CHAPTER I
INTRODUCTION

1.1 About this Report

This Report of the Comptroller and Auditor General of India (C&AG) relates to matters arising from performance audit of selected programmes and activities and compliance audit of Government departments and autonomous bodies.

Compliance audit refers to examination of transactions relating to expenditure of the audited entities to ascertain whether the provisions of the Constitution of India, applicable laws, rules, regulations and various orders and instructions issued by the competent authorities are being complied with. On the other hand, performance audit, besides conducting a compliance audit, also examines whether the objectives of the programme/activity/department are achieved economically and efficiently.

The primary purpose of the Report is to bring to the notice of the State Legislature, important results of audit. Auditing Standards require that the materiality level for reporting should be commensurate with the nature, volume and magnitude of transactions. The findings of audit are expected to enable the Executive to take corrective actions as also to frame policies and directives that will lead to improved financial management of the organisations, thus, contributing to better governance.

This chapter, in addition to explaining the planning and extent of audit, provides a synopsis of the significant deficiencies and achievements in implementation of selected schemes, significant audit observations made during the audit of transactions and follow-up on previous Audit Reports.

1.2 Profile of units under audit jurisdiction

There are 36 departments in the State at the Secretariat level, headed by Additional Chief Secretaries/Principal Secretaries/Secretaries, who are assisted by Directors/Commissioners and subordinate officers under them, and 23 autonomous bodies which are audited by the Principal Accountant General (Civil and Commercial Audit), Thiruvananthapuram.

The comparative position of expenditure incurred by the Government during the year 2010-11 and in the preceding two years is given in **Table 1.1**.

Table 1.1: Comparative position of expenditure

(₹ in crore)

Disbursements	2008-09			2009-10			2010-11		
	Plan	Non plan	Total	Plan	Non plan	Total	Plan	Non plan	Total
Revenue expenditure									
General Services	158.95	12508.42	12667.37	370.83	13564.69	13935.52	184.43	15233.96	15418.39
Social Services	1910.30	7452.54	9362.84	2347.98	8119.17	10467.15	2505.61	9605.19	12110.80
Economic Services	1142.61	2785.92	3928.53	1460.24	2780.48	4240.72	1505.70	2851.76	4357.46
Grants-in-aid and contributions	---	2265.12	2265.12	---	2488.98	2488.98	---	2778.16	2778.16
Total	**3211.86**	**25012.00**	**28223.86**	**4179.05**	**26953.32**	**31132.37**	**4195.74**	**30469.07**	**34664.81**
Capital Expenditure									
Capital outlay	1670.76	24.84	1695.60	1902.16	157.23	2059.39	2765.66	598.03	3363.69
Loans and advances disbursed	579.25	404.44	983.69	704.20	172.48	876.68	319.31	442.43	761.74
Repayment of public debt[1]			1650.34	---	---	1765.06			1975.03
Contingency Fund			5.84	---	---	26.27			33.92
Public Account disbursements			53627.80	---	---	57271.53			70558.27
Total			**57963.27**			**61998.93**			**76692.65**
Grand Total			**86187.13**			**93131.30**			**111357.46**

1.3 Authority for Audit

The authority for audit by the C&AG is derived from Articles 149 and 151 of the Constitution of India and the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971. C&AG conducts audit of expenditure of the departments of the Government of Kerala under Section 13[2] of the C&AG's (DPC) Act. C&AG is the sole auditor in respect of 23 autonomous bodies which are audited under sections 19(2)[3] and 20(1)[4] of the C&AG's (DPC) Act. In addition, C&AG also conducts audit of 231 other autonomous bodies, under Section 14[5] of C&AG's (DPC) Act, which are substantially funded by the Government. Principles and methodologies for various audits are prescribed in the Auditing Standards and the Regulations on Audit and Accounts, 2007 issued by the C&AG.

[1] Excluding net transactions under ways and means advances

[2] Audit of (i) all transactions from the Consolidated Fund of the State, (ii) all transactions relating to the Contingency Fund and Public Accounts and (iii) all trading, manufacturing, profit & loss accounts, balance sheets & other subsidiary accounts.

[3] Audit of the accounts of Corporations (not being Companies) established by or under law made by the State Legislature in accordance with the provisions of the respective legislations.

[4] Audit of accounts of any body or authority on the request of the Governor, on such terms and conditions as may be agreed upon between the C&AG and the Government.

[5] Audit of all (i) receipts and expenditure of a body/authority substantially financed by grants or loans from the Consolidated Fund of the State and (ii) all receipts and expenditure of any body or authority where the grants or loans to such body or authority from the Consolidated fund of the State in a financial year is not less than ₹ one crore.

1.4 Organisational structure of the Offices of the Principal Accountant General (C&CA) and Accountant General (WF&RA), Kerala

Under the directions of the C&AG, the offices of the Principal Accountant General (C&CA) and Accountant General (WF&RA), Kerala conduct audit of Government departments/offices/autonomous bodies/ institutions under them, which are spread all over the State. The Principal Accountant General and Accountant General are assisted by three Group Officers.

1.5 Planning and Conduct of Audit

The audit process starts with the assessment of risks faced by various departments of Government based on expenditure incurred, criticality/ complexity of activities, level of delegated financial powers, assessment of overall internal controls and concerns of stakeholders. Previous audit findings are also considered in this exercise. Based on this risk assessment, the frequency and extent of audit are decided.

After completion of audit of each unit, Inspection Reports containing audit findings are issued to the heads of the departments. The departments are requested to furnish replies to the audit findings within four weeks from the date of receipt of the Inspection Reports. Whenever replies are received, audit findings are either settled or further action for compliance is advised. The important audit observations arising out of these Inspection Reports are processed for inclusion in the Audit Reports, which are submitted to the Governor of State under Article 151 of the Constitution of India.

During 2010-11, 13,006 party-days were used to carry out audit of 1,942 units (compliance audits and performance audits) of the various departments/ organisations. The audit plan covered those units/entities which were vulnerable to significant risks as per our assessment.

1.6 Significant Audit Observations

In the last few years, Audit has reported on several significant deficiencies in implementation of various programmes/activities through performance audits, as well as on the quality of internal controls in selected departments which impact the success of programmes and functioning of the departments. Similarly, the deficiencies noticed during compliance audit of the Government departments/organisations have also been reported upon.

1.6.1 Performance audits of programmes/activities/departments

The present Report contains the findings of a district-centric audit of Palakkad District; one long paragraph regarding the Kerala State Transport Project; a thematic review of the implementation of the scheme 'Special Development Fund for Members of Legislative Assembly'; another thematic review on the compliance of Standards of Weights and Measures Acts and Rules by the Legal Metrology Department and a Chief Controlling Officer-based audit of the Directorate of Industries and Commerce. The highlights are given in the following paragraphs.

1.6.1.1 District-centric Audit of Palakkad District

With increasing investment by the Governments with districts as the focal points, a district-centric audit was conducted in Palakkad District to assess the status and impact of implementation of various socio-economic developmental programmes there. The District Planning Committee (DPC) was required to prepare an Integrated District Development Plan (IDDP) for the district and finalise local development plans (LDPs) for local self-government institutions (LSGIs). The DPC had not prepared either an IDDP or LDPs as a result of which, gaps in various developmental schemes remained unidentified. There was no system in place at the district level to have a consolidated picture of the year-wise funds received and utilised under various schemes implemented in the district. The district had six hospitals, one Tribal Speciality Hospital, 20 Community Health Centres, 75 Primary Health Centres and 504 Sub Centres. Adequate manpower and infrastructure as per the Indian Public Health Standards were not provided. Medical instruments supplied were not properly utilised. Despite the intervention of the Sarva Shiksha Abhiyan, strength of students in Government/aided schools decreased and the strength of students in unaided schools recorded increases. Nine water supply schemes taken up under the Accelerated Rural Water Supply Programme to benefit a population of 2.93 lakh in nine panchayats remained incomplete due to improper planning. Quality tests of water samples of the Comprehensive Water Supply Scheme (CWSS) to Nemmara and Ayilur showed the presence of bacteria and other impurities. Inordinate delays were noticed in the completion of houses taken up by the Scheduled Castes (SCs) and Scheduled Tribes (STs) Development Department under housing schemes for SCs and STs. In respect of the Special Development Fund for Members of Legislative Assembly, several works remained incomplete for reasons like non-availability of materials, public objections, vagaries of nature etc. In the Attappady Wasteland Comprehensive Environmental Conservation Project, delays were noticed in completion of houses and several assets created by AHADS were lying unutilised or had not been handed over to the beneficiary departments. The e-District programme had not been fully implemented. Only 23 out of 46 Government services envisaged under e-District programme were made available in 97 villages out of 156 villages.

(Paragraph 2.1)

1.6.1.2 Kerala State Transport Project

The Kerala State Transport Project (KSTP), aided by the International Bank for Reconstruction and Development (IBRD), was launched in June 2002 by the Government for improving the infrastructure in the State road sector. The main thrust of the project was to upgrade the State roads by widening and strengthening 578.90 km of roads and by providing maintenance to 1,009 km of roads.

Audit scrutiny of the implementation of the project revealed that in the case of corridor upgradation works, targets were reset midway by reducing more than 50 *per cent*. Defective planning in land acquisition process resulted in non-availability of land for execution of works. Indecision of KSTP resulted in hardship to the public and extra expenditure of ₹ 60.75 crore in an upgradation work for KSTP I. KSTP also paid price adjustment claims of ₹ 12.56 crore violating contract conditions.

(Paragraph 2.2)

1.6.1.3 Special Development Fund for Members of Legislative Assembly

The 'Special Development Fund for Members of Legislative Assembly' was launched by the State Government in October 2001 to enable Members of the Legislative Assembly (MLAs) to create durable assets for public use at large. The annual allotment under the scheme to each MLA was ₹ 75 lakh per annum. The scheme was fully funded by the State Government and the funds released were non-lapsable.

An audit of the implementation of the scheme revealed that the utilisation of funds during 2006-11 was in the range of 28 to 38 *per cent* of the available funds. In 21 *per cent* of the works sanctioned by the District Collectors of four districts selected for audit, the delays in issue of administrative sanctions were more than six months from the dates of receipt of proposals from MLAs. Audit noticed execution of works prohibited under the guidelines. The large number of relaxations accorded for taking up works prohibited under the guidelines was indicative of lack of sanctity for the guidelines. The works were seen to have been entrusted to societies/trusts without entering into formal agreements with them. Monitoring at the district level was not done as envisaged in the guidelines.

(Paragraph 2.3)

1.6.1.4 Compliance of Standards of Weights and Measures Acts and Rules by the Legal Metrology Department

The Standards of Weights and Measures Act, 1976 provide for the establishment of standards of weights and measures and the Standards of Weights and Measures (Enforcement) Act, 1985 provides for the enforcement of the provisions of the Act in the country. The Standards of Weights and Measures (Packaged Commodities) Rules, 1977 regulate the sale of commodities in a packaged form. These Acts and the Rules stipulate consumer protection in respect of weights and measures used in trade and commerce. The Legal Metrology Department in the State is the authority which implements the above enactments so as to protect consumers from exploitation and unfair trade practices.

Scrutiny by Audit regarding compliance of provisions in the various Acts/Rules relating to the Legal Metrology Department revealed delays in utilisation of Central funds, inadequate verification of auto-rickshaw fare meters, deficiencies in inspection of petrol pumps and 'net content' in packages. There was lack of proper follow-up action in prosecution cases.

(Paragraph 2.4)

1.6.1.5 Chief Controlling Officer based audit of Directorate of Industries and Commerce

The Directorate of Industries and Commerce is responsible for promoting/sponsoring, registering, financing and advising micro, small and medium enterprises in the State. Creation of a conducive environment is essential for the rapid industrialisation of the State. The micro, small and medium enterprises (MSME) sector contributes significantly to the manufacturing output and employment opportunity in the country. Deficiencies were noticed in monitoring of industrial plots allotted to entrepreneurs. Financial assistance by way of margin money loans, State investment subsidies and share capital contribution were disbursed without assessing the capability of the beneficiary to utilise the amount for the intended purpose. No effective safeguards were put in place to recover the funds in case of non-adherence to the stipulated conditions. This resulted in very high default rates in repayment of loans and retirement of share capital contribution. Delays ranging from four to 34 months were noticed in sanctioning of State investment subsidies. The internal control mechanism in the Directorate was not effective.

(Paragraph 4.1)

1.6.2 Compliance audit of transactions

Audit also found several significant deficiencies in critical areas which could impact the effective functioning of the departments. These are broadly categorised and grouped as:

- Non-compliance with rules
- Audit against propriety/expenditure without justification
- Persistent and pervasive irregularities
- Failure of oversight/governance

1.6.2.1 Non-compliance with rules

For sound financial administration and financial control, it is essential that expenditure conforms to financial rules, regulations and orders issued by the competent authority. This not only prevents irregularities and misappropriation and frauds, but helps in maintaining good financial discipline. This report contains instances of non-compliance with rules involving ₹ 2.33 crore. Some significant audit findings are as under:

- Failure to comply with the provisions of Income Tax Act, 1961 by the Sree Sankaracharya University of Sanskrit led to loss of interest amounting to ₹ 92.15 lakh accrued on its deposits.

  (Paragraph 3.1.1)

- Non-compliance with the provisions of the Stores Purchase Manual resulted in short collection of cost of tender forms amounting to ₹ 63.24 lakh in Infopark and the Malabar Cancer Centre.

  (Paragraph 3.1.2)

- Excess payment of ₹ 77.46 lakh was made to contractors due to non-recovery of overhead charges and contractor’s profit on the cost of bitumen in seven works executed by two Public Works Roads Divisions (Muvattupuzha and Thrissur) and two National Highway Divisions (Muvattupuzha and Kodungallur).

(Paragraph 3.1.3)

1.6.2.2 Audit against propriety/expenditure without justification

Authorisation of expenditure from public funds is to be guided by the principles of propriety and efficiency of public expenditure. Authorities empowered to incur expenditure are expected to enforce the same vigilance as a person of ordinary prudence would exercise in respect of his own money and should enforce financial order and strict economy at every step. Audit has detected instances of impropriety and extra expenditure involving ₹ 39.54 crore, some of which are as under:

- The Director of Industries and Commerce released ₹ 2.56 crore in March 2009 to a Special Purpose vehicle for setting up a Common Effluent Treatment Plant even before taking possession of land for the purpose which resulted in blocking of Government money outside Government account for over two years and the objective of reducing pollution of Periyar river could not be achieved.

(Paragraph 3.2.1)

- Undue favour was extended to Pinarayi Industrial Co-operative Society by giving financial assistance of ₹ two crore initially in the form of loan and subsequently converting the loan as share capital participation, in gross violation of rules and instructions.

(Paragraph 3.2.2)

- An expenditure of ₹ 28.66 crore was incurred by the Information and Public Relations Department during 2010-11 on display advertisements, violating the canons of financial propriety, rules of empanelment and norms for release of advertisements.

(Paragraph 3.2.3)

- Payment of enhanced rates of cement and steel amounting to ₹ 59.42 lakh made to a contractor for the work of construction of the Olassery-Palayangad Road, including a bridge across Chitturpuzha at Palayangad' in Palakkad district was beyond the scope of the contract agreement.

(Paragraph 3.2.4)

- Erroneous calculation of rebate at the time of payment for an item of work 'widening and improvement of riding quality of a major district road' in Thiruvananthapuram district under the Central Road Fund Scheme resulted in excess payment of ₹ 65.03 lakh to a contractor.

(Paragraph 3.2.5)

- The Kerala Water Authority allowed irregular refund of works contract tax amounting to ₹ 50.95 lakh to M/s.Noble Tech Engineering (P) Limited in violation of statutory provisions.

(Paragraph 3.2.6)

- Due to abnormal delays in finalisation of tenders, the department could not consider the lower rates offered by some bidders, resulting in avoidable extra expenditure of ₹ 4.57 crore in four canal works of the Idamalayar Irrigation Project.

(Paragraph 3.2.7)

1.6.2.3 Persistent and pervasive irregularities

An irregularity is considered persistent if it occurs year after year. It becomes pervasive when it is prevailing in the entire system. Recurrence of irregularities, despite being pointed out in earlier audits, is not only indicative of non-seriousness on the part of the Executive but is also an indication of lack of effective monitoring. This, in turn, encourages wilful deviations from the observance of rules/regulations and results in weakening of the administrative structure.

- Against the admissible rate of ₹ 150 per month, the employees working in the headquarters of Calicut, Kannur and Mahatma Gandhi Universities which are situated in unclassified cities were paid HRA ranging from ₹ 250 to ₹ 1200 applicable to B class cities, resulting in excess payment amounting to ₹ 2.70 crore.

(Paragraph 3.3.1)

1.6.2.4 Failure of oversight/governance

The Government has an obligation to improve the quality of life of the people for which it works towards fulfilment of certain goals in the area of health, education, development and upgradation of infrastructure and public service, etc. However, Audit noticed instances where the funds released by the Government for creating public assets for the benefit of the community remained unutilised/blocked and/or proved unfruitful/unproductive due to indecisiveness, lack of administrative oversight and concerted action at various levels involving ₹ 144.07 crore. A few such cases are mentioned below:

- Release of ₹ 1.05 crore to the Kerala State Seed Development Authority by the Director of Agriculture for construction of five seed storage godowns and two seed processing units even before ensuring availability of land resulted in blocking of funds during the period March 2003 to June 2009. Besides, ₹ 1.19 crore was incurred towards hire charges of godowns from April 2004 to March 2011.

(Paragraph 3.4.1)

- Rupees three crore released to District Collectors of Kollam, Thrissur and Kannur for protecting an ecologically fragile mangrove ecosystem remained unutilised for more than four years.

(Paragraph 3.4.2)

- Effective functioning of the Vigilance & Anti - Corruption Bureau has the potential to yield substantial benefits to the Government. The constraints faced by the VACB at various stages of its operations have seriously impaired achievement of the objective of effectively combating corruption and misconduct by Government servants and public servants.

(Paragraph 3.4.3)

- Acceptance of bank guarantees (₹ 2.62 crore) without taking possession of documents relating to their verification resulted in non-detection of their not being genuine.

(*Paragraph 3.4.4*)

- Failure of the Government in selecting suitable land for development of an Information Technology Park based on environment considerations led to abandonment of the site after incurring an expenditure of ₹ 2.61 crore and subsequent relocation of the park to an alternative site.

(*Paragraph 3.4.5*)

- The Thiruvananthapuram City Road Improvement project remained incomplete even after seven years of award of a contract to the Thiruvananthapuram Road Development Company Limited. The Government had already incurred arbitration liability of ₹ 125 crore (as against the estimated cost of ₹ 140 crore) towards escalation cost, idling of resources, delay in handing over land, etc.

(*Paragraph 3.4.6*)

- The Public Works Department carried out surface renewal works on the Palakkad-Meenakshipuram Road (State highway) immediately before the execution of heavy maintenance work under the Kerala State Transport Project, which resulted in wasteful expenditure of ₹ 73.19 lakh.

(*Paragraph 3.4.7*)

- Execution of a work without proper investigation and delay in rearranging the balance work rendered the foundation work of Muttakavu Bridge in Kollam-Ayoor Road, already executed at ₹ 52.39 lakh wasteful and also created additional financial commitment of ₹ 74.03 lakh due to change in design of the foundation.

(*Paragraph 3.4.8*)

- Failure to install static capacitors/capacitors with sufficient rating by Kerala Water Authority and other departments resulted in avoidable expenditure of ₹ 6.61 crore towards power factor penalty.

(*Paragraph 3.4.9*)

1.7 Lack of responsiveness of Government to Audit

1.7.1 Outstanding Inspection Reports

The Handbook of Instructions for Speedy Settlement of Audit Objections/Inspection Reports issued by the State Government in 2010 provides for prompt response by the Executive to the Inspection Reports (IRs) issued by the Accountant General (AG) to ensure rectificatory action in compliance with the prescribed rules and procedures and accountability for the deficiencies, lapses, etc., noticed during the inspection. The Heads of Offices and next higher authorities are required to comply with the observations contained in the IRs, rectify the defects and omissions promptly and report their compliance to the Principal Accountant General within four weeks of receipt of the Inspection Report. Half-yearly reports of pending IRs are being sent to the Secretary of the Department to facilitate monitoring of the audit observations.

As of 30 June 2011, 627 IRs (2,475 paragraphs) were outstanding against Collegiate Education, Industries and Water Resources Departments. Year-wise details of IRs and paragraphs outstanding are detailed in **Appendix 1.1.**

A review of the IRs pending due to non-receipt of replies, in respect of these three departments revealed that the Heads of Offices had not sent even the initial replies in respect of 189 IRs containing 1,054 paragraphs issued between 2003-04 and 2010-11.

1.7.2 Response of departments to the draft paragraphs

Draft Paragraphs and Reviews were forwarded demi-officially to the Principal Secretaries/Secretaries of the departments concerned between May and September 2011 with a request to send their responses within six weeks. The departmental replies for none of the five reviews and only six out of 20 paragraphs featured in this Report were received. These replies have been suitably incorporated in the Report.

1.7. 3 Follow-up on Audit Reports

The Finance Department issued (April 1997) instructions to all administrative departments of the Government that they should submit Statements of Action Taken Notes on audit paras included in the Audit Reports directly to the Legislature Secretariat with copies thereof to the Audit Office within three months of their being laid on the Table of the Legislature.

The administrative departments did not comply with the instructions and 14 departments, as detailed in **Appendix 1.2,** had not submitted Statements of Action Taken for 44 paragraphs for the period 2007-08 to 2009-10 even as of September 2011.

1.7. 4 Paragraphs to be discussed by the Public Accounts Committee

The details of paragraphs pending discussion by the Public Accounts Committee as of September 2011 are given in **Appendix 1.3.**