the consumers are also punishable with imprisonment of one to six months or with fine of Rs.500 to Rs.3000 or both.

Records of Water Supply Maintenance Division-I (which is the only Division that collects water tax in Imphal area), revealed that 63 to 85 *per cent* of the consumers did not pay water tax during 2003-04, 2004-05 and 2005-06. Action taken by the Department against them was negligible. Water supply in respect of only 59 defaulters, out of 18,477, was disconnected, as shown in *Appendix 5.2*.

Records also showed that water tax amounting to Rs.5.76 crore was yet to be collected as of 31 March 2006. The percentage of collection was also meagre and varied from 12 to 19 *per cent* during last three years. The details are shown in *Appendix 5.3.*

These findings indicate that collection of water tax was ineffective and the Department's enforcement mechanism was totally non-functional. Failure to prosecute defaulters has encouraged the practice of non-payment of water tax amongst the consumers.

Operational Controls

Operational controls indicate the extent of control over the day to day operations in an organisation. Test-check of records in selected Divisions revealed the following instances of absence of operational controls in the Department.

5.1.16 Stock held in excess of permissible limits

According to para 37.8 of the CPWD Manual, the Chief Engineer has full power to fix annual limit of reserve stock of the Divisions under his control. When the reserve stock limit has been sanctioned, the Divisional Officer is authorized to purchase material to the extent sufficient to keep the stock level within the limit fixed by the competent authority.

The Department intimated that the reserve stock limit sanctioned for the Water Supply Stores Division was Rs.2.75 crore. However, monthly accounts for March 2005 revealed that the stock balance of the Division amounted to Rs.10.47 crore, indicating excess procurement of material worth Rs.7.72 crore. This also indicates that the Division had been allocated funds far in excess of its requirements. As a result, substantial amount of Government funds had been blocked in construction material.

5.1.17 Inefficient Material Management

Where stores are purchased centrally it is but expedient that the working divisions prepare a statement of annual requirement of stores by first of April every year indicating therein the items of material and their quantities to be procured and send it to the central division for arranging bulk purchase of material. Audit scrutiny, however, revealed that none of the working divisions furnished their annual requirements. The Department stated (April 2006) that during the last three years no new work programmes were undertaken due to shortage of funds. Hence no proper material planning could be done and the store material were procured based on immediate requirements submitted by the Divisions with the approval of the Government within the available budget provision. Thus, due to lack of proper planning the Store Division purchased material as and when Cheque Drawal Authority was received from the Government, indicating improper and inadequate internal control system in respect of material management.

According to GFRs [Rule 119 (3)], material remaining in stock for over one year shall be considered surplus unless adequate reasons to treat it otherwise exist as the inventory carrying cost is an expenditure that does not add value to the material being stocked.

Scrutiny of Priced Store Ledgers of Water Supply Stores Division revealed that huge quantity of CI Flanges, CI Sluice Valves of various diameters and specifications valued at Rs.1.21 crore were lying as balance in stock for two to 11 years as of March 2006. Retention of such large quantities of material for years together indicated unfruitful blocking of Government funds and the associated opportunity cost.

While the Central Store (Water Supply Stores Division) was thus carrying huge inventory of CI material for years and was unable to dispose of them, audit scrutiny revealed that the Water Supply Maintenance Division–II had procured similar material worth Rs.14.74 lakh from the local market during 2004-05. This highlights absence of coordination and control over purchases and inefficient material management in the Department.

5.1.18 Ineffective monitoring and surveillance of drinking water quality

Public Health Engineering Department is a service department. Providing clean, potable drinking water to people and maintaining hygiene are its main functions. To ensure the minimum quality, the Department is required to regularly check the quality of water supplied and take the required corrective action.

The Monitoring and Evaluation Division is responsible for monitoring drinking water quality and conducting surveillance of water sources to ensure potable water supply. It has one Central Laboratory and one Mobile Laboratory to discharge its functions.

An analysis of the reports of Central Laboratory regarding collection and testing of samples from the peripheral water supply schemes/treatment plants disclosed that during the year 2005-06, only 72 samples were collected from 10 different water supply schemes/treatment plants serving 2.45 lakh people against 468 samples required to be collected as per the Manual of Water Supply and Treatment. The shortfall varied from 71 to 96 *per cent*, as shown in *Appendix 5.4*. The results of testing of the samples and remedial action taken, if any, were not intimated to Audit.

There was no vigilance team at the disposal of the Monitoring and Evaluation Division. No records of any activities of sanitary survey and its reporting, water sampling, data analysis of quality of water and assessment of sanitary conditions were produced to audit.

The Department stated (May 2006) that the existing infrastructure was not adequate for ensuring smooth functioning of the Division due to non existence of laboratory network at municipal/district level and Primary Health Centre/village level, lack of office accommodation with modern equipment, well trained staff and financial support. But there was no evidence on record to show departmental efforts in streamlining the functioning of this Division or securing any financial support from the Government in this regard. The failure of the Department to ensure proper monitoring and control of the quality of the water supplied has serious implications for public health.

Supervisory Controls

The management needs to involve itself in execution of important projects as well as routing activities to ensure that all activities executed follow prescribed procedure. Test-check by audit, however, revealed several instances of lack of supervision by management, as discussed below.

5.1.19 Faulty contract management and lack of supervision

According to Clause 36 of the agreement (prescribed under CPWD Manual Vol-II) that the Department enters into with its contractors, the contractor is required to employ a Graduate Engineer/diploma holder with five years' experience for works costing above Rs.5 lakh and a qualified diploma holder for works between Rs.2 lakh and Rs.5 lakh for receiving Divisional Officer's orders at site.

In case the contractor is unable to employ such technical people, he is required to pay as compensation to the Department @ Rs.2,000 in the case of an Engineer and @ Rs.1,000 in the case of a diploma holder per month of default.

It was noticed in Audit that four Divisions failed to recover such compensation from defaulting contractors amounting to Rs.13.27 lakh[4] which indicates lack of supervision and faulty contract management. In addition, the Department had not taken any action to review the rates of penalty to determine whether they continued to be a deterrent for not employing technically qualified people, which has serious implications on the overall quality of works due to lack of proper technical supervision at the site.

5.1.20 Lack of control on General Provident Fund (GPF) accounts

GPF accounts of Grade IV employees are maintained by the Department. Audit scrutiny revealed that advances and non-refundable withdrawals had not been deducted from the GPF accounts of the Grade IV employees in some of the divisions. The details are shown in *Appendix 5.5*.

Inadequate internal control resulted in these irregularities which may further result in excess withdrawal. The Department should strengthen the supervisory controls to prevent such irregularities.

5.1.21 Unclaimed deposits not credited to Government account

Paragraph 15.4.1 of CPWA-Code provides that balances of Public works deposit remaining unclaimed for more than three complete accounting years should be deposited into Government account as lapsed deposit. Records of

[4] Bishnupur PHED (Rs.3.69 lakh), Water Supply Maintenance Division II (Rs.4.46 lakh), Tamenglong PHED (Rs.0.76 lakh) and Churachandpur PHED (Rs.4.36 lakh).

the Water Supply Project Construction Division disclosed that 140 and 168 items of deposits involving Rs.10.89 lakh and Rs.1.40 lakh were lying under deposit Part-II and Part-V respectively for three to 14 years, but were not credited to Government account.

5.1.22 Outstanding cash settlement suspense account (CSSA)

As per para 17.2.1 (b) read with *Appendix 7* of CPWA Code, at the end of the financial year, there should be no balance under CSSA.

Monthly accounts of the EE, Water Supply Store Division revealed that at the end of February 2006, Rs.9.82 crore was lying outstanding under this suspense head against 17 PHE Divisions, which indicated poor financial management and lack of financial controls.

5.1.23 Internal Audit

Internal Audit is one of the major components of internal control mechanism. To provide reasonable assurance for a free and independent audit system, the Department is required to establish a separate internal audit wing. However, the Department did not have an internal audit wing. Although the Department is under the audit jurisdiction of Directorate of Local Fund Audit, Government of Manipur, none of the test-checked offices/divisions were inspected by Local Fund Audit during the period covered in the review.

5.1.24 Lack of response to Audit

Accountant General (Audit), Manipur conducts periodic inspections of Government transactions and the audit findings communicated through Inspection Reports (IRs) to the Heads of the Offices/Departments are required to be addressed within a specified period. A half yearly report of the pending IRs is sent by the Accountant General to each Department, to facilitate monitoring and compliance of audit observations.

As of March 2006, 581 paragraphs involving Rs.113.88 crore relating to 106 IRs of the PHED were lying unattended. In 35 cases even the first replies to the IRs were not furnished. Failure to comply with the issues raised by Audit facilitated continuation of serious financial irregularities, and adversely affected the accountability mechanism. The details are shown in *Appendix-5.6.*

5.1.25 Lack of Computerisation

Presence of a computer based MIS would have helped the management in assuming a more proactive role in financial and works management, reducing errors in accounts and assisting in State-wide material management. However, Audit scrutiny revealed that the Department has not adopted Information Technology in its day to day functioning.

5.1.26 Conclusion

Internal control system in the Department was not effective and adequate. Rules and procedures were not strictly adhered to in many cases. There was indiscipline in budgetary control and financial reporting. Stores were purchased without proper planning, resulting in excess material in stock lying unutilized for years. Drinking water quality control and surveillance was virtually non-existent due to inadequate infrastructure like laboratory net-work, lack of office accommodation with modern equipment, shortage of well trained staff and financial support. Collection of water tax was very poor resulting in non-realisation of substantial portion of Government revenue.

5.1.27 Recommendations

- Budget estimation should be based on basic information received from the working Divisions to make it realistic.
- Monthly accounts of the Divisions should be submitted to office of the Sr. Deputy Accountant General (A&E) on time.
- Material should be procured with proper planning and estimation to ensure that there is no mismatch between the procurement of stores and their actual requirements.
- Action should be taken for timely collection of water taxes.
- Effective and reliable quality control system should be established to ensure supply of safe drinking water to the public.