# CHAPTER – V
# INTERNAL CONTROL SYSTEM AND INTERNAL AUDIT

## FINANCE, REVENUE AND EXPENDITURE DEPARTMENT

### 5.1 Internal Control System in FRED

*Audit review of the internal controls in the Finance, Revenue and Expenditure Department (FRED) and its five Directorates revealed deficient budgetary, receipts and expenditure control. Much was desired in the areas of operational controls pertaining to maintenance of records, cash, liabilities, deposits, investment, stores, suspense accounts etc. Even supervisory controls in respect of adjustment of advances, purchase and allotment of vehicles, recovery of outstanding dues, payment of allowances, reimbursement of pension already paid, regulation of General Insurance Scheme/General Provident Fund, operation of separate bank accounts, and drawal and disbursement through Chief Pay and Accounts Office etc. was extremely lax and inadequate. The system of internal audit and mechanism for settlement of audit objections was grossly deficient.*

### Highlights

**Absence of budgetary control led to unnecessary supplementary provisions, persistent savings, and non-surrendering of anticipated savings, both in FRED and other departments. FRED was also unaware of the spill over liabilities of the Government incurred by other departments which stood at Rs. 2.83 crore at the end of 2005-06.**

**(Paragraphs 5.1.7.1 to 5.1.7.4)**

**Failure to identify false certificates of adjustments of AC bills resulted in non-adjustment of outstanding advances in FRED itself to the tune of Rs. 60.49 lakh, besides Rs. 101.50 crore in other departments.**

**(Paragraph 5.1.8.1)**

**FRED failed to monitor and ensure clearance of suspense of Rs. 2.79 crore in 2006-07 under the Major Head of account 8658.**

**(Paragraph 5.1.8.5)**

**Despite orders of the Supreme Court, FRED failed to recover outstanding dues of Rs. 49.96 lakh from a private party. Failure to comply orders of Supreme Court also resulted in irregular annual expenditure of Rs. 30.71 lakh towards payment of special duty allowance.**

**(Paragraphs 5.1.9.1 and 5.1.9.3)**

**FRED failed to obtain re-imbursement of expenditure on pension to the tune of Rs. 1.64 crore from other agencies.**

**(Paragraph 5.1.9.6)**

**Internal Audit could not ensure effective internal control mechanism in expenditure in Government due to low coverage of units and non-existent follow up action on its inspection reports.**

**(Paragraph 5.1.10)**

### 5.1.1 Introduction

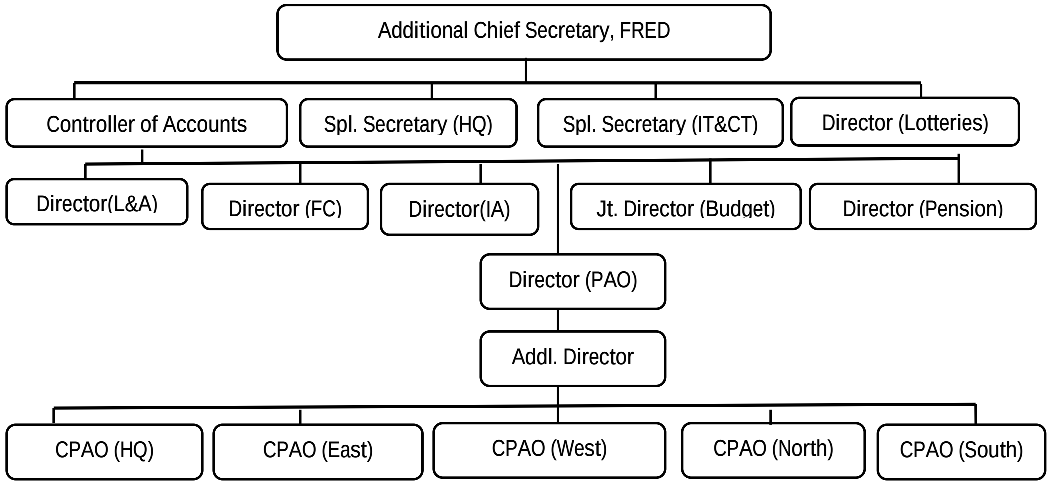
Internal Control Mechanism (ICM) in an organization aims at ensuring that its operations are carried out within applicable laws, rules and regulations in an economical, efficient and effective manner. It provides reasonable assurance to the top management about the achievement of the organizational objectives and safeguards the assets and other resources of the organization from wastage, mismanagement, fraud, etc.

The Government has an internal control system where the overall financial control (budgetary and expenditure control, internal audit etc.) is exercised by the FRED whereas, administrative and operational controls over specific functional activities are exercised by the respective departments. But the FRED itself also functions within this overall internal control frame work of the Government and is therefore, subject to the same internal, financial, administrative and operational controls to manage its own functions as is applicable to any other department of the Government.

### 5.1.2 Organisational set up

The Additional Chief Secretary (ACS) to the Government of Sikkim is the overall in-charge of the Department and is assisted by other subordinate officers as mentioned below in the organogram. The Director of Pay and Accounts Office, Director of Lotteries and Special Secretary of Income Tax and Commercial Tax Divisions function as independent Heads of Departments under the control of FRED.

**Chart-5.1**




## 5.1.3 Audit coverage

The functioning of ICM of the FRED covering a period of five years (2002-03 to 2006-07) was reviewed in April-May 2007with reference to information furnished and the records maintained in the office of the ACS (including Director, Loans & Accounts and Director, Finance Commission), Director of Internal Audit, Director of Pension, Group Insurance Scheme (GIS), General Provident Fund (GPF) and Director of Pay and Accounts Office (PAO).

## 5.1.4 Audit objectives

The Audit was carried out with a view to assess and ascertain the adequacy and efficacy of various internal controls in the Department and evaluate if these were in place and were being implemented/complied with appropriately not only in FRED, but also in relevant context in other departments of the State Government to ensure achievement of the broad goals of the Government in an economic, effective and efficient manner. The following internal controls were assessed in this regard:

- Financial controls (budgetary and expenditure controls, control over revenue etc);
- Operational controls;
- Supervisory and Monitoring controls (mainly over the finances of other departments); and
- Internal Audit.

## 5.1.5 Audit criteria

For fulfillment of the above objectives, the following criteria were used:

- Rules of Business;
- Sikkim Financial Rules 1979;

- General Provident Fund (Sikkim Services) Rules 1984;
- Sikkim Services (Pension) 1990;
- Sikkim Government Employees' Group Insurance Scheme 1993;
- Handbook of Payment and Accounting Instructions under the Pay and Accounts System; and
- Internal Audit Manual.

## 5.1.6 Audit methodology

The audit process started with an entry conference with the Controller of Accounts on 9 April 2007. The audit methodology adopted involved examination of records on the basis of criteria fixed and with reference to the audit objectives. The audit findings were discussed with ACS in an exit conference on 11 September 2007 and the replies of the Department are incorporated in the review as appropriate. The results of audit are brought out in the succeeding paragraphs.

***Audit findings***

## 5.1.7 Financial controls

***Budgetary controls***

The Sikkim Financial Rules, 1979 (SFR) require the administrative departments to prepare budget (including revenue) estimates based on inputs from lower formations, project estimated revenue collection, expenditure within budget, timely surrender of anticipated savings and avoid rush of expenditure. Supplementary provision should be asked only when the original allotment proves insufficient. This requires regular monitoring of monthly receipts and expenditure incurred by the Drawing and Disbursing Officers (DDOs) at various levels in the administrative departments as well as FRED.

FRED had not prepared any Budget Manual as yet to regulate functions incidental to preparation of budget. This coupled with non-adherence to the provisions of SFR and instructions issued by the FRED itself from time to time, led to unnecessary supplementary provisions, persistent savings, anticipated savings not surrendered, spill over liabilities, diversion and blocking of funds etc. not only in the FRED itself, but also in other departments. Despite these deficiencies being pointed out year after year by Audit in Chapters II and VI of Comptroller and Auditor General's Audit Reports, the problem persists. The Department stated (October 2007) that it was not necessary to have a budget manual, which is not tenable in the face of the irregularities discussed in the succeeding paragraphs.

***Finance Department***

### *5.1.7.1 Unrealistic budgeting*

The actual expenditure vis-à-vis budget provision of the FRED during 2002-07 was as follows:

**Table - 5.1**

***(Rupees in crore)***

| Particulars | 2002-03 | | 2003-04 | | 2004-05 | | 2005-06 | | 2006-07 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Revenue | Capital | Revenue | Capital | Revenue | Capital | Revenue | Capital | Revenue | Capital |
| Original grant/Appropriation | 1151.16 | 27.82 | 1308.48 | 32.54 | 1035.88 | 40.35 | 1047.38 | 45.58 | 1110.33 | 39.75 |
| Supplementary grant/Appropriation | 157.97 | 12.94 | 27.13 | 51.94 | 2.76 | 18.67 | 0.48 | Nil | 5.12 | Nil |
| Total | 1309.13 | 40.76 | 1335.61 | 84.48 | 1038.64 | 59.02 | 1047.86 | 45.58 | 1115.45 | 39.75 |
| Actual expenditure | 1309.56 | 40.41 | 594.51 | 84.27 | 1032.32 | 83.79 | 1043.41 | 32.40 | 1103.67 | 39.23 |
| Savings (-) / Excess (+) | (+) 0.43 | (-) 0.35 | (-) 741.10 | (-) 0.21 | (-) 6.32 | (+) 24.77 | (-) 4.45 | (-) 13.18 | (-) 11.78 | (-) 0.52 |
| Percentage of savings/excess | 0.03% | 0.86% | 55.49% | 0.25% | 0.61% | 41.97% | 0.42% | 28.92% | 1.06% | 1.31% |

***Source: Appropriation Accounts***

From the above table, it will be seen that the supplementary provisions were not justified during 2003-04 (revenue). Similarly, while the expenditure in capital section of 2004-05 exceeded the provision including supplementary by 41.97 *per cent*, the savings in revenue section of 2003-04 and capital section of 2005-06 was to the extent of 55.49 and 28.92 *per cent* respectively of the total provision. The supplementary provisions were, therefore, either inadequate or unnecessary during these years. This indicated lack of care in budget preparation as well as inadequate control and monitoring.

FRED stated (October 2007) that the excess during 2004-05 was due to time bound repayment of some institutional loans for availing of Debt Swap Scheme introduced by GOI at the fag end of the year. It was further stated that adjustment of funds was admissible only within the same sector. But the fact remained that funds that could not be spent within a year should have been surrendered before the end of the year.

***Other departments***

### *5.1.7.2 Deficiency in preparation of State budget*

While the FRED failed to control its own departmental budget as indicated above, it also failed to effectively control the budgets of other departments while scrutinising and approving their budget proposals. During 2002-07, there were excesses or savings under several Demands for Grants at the end of all the years as reflected below:

**Table – 5. 2**

***(Rupees in crore)***

| Year | Number of Grants in which there was | | | | | |
|---|---|---|---|---|---|---|
| | Excess | | | Savings | | |
| | Number of Grants/Appropriation | | Amount | Number of Grants/Appropriation | | Amount |
| | Revenue | Capital | | Revenue | Capital | |
| 2002-03 | 02 | 06 | 2.31 | 42 | 22 | 145.35 |
| 2003-04 | 03 | 03 | 1.21 | 41 | 24 | 128.34 |
| 2004-05 | 03 | 01 | 0.12 | 40 | 24 | 73.43 |
| 2005-06 | 08 | Nil | 7.63 | 35 | 26 | 259.69 |
| 2006-07 | 05 | 01 | 2.64 | 38 | 22 | 442.14 |

***Source: Appropriation Accounts.***

The position shown in the above table reflects the lack of effective monitoring by the FRED to control such excesses or savings through monthly reports and/or mid-term review meetings. Audit scrutiny further revealed that though the individual departments had been asked to send the monthly reports and expenditure under both plan and non-plan heads to the FRED, the latter seldom made use of such reports. These reports were also generally received late in FRED. FRED stated (October 2007) that the primary responsibility of monitoring and control over expenditure rested with the concerned departments. The fact is that FRED is responsible for effective, efficient and economical management of the State Government finances.

### *5.1.7.3 Persistent savings*

Persistent savings in respect of the entire State became a regular feature in the budget every year as detailed below:

**Table – 5.3**

***(Rupees in crore)***

| Year | Number of Grants in which there was persistent savings | | | |
|---|---|---|---|---|
| | Number of total Grants/Appropriation | Total Budget Provision | Number of Grants/Appropriation with persistent Savings | Amount |
| 2002-03 | 44 | 937.47 | 42 | 145.25 |
| 2003-04 | 44 | 937.21 | 41 | 118.86 |
| 2004-05 | 43 | 1296.24 | 36 | 228.07 |
| 2005-06 | 43 | 1437.43 | 35 | 258.44 |
| 2006-07 | 43 | 2724.54 | 37 | 434.54 |

***Source: Appropriation Accounts.***

It indicated lack of effective monitoring of Review of Expenditure statements every month by both the concerned administrative departments and the FRED. Besides, FRED had also failed to give timely advice for surrender during supplementary and pre-budget scrutiny stages.

## *Expenditure controls*

### *5.1.7.4 Failure to control spill over liabilities*

In terms of SFR (Sanction of New Schemes), all schemes and extension of schemes already in operation, whether within the Plan or Non-Plan**,** require the sanction of the FRED, which is to exercise proper due diligence while giving such sanction. Further, no work is to commence or liability incurred until funds to cover the charge during the year are provided by the competent authority. In terms of circulars issued by the FRED on 24 January 2000 and 06 May 2002, every Head of Department is to submit statements of liability and summary of expenditure in the prescribed proforma before 10$^{th}$ of every succeeding month to the FRED, failing which the Pay and Accounts Offices were to withhold the issue of cheques and release of resources to the defaulting departments.

Audit scrutiny revealed that the system of submission of liability statement by the individual departments was not adhered to except in 2005-06, when 42 out of 44 departments submitted (August 2005) the liability statements at the end of 2005-06 which stood at Rs. 2.83 crore. Despite non-submission, the PAOs failed to withhold the payments of these departments with the result that the spill over liabilities had spiralled to huge proportions. The FRED was unaware of the liability position of the Government from time to time while approving the budget for these departments. The budget scrutiny exercise carried out by the FRED was thus ineffective and deficient to this extent.

### *5.1.7.5 Failure to monitor expenditure*

It was observed that 89 works (Rs. 70.15 crore) pertaining to three sampled departments[1] were not completed within specified time and there were delays upto five years eight months. As a result of failure to monitor expenditure *vis a vis* completion, expenditure was spread over six years and this affected financing of other developmental projects.

In reply FRED stated (October 2007) that the implementing departments were responsible. Fact is that FRED is responsible for managing finances in the State and its responsibility does not end with sanction.

### *Receipt controls*

### *5.1.7.6 Failure to monitor recovery of arrears of revenue*

Timely assessment and collection of taxes/fees is to be ensured by all the revenue collecting authorities in Income and Commercial Tax Divisions and Directorate of Lotteries under the FRED itself as well as other departments like SNT Division of Transport Department, Urban Development and Housing Department, Water Security and Public Health and Engineering Department etc. The position of arrears in revenue is being regularly pointed out in Chapter VI (Revenue Receipts) of the Comptroller & Auditor General's Audit Report since 2005-06.

While the collection during the last 5 years varied from 12 *per cent* (2004-05) to 95 *per cent* (2002-03) of the arrears, the amounts remaining unrealised in the respective divisions / departments amounted to Rs. 8.11 crore in 2002-03 and Rs. 91.34 crore (including Rs. 76.33 crore under arbitration since 2004-05 in respect of State Lottery) in 2006-07, depicting an increase of 1126 *per cent*. The gigantic increase in accumulation of arrears indicated that FRED had not made any concerted efforts to reduce arrears. Further, the information on arrears of revenue as furnished by FRED varied from those furnished by the concerned individual departments as under:

[1] *Energy and Power Department, Human Resource Development Department, Building and Housing Department*

**Table - 5.4**

*(Rupees in crore)*

| Year | State Lotteries | | SNT | | Income Tax | | Commercial Tax/VAT | |
|---|---|---|---|---|---|---|---|---|
| | Departmental figure | FRED figure | Departmental figure | FRED figure | Departmental figure | FRED figure | Departmental figure | FRED figure |
| 2005-06 | Not furnished | 76.33 | 3.20 | 2.83 | 0.19 | 1.10 | Not furnished | 0.87 |
| 2006-07 | 24.75 | 76.33 | 3.84 | 3.84 | 7.58 | 8.34 | 0.61 | 1.07 |

Out of the 4 revenue collecting divisions mentioned above, 3 divisions were under the jurisdiction of FRED itself. It is thus evident that FRED is not adequately monitoring the realisation of arrears of revenue which is necessary while preparing revenue estimates for the next financial year and ultimately budget allocation of all Government departments.

### *5.1.7.7 Non-assessment of taxes*

Delay in assessment of taxes is also a regular feature of the revenue receipt collecting authorities in the Income and Commercial Tax Divisions under the FRED. The position in this regard at the end of 2006-07 was as under:

**Table - 5.5**

| Name of tax | Number of cases | | | |
|---|---|---|---|---|
| | Opening balance | Assessments due (arrear + new) | Assessments done (%age) | Closing balance |
| Sales Tax/VAT | 721 | 774 | 335 (43) | 439 |
| State Income Tax | 2011 | 2427 | 1320 (54) | 1107 |

As would be seen from above, only 43 to 54 *per cent* of due assessments could be completed as at the end of 2006-07. FRED could neither issue any instruction to the Income and Commercial Tax Divisions nor evolve any mechanism to clear the backlog of assessments resulting in delay and non-realisation of Government dues.

### *5.1.7.8 Failure to follow procedures*

Internal Audit under FRED ensures that all the Government receipts were properly and promptly assessed, collected and credited into Government account. However, it was noticed that in one case of Motor Vehicles Division of Transport Department, an amount of Rs. 0.95 lakh shown to have been credited to Government revenues was actually not credited to the Government account. Further scrutiny revealed that the Department was entertaining the depositors' copy of challans towards the proof of deposit instead of cross checking the actual deposit from the departmental copy received from the banks receiving the deposits. This left scope for fraud. On this being pointed out by Audit, the Principal Secretary, Transport Department (08 December 2006) took up the matter for investigation through IA. From the reply furnished (October 2007) by FRED, it was seen that FRED issued (December 2006) instruction to the concerned bank for verification and the matter was closed (February 2007) by

FRED after effecting recovery of the fraudulent amount (December 2006). Thus failure to follow prescribed procedures exposed the system to fraud.

### *5.1.7.9 Control over receipts from lottery*

The receipts from lottery being very high in the State contributing about 77 *per cent* (Rs. 963.30 crore of State's own revenue of Rs. 1258.22 crore in 2006-07), records relating to the controls by FRED in this regard were test checked. The following was revealed.

- *Delay in realization of lottery receipts*

In terms of agreement entered with marketing agent (MA) (M/s Sugal and Damani), the realization of revenue towards sale proceeds should be made on a monthly basis. However, scrutiny revealed that although the revenue was realized on a monthly basis, the same was not in full realization of the sale proceeds. The delay in payment of full amount ranged from 2 months to 7 months and involved Rs. 1388 to Rs. 2.72 crore.

In the case of another MA (M/s Tashi Delek Gaming Solutions Private Limited), despite the stipulations for deposit of sale proceeds within 15 days from the date of draws, the delays ranged from 4 to 74 days beyond admissible limit of 15 days.

There being no penal clause for delayed payment, no action could be taken by Director of Lotteries under FRED in any of the cases mentioned above.

- *Absence of control over sale and printing of lottery tickets*

In the agreement with the MA, M/s Tashi Delek Gaming Solutions Private Limited, a clause to the effect that the issue of tickets should be monitored, supervised and controlled by the Director of Lotteries was found inserted. However, in respect of M/s Martin Lottery Agency and M/s Sugal and Damani, the remaining MAs, no such clause was inserted. Further, no control mechanism relating to issue and sale of tickets in any of the lotteries being arranged through the MAs had yet been evolved and implemented. In a case of investigation, Vigilance of Kerala Government observed (September 2006) that as per the statement filed by M/s Megha Distributor, Palakkad at the time of remitting advance tax for conducting the draws of the various lotteries for the period from 9 October 2006 to 15 October 2006, they had stated that the number of series of tickets of Kiul scheme proposed to be sold for the said period are 500. But on verification of the copy of the delivery challan produced by themselves along with the statement, it was revealed that only 20 series of tickets were printed by the printing press (Ext. H). Thus the possibility of lottery tickets being printed by the sole agents without the knowledge of the State can not be ruled out. Also, as revealed from the statements filed by the sole agent of Bhutan and Sikkim Lotteries at the time of remittance of the advance tax for the sale of lottery tickets in Kerala, about 15 lakhs of the lottery tickets each of Bhutan Data and Bhutan Sree Deepam worth Rs. 10 crores and about 12.60 crores of tickets of

Sikkim lottery valuing Rs. 12.60 crore are being sold per day in the State.

## 5.1.8 Operational controls

### *5.1.8.1 Failure to monitor settlement of AC Bills*

According to financial rules, amounts drawn under Abstract Contingent (AC) bills are required to be adjusted by submission of Detailed counter signed Contingent (DC) bills within 90 days from the date of drawal to the Controlling Officers for counter-signature and onward transmission to the Accountant General (A & E). However, the FRED did not submit DC bills against AC bills within the prescribed time limit as shown in **Table 5.6**. Therefore the FRED itself certified falsely that all advances drawn beyond the last 90 days had been adjusted when it came to drawing a fresh advance.

**Table – 5.6**

| Year | No. of outstanding AC Bills in FRED | Amount outstanding *(Rs. in lakh)* |
|---|---|---|
| 2002-03 | 19 | 15.82 |
| 2003-04 | 26 | 7.92 |
| 2004-05 | 23 | 7.45 |
| 2005-06 | 19 | 12.13 |
| 2006-07 | 30 | 17.17 |
| **TOTAL** | | **60.49** |

The position of outstanding AC bills in respect of 41 other departments were as under:

**Table – 5.7**

| Year | No. of outstanding AC Bills | Amount outstanding *(Rs. in crore)* |
|---|---|---|
| 2002-03 | 714 | 14.32 |
| 2003-04 | 995 | 8.51 |
| 2004-05 | 871 | 46.19 |
| 2005-06 | 725 | 12.98 |
| 2006-07 | 951 | 19.50 |
| **TOTAL** | | **101.50** |

***(Source: VLC data from A&E Office)***

In reply (May 2007), FRED stated that the Directorate of PAO is not required to maintain any OB Register in respect of AC bills with effect from April 1984 vide Finance Circular dated 27 December 1983. The Directorate further stated that they invariably obtain a certificate from the DDOs of various departments to the effect that there was no outstanding AC bill for more than three months before passing any fresh AC bill. The reply of the Directorate is not acceptable as the purpose of the order was defeated as there was huge number of outstanding AC bills pertaining to the year 2004-05 to 2006-07. Further, the position of outstanding AC bills is intimated to the Additional Chief Secretary demi-officially by the Accountant General every month on the closure of Civil

Account for the month since November 2005 (19 times till the accounts of May 2007). Despite this, the outstanding AC bills only increased year after year. FRED stated (October 2007) that action is being taken for settlement of outstanding advances.

#### *5.1.8.2 Inadequate control over investments*

***Failure to control investments resulted in low return***

The FRED could not furnish the information about investments and return on such investment except cash balance investment on which records were produced to Audit. However, scrutiny of Finance Accounts for the year 2006-07 revealed that the Government had invested an amount of Rs. 83.40 crore in companies, corporations, joint stock companies, co-operatives etc. with an average return of only 1.05 *per cent* at the end of 2006-07 as against average interest rate of borrowing of 9.57 *per cent.*

It was seen that despite FRED designating (August 2003) officers for attending meetings as Directors in the Board Meetings of the PSUs/Joint Sectors/Government Undertakings as representatives of the Government to have a say in the management of these entities, no officer of the FRED ever attended such Board Meeting of PSUs/Joint Sectors/Government Undertakings. In reply, FRED stated (October 2007) that it had requested the administrative departments to submit feed back on the subject.

#### *5.1.8.3 Non-adherence to rules governing maintenance of Cash Book*

Rule 49 of SFR provides several internal control measures in cash management like maintenance of cash book in the prescribed form, attestation of entries by the DDO, check of totaling by an officer other than the writer of the cash book, monthly physical verification of cash balances by the DDO etc. Audit scrutiny revealed that these were not being followed in the FRED itself. Therefore, the true and fair view of transactions occurring in the Department cannot be vouched. While accepting the audit observation, the FRED stated (October 2007) that corrective measure had been initiated.

#### *5.1.8.4 Non-adherence to control in imprest amount*

In terms of FRED Circular dated 26 December 1998, the heads of departments and offices granted cash imprest were required to surrender the said imprest amount held by them before 31 March of every financial year and apply for a fresh imprest amount, justifying their need. Imprests sanctioned before issue of the orders dated 26 December 1998 were also to be surrendered within 31 March 1999.

Scrutiny of records revealed that in 128 cases, the departmental authorities failed to surrender their imprest amount to the tune of Rs. 3.84 lakh held by them since 1976-77 to 2006-07, It was also noticed that many departments had been granted imprest amount for the subsequent years before adjustment of previous accounts by the FRED. While accepting the audit observation, FRED stated that most of the imprest accounts were very old and regularisation of these would definitely take sometime. This indicated that the financial control mechanism towards sanctioning and recovery/adjustment of imprest amount did not exist in FRED.

#### *5.1.8.5 Absence of control on operation of bank accounts by various departments*

The FRED routinely approves proposals of other departments for opening of bank account outside Government accounts but does not maintain any record of the bank accounts being operated by various departments and whether these accounts were opened after taking necessary approval from FRED as well as from the AG's office. A cross examination of the records maintained in the office of the AG Sikkim with the records of the Department revealed that there were 38 bank accounts being operated by various departments during May 2000 to November 2006 whereas FRED stated (28 April 2007) that only 15 bank accounts were being operated and could also not furnish information regarding date/purpose, opening, closing balance etc. in respect of any of the bank accounts. This indicated that the FRED with whose approval these accounts had been opened, was not keeping any watch over the operation of these accounts which is fraught with the risk of fraud and embezzlement of Government money going undetected.

It was further observed that FRED had been approving their proposals under Rule of SFR which talked of opening Personal Deposit Accounts in the bank, which as per accounting classification norms within Government accounts, should have actually remained as a part of Public Accounts within the Government account and not outside as in case of separate bank accounts which was being routinely approved by the FRED. Thus, the Department had inadequate supervisory control over these accounts and also encouraged financial indiscipline by other departments by allowing them to park Government funds in private bank accounts outside Government account. When objected (20 June 2007) to by the Accountant General's office, the FRED appreciated the observation, but replied (6 July 2007) that total ban on operation was subject to certain limitations or directives of Government.

#### *5.1.8.6 Non-adherence to rules governing allotment of pool vehicles*

Home Department, through a notification of January 1997 imposed restrictions on the use of Government vehicles by officers below the rank and level of Joint Secretary to the State Government. These officers were allowed to use departmental pool vehicle, each to be shared by three officers.

Despite issue of requisition for information on the number of vehicles maintained by FRED, it could furnish information as regards the FRED Secretariat only, where it had retained three extra vehicles in contravention of the above norm. Despite retaining excess of two vehicles, the FRED had purchased one more vehicle on 22 December 2004 at an expenditure of Rs. 4.70 lakh.

In reply FRED stated (August 2007) that the question of excess vehicles with the Department did not arise. The reply is not acceptable in view of actual excess number of vehicles[2] on the ground as per records of the Department itself. Non-adherence to this control by the Department itself puts it at a disadvantage while regulating this control in so far as other Departments of the State are concerned.

## 5.1.9 Supervisory controls

### *5.1.9.1 Non-recovery of outstanding dues*

As per Statement No.18 of Finance Accounts 2005-06, an amount of Rs. 49.96 lakh was to be recovered from a private party from the sale proceeds of his own property located at Sikkim under the order of the Supreme Court of India. However, despite being the controlling authority for recovery of such dues to the Government, the amount had not been recovered by the FRED. In reply FRED stated (October 2007) that it had initiated necessary action to recover the due amount.

### *5.1.9.2 Non-adherence to HBA rules regarding recovery*

The Department had been sanctioning House Building Advances (HBA) to the Government employees including All India Service Officers. Out of 755 unsettled HBA cases, the FRED could produce details of only 146 employees involving outstanding loan of Rs. 1.43 crore[3] as on 31 March 2007. Despite requirement of monthly recovery, recoveries were not being made on a regular basis. No correspondence had ever been made with either the loanee or the concerned DDOs about the non-recovery/ missing credits in the loan account. In some loan cases, the FRED failed to close the accounts and continued to recover amount not outstanding in the loan account resulting in minus balance in the account. Neither any directive from FRED regarding non-recovery, irregular recovery, excess recovery etc. was given to the concerned DDOs for taking remedial measures nor had the position ever been reviewed to ascertain the actual loan outstanding. In reply FRED stated (October 2007) that it had initiated action to issue instructions to all defaulters and ensure correct record of recoveries.

### *5.1.9.3 Failure to comply with orders of Supreme Court and irregular annual expenditure of Rs. 30.71 lakh*

In pursuance of the judgments dated 20 September 1994 and 05 October 2001 of the Supreme Court of India regarding drawal of Special Duty Allowance

2 *10 vehicles for above Jt. Secretary and 3 vehicles for 9 officers on pool against which 16 vehicles were maintained.*

3 *(Principle – Rs. 53,13,567 + Interest – Rs. 89,61,063).*

(SDA), the Union Ministry of Finance, issued notifications dated 12 January 1996, 22 July 1998 and 29 May 2002 clarifying the entitlements for payment of SDA to Central Government Civilian employees having all-India transfer liability posted in the North Eastern Region. It was clarified that persons not posted from outside the NE region were not entitled, when posted in NE region including Sikkim, for drawal of SDA. However, all the All India Service Officers, irrespective of whether eligible or not, are drawing SDA. At present, 91 ineligible All India Service Officers in the State Government are drawing SDA at the rate of 12.50 *per cent* of basic pay ever since their posting in Sikkim. The financial implication for such irregular payment worked out to Rs. 30.71 lakh per annum (taking the average basic pay of Rs. 15,000 per month).

In reply FRED stated (October 2007) that the allowance being drawn is conditional and subject to adjustment. However, no recovery had yet been made (October 2007) against the inadmissible payments.

#### *5.1.9.4 Absence of control in the functioning of General Provident Fund (GPF) Section under FRED*

The functioning of the GPF Section was deficient in the following areas:

The Section maintains GPF accounts in respect of all Government servants. However, it is not in a position to close the accounts of all the subscribers and tally the same with the figures of the PAOs and AG (who compiles it from the challans and vouchers sent by the PAOs) as it did not post the details of subscription and recovery of advance from the deduction schedules as received from the Pay and Accounts Offices. At the end of the financial year, the subscribers who could bring their pass books duly certified by the DDOs get their accounts updated leaving the accounts of major portion of subscribers incomplete and unauthenticated.

FRED stated (October 2007) that in the absence of correct account numbers, updated employee data coupled with either delay or non-receipt of deduction schedules from PAOs, the GPF functionaries could not complete the postings and the system of authentication of ledgers was not introduced. The reply is an admission of State of affairs in the GPF Section and in such a situation, the possibility of fraud and mis-appropriation remaining undetected cannot be ruled out. Further, while correctness of account numbers and submission of deduction schedules by PAOs under FRED itself is not ensured as yet, debits, credits and balances being shown under Major Head 8009–GPF in accounts remained unconfirmed. Also, the GPF Section is not in a position to cross check any manipulation in the figures certified by the DDOs.

➢ The figures in Watch Control Register (WCR) and Cheque Drawn Register (CDR) did not match with each other. While accepting the audit observation, the Sr. Accounts Officer stated (14 May 2007) that several measures have been initiated to reconcile the figures of WCR and CDR.

- Despite incurring an expenditure of Rs.11.89 lakh during 2005-06 and 2006-07, the GPF section failed to computerise the GPF information system in its entirety as originally envisaged. The Directorate stated (3 May 2007) that the full GPF package would require some more time before it could incorporate all requirements of the cell.

- GPF Section is also not ensuring recovery of temporary advances from its own employees. The Sr. Accounts Officer stated (14 May 2007) that henceforth the recovery of temporary advances would be affected in time.

This indicated that there was no supervisory control of FRED over the functioning of the GPF Section working under its own administrative control.

### *5.1.9.5 Inadequate controls in the functioning of the General Insurance Scheme (GIS) Section*

The control over subscription, obtaining nomination etc. was deficient as discussed below:

- Rule 18(2) of State Government Employees General Insurance Scheme 1993 required GIS Section of the FRED to maintain class-wise Register for each Department, Head Office-wise/Drawing and Disbursing Officer-wise in Form No.10. Test check of GIS accounts of 3,000 employees showed that in 2,369 cases, recovery of subscription had not been noted in the Register.

- Against 27,260 registered subscribers, the Directorate of GIS had nomination records of only 8,491 subscribers. The Directorate, in consultation with the concerned DDOs, did not evolve any mechanism to ensure that every member under GIS submits his/her nomination in the prescribed format at the time of entry to the scheme.

While accepting the audit observation, FRED stated (October 2007) that in the absence of correct account numbers and timely submission of required schedules, the GIS functionaries could not update the accounts.

Thus, the purpose of maintaining consolidated registers in GIS Section to have a proper check on regular and correct deductions of subscription and payment there against from the fund was completely defeated. Neither the Directorate nor the FRED was found to have paid any heed to the controls prescribed.

### *5.1.9.6 Deficient controls in the functioning of Pension Section*

*Failure to ensure reimbursement of pension payments*

It was seen that an amount of Rs. 1.64 crore was lying unrealised for a long period towards reimbursement of pension payments made by the State Government to central pensioners of Civil and Army Wing from the concerned Accounting authorities. Occasional reminders sent by Pension wing in this respect were neither adequate nor effective. While accepting the audit observation, the Directorate of Pension stated (May 2007) that from now onwards they would pursue the matter by issue of quarterly reminders. Owing to lack of effective supervisory control, the Directorate failed to get the dues of the Government reimbursed in time for the benefit of Government.

### *5.1.9.7 Deficient controls in the functioning of the Chief Pay and Accounts Office (HQ)*

*Failure to ensure proper checking of bills*

As noticed during local audit and reported to the concerned officers/departments through Inspection Reports of the AG, there were numerous instances of excess payments, unauthorised payments, non-deduction of IT, VAT, diversion of funds etc. in the State Government's transactions passed through the PAO. This was despite pre-check system to be exercised in the Pay and Accounts offices.

*Failure to carry correct/complete classification on bills/ vouchers*

PAOs are to satisfy themselves about full and correct classification in the vouchers/challans submitted by DDOs as per the Demand for Grants before admitting any claim for payment. However, actual cases of misclassification, incomplete classifications and passing of bills without budget provision etc. was being regularly pointed out in Treasury Inspection Reports by the Accountant General to the Directorate and the Department from time to time. Thus, these controls to be exercised by the PAOs and the Directorate were lax.

*Failure to inspect treasuries and PAO by the Director*

There was no system prescribed, duly specifying the periodicity, number and authority, of conducting periodical inspection on the functioning of the five treasuries (HQ + 4 Districts) by the Director, PAO. Dy. CPAO (HQ) stated that as far as day to day functioning was concerned, the district CPAOs were functionally independent. However, periodical meetings or short notice meetings were held for discussion and deliberation on various official matters. It indicated that there was no supervisory mechanism to oversee the functioning of the CPAOs by the Directorate, PAO which was fraught with the risk of PAO oriented deficiencies and inadequacies and possibilities of irregular/fraudulent payments remaining undetected.

*Failure to reconcile cash balance*

Cash balance position at the end of 2004-05, 2005-06 and 2006-07 were as under:

**Table – 5.8**

***(Rupees in lakh)***

| Year | State Bank of Sikkim figure | PAO figure | Difference |
|---|---|---|---|
| 2002-03 | 17552.98 | 14954.97 | (+) 2598.01 |
| 2003-04 | 8574.40 | 5808.53 | (+) 2765.87 |
| 2004-05 | 7480.79 | 7352.83 | (+) 127.96 |
| 2005-06 | 15991.53 | 16280.96 | (-) 289.43 |
| 2006-07 | 5491.86 | 5367.77 | (+) 124.09 |

The huge gap in the figures shown by the PAO and the SBS remained un-reconciled for which no reply could be furnished by CPAO, HQ. Absence of any control mechanism to ensure the same is fraught with the risk of fraudulent irregular payments, if any, remaining undetected. This position was being intimated demi-officially to the Additional Chief Secretary-cum-Finance Secretary every month since the accounts for the month of May 2005; but instructions/directives, if any, issued by the FRED to remedy the situation was not found on record. In reply FRED stated (October 2007) that PAO was constantly working to reduce the gap and improve the position.

### 5.1.10 Internal Audit

Internal Audit, as an independent entity within or outside the department is to examine and evaluate the level of compliance to the departmental rules and procedures so as to provide independent assurance to senior management on the adequacy of the risk management and internal control framework in the department. The Directorate of Internal Audit (IA) was established in 1990 under the overall control of the FRED to examine and evaluate the activities of all departments, PSUs of the State Government, Pay and Accounts Office and the Drawing and Disbursing Officers (DDOs)

#### *5.1.10.1 Inadequacies in reporting and follow up of Inspection Reports*

After completion of audits by the IA, the Inspection Reports (IRs) are being sent to FRED and the respective heads of the departments. There was no system of monitoring through monthly progress reports, Objection Books, Monthly/Quarterly Reports and register on settlement of old outstanding observations etc. The follow-up action against audit observations was stated by Director of IA (April 2007) to be dealt with by FRED. But, it was noticed that the FRED itself did not keep any record on follow up of IRs issued by the IA.

For efficient and optimum utilization of the available manpower and financial resources, audit planning was essential for ensuring coverage of all required units over a period of time, duly taking into consideration the available resource and the risks involved in the auditee organizations and their prioritisation accordingly and the time required for audit etc. But it was revealed that no such plan existed. Only 8 PSUs and 10 units were audited (out of 44 departments having 201 DDOs and PSUs) during 2004-05 to 2006-07 and consequently most of the auditee units remained uncovered. Due to non-coverage of auditee units the following risks were not taken care of:

- Improper accounting procedures relating to fund accounts.
- Authenticity for loans and advances.
- Possibilities of frauds or defalcations either individually or in collusion.
- Excess/short payment of Government servants claims.

- Incorrect assessment and non-realisation of Government revenue and dues.
- Improper accounting under different heads of accounts.

The Director stated (April 2007) that due to limited staff as well as additional assignment ordered by the authority, the IA could not undertake the audit as per the Audit Plan. While no documentary evidence of Audit Plan having been prepared and additional assignments having been assigned to the Directorate could be shown to audit, the reply was silent on follow-up action on audit findings and taking remedial measures on manpower constraints.

In the absence of proper audit plan envisaging coverage of all auditee units within a specified time-frame in accordance with prioritisation, and follow-up action/pursuance and monitoring of IRs at the Directorate, the very objective of establishing IA is frustrated and the risks to Government relating to economy, efficiency and effectiveness of financial transactions increases manifold. In reply FRED stated (October 2007) that due to poor response from auditee departments and limited manpower, proper follow up could not be ensured.

### *5.1.10.2 Lack of response to audit*

The AG (Audit), Sikkim arranges to conduct periodic inspection of Government transactions. The audit findings are communicated through Inspection Reports to the head of the Offices/Departments to comply with the audit observations and rectify the defects and promptly report compliance to the AG. A half yearly report on the pending IRs is sent to each Department to facilitate monitoring and compliance with audit observations.

- As per the guidelines, the IA is required to suggest corrective measures for setting right the irregularities, if any, noticed during the course of audit conducted by the Office of the AG with a view to minimizing the quantum of audit objections eventually raised. However, as on 31 March 2007, 856 IRs of AG containing 2042 audit paragraphs pertaining to 1990-91 to 2006-07 remained unsettled for want of satisfactory replies from various departments. This indicated that no effective measures were taken by the IA and no controls were in place for ensuring prompt settlement of audit findings.
- Further, 10 IRs containing 31 paras for the period from 1993-94 to 2006-07 pertaining to FRED itself remained unsettled due to non-furnishing of convincing replies. This indicated that the FRED itself is not serious about the audit observations and enforcing control of internal and external audit to obtain assurance about the functioning of its own departments as well as other departments of Government.

### 5.1.11 Conclusion

*Adequacy and efficacy of various internal controls in the areas of preparation of budget, revenue receipts, arrears of revenue, expenditure, liabilities, cash management, operation of bank accounts, investments and monitoring mechanism were grossly deficient in the Department. The basic checks to be exercised by PAO in the area of propriety, regularity of expenditure, ex-chequer control, proper classification, settlement of previous advances before payment of subsequent advances, issue of cheques etc. were not ensured. Even periodic inspection of treasuries was not ensured. The functioning of GPF, GIS and Pension wings left much to be desired. Internal Audit system, expected to bring reliability and transparency into the internal control mechanism failed in discharging its objectives.*

### 5.1.12 Recommendations

The following recommendations are made:

- Budget Manual should be prepared expeditiously and strict adherence to financial rules and procedures should be ensured.
- Creation of liability without budgetary provision should be strictly avoided. Information about the liability created by any department should be with the knowledge and approval of FRED and strict monitoring and control of the same should be ensured.
- Revenue collection mechanism should be improved and the position of arrears in revenue should be regularly monitored and recovered.
- Balance in GPF Account (MH 8009) has to be cross checked from the balances of the individual account holders. Receipt of deduction schedule from individual DDOs has to be ensured.
- Mechanism for proper watch over payment and recovery of various advances made to the Government servants should be put in place.
- Periodic inspection of treasuries (Pay and Accounts Offices of HQ and 4 districts) by the Director of Treasuries should be introduced.
- Internal Audit System should be streamlined and vitalised to improve risk management and internal control framework in the Department.