

## CHAPTER III

### 3. Compliance audit observations

Important audit findings emerging from test check of transactions made by the State Government companies/ Statutory corporations have been included in this chapter.

#### Government companies

#### 3.1 Implementation of Vizhinjam International Deepwater Multipurpose Seaport Project

##### Introduction

**3.1.1** The project for developing an International Deepwater Seaport at Vizhinjam located on the south western coast of Kerala near the State capital Thiruvananthapuram is two decades old. The project was initially proposed to be implemented directly by Government of Kerala (GoK). The first global tender in 2003-04 issued by GoK did not succeed. Vizhinjam International Seaport Limited (VISL), a company fully owned by GoK, was constituted in 2004 as implementing Agency for the project. The subsequent tenders in 2007 and 2011 issued by VISL to execute the project through Public-Private Partnership (PPP) mode were also not successful. GoK approved (November 2013) a new model as suggested by the Technical Consultants, AECOM India Private Limited (AECOM) for development of the project. As per the new model, development and operation/ maintenance of Vizhinjam International Deepwater Multipurpose Seaport Project through PPP were proposed on Design, Build, Finance, Operate and Transfer (DBFOT) basis. The Project was to be implemented as a landlord port model, wherein the land procurement, external infrastructure and construction of breakwater<sup>1</sup> would be undertaken by GoK through VISL, the implementing agency for the project. The chosen private Concessionaire shall be responsible for funding and development of dredging and reclamation (53 hectares) of land from the sea, construction of berths, roads, substations, superstructure and equipment and for operation of the Port.

Accordingly, VISL invited (December 2013) two International Competitive Bids (ICB)/ Global Tenders; one for selection of PPP Concessionaire and one for selection of Engineering, Procurement and Construction (EPC) contractor for the construction of breakwater and external infrastructure. The tender for EPC was not pursued by GoK since it was included in the PPP part. Against Request for Qualification (RFQ) for selection of PPP Concessionaire, five<sup>2</sup>

<sup>1</sup> Breakwaters are structures constructed on coasts as part of coastal defense or to protect an anchorage from the effects of both weather and long shore drift. Breakwaters reduce the intensity of wave action in inshore waters and thereby reduce coastal erosion or provide safe harbourage.

<sup>2</sup>Adani Ports and SEZ Limited, Comcast - Hyundai Consortium, ESSAR Ports Limited, Gammon Infrastructure Projects Limited and SREI- OHL Consortium.

applicants submitted RFQ and all were shortlisted based on the financial and technical qualification criteria. Three out of the five qualified bidders purchased the Request for Proposal (RFP). RFP document approved<sup>3</sup> by GoK was issued along with the Draft Concession Agreement (DCA) and Manual of Specifications and Standards to the three bidders. The estimated total project cost (TPC) of the project was pegged at ₹4,089 crore, excluding the cost of funded works. According to the terms of RFP, selection of bidder was to be based on the highest premium offered to GoK or lowest grant demanded from GoK. Maximum grant that can be demanded by way of Viability Gap Funding (VGF)<sup>4</sup> was capped at ₹1,635 crore, being 40 per cent of the TPC.

Adani Ports and SEZ Private Limited (APSPL) was the lone bidder with a quoted grant amount of ₹1,635 crore. The Letter of Award was issued (July 2015) to APSPL and the Concession Agreement was signed between Adani Vizhinjam Port Private Limited<sup>5</sup> (Concessionaire) and the GoK on 17 August 2015. The GoK also signed (16 January 2016) an agreement with VISL conferring VISL full powers and authority of the GoK under the Concession Agreement.

### Features of the Project

3.1.2 Salient features of the project are highlighted in *Table 3.1*.

**Table 3.1: Total cost of the Project and its funding**

Sl. No.	Nature of work	Total cost (₹ in crore)	Funding pattern
1	Dredging and reclamation, development of berths, roads, substations, superstructure and equipment and operation	4,089	₹2,454 crore by the Concessionaire and ₹1,635 crore through VGF equally by Government of India and GoK. The project was to be implemented in four phases <sup>6</sup> with a rated capacity of 6 lakh (0.6 million) TEUs <sup>7</sup> on commercial operation date (COD), to be enhanced to one million TEUs within 10 years of COD. The port shall be capable of accommodating vessels with capacity up to 18,500 TEUs. The Concession period would be 40 years commencing from the Appointed Date <sup>8</sup> which shall be extendable for further 20 years at the option of the Concessionaire subject to capacity augmentation to three million TEUs by 30 <sup>th</sup> year of the concession period.
2	Funding and Development of breakwater and fishing harbour	1,463	The construction of 3.1 kilometre (km) long breakwater and a new fishing harbour would also be done by the Concessionaire as “funded works” for which the GoK would finance the entire amount of ₹1,463 crore.
3	Cost of external infrastructure	1,973	Entire funding by GoK.
	<b>Total</b>	<b>7,525</b>	

<sup>3</sup> Vide Order No. G.O (MS) No.36/2014/F&PD dated 12 May 2014.

<sup>4</sup> Viability Gap Funding is designed to provide capital support to PPP projects which would not otherwise be financially viable. VGF has the effect of reducing the revenue required to recover costs and provide a financially attractive return for the private partner.

<sup>5</sup> Company incorporated as a subsidiary of APSPL.

<sup>6</sup> Phase I-1 MTEU, Phase II-1.5 MTEU, Phase III-2.2 MTEU and Phase IV-3 MTEU.

<sup>7</sup> Twenty Foot Equivalent Units.

<sup>8</sup> As defined in the Concession Agreement, the date on which Financial Close is achieved and every Condition Precedent is either satisfied or waived.

As per the terms of the Concession Agreement, the project shall commence commercial operation within four years of signing (August 2015) the agreement i.e., by 2019.

Government of India (GoI) granted in-principle sanction for VGF of ₹817.50 crore which shall be released within five years of the Appointed Date (5 December 2015).

- The GoK will receive one *per cent* of the total Realisable Fee annually starting from the 15<sup>th</sup> anniversary of Commercial Operation Date (COD) (i.e., 16 August 2019). Revenue share of the GoK will be increased by one *per cent* of the total Realisable Fee every subsequent year, subject to a maximum of 40 *per cent*.

Twenty *per cent* of the annual revenue received by the GoK would be repaid to the GoI till full settlement of the VGF share of ₹817.50 crore.

- The Concessionaire can utilise 30 *per cent* of the land acquired for the project by GoK for “Port Estate Development” which may include residential and commercial buildings/ space. The Concessionaire would pay 10 *per cent* of the annual revenue earned from such ventures to the GoK starting from the seventh year after COD.
- The GoK would ensure availability of land for the project and also provide rail and road connectivity.

Against the above background, we analysed the conceptualisation, award of work and Concession Agreement. The audit objectives were to assess whether:

- i. tendering process was competitive, equitable, fair and transparent; and
- ii. the key clauses of the concession agreement were drawn up in such a way as to allocate risks and benefits between the Concessionaire and GoK in a balanced manner.

Revenue/ cash flows of the Vizhinjam project for 40 years of the concession period were estimated as part of the feasibility study conducted (April 2015) by Ernst & Young (E&Y), the financial consultants appointed by VISL. All calculations in respect of cash flows from the project included in succeeding paragraphs were based on the revenue projections appearing in the E&Y Report.

### **Audit Findings**

**3.1.3** Audit findings are discussed below.

### **Preparation of cost estimates and viability of the project**

**3.1.4** We examined the reasonableness of cost and viability of the project and the findings are discussed below:

- The TPC worked out (September 2015) for the development of Colachel Port in Tamil Nadu, which is proposed to be located at an approximate distance of 50 km from the Vizhinjam project site was ₹3,693.48 crore<sup>9</sup> for a capacity of 1.6 million twenty-foot equivalent units (MTEU), which translates to ₹2,308.43 crore per MTEU. Compared to this, TPC per MTEU for Vizhinjam Port was higher (₹3,271<sup>10</sup> crore), mainly due to unreasonable and unjustified rates adopted for estimating the cost of equipment as detailed below.
- ✓ Final TPC of ₹4,089 crore was worked out based on Basic Engineering Report (BER)<sup>11</sup> prepared by AECOM. While preparing the BER in December 2014, AECOM hiked the rates of equipment included in the Detailed Project Report (2013) from ₹631.87 crore to ₹934.61 crore. However, there was nothing on record to justify the increase. We worked out the reasonable cost of eight equipment by taking the rates in the DPR (2013) as base, allowing 5 per cent year on year escalation from 2013 to 2014 and adopting the exchange rate as 1 USD = 64 INR (Rate as on 31 December 2014) at ₹825.65 crore as detailed in **Appendix 9**. We observed that the equipment cost was unreasonably hiked by AECOM while preparing the BER. The net increase over reasonable cost was ₹130.85 crore<sup>12</sup>. This has also resulted in excess grant of ₹52.34 crore to the Concessionaire (40 per cent of ₹130.85 crore).

GoK replied (August 2016) that the equipment meant for a Container Transshipment Port were generally imported and not indigenously developed by Indian manufacturers. Even if manufactured indigenously, it would involve significant foreign exchange component. As such, AECOM had also taken into account the fluctuation in foreign exchange for revision of cost.

The reply was not acceptable since we accounted for the variation in exchange rates while working out the reasonable cost. Further, the actual basis of revision of cost of equipment was not made available by AECOM. VISL/ GoK accepted the estimates in the DPR/ BER prepared by the external consultants *in toto*.

- ✓ As per data collected by Audit, per unit cost of Rail Mounted Quay Crane (RMQC)<sup>13</sup>, a major equipment for Container Transshipment, procured (2013) by Jawaharlal Nehru Port Trust (JNPT), Mumbai for their project was ₹32.26 crore. Even after allowing for year on year escalation, the rate would be ₹37.34 crore per unit in 2014, whereas base cost of the same equipment as included in the cost estimates of Vizhinjam project was ₹75.44

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<sup>9</sup> Excluding cost of breakwater and external infrastructure and interest during construction.

<sup>10</sup> Total Project Cost- ₹4,089 crore less Interest during construction - ₹818 crore.

<sup>11</sup> BER prepared (December 2014) by AECOM describes the basic engineering carried out for the various components of the port facility.

<sup>12</sup> ₹108.96 crore plus proportionate escalation and Interest During Construction.

<sup>13</sup> RMQC Specification: Super Post Panamax with outreach of 65 metres.

crore. Thus, for eight RMQCs required for the Vizhinjam project, there was excess cost estimation to the extent of ₹304.80 crore.

GoK replied (August 2016) that the RMQCs compared in the audit finding (that of JNPT) do not cater to design vessels of size 18,000 TEU and were, therefore, cheaper. GoK also asserted that the Consultants, AECOM, had arrived at the base cost of RMQC after taking into account budgetary proposals and experience of similar projects in the past.

The reply was not acceptable because the RMQCs installed at JNPT were of specification “Super Post Panamax” having an outreach of 65 metres. The RMQCs proposed to be procured for Vizhinjam Port are of the same specifications.

- ✓ Similarly, the cost of Reach Stacker per unit included in the TPC of Vizhinjam project was ₹3.31 crore (base price) whereas the Directorate of Ports, GoK had purchased the same item in March 2014 (delivered in March 2015) at a landed cost of ₹2.35 crore only.

GoK stated (August 2016) that the Reach Stackers to be procured for Vizhinjam project were for heavy duty transshipment use. The reply was not acceptable because the reach stackers procured by the Directorate of Ports were capable of such use as evident from the specifications attached to the e-tender notice.

### Development of funded works

**3.1.5** Development of breakwater and fishing harbour was initially planned to be executed through Engineering Procurement and Construction (EPC) contract as a separate work. As per the terms of the tender, the Concessionaire had the right of first refusal (ROFR) for the EPC contract if its bid was within 15 *per cent* of the lowest bid. Subsequently, following adoption of Model Concession Agreement (MCA<sup>14</sup>) for PPP projects in the Ports Sector, tender for EPC contract was cancelled (August 2015). The construction of breakwater and fishing harbour was included as funded work as part of the PPP project to be executed by the Concessionaire at a cost of ₹1,463 crore. The entire cost of funded work was to be borne by GoK.

Due to cancellation of EPC tender, GoK could not assess the market rate for executing the work. The work was, thus, awarded to the Concessionaire at the estimated cost. We noticed that:

- the cost (₹767 crore) of breakwater and fishing harbour estimated (May 2013) by AECOM for EPC contract was revised (March 2014) to

<sup>14</sup> MCA is a regulatory framework for sustaining private investment in PPP projects. MCA addresses issues such as mitigation and unbundling of risks, allocation of risks and rewards; symmetry of obligations between the principal partners; precision and predictability of costs and obligations; reduction of transaction costs; *force majeure* and termination (Source: [www.planningcommission.gov.in/reports/genrep/overviewMCA.pdf](http://www.planningcommission.gov.in/reports/genrep/overviewMCA.pdf)).

₹1,210 crore to account for exchange rate fluctuations. The cost was again revised (April 2015) to ₹1,463 crore after acceptance of the concept of funded works. There was no justification for applying exchange rate variation on indigenously sourced material such as rocks and concrete armour units.

GoK replied (August 2016) that the cost of funded work was earlier set as ₹1,210 crore at 2014 level. Considering the risks and cost involved, prospective bidders requested for an upward revision to the tune of ₹1,500 crore at 2015 level. Based on the recommendation of the Financial Consultant and the Technical Consultant, Empowered Committee (EC)<sup>15</sup> of Secretaries to GoK decided to revise the cost of Funded works to ₹1,463 crore at 2015 level. GoK also stated that cost of funded works was increased to minimise the VGF quoted in the PPP tender.

The reply was not acceptable because in spite of increasing the cost of funded works, only one bid was received and that too quoting the highest possible grant. Thus, increase in the cost of funded work did not result in lower grant. The reply is also silent about the justification for applying exchange rate variation to rocks, etc., to be procured indigenously.

- The cost estimates (₹312.85 crore) prepared by AECOM for the rocks to be used for the construction of breakwaters was on the higher side. The cost (₹250.48 crore) based on market rates prevailing in Kerala as per Harbour Engineering Department (HED) database was significantly low. The difference between rates worked out to ₹62.37 crore.

GoK stated (August 2016) that considering the large volume, larger lead and difference in the method of placement of rock, method adopted for blasting, extraction, sorting, transportation, loading, unloading, inclement weather, etc., higher rates for rock in the case of Vizhinjam Project was not comparable with rates in HED database.

The reply is not acceptable as we had compared only the cost of rocks of similar weight and other specifications included in HED database and AECOM's estimates.

## **Financial and Economic Viability of the Project**

**3.1.6** Net Present Value (NPV) shows the difference between a project's financial benefits and costs in current money terms. Only projects with positive NPV should be developed because negative NPV would mean that the costs are greater than the benefits. Internal Rate of Return (IRR) is the rate at which financial benefits accrue from an investment.

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<sup>15</sup> Constituted by GoK for evaluation of bids received.

Economic IRR (EIRR) and Economic NPV (ENPV) also take into account the perceived economic costs and benefits of a project such as employment generation, infrastructure development, etc., in addition to financial costs and benefits. According to the guidelines issued by the Ministry of Finance, GoI for PPP projects, NPV and EIRR provide a decision criterion on whether the project should proceed at all. In general, a project with a negative NPV should not be pursued.

A comparison of investment and NPV/ IRR<sup>16</sup>/ EIRR<sup>17</sup> of GoK *vis-a-vis* the Concessionaire is given in *Table 3.2*:

**Table 3.2: Comparison of investment and returns to GoK *vis-a-vis* the Concessionaire**

Particulars	Value of investment (₹ in crore)	Undiscounted Cash inflow (₹ in crore)	NPV (₹ in crore)	IRR (per cent)
GoK	5,071 (67 per cent)	13,947	(-) 3,866.33	3.72
Concessionaire	2,454 (33 per cent)	1,30,706	607.19	15.00
<b>Total</b>	<b>7,525</b>	<b>1,44,653</b>		

Source: Feasibility report prepared by Ernst & Young (excluding NPV and IRR of GoK).

Thus, it could be observed that in spite of 67 per cent investment by the GoK, the NPV of its investment in the project is (-)₹3,866.33 crore and at the same time the NPV of the investment accrued to the Concessionaire for the 40 year period with 33 per cent investment is ₹607.19 crore. Further, ENPV<sup>18</sup> and EIRR from the project is (-)₹834.60 crore and 8.9 per cent respectively. Therefore, the financial benefit accruing to the State is not commensurate with its investment.

GoK replied (August 2016) that the cost of land acquisition should not be taken into account while computing the Return on Investment. GoK also stated that the economic benefits were also to be considered while considering the benefits to the State.

The reply is not acceptable. ENPV, worked out considering all probable benefits was negative and the EIRR, far below the IRR of 15 per cent fixed for the Concessionaire. Cost of land was factored in while computing the NPV/EIRR of GoK because the land was not Government land but acquired specifically for the project at high cost. Further, cost of land acquisition has been included in the calculation of NPV/IRR for Colachel project. GoK/VISL at no time had analysed the NPV/IRR/EIRR on the State's investment in the project. Even the EIRR included under Cost-benefit analysis in the Environment Impact Assessment (EIA) Report was worked out for the investment by the private partner only.

<sup>16</sup> IRR is the rate that equates the present value of cash inflows to the present value of cash outflows of the project.

<sup>17</sup> EIRR indicates the rate of return at which the present value of the economic costs and benefits of the project are equal. In other words, it is the discount rate at which the net present value is zero.

<sup>18</sup> The cash flows for economic benefits are taken from EIRR report prepared by M/s Deloitte Tohmatsu for VISL.

## Termination Payment

**3.1.7** As per Clause 38.3.5 of the Concession Agreement, termination payment equal to the product of 30 (thirty) and the Realisable Fee recovered for and in respect of the last month of the Concession Period shall be due and payable to the Concessionaire.

As per the Feasibility Report of the Vizhinjam project prepared by E&Y in April 2015 which was approved by GoK, the Realisable Fee during the 40<sup>th</sup> year of the concession would be ₹7,822 crore. Assuming that the Concession is terminated at the end of the prescribed concession period (without considering the 20 year extension), the termination payment payable to the Concessionaire in accordance with the above clause would be ₹19,555 crore<sup>19</sup>. The NPV of the payment worked out to ₹567.10 crore.

We observed the following:

- Based on the E&Y estimates, the total revenue that would accrue to GoK during 40 years of the concession period would be ₹13,947 crore. The termination payment of ₹19,555 crore would mean that the net receipts of GoK from the project after 40 years would be (-)₹5,608 crore.
- The project parameters, including the concession period, the amount of grant (VGF) and the revenue share payable to GoK were structured in such a way that the Concessionaire would get equity IRR of 15 *per cent* from their investment in the project. We, however, observed that the termination payment was not considered while working out the IRR/NPV. If the same is factored in, the IRR obtained by the Concessionaire for his investment of ₹2,454 crore in the project would be 16.08 *per cent* and the NPV of his investment would be ₹842.57 crore. At the same time, the financial IRR of the State Government would be negative and the NPV of the ₹5,071 crore invested by GoK in the project would be (-)₹4,441.40 crore.
- Further, the EIRR of the project as far as GoK is concerned worked out to 7.59 *per cent* only and the ENPV (-)₹1,409.70 crore.
- We also observed that clauses empowering similar termination payment as envisaged in the Concession Agreement for Vizhinjam project were not included in the Concession Agreements executed for other infrastructure PPP projects such as the Hyderabad Metro project, JNPT fourth terminal, etc.

VISL replied (March 2017) that the clause was incorporated as per the MCA. The reply is not tenable as the cash inflow to the Concessionaire on account of the termination payment had neither been estimated nor factored into the NPV/IRR calculation.

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<sup>19</sup> ₹7,822/12\*30.



### Award of project

**3.1.8** According to the guidelines issued by the Central Vigilance Commission (CVC), prequalification criteria (PQ) should be framed with a view to attracting participation of reputed and capable firms with proper track record. Therefore, the PQ criteria should be exhaustive, yet specific and unambiguous.

We noticed deviations from these guidelines as discussed below:

#### Modification in Project Structure

**3.1.8.1** VISL changed the entire structure of the project after pre-qualifying five bidders. The changes were made on the adoption of Model Concession Agreement (MCA) for State Ports issued by the Planning Commission of India and were intended to make the project more attractive to private investors. The significant changes in the project parameters consequent to adoption of the MCA, when compared to the same as per the RFQ, were as given in *Table 3.3*.

**Table 3.3: Details of changes made to the structure of the project**

Sl. No.	Particulars	RFQ	RFP/Draft Concession Agreement (DCA)
1	Model for project development	Land lord model	Combination of land lord and private services models.
2	Concession Period	Not specified	Specified as 40 years extendable by 20 years.
3	Total Project Cost	₹3,900 crore	₹4,089 crore
4	Construction of breakwater and fishing harbour	To be awarded as per EPC tender	To be done by Concessionaire as funded work at a total cost of ₹1,463 crore.
5	Port Estate Development	Not mentioned	30 per cent of project land to be given on licence to Concessionaire for commercial development including real estate development.
6	Mortgage of project assets	Not mentioned	Concessionaire allowed to mortgage project assets including land to finance the project.
7	Capacity of the Port	1 MTEU by COD	0.6 MTEU by COD and 1 MTEU within 10 years after COD.

As the changes were not incorporated in the RFQ/DPR/Master Plan made available to prospective investors at the RFQ stage, unfair advantage was given to the qualified bidders. We observed that by incorporating major changes in the project parameters after shortlisting the bidders, GoK/VISL had violated the spirit of the MCA in which it was stated that “All project parameters such as concession period, tariff, price indexation and technical parameters should be clearly stated upfront”<sup>20</sup>.

GoK stated (August 2016) that none of the project elements or structure was changed after issue of the RFQ which significantly changed the attractiveness

<sup>20</sup> MCA, Overview of the Framework (Page xxiv).

of the project. The reply was not convincing because inclusion of provision for Port Estate development, enhancement of concession period from the standard 30 years to 40 years, inclusion of funded works, etc., were major changes altering the nature of the project. Since there were major changes in the project parameters, the tender process should have been cancelled and fresh global tenders invited. This would have increased the attractiveness of the project and ensured transparency in the award of work.

### Concession Agreement

**3.1.9** Concession in a PPP project is the exclusive right, license and authority to construct, operate and maintain the Project during the concession period. Concession period is ideally the minimum period required for collecting the required user fee such that the investment made by the private partner is fully recovered with interest thereon. Terms and conditions of the concession are governed by the Concession Agreement.

GoK adopted (12 May 2014) the Model Concession Agreement (MCA) for Ports issued by the Planning Commission of India for preparation of the Draft Concessionaire Agreement (DCA) of Vizhinjam project. MCA was only recommendatory in nature and it was not mandatory for GoK to adopt it since Vizhinjam Port is a minor port<sup>21</sup> falling within the exclusive jurisdiction of the State Government. Based on feedback from bidders, suggestion by PPP cell of Department of Economic Affairs (DEA), GoI and drafting changes suggested by the Planning Commission of India and Legal Consultants, certain changes were made to the DCA by VISL, with the approval of the EC, duly authorised by GoK. These changes were intimated to the bidders who had purchased the RFP by issuing Addenda 1 to 9.

### Conditions not favourable to the interests of the State

**3.1.9.1** Scrutiny of Concession Agreement executed with the Concessionaire revealed inclusion of conditions not favourable to GoK as discussed below:

- The standard concession period for PPP projects is 30 years. This was also fixed as the base concession period for projects with private participation in the policy on Ports and Shipping Development approved in 2005 by GoK. Further, in the study report on Vizhinjam project by the International Finance Corporation (IFC), the Concession period was recommended as 30 years<sup>22</sup> and the concession period was specified as 30 years in all the three tenders issued for Vizhinjam project prior to the 2013 tender. In the current agreement, however, the concession period was fixed as 40 years. By allowing 10 years' extra concession period, the Concessionaire would be collecting additional revenue of ₹29,217 crore<sup>23</sup>.

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<sup>21</sup> Major ports are ports notified as such by the Central Government as per the Indian Ports Act, 1908 while other ports are classified as minor ports and are administered by the respective State Government. Vizhinjam Project being a minor port is under the administrative control of State Government.

<sup>22</sup> Para 5.2 (iii) of the Strategic Options Report prepared by IFC in September 2010.

<sup>23</sup> Based on revenue estimates in Feasibility Report (April 2015) by Ernst & Young.

GoK replied (August 2016) that the concession period envisaged in the Concession Agreement was 40 years as per the MCA adopted for the project. GoK also stated that the standard Concession Period of 30 years was applicable for brownfield<sup>24</sup> terminal development projects where investment and risk were limited. For any major greenfield<sup>25</sup> development, the risk and cost involved would be significantly high. Further, a longer concession period would reduce the grant requirement of the project.

The reply was not acceptable as in the case of the proposed port at Colachel, a greenfield project similar to Vizhinjam project, the concession period has been fixed at 30 years. Further, there was no reduction in the grant demanded by the bidder even after the elongation of the concession period to 40 years.

- As per the Concession Agreement, the VGF (₹1,635 crore) was payable to the Concessionaire in two parts-equity support payable during the construction of the project and operation and maintenance (O&M) support payable after COD. Equity support was to be 150 *per cent* of the equity brought in by the Concessionaire subject to a limit of 30 *per cent* of the TPC.

We observed that as per the MCA, for calculation of equity support, TPC was not to include amount payable as equity support. Accordingly, equity support payable to the Concessionaire was ₹943.62 crore<sup>26</sup> and the balance VGF i.e., ₹691.38 crore would be payable (as per Article 25.3.1 of the Concession Agreement) only as O&M support in quarterly instalments<sup>27</sup> after COD. But, in the Concession Agreement, TPC for calculation of equity support was, however, made inclusive of equity support and consequently, the amount payable as equity support by GoK to the Concessionaire increased to ₹1,226.70 crore (30 *per cent* of ₹4,089 crore). This modification was made (31 December 2014) by the Empowered Committee (EC) to improve “clarity” without any specific demand from the prospective bidders. Due to this modification, GoK had to pay excess equity support of ₹283.08 crore in advance resulting in interest loss of ₹123.71 crore<sup>28</sup>.

GoK stated (August 2016) that the modification was completely based on the opinion of the legal consultant for removing ambiguity. GoK also stated that the modification did not entail any additional financial outflow to GoK and non-modification may have decreased the viability, attractiveness and competitiveness of the project.

<sup>24</sup> Brownfield projects are those projects where existing assets are developed further.

<sup>25</sup> Greenfield projects refer to projects on the unused lands where there is no need to re-model or demolish an existing structure.

<sup>26</sup> 30 *per cent* of the TPC of ₹4,089 crore less the equity support calculated as follows.

Let Equity Support = X and TPC=4,089.

Then  $X = (4,089 - X) * 0.30$ , i.e.  $X = 4,089 * 0.3 - 0.3 * X$ .

∴  $1.3X = 1,226.70$ . Hence  $X = 1,226.70 / 1.3 = 943.62$

<sup>27</sup> Each quarterly instalment being 7.50 *per cent* of the Equity Support.

<sup>28</sup> Worked out at the rate of 10 *per cent* per annum for four years from December 2015 to November 2019.

The reply was not acceptable since there was no ambiguity in the Article in the Concession Agreement regarding computation of equity support. Further, there would be an indirect financial gain to the Concessionaire to the tune of ₹123.71 crore due to the modification.

- As per Article 41 of the MCA, Project Assets (which included right of way over the site) were excluded from the assets and rights which could be mortgaged or pledged to lenders as security for debt incurred by the Concessionaire. However, in the Concession Agreement (Article 41.5) executed, the Concessionaire was given the right to mortgage all assets (except funded works) on the ground that “*it would provide an additional layer of security to Lenders*”, and that the Legal Consultants had opined that “*the change did not have any adverse impact on the financial obligations of the Authority*”.

We noticed that the request (March 2015) of one of the bidders for such a modification, prior to opening of bids, was rejected (March 2015) by the Empowered Committee (EC) of Secretaries to GoK on the basis of advice rendered by the Technical Consultant. Hence, the modification post award of concession was contrary to the advice of the Technical Consultant and conferred upon the Concessionaire the right to mortgage assets which includes land taken over by the GoK at a total cost of ₹548 crore.

GoK stated (August 2016) that permission to mortgage Project Assets including land was only an enabling clause exercisable only on a request made by the lenders. GoK also stated that similar provisions were there in other MCAs such as Power Purchase Agreements (PPAs) in Power Sector.

The reply is not convincing as the GoK/ VISL had adopted the MCA for Ports *in toto* and no such provision was envisaged in the MCA. GoK is treating the MCA as justification for providing additional benefits to the Concessionaire such as a longer concession period, but at the same time deviating from the MCA as pointed out above to provide undue benefit to the Concessionaire. Thus GoK was mixing and matching clauses as per convenience, all of which resulted in providing additional benefits to the Concessionaire. Further, the Legal Consultants had earlier opined that no such modification was necessary.

- As per Clause 3.1.1 of the Concession Agreement, the Concession Period of 40 years was extendable by 20 years on augmentation of capacity of the project to three MTEUs by the 30<sup>th</sup> year of the concession period and issuance of a notice by Concessionaire for extension during 36-37 year of the concession period.

Draft Concession Agreement had initially limited Concession Period to 40 years, extendable by 10 years. The extension was allowed by the DEA, GoI on the request (24 November 2014) of the Chief Secretary to GoK on the ground of concerns raised by bidders in pre-bid meeting,

Greenfield nature of the project, longer gestation period, mandatory capacity augmentation etc. Later, the DEA extended extendable period of Concession to 20 years.

We observed that if the GoK had retained the originally envisaged extension period of 10 years, additional revenue of ₹61,095 crore (Present Value - ₹353 crore) would have accrued to the State<sup>29</sup>. Further, as per the Master Plan approved for the project, the cost estimated for capacity expansion to three MTEUs was ₹3,390 crore. Since this expenditure is to be incurred by the 30<sup>th</sup> year, the cost may escalate to ₹14,651 crore<sup>30</sup> at the time of execution. As such, by incurring an expenditure of ₹14,651 crore, the Concessionaire would be benefited by ₹61,095 crore.

GoK stated (August 2016) that the financial analysis by Audit did not take into account the revenue sharing starting with 21 *per cent* at the beginning of extended period and ending with 40 *per cent* towards the end of the extended concession period. Considering such huge revenue share averaging to almost 30 *per cent*, the condition was actually not detrimental to the State. In fact, the condition facilitates continuity in the operation of the Port and better revenue share for the State.

The reply is factually incorrect since we had, in fact, factored in the revenue share of the State. GoK has not contradicted the fact that the Concessionaire, by spending ₹14,651 crore, would get 400 *per cent* returns.

- Article 26 of the Concession Agreement provides that the Concessionaire shall pay GoK by way of Concession Fee a sum of ₹1 *per annum* and an additional concession fee (premium) equal to one *per cent* of the total Realisable Fee from the 15<sup>th</sup> anniversary of COD. Thereafter, premium for the subsequent years shall be increased by one *per cent* of the total Realisable Fee, subject to a ceiling of 40 *per cent* of the total Realisable Fee in the respective year.

We observed that as per the projected cash flow statements prepared by the consultants<sup>31</sup> engaged by VISL, the Concessionaire would recoup their investment of ₹2,454 crore by the eleventh year from COD, i.e., by 2030. Since GoK bears 67 *per cent* of the total investment required for the project, the revenue sharing with the Concessionaire should have commenced from the date on which the private partner recoups his investment i.e. from 2031. By postponing the commencement of sharing revenue to the fifteenth year after COD, GoK/ VISL has foregone revenue of ₹2,153 crore<sup>32</sup> and allowed undue benefit to the private

<sup>29</sup> Net cash flow of ₹78,222 crore as per the feasibility report prepared (April 2015) by Ernst & Young as reduced by revenue share of ₹17,127 crore payable by the Concessionaire to GoK during the 50<sup>th</sup> year to the 60<sup>th</sup> year.

<sup>30</sup> Providing year on year escalation of five *per cent* per annum as assumed by VISL while working out the Total Project Cost of Phase I, ₹4,089 crore.

<sup>31</sup> Ernst & Young.

<sup>32</sup> Difference between total revenue from traffic to GoK if revenue share commenced from 11<sup>th</sup> year- ₹8,981 crore and revenue receivable by GoK from 15<sup>th</sup> year as per Concession Agreement - ₹6,828 crore.

partner. There was also no basis for fixing revenue share at one *per cent* on the 15<sup>th</sup> anniversary of COD.

GoK replied (August 2016) that the period of commencement of revenue share to GoK was market determined and the 15 year period also related to the period provided by bank for project debt financing. GoK also stated that the development of port and its allied facilities would significantly contribute to the large scale growth of industry and economy in Kerala, besides generating direct and indirect employment opportunities.

The reply was not acceptable since it was clarified in the RFP that the payment of premium of one *per cent* shall commence either from COD or from any other date falling between COD and the 15<sup>th</sup> anniversary whereas the date of commencement of revenue sharing was given as “from the fifteenth anniversary of COD” in the DCA submitted along with RFP. Further, the contention of the GoK in respect of the perceived economic benefits to the State from the project was doubtful, since as described in *Paragraph 3.1.6*, the ENPV of GoK’s investment was negative.

- Clause 12.6.6 of the Concession Agreement empowered the Concessionaire to levy, collect and appropriate the User Fee payable in respect of funded works in lieu of its obligations relating to operation, maintenance, defect liability and other functions. But, in Article 12.6.10, it was stated that the operation and maintenance of the fishing harbour shall at all times be undertaken by GoK.

We observed that the above two Articles were mutually contradictory and had the effect of enabling the Concessionaire to charge user fee on the fishermen for using the facilities in the fishing harbour constructed as funded work. Since the cost of the funded works (₹1,463 crore) was entirely borne by GoK this would be tantamount to conferring undue benefit to the Concessionaire at the cost of GoK.

GoK replied (August 2016) that operation and maintenance of fishing harbour component did not form part of the obligation of the Concessionaire and as such the Concessionaire would not levy User Fee in respect of Fishing Harbour component of the Funded Work.

The fact remains that the ambiguity in respect of User Fee on funded works exists and needs to be clarified by amending the Concession Agreement.

- According to the Concession Agreement, annual traffic estimated was six lakh<sup>33</sup> TEUs. Article 29 of the Concession Agreement provided for modification in the concession period if the actual Average Traffic during 20 years after COD increased or decreased by more than five *per cent* of target traffic. For every two *per cent* shortfall, the concession

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<sup>33</sup> Traffic equivalent to 60 *per cent* of the capacity of the port i.e. six lakh TEUs per annum.

period shall be increased by one year subject to a maximum of ten years. Similarly, for every two *per cent* excess, the reduction in concession period shall be by six months; subject to a maximum of three years. Reduction in Concession period shall, however, be waived if the Concessionaire pays a further premium equal to ten *per cent* of the Realisable Fee in the respective years.

We observed that the above conditions in the Concession Agreement were skewed in favour of the Concessionaire as illustrated in *Table 3.4* (*The figures are for illustrative purpose only*).

**Table 3.4: Impact of increase or decrease in volume of traffic**

	Event	Impact
Scenario A	Actual Average traffic decreases by 20 <i>per cent</i> from target traffic.	Concession period extended by ten years i.e. up to 2066. Benefit to the Concessionaire would be ₹24,620 crore <sup>34</sup> .
Scenario B	Actual Average traffic increases by 20 <i>per cent</i> .	Concession period reduced by three years. Benefit to GoK would be ₹7,386 crore <sup>35</sup> .
Scenario C	Actual Average traffic exceeds target traffic by 20 <i>per cent</i> and Concessionaire opts to pay 10 <i>per cent</i> additional Realisable Fee for six years	Concession period not reduced and the Concessionaire is benefitted by ₹6,381 crore <sup>36</sup> .

We also observed that the Department of Economic Affairs (DEA) had, while considering the VGF application submitted by GoK/ VISL, stated that the proposal of a two *per cent* trigger for traffic for adjustment of concession period was too small and that normally, a band of 10 *per cent* was factored in bids.

The DEA had, therefore, requested GoK to set the trigger at a reasonable level of 10 *per cent* which was not acted upon by GoK.

GoK replied (August 2016) that the unequal adjustment for decrease and increase in traffic was done to incentivise the Concessionaire.

The reply is not tenable since the Concessionaire stood to gain disproportionately both when the traffic increased and decreased.

- According to Clause 30.1.1 of the Concession Agreement, if a Government Instrumentality opens any competing port within 100 kilometres (km) of the Vizhinjam Port before the fifteenth anniversary of the Appointed Date, the Concessionaire shall be entitled to an additional concession period equal to three times the duration between the commissioning of the competing port and the fifteenth anniversary

<sup>34</sup> ₹2,462 crore (net cash inflow of the Concessionaire in 2056 from Traffic and Port estate) \* 10 years.

<sup>35</sup> ₹2,462 crore (net cash inflow of the Concessionaire in 2056 from Traffic and Port estate) \* 3 years.

<sup>36</sup> ₹7,386 crore being the net cash inflow for three years of reduction in concession period as reduced by ₹1,005 crore being the additional Realisable Fee payable by the Concessionaire for six years at the rate of 10 *per cent* per year of 2040 Realisable Fee of ₹1,675 crore.

of the Appointed Date (5 December 2015). Further, the Concessionaire shall be relieved of his obligation to undertake mandatory capacity augmentation. This condition would not apply if the average traffic exceeds 90 *per cent* of the existing capacity of the Port in any year.

We observed that the term “Government Instrumentality” as defined in the Concession Agreement included GoI which was significant as GoI decided (July 2016) to establish a Container Transshipment Terminal at Colachel in Tamil Nadu, 51 km away from Vizhinjam Port, at a total cost of ₹24,969 crore. As such, the Concessionaire would be legally within their rights to invoke the Articles relating to the establishment of a competing port.

GoK replied (August 2016) that the relevant clauses are as adopted from the MCA and the definition of “Government Instrumentality” is as provided by the MCA. The definition is clear and the applicability of the same shall be evaluated on a case to case basis.

Thus, there is a risk that the clause will be invoked if the proposed port in Colachel comes up and would cause additional elongation of the concession period.

- Clause 27.1.1 empowers the Concessionaire to collect fee at lower rates by giving public notice to the users, specifically in respect of all or any category of users. This clause would enable the Concessionaire to collect reduced or nil user fee from users of their choice which would adversely affect the revenue share of GoK. As such, the Concessionaire has been given the option to provide vessels of his choice to use the Port facilities free of cost.
- Clause 3.1.3 of the Concession Agreement conferred on the Concessionaire the right to undertake the development, operation and maintenance of the real estate and to exploit such development for commercial purposes (Port Estate Development) with the right to sublicense any or all parts thereof by means of Project Agreements. It was also stipulated in the Agreement that the land used for Port Estate Development shall not exceed 30 *per cent* of the total area of the Site and the maximum area used for residential purposes shall not exceed one-third thereof.

We observed that:

- ✓ DEA had granted in-principle approval to the VGF application submitted by GoK on the basis of the assurance furnished by GoK that all activities proposed in Port Estate Development are port related and envisaged as part of the requirements of the project. However, this condition was not incorporated in the Concession Agreement.
- ✓ The permissible area for Port Estate Development as specified in Annex-IV of Schedule A of the Concession Agreement was 30 *per cent* of the total area of the “Site” and the maximum area



used for residential purposes shall not exceed one-third thereof. The total area of the “Site” has not been quantified anywhere in the Concession Agreement. As such, the Concessionaire is entitled to claim for Port Estate Development, 30 *per cent* of the total area of the project which may include the reclaimed area (53 hectares) and even the area acquired/ to be acquired for road/ rail connectivity, etc.

- ✓ As per the Master Plan, total area to be acquired for the project is 296.40 acres. Computed at the average cost of acquisition of ₹2.62 crore per acre, the value of land (88.92 acres) to be handed over to the Concessionaire for Port Estate Development was ₹232.97 crore.
- DEA had opined that the commercial development rights should be made *pari passu*<sup>37</sup> and *coterminus*<sup>38</sup> with the concession period for the port and enable return of this development created to GoK.

We, however, observed that as per Article 31.5 of the Concession Agreement, the Concessionaire is permitted to sub-license the Port Estate Development including residential buildings for a period co-existent with the concession period, and the sub-license would endure even if the Concession is terminated. This essentially means that the Port Estate Development including residential building was not made *coterminus* with the concession period as directed by DEA. Thus, VISL/ GoK failed to address the specific concerns raised by the DEA especially concerning return of land to GoK on completion of the concession period.

### **Non-compliance with provisions of Concession Agreement**

**3.1.10** Clause 3 of Schedule L of the Concession Agreement mandated GoK to appoint Safety Consultant within 90 days of agreement for carrying out safety audit of the Port at the design stage. We, however, observed that VISL had not appointed Safety Consultant in spite of the fact that the Concessionaire had commenced the construction activities from 05 December 2015 and as per information furnished to Audit, has completed works estimated at ₹16 crore as on date (April 2016).

GoK assured (August 2016) that Safety Consultant would be appointed at the earliest.

### **Conclusion**

**The technical and financial estimates prepared by external consultants were not scrutinised with due diligence resulting in inflation of cost estimates. The interests of the GoK were not protected adequately while drawing up the Concession Agreement.**

<sup>37</sup> On equal footing.

<sup>38</sup> Ending at the same time.

## Recommendations

The GoK may:

1. Subject cost estimates prepared by External Consultants for PPP projects to scrutiny by qualified and responsible Government officers/departments before approving the same.
2. Exercise due diligence to protect the interests of the Government while drawing up agreements in respect of PPP projects.

## 3.2 Sub-contract Management by Public Sector Undertakings

### Introduction

**3.2.1** Public Sector Undertakings (PSUs) in Kerala carry out supply and installation of equipment and execution of civil works on behalf of Departments/ agencies of Government of Kerala (GoK). These PSUs in turn engage sub-contractors for procurement of equipment and execution of work awarded by Departments of GoK/ agencies.

In order to examine compliance with rules and regulations and transparency in sub-contract management by PSUs, we examined 50 works<sup>39</sup> relating to supply and installation of equipment and 107 works relating to civil construction in seven<sup>40</sup> PSUs during the period 2010-11 to 2015-16. Out of these, 29 work orders valuing ₹178.79 crore for supply and installation of equipment were issued to the PSUs by GoK on nomination basis of which 20 work orders costing ₹51.47 crore were issued to the PSUs without preparing cost estimate. The cost estimates for these works were prepared by the PSUs based on which, work orders were issued by GoK to them on back to back basis<sup>41</sup>. The cost estimate in respect of 10 work orders for ₹27.77 crore was prepared with the help of business partners of the PSUs to whom these works were later sub-contracted.

Audit findings are discussed below.

## Audit Findings

### Supply and installation of equipment

**3.2.2** Kerala State Electronics Development Corporation Limited (KELTRON) and Kerala Small Industries Development Corporation Limited

<sup>39</sup> 41 works executed by Kerala State Electronics Development Corporation Limited (KELTRON) on behalf of 18 Departments/ agencies of GoK and nine works executed by Kerala Small Industries Development Corporation Limited (SIDCO) for one Department/ three agencies of GoK.

<sup>40</sup> Kerala State Electronics Development Corporation Limited, Kerala Small Industries Development Corporation Limited, Roads and Bridges Development Corporation of Kerala Limited, Kerala State Construction Corporation Limited, Kerala State Coastal Area Development Corporation Limited, Kerala Irrigation Infrastructure Development Corporation Limited and Forest Industries Travancore Limited.

<sup>41</sup> 'Back to back basis' is a term used by PSUs. It refers to purchases done by PSUs for GoK/ agencies whereby PSUs get orders from GoK / agencies who then pass it on to private parties with payment terms that PSU would make payment to private parties only after receipt of payment from GoK/ agencies.

(SIDCO) supply and install equipment for departments of Government of Kerala (GoK) and other PSUs.

Issues noticed in the works relating to supply and installation of equipment are discussed in succeeding paragraphs.

### Agreement with business partners

**3.2.2.1** According to Section 3 of the Competition Act, 2002, no enterprise shall enter into any agreement for production, supply, etc., of goods or provision of services, affecting competition within India. As per guidelines (July 2004) of Central Vigilance Commission (CVC), while making procurement or executing work through a system of approved/ registered vendors and contractors, there should be wide publicity through website as well as through other traditional channels at regular intervals for registration of contractors/ suppliers.

We observed that for executing major works, KELTRON and SIDCO had entered into business agreements with eleven agencies, with the intention of obtaining work orders from GoK and getting them executed through these sub-contractors, as detailed in *Table 3.5*.

**Table 3.5: Entities with whom business agreements were entered into**

Name of the entity	Agreement since	Terms of agreement/Particulars
<b>KELTRON</b>		
Mediatronix Private Limited (Mediatronix)	March/ April 2011	KELTRON was to solicit orders for city surveillance solutions and road traffic enforcement systems developed by Mediatronix. KELTRON would sell these items in the brand name 'KELTRON' to its customer base. As per clause 4 of the agreement, Mediatronix and KELTRON would arrive at suitable pricing of the products on case to case basis.
Net X Technologies Limited (Net X Technologies)	June 2011	The parties to the Memorandum of Understanding (MoU) became strategic partners for selling products and services including digital library, learning management system, digital content creation and supply of servers and storage, etc., to various customers of KELTRON.
Stellar Green Tech Private Limited (SGPL), Gurgaon.	July 2011	Business partner for installation of solar projects.
Eram Scientific Solutions Private Limited (Eram Scientific)	March 2011	KELTRON obtained works from Local Self Government Department (LSGD) of GoK (based on a Government Order issued in March 2012) and had them executed by Eram Scientific.
Expedien E-Solutions Limited (Expedien)	April 2011	KELTRON obtained work of implementation of 'e-Vet Connect' in Kerala Veterinary and Animal Sciences University and executed it through Expedien.
Ospyn Technologies Private Limited (Ospyn)	February 2009	KELTRON obtained work of File Management System for Kerala Prisons and Correctional Services Department (Prisons Department) executed through Ospyn.
Webex Systems and Networks Private Limited (Webex)	January 2012	Preferred outsourcing partner for marketing and selling IT products for Government Departments, Corporate consultancy and other related services in IT.
<b>SIDCO</b>		
Stohos Infotech Private Limited (SIPL)	September 2013	As per Teaming Agreement, SIDCO would act as the team leader for participating in tenders floated by GoK and SIPL would supply the technology and equipment.

Name of the entity	Agreement since	Terms of agreement/Particulars
Kerala SIDCO Hitech Security Printing Solutions Private Limited <sup>42</sup>	May 2014	As per the Strategic Business Agreement, SIDCO would canvas with Government agencies and submit quotations/tender based on the predetermined pricing policy agreed upon. On obtaining the order from Government and Government agencies, SIDCO would issue the work order to the JV which would execute the work.
Sinelab Technologies Private Limited (Sinelab)	March 2015	SIDCO obtained orders from Government/PSUs which were passed on to Sinelab/ Nautical Lines, empanelled vendors, on nomination basis.
Nautical Lines	June 2013	

We observed that KELTRON and SIDCO selected business partners (strategic partners) without following any transparent procedure, such as identifying and empanelling firms through open tender process. Instead, the selection was based on unsolicited offers from the business partners who were private entities.

KELTRON stated (August 2016) that it took initiative and signed agreement with Mediatronix for projects related to purchase and installation of SVDS and RLVDS<sup>43</sup> on exclusive basis and that the system and solutions were proven for Indian conditions and were cost effective. The reply was not tenable as selection of business partners was not done transparently and cost effectiveness can be gauged only through a transparent tender system.

GoK stated (February 2017) that the PSUs had been instructed that criteria for selection of units whose products were marketed, terms of marketing arrangements, etc., should be brought to their Board of Directors (BoD) and got approved by them in advance. The reply is not acceptable as equal opportunity was not given to all interested parties.

### Award of work to business partners without tenders

3.2.2.2 Rule 7.11 of Stores Purchase Manual (SPM) of GoK required that purchase orders/ work orders be issued only after inviting open tenders when the value of works exceeded ₹10 lakh.

We noticed that KELTRON and SIDCO had issued 12 work orders valuing ₹51.90 crore and 4 work orders valuing ₹8 crore respectively to their business partners without invitation of tenders as shown in **Appendix 10**. Out of these, eight work orders received by KELTRON and all the work orders received by SIDCO from GoK/ its agencies were on nomination basis. We also noticed that:

- For the work of printing text books (Serial number-8 of **Appendix 10**) of Sarva Siksha Abhiyan (SSA), SIDCO requested (February 2014) GoK to allot the job to it on nomination basis. GoK, however, directed SIDCO to take part in tenders and operate on commercial basis. Yet, SIDCO approached SSA and obtained the printing job of activity books for

<sup>42</sup> A joint venture (JV) of SIDCO and Solar Offset Printers Private Limited.

<sup>43</sup> Speed/ Red Light Violation Detection System used for traffic enforcement.

schools. Thereafter, SIDCO assigned the work to a Joint Venture (JV), thus, bypassing the prescribed procedure for awarding contracts.

GoK in its reply stated (February 2017) that the work was awarded to SIDCO on the basis of quotations invited by SSA, and that there was no harm in SIDCO sub-contracting the work to the JV. The reply is not acceptable as SIDCO invited quotations from only one firm and awarded the work to the same firm.

- Three work orders for supply of 15-seater, 12-seater and 6-seater speed boats for Forest Department, GoK (Serial number 9 of *Appendix 10*) was issued (March 2015) to Nautical Lines, business partner of SIDCO. Work order for supply of 15 seater boat was issued based on a price comparison of three quotations, including quotations of two other firms collected and submitted by Nautical Lines themselves to SIDCO. The delivery schedule was not mentioned in the work order for the 15 seater boat and Nautical Lines was yet (December 2016) to deliver the boat. Wildlife warden, Shenduruny had, however, given (17 June 2015) a false acceptance certificate for receipt of the boat and payment of ₹0.66 crore released (March 2015).

The six-seater and 12-seater boats were delivered by Nautical Lines between May and June 2015, but the 12-seater boat could not be put to use as Nautical Lines had not furnished Fitness Certificate and Registration Certificate<sup>44</sup> in line with the terms of the work order.

GoK, in its reply (February 2017), accepted that the award of work by SIDCO was irregular and assured that action would be taken against those concerned. Government also confirmed that the 15-seater boat is yet to be delivered. The reply did not explain how acceptance was issued by the Wildlife Department and payment released to the supplier for an item that is yet to be supplied. Responsibility was also not fixed for issuing false acceptance certificate.

### **Loss due to award of work without tenders**

**3.2.2.3** Issue of work orders to business partners on nomination basis resulted not only in violation of codal provisions but failure to obtain competitive rates as well. We worked out extra expenditure of ₹0.66 crore in award of works on nomination basis in two cases where comparable rates were available, as discussed below:

- According to the guidelines issued by Ministry of New and Renewable Energy (MNRE), Government of India (GoI), 30 *per cent* of cost or benchmark price of solar high mast lights was receivable as subsidy from GoI, if equipment were procured from MNRE-approved channel partners.

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<sup>44</sup> From Coastal Shipping and Inland Navigation Department.

The work of supply and installation of solar high mast lights (Serial number-6 of **Appendix 10**) was awarded to Sinelab, business partner of SIDCO. But Sinelab was not an approved channel partner of MNRE for supply of solar high mast light. Due to procurement from a non-approved channel partner, Kerala State Coastal Area Development Corporation Limited (KSCADC) became ineligible for subsidy of ₹0.11 crore<sup>45</sup>.

GoK replied (February 2017) that there was no condition in the work order issued by SIDCO to execute the work through MNRE approved channel partners. The reply is not acceptable as by awarding the work to a firm not approved by MNRE, subsidy to the extent of ₹0.11 crore was foregone.

- Prisons Department, GoK awarded (March 2012) work relating to implementation of solar energy system in Central Prison, Thiruvananthapuram to KELTRON (Serial number 2 of **Appendix 10**) at ₹7.27 crore on nomination basis based on the project proposal submitted by KELTRON. As KELTRON had no previous experience in implementing solar projects, the project proposal was prepared with the assistance of KELTRON's business partner, SGPL. KELTRON subcontracted (April 2012) this work to Rajasthan Electronics and Instrumentation Limited (REIL)<sup>46</sup> and SGPL without any tendering process.

We noticed that SGPL expressed (May 2012) its inability to execute the order. Consequently, the order was issued (May 2012) to Megatech Power Equipments Private Limited (MPEPL), business partner of SGPL on their recommendation at the same rate. On a comparison of rates of solar panels procured (September 2012) for Thevancode Prison, we noticed that KELTRON had incurred extra expenditure of ₹0.55 crore.

GoK replied (February 2017) that award of work to MPEPL without tender was not justifiable. GoK also stated that the cost may vary from one jail to another depending on the layouts. The reply was not acceptable as we worked out the extra expenditure reckoning the cost of identical solar panels per unit (watt peak) supplied by REIL in both the jails. Cost per unit was also not dependent on the layouts.

### **Award of work after defective tendering**

**3.2.2.4** As per Rule 7.33 of Stores Purchase Manual (SPM), minimum time of 15 days (one month before revision of SPM in June 2013) was to be given for submission of bids. Short tender notice is also to be published in Gazette of GoK as mandated by the provisions of Rule 7.19 of SPM. Further, according to the directions (May 2004) of Central Vigilance Commission (CVC), pre-

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<sup>45</sup> 30 per cent on the cost of solar plants procured through SIDCO.

<sup>46</sup> Design, manufacture, supply and testing of 229 KWp SPV power pack at ₹2.56 crore, excluding subsidy of ₹1.65 crore and installation charge of ₹1.28 crore to be done by KELTRON.

qualification criteria should be specified in tender documents and qualification of bidders should be carried out against these criteria.

In 1,212 e-tenders invited by KELTRON during September 2012<sup>47</sup> to March 2016, provisions of SPM were violated in 1,147 cases as time given for submission of bids was less than the minimum period prescribed. In respect of 41 sample-selected works which were sub-contracted by KELTRON, we observed that:

- In respect of 13 works received (2011-12 to 2015-16) from agencies of GoK on nomination basis<sup>48</sup>, time given for submission of bids by KELTRON ranged between 2 to 18 days (18 days given when 30 days were to be given). KELTRON also did not publish short tender notices in Gazette of GoK. Insufficient time for submission of bids and lack of adequate publicity create a risk that adequate number of bids will not be received and competition will be reduced. Due to their proximity to KELTRON, business partners/ regular suppliers of KELTRON and their agents, however, participated in the tender and 13 work orders valuing ₹71.29 crore were awarded to them as shown in *Appendix 11*.
- In 2 out of the above 13 works, where comparable rates were available, GoK incurred extra expenditure of ₹4.17 crore as given in *Table 3.6*.

**Table 3.6: Extra expenditure incurred by IT@School<sup>49</sup> for purchase of computers.**

Name of work	Supply of laptops to IT @ School	Supply of desktops to IT @ School
Days given for bid submission	7	4
Quantity (Number)	4,400	2,200
Rate/ piece at which supplied to IT @ School (₹)	35,857	32,642
Rate for comparable item (₹)	27,610	30,200
Extra cost per piece (₹)	8,247	2,442
Extra cost on supplied quantity (₹ in crore)	3.63	0.54
Remarks	Toshiba-make laptop with better specifications was purchased (January 2015) by Kerala Motor Transport Workers Welfare Fund Board, Kollam at the rate of ₹27,610.	15 Acer-make computers with same specifications were purchased (February 2015) by Chemical Examiners Laboratory, Thiruvananthapuram at the rate of ₹30,200.

Accepting the audit observation, GoK stated (February 2017) that floating tenders with lesser number of days than that prescribed in SPM was not

<sup>47</sup> KELTRON started e-tendering from September 2012 only.

<sup>48</sup> Except one work included as Serial number 13 in *Appendix 11* which was awarded to KELTRON after tendering.

<sup>49</sup> A project to integrate computer technology into school curriculum with the primary objective of improving the quality of education and imparting computer education to school students.

justified. GoK further stated that BoD of PSUs needed to be involved in case of deviations, either on a case to case basis or through getting a policy laid down.

We also noticed manoeuvring of tenders to suit business partners/ regular suppliers as described below:

- ✓ State Police Chief, Kerala awarded (October 2012) the work of installation of 100 SVDS to KELTRON. It invited tenders after splitting the work into three parts. Of these, KELTRON invited (November 2012) e-tenders for setting up of Control Room for SVDS in Thiruvananthapuram. Five parties participated in the pre-bid meeting held on 30 November 2012. On the date of opening of the tender (13 December 2012), KELTRON decided to collect physical bid documents instead of e-documents and to finalise the bids on 14 December 2012. This fact was not informed to all bidders who participated in the tender. The reason attributed by KELTRON for the change in the method of tendering was technical glitch in the e-tender website which prevented uploading or downloading the e-tender details.

According to the Kerala State IT Mission, which maintains the e-tendering website of GoK, there was no technical glitch in the website. This indicates that the officials of KELTRON wanted to finalise the tender outside the e-tender website when there was possibility of competition as five bidders had participated in pre-bid meeting. KELTRON opened (14 December 2012) the only bid received from RP Tech International Private Limited (RP Tech), who was authorised by Mediatronix to submit bids and awarded (20 December 2012) the work for ₹5.99 crore to RP Tech.

- ✓ In respect of works at serial number 1 and 2 of *Appendix II* which were parts of the same work, tender conditions were arbitrarily fixed suiting the ultimate awardees of the works. In the work awarded to Mediatronix, Thiruvananthapuram for supply of SVDS, the criteria fixed was having an existing service centre in Thiruvananthapuram, whereas for the work awarded to ITMG, Malappuram (who did not have a service centre in Thiruvananthapuram) for installation of SVDS, the criteria fixed was that it should have an existing service centre anywhere in Kerala. In both the tenders, there was only one bidder each viz. Mediatronix and ITMG.

Accepting the audit observation, GoK stated (February 2017) that they had instructed PSUs to have standard tender template, with deviations there from duly approved by the BoD.

Regarding tender condition of having service centre in Thiruvananthapuram for the work of supply of SVDS, GoK stated that as the control room was installed at Police Training College, Thiruvananthapuram, KELTRON's stipulation of having a service



centre at Thiruvananthapuram was justifiable. The reply is not acceptable as the work pertains to supply of SVDS to different locations throughout Kerala and not for installing control room.

- ✓ In respect of works at serial numbers 6 and 7 of *Appendix 11*, one of the conditions for bidding was that the bidders should be strategic partners/ MoU partners of KELTRON. In the case of these works valuing ₹1.99 crore, there was only one strategic partner viz., Net-X Technologies to submit bids.
- In the following tender, minimum previous experience was fixed in violation of CVC guidelines as detailed in *Table 3.7*.

**Table 3.7: Requirement of experience as per CVC guidelines and that fixed by KELTRON**

Name of work	Requirement of experience during last seven years		Audit Observation
	CVC guidelines	Fixed by KELTRON	
Networking and OFC backbone networking for Directorate of Collegiate Education (February 2016)	One similar work valuing not less than ₹5 crore.	One similar work valuing not less than ₹2 crore.	Work was awarded to Net-X Technologies. Eligibility was fixed to suit the requirement of Net-X Technologies, business partner of KELTRON as it had previous experience of only one similar work valuing ₹3.08 crore. On comparison of rates of nine comparable items of a similar work <sup>50</sup> , excess expenditure of ₹0.19 crore (17.12 per cent) was noticed.

- For the works of supply of computer equipments for IT@School<sup>51</sup>, notice inviting tenders issued by KELTRON stipulated that bidders should have experience, preferably of supplying to GoK/ its undertakings. RP Infosystems Limited was awarded the work of supplying Chirag brand computers. Out of 14,061 systems supplied, 135 had to be replaced and 5,301 had to be serviced by KELTRON at a cost of ₹1.27 crore as RP Infosystems Limited failed in after-sale service against which KELTRON recovered ₹3.38 crore through invocation of Bank Guarantee and retention money. Even though ₹0.32 crore<sup>52</sup> remained to be recovered from RP Infosystems, KELTRON did not encash three BGs worth ₹0.58 crore which expired in June/ July 2013.

GoK replied (February 2017) that the figure of ₹1.27 crore was overstated and KELTRON's actual expenses were ₹0.74 crore. This reply is not acceptable because the figure of ₹1.27 crore was based on the figures provided by KELTRON itself and included the cost of manpower for service and overheads, whereas ₹0.74 crore was excluding these.

<sup>50</sup> Nine items in order valuing ₹7.83 lakh given (March 2016) by Government College of Engineering, Kannur.

<sup>51</sup> Order Acceptance (OA) nos. 946 and 947 of 2010-11 and 1409 and 1410 of 2011-12.

<sup>52</sup> (Liquidated Damages deducted by IT@School: ₹2.43 crore plus service charges incurred: ₹1.27 crore) less ₹3.38 crore = ₹0.32 crore.

### Award of work to single bidders

3.2.2.5 According to the directions (October 2013) of GoK, in cases where there was only single bidder, retendering should be resorted to. If after retendering also there was only single bidder, the work can be awarded to the single bidder with justification for the same. Further, as per Rule 8.15 of SPM, Earnest Money Deposit (EMD) of a tenderer will be forfeited, if the tenderer withdraws from the tender.

- We noticed that KELTRON had awarded eight works, obtained from GoK/ agencies on nomination basis, to single bidders for ₹24.60 crore without retendering (*Appendix 12*). The time given for bid submission in these cases was also lesser than that mandated by SPM. In respect of tenders for the works of Motor Vehicle Department, GoK and Transport Commissioner (Serial numbers 4 and 6 of *Appendix 12*) request of one contractor for extension of bid submission time for each work was not considered by KELTRON.

In respect of tenders invited for three works, there were two bidders each. Though the bidders were related entities which made their bids equivalent to single bids, KELTRON/ SIDCO did not retender the works as warranted by the Order (October 2013) of GoK as detailed in *Table 3.8*.

**Table 3.8: Bidding by related entities**

Sl. No.	Items of supply	Name of bidders	Name of PSU	Work awarded to	Purchase Order Value (₹ in crore)	Remarks
1	Compactors <sup>53</sup> for KLIM	SIPL and Net-X Technologies	SIDCO	SIPL	4.21	SIPL and Net-X Technologies were the business partners of SIDCO and KELTRON respectively. In the tender invited by KELTRON, the bid submitted by Smartsoft (another vendor) was rejected during technical evaluation though it complied with all the tender conditions. The seal of SIPL was found on the bid documents submitted by Net-X Technologies to KELTRON. The contact e-mail given by SIPL in the e-tender website was biju@netx.co.in i.e. an email address registered in the domain of Net-X Technologies.
2	Two Database servers for IT @ School	SIPL and Net-X Technologies	KELTRON	Net-X Technologies	1.00	
3	Supply of solar equipment in various coastal areas on behalf of KSCADC	Sinelab and SARK Cables Private Limited	SIDCO	Sinelab	2.31	Both the bidders were related entities because both had common directors.

<sup>53</sup> Compactors are storage systems which can store large number of files/documents etc., utilising comparatively less floor space.

GoK admitted (February 2017) that SIDCO should not have awarded the work related to KLIM to SIPL and assured that the officials concerned would be taken to task. In case of the award of work to Sinelab, GoK stated that SIDCO was not aware of the fact that the two bidders were related.

We further noticed that:

- In respect of the work of installation of speed cameras and surveillance system for Transport Department, GoK (serial number 6 of *Appendix 12*), Proxs Infocomm Limited (Proxs) was Mediatronix's partner and an authorised agency to quote, supply, install and maintain traffic enforcement systems developed by Mediatronix. In the tender documents submitted by Proxs, employees of Mediatronix were mentioned as the contact persons for financial and technical enquiries.

Work was awarded to Proxs on 1 November 2013 and on the same day KELTRON, Mediatronix and Proxs entered into a teaming agreement for joint development, implementation and maintenance of the required system and software for the project.

As Proxs did not start the work even after three months of the issue of the Purchase Order, KELTRON cancelled (3 February 2014) the Purchase Order and the supply order was directly issued (6 February 2014) to Mediatronix without re-tendering for a total value of ₹9.34 crore. KELTRON, Mediatronix and Proxs, thereafter, entered (25 February 2014) into a compromise deal and KELTRON refunded (26 February 2014) the earnest money deposit (₹20 lakh) submitted by Proxs. Such instances highlight the non-transparent dealings of KELTRON.

- For the work of setting up of vehicle testing stations (VTS) in Thiruvananthapuram and Ernakulam (serial number 4 of *Appendix 12*), KELTRON published (16 January 2014) e-tenders, giving only five days for submission of bids. A private company<sup>54</sup> had complained to KELTRON that the dates given in the tender were in violation of the provision of General Financial Rules 2005. KELTRON did not consider this complaint even though there was violation of SPM provisions, thereby limiting competition. Only one bid was submitted which was accepted though the bidder (Webex Systems and Networks Private Limited – Webex) did not submit documents such as declaration about non-blacklisting by Government Departments, registration certificate, service centre details, PAN details, etc. KELTRON had earlier obtained works of VTS at Kozhikode and Kannur by submitting proposals obtained from Webex and thereafter passed on (October 2011- March 2012) these work to Webex on nomination basis.

Webex, incorporated in 2007, obtained VAT registration in February 2012. After obtaining the works of VTS through KELTRON, the VAT

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<sup>54</sup> Environmental Systems Products India Private Limited.

registration was cancelled in August 2014. Webex collected (March 2012 - March 2014) VAT amounting to ₹0.68 crore from KELTRON in the deal, which was not duly remitted to the Commercial Taxes Department, GoK. Due to this, KELTRON would be disallowed the input VAT credit of ₹0.68 crore availed of by it.

Commercial Taxes Department, GoK, replied (November 2016) that notice had been issued to Webex for recovery of VAT. Recovery was, however, pending as of February 2017.

### **Award of work to regular suppliers after defective evaluation of bids**

**3.2.2.6** GoK/ its agencies issued (January 2011- January 2016) nine work orders to KELTRON through tender process. In respect of one tender for supply and installation of 3,720 all-in-one desktop computers for Additional Skill Acquisition Programme (ASAP) of Higher Education Department, the eligibility criteria for technical qualification required that the bidder should be a manufacturer or authorised dealer or authorised distributor and the equipment should have EPEAT<sup>55</sup> gold certificate.

ASAP rejected one of the bidders who had quoted with Dell make stating that it did not furnish list of service centres, whereas Dell followed onsite service support. ASAP rejected another bid as it did not meet the annual turnover criteria of ₹20 crore, which was more than the probable amount of contract (PAC) of ₹15 crore. ASAP qualified KELTRON and Steel Industrials Kerala Limited<sup>56</sup> (both with Acer brand) technically, even though neither of them were manufacturers or authorised dealers/ distributors. They neither submitted EPEAT gold certificate nor did have any service network. Despite these defects, ASAP placed (6 March 2015) work order on KELTRON, the lower of two bidders at the rate of ₹37,000 per piece.

We observed that KELTRON had invited (4 March 2015) tenders in which two bidders, ACS Technologies and LR Infotech System had participated. Both the bidders were regular suppliers of KELTRON during 2010-11 to 2015-16 with nearly 30 to 82 *per cent* of their annual turnover coming from KELTRON. Work order was issued (11 March 2015) to ACS Technologies, the lowest bidder who quoted ₹35,233 per piece even though it did not produce EPEAT gold certificate.

KELTRON replied (August 2016) that the equipment supplied by ACS Technologies had EPEAT gold certification. The reply was incorrect as EPEAT gold certification was obtained (24 March 2015) after placing supply order by KELTRON.

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<sup>55</sup> Electronic Product Environmental Assessment Tool (EPEAT) is a free and trusted source of environmental product ratings that makes it easy to select high-performance electronics that meet an organisation's IT and sustainability goals. Manufacturers register products based on the devices' ability to meet various criteria developed and agreed upon by diverse stakeholders to address the full lifecycle of an electronic product.

<sup>56</sup> A Public Sector Undertaking.

### **Lapses in installation of integrated security system for Sree Padmanabha Swamy Temple**

**3.2.3** GoK approved (27 October 2012) KELTRON's proposal for integrated security system for Sree Padmanabha Swamy Temple and State Police Chief, Kerala made advance payment (March 2013) of ₹9.54 crore to KELTRON for it.

We observed that KELTRON could not complete the installation of seven speed folding doors costing ₹1.61 crore as the Executive Committee of the Temple did not permit it. Permission of the Thanthri (priest) was required for any changes to be made inside the temple, which was not obtained by KELTRON. We also observed (April 2016) in a joint physical verification that KELTRON purchased excess material valuing ₹0.25 crore. Similarly, bollards installed in the North, East and West Nadas were not working and road blockers installed in East, West and South Nadas were also not working.

GoK replied (February 2017) that road blockers and bollards were being rectified. The fact, however, remains that these equipment were not fully rectified and warranty for road blockers and bollards would expire in December 2017 while that of speed folding doors would expire in August 2017.

#### **Payment for supplies not conforming to specifications**

**3.2.4** KELTRON ordered (06 March 2014) four day-night vision binoculars from Trident Infosol Private Limited (Trident) after inviting limited tenders, for Integrated Security System (ISS) in Sree Padmanabha Swamy Temple. According to the terms of purchase order, payment was to be made against delivery and acceptance of material.

We noticed that KELTRON staff had taken the binoculars into stock and paid ₹6.53 lakh (80 *per cent* of value of supply, including tax) on the day of receipt (15 May 2014). Deputy Commissioner of Police, Sree Padmanabha Swamy Temple Security rejected (March 2015) the binoculars due to non-conformity to order specifications. Thus, ₹6.53 lakh were spent wastefully due to KELTRON's undue haste in making payment to Trident. Trident did not replace the items (April 2016).

#### **Execution of civil works on behalf of agencies of GoK**

**3.2.5** GoK and its agencies executed various civil construction works through PSUs such as SIDCO, Kerala State Construction Corporation Limited (KSCC), Kerala Irrigation Infrastructure Development Corporation Limited (KIIDC), Forest Industries Travancore Limited (FIT), Kerala State Coastal Area Development Corporation Limited (KSCADC) and Roads and Bridges Development Corporation of Kerala Limited (RBDCK). These PSUs received (2013-14 to 2015-16) 166 work orders valuing ₹2,111.67 crore from various departments of GoK for execution of civil works. Out of these, we examined 107 work orders valuing ₹1,718.81 crore in order to ascertain transparency in award of work and efficient execution.

All 107 work orders examined by us were issued to PSUs on nomination basis in violation of the provisions of Kerala Financial Code (KFC). These works were subsequently sub-contracted by the PSUs. Deficiencies noticed in the award of work by PSUs and their execution is discussed below.

### Award of work to sub-contractors

3.2.5.1 We noticed violation of codal provisions in award of 69 works to sub-contractors by four PSUs as detailed in Table 3.9.

**Table 3.9: Irregularities in award of work to sub-contractors**

Sl. No.	Criteria/ Norm	Audit Observation
1	One of the conditions prescribed for empanelment of a firm with SIDCO for execution was that they should possess at least one year's experience in their field of activity.	One firm, DNA Creatives (DNAC) was empanelled (July 2014) by SIDCO just after registration (5 July 2014) of the firm. We also noticed that two <sup>57</sup> work orders received from Department of Museums and Zoos were awarded (September 2014) to DNAC for ₹2.17 crore against estimate of ₹2.66 crore.
2	As per Rule 7.7 of SPM, tenders should be invited for purchase of stores if the estimated value of stores is above ₹1 lakh.	KIIDC issued (May 2014 to February 2015) five work orders for installation of biogas plants at a cost of ₹1.67 crore under project of Implementation of Urban Environment Improvement Project to six suppliers without invitation of tenders.
3	According to Paragraph 217 of Kerala PWD manual, work cannot be started before preparation of estimate and sanction by the competent authority. Administrative Sanction (AS) and Technical Sanction from competent authority shall precede a tender.	KSCC executed (February 2016) extra work in connection with construction of new bridge across river Payaswini (Athanadi Bridge) in Kasargod district before obtaining AS for the extra work.
4	As per CVC direction, limited tenders should be invited from the panel of approved contractors.	All the 55 sub-contracts valuing ₹930.16 crore entered into (during the three years from 2013-14 to 2015-16) by KSCC, which were selected for scrutiny, were awarded to contractors on nomination basis. As against the directions of BoD of KSCC, in the initial empanelment (2011-12), 10 out of 67 contractors did not meet 5 out of the 6 criteria fixed by the BoD for empanelment.
5	According to the guidelines issued (November 2002) by CVC for award of works, it was stated (paragraph 18) that security deposit (Bank Guarantee) of a reasonable amount and valid up to the defect liability period should be obtained from the contractor.	KSCC executed six <sup>58</sup> works without obtaining Security Deposit from the sub-contractors.

<sup>57</sup> Work order for modification of the interior of the enclosure in reptile house at ₹0.39 crore and work order for construction of enclosure for Anaconda and King Cobra at ₹1.78 crore.

<sup>58</sup> Heavy Maintenance to Ottappalam- Mannarkkad Road, Construction of Academic Block in Medical College campus, Thrissur, Construction of new bridge across river Payaswini (Athanadi Bridge) in Kasargod District, Nettoor-Kundannur Bridge (Parallel) across Nettoor-Kundannurpuzha, Construction of Regulator cum Bridge at Purapallikkavu across Periyar river, Construction of Nanichery Kadavu Bridge across Baliapattanam river in Kannur District.

**Execution of civil works by sub-contractors**

3.2.5.2 Issues noticed in execution of civil works by sub-contractors are discussed below:

- There was delay in execution of five civil works sub-contracted by SIDCO and five works by KSCC as detailed in *Table 3.10*.

**Table 3.10: Delay in execution of civil works**

Sl. No.	Name of work	Name of contractor (Date of award of work)	Awarded cost (₹ in crore)	Scheduled date of completion	Progress as of February 2017 (per cent)	Remarks
<b>Kerala Small Industries Development Corporation Limited</b>						
1	Construction of roads, retaining wall, community hall in Karakulam Panchayath (Maruthur/Manjamcode SC Colony) for Scheduled Castes and Scheduled Tribes Development Department.	Angle Plus Private Limited (September 2014)	0.69	May 2015	33.70	Work was delayed as the revised estimate was not approved by Scheduled Castes and Scheduled Tribes Development Department.  GoK replied (February 2017) that the works were delayed due to lack of supervisory personnel in SIDCO. Reply was not acceptable as GoK had issued work to SIDCO on nomination basis without ensuring its capability.
2	Construction of water tank, community hall in Andoorkonam Panchayath (Apollo Colony) for Scheduled Castes and Scheduled Tribes Development Department.	Shri D. Sasidharan (January 2015)	0.60	October 2015	0.09	Work was delayed as the revised estimate was not approved by Scheduled Castes and Scheduled Tribes Development Department.  GoK replied (February 2017) that the delay was due to dispute with the contractor which had since been resolved and the contractor given instructions to restart the work. The fact, however, remains that work is yet to be completed.
3	Construction of well, water tank, Mini community hall in Andoorkonam Panchayath (Sreepadam Colony) for Scheduled Castes and Scheduled Tribes Development Department.	Angle Plus Private Limited (September 2014)	0.81	July 2015	48.15	Work was delayed as the revised estimate for digging a bore well in addition to well already constructed was not approved by Scheduled Castes and Scheduled Tribes Development Department.  GoK replied (February 2017)

						that the construction of the well was completed as per original estimate. Reply is not acceptable since the actual requirements of the residents were not properly assessed.
4	Work for setting up a museum at Kanakakkunnu Palace for Department of Tourism (DoT).	Not yet (as of March 2016) awarded by SIDCO.	0.60	NA	NA	The work was entrusted to SIDCO in May 2010. DoT released (September 2010) ₹29.96 lakh to SIDCO but the work was not completed even after five years as the details of the project was not forwarded to SIDCO by DoT. GoK in its reply (February 2017) admitted the audit finding and stated that DoT did not forward the details of project to SIDCO.
5	Construction of multi storeyed industrial estate at Puthussery, Palakkad for Director of Industries and Commerce.	Entec Engineers (June 2013)	5.97	June 2015	Nil	Work is yet to be commenced as the site is not cleared yet (December 2016). GoK replied (February 2017) that the work was re-allotted to another implementing agency.
<b>Kerala State Construction Corporation Limited</b>						
6	Construction of new block for nephrology unit and dialysis centre at General Hospital Pala for Public Works Department.	Theruvath Builders (March 2014)	8.04	April 2015	Nil	Due to intervention of the Hon'ble High Court of Kerala, the work was stalled as a writ petition was filed by an individual residing near the construction site alleging that the construction was carried out without providing the required minimum set back of 5 metres-as provided in the site plan-from the petitioner's property. It was also alleged that there was no approved Building Plan for the project. Considering the allegations, the Honourable High Court ordered (April 2016) KSCC to restrain from undertaking the construction.
7	Construction of Nettoor – Kundannur Bridge for Public Works Department.	Greenworth Infra Structures Private Limited (October 2013)	26.57	June 2016	53	As per PWD Manual 2012, (Paragraph 2102.1 and 2101.1) after executing the agreement, the site has to be taken over from the Assistant Engineer (PWD) to commence the work immediately and where any



8	Construction of bridge near Mankombu Civil Station across Manimala river for Public Works Department.	Contour Constructio ns Private Limited (March 2014)	24.47	March 2016	42	delay is anticipated, the matter shall be brought to the notice of the authority who executed the agreement.  KSCC did not analyse the site condition before awarding (June 2013 to July 2015) the works which resulted in unnecessary delay due to hindrances at site.
9	Construction of Nilambur bypass road for Public Works Department.	Thrimathy Contracting Company (February 2014)	18.34	July 2015	Not commenced	
10	Construction of regulator cum bridge at Purapallikkavu across Periyar River for Irrigation Department.	Seguro Foundations and Structures Private Limited (March 2015)	99.86	September 2017	12	

- According to CVC directions (April 2007), payment of mobilisation advance (MA) should be made only if it is clearly stipulated in the tender document. Amount of MA, interest to be charged, recovery schedule, etc., should be stipulated in the tender document upfront. CVC further clarified (February 2011) that in order to enable recovery, MA should be granted only after obtaining Bank Guarantee equivalent to 110 *per cent* of MA.

SIDCO had granted MA of ₹1.51 crore in respect of two work orders<sup>59</sup>, despite there being no such stipulation in the tender document. In both the above cases, MA was granted interest-free, resulting in loss of interest of ₹0.16 crore<sup>60</sup>. Similarly, KSCC released (October 2013 to December 2015) MA of ₹11.43 crore without obtaining required Security Deposit of ₹12.56 crore in respect of five<sup>61</sup> work orders of Public Works Department (PWD).

GoK accepted (February 2017) the audit observation and stated that the amount paid as MA in SIDCO had since been recovered with interest.

- According to the directions (September 2007) of GoK, PSUs executing civil works on behalf of GoK were eligible for centage/ consultancy charge ranging between five and eight *per cent*<sup>62</sup> on the estimated cost or the actual cost of construction, whichever was lower.

<sup>59</sup>(Amount of MA in brackets) Construction of District Youth Bhavan at Panamaram, Wayanad at ₹2.21 crore (₹0.50 crore during July-August 2014) and Construction of multi-storeyed industrial estate building at Puzhakkalpadam, Thrissur at ₹10.09 crore (₹1.01 crore in January 2013).

<sup>60</sup> Up to March 2016- Panamaram: ₹0.04 crore, Puzhakkalpadam: ₹0.12 crore.

<sup>61</sup>Amount of SD required given in brackets. Heavy Maintenance to Ottappalam Mannarkkad Road (₹1.13 crore), Construction of Academic Block in Medical College campus, Thrissur (₹4.12 crore), Construction of new bridge across river Payaswini (Athanadi Bridge) in Kasargod District (₹3.85 crore), Nettoor-Kundannur Bridge (Parallel) across Nettoor-Kundannurpuzha (₹1.48 crore) and Construction of Bridge near Mankombu Civil Station across Manimala river in Alappuzha District (₹1.98 crore).

<sup>62</sup> ₹5 crore and above- 5 *per cent*, between ₹3 crore and ₹5 crore – 6 *per cent*, between ₹50 lakh and ₹3 crore - 7 *per cent*, less than ₹50 lakh - 8 *per cent*.

In respect of eight<sup>63</sup> work orders issued (August 2014 to May 2015) by Department of Museums and Zoos, GoK, SIDCO received an amount of ₹8.83 crore in advance being the estimated cost of the works plus 7 per cent centage charges. Actual cost of execution of the eight works was ₹7.83 crore. As such SIDCO was eligible for an amount of ₹8.38 crore (actual cost ₹7.83 crore + ₹0.55 crore as centage charges being 7 per cent of the actual cost). However, SIDCO retained ₹1 crore as centage charges and not refunded the difference amount of ₹0.45 crore (₹8.83 crore - ₹8.38 crore). Thus, SIDCO obtained undue benefit of ₹0.45 crore by charging excess centage.

GoK accepted (February 2017) the audit observation and stated that charging excess centage was against the Government direction.

- The work of development of Manappattuchira Environs at Malayattoor was awarded (September 2010) to SIDCO by Tourism Department and subcontracted by (October 2010) SIDCO to Shri P.A George. Though the work was completed on 31 December 2012, the building was handed over by SIDCO to Tourism Department only in October 2016. Due to this, local people had occupied the building using its rooms and toilet facilities. The expenditure of ₹77.20 lakh incurred for the project, remained blocked up for nearly four years and the loss caused due to unregulated use and lack of maintenance was not ascertainable.

GoK replied (February 2017) that the said problem had already been solved and the building was handed over to the Tourism Department on 6 October 2016. The fact, however, remains that there was avoidable delay of nearly four years in utilising completed asset.

### Quality of construction work

3.2.5.3 We noticed poor quality of construction and violation of codal provisions in respect of six civil works executed by three PSUs as given in Table 3.11.

**Table 3.11: Details of poor quality of construction of civil works**

Sl. No.	Name of work sub-contracted	Audit Finding
<b>Kerala Small Industries Development Corporation Limited (SIDCO)</b>		
1	Construction of industrial complex at Kakkanad for Directorate of Industries and Commerce awarded (June 2010) to Shri. Kunju Makkar for ₹1.69 crore.	Since the work was completed within the scheduled period, the contractor was given a bonus of ₹0.94 lakh in accordance with extant directions (August 1997) of GoK. The Vigilance Officer, SIDCO noticed that the material used for plastering and for the toilets were inferior in quality and the correct percentage of material mixing was not adhered to. As a result,

<sup>63</sup> Construction of enclosures for Blue Bull at the Zoological Gardens, Construction of enclosures for Hyena at the Zoological Gardens, Construction of enclosures for Barking Deer at the Zoological Gardens, Construction of enclosures for Jackal at the Zoological Gardens, Construction of enclosures for Malabar Giant Squirrel at the Zoological Gardens, Construction of enclosures for Anaconda and King Cobra at the Zoological Gardens, Modification of interior of the enclosure in Reptile House of Museum and Zoo at Thiruvananthapuram and Construction of Kids' park at Museum and Zoo at Thrissur.

Sl. No.	Name of work sub-contracted	Audit Finding
		<p>the building was in shabby condition. Though as per the terms of work order the contractor was to rectify all these defects, maintenance of the building was entrusted (June 2015) to another contractor at an agreed amount of ₹0.93 lakh. SIDCO neither initiated any action to recover the extra expenditure caused by the negligence of the original contractor nor fixed responsibility on SIDCO officials who had not ensured quality of the work executed.</p> <p>GoK replied (February 2017) that SIDCO completed the work to the satisfaction of DI&amp;C and the cost of maintenance was met within the bonus amount received by SIDCO for the early completion of the work. The reply is not acceptable as the quality of the work executed was not ensured by SIDCO.</p>
2	Project of execution of “Storm water stream management at Edakkal area Kovalam” for Department of Tourism (DoT) awarded (May 2013) to Shri. P.A. George for ₹0.86 crore.	<p>Due to unscientific construction, the floor level of the <i>thodu</i><sup>64</sup> was raised from the previous level causing water logging in the area which turned into a reason for agitation including filing of cases before the Hon’ble Court by the residents. District Collector requested (19 July 2014) SIDCO to look into the matter and take urgent steps to make changes in the construction to ensure free flow of water through the <i>thodu</i> by avoiding accumulation of water around the new construction.</p> <p>GoK replied (February 2017) that SIDCO completed the work as per the plan approved by DoT. Even though SIDCO suggested (30 October 2014) corrective measures in the drawings of the said plan, no response was received from DoT.</p>
3	Implementation of ‘Development of gateway of Nilambur at Unarvu, Malappuram’ for DoT awarded (April 2012) to Shri. N.S. Luka for ₹0.97 crore.	<p>The project executed so far did not satisfy the requirements of the DoT. SIDCO had carried out the work without consulting either the DoT or the Architect. Though ₹0.93 crore was paid to the contractor, the scope of the work was not as envisaged in the administrative sanction for the project, thereby the whole expenditure became unfruitful. DoT reported that the deviations was done by the contractor without approval and fixed responsibility for the same on SIDCO.</p> <p>GoK replied (February 2017) that the bills of the contractor had since been accepted. The reply is not acceptable as the issue pointed out by us has not been addressed.</p>
<b>Kerala State Coastal Area Development Corporation Limited (KSCADC)</b>		
4	Revamping of Government Regional Fisheries Technical HS & VHS Thanur, Malappuram for Fisheries Department, awarded (January 2015) to Shri. K. Manikantan for ₹2.28 crore.	<p>As per soil investigation report for the work the ideal foundation of the building was large bored piles with diameter of 1.5m to 1.8m. KSCADC, however, tendered and awarded the work without making provision for piling by ignoring the recommendation in the soil investigation report. The work was completed in July 2016.</p>
5	Construction of New Academic Block for Government LPS, Thrikkunnappuzha for Fisheries Department	<p>Estimate presented before NABARD was prepared without considering required pile foundation. Due to this, essential structures (compound wall as well as toilet block) had to be deleted by settling for a smaller pile than recommended one thus, compromising the structural stability of the building.</p>

<sup>64</sup> A small stream.

Sl. No.	Name of work sub-contracted	Audit Finding
	awarded (June 2015) to Shri. P.I. Noushad for ₹0.44 crore.	
<b>Roads and Bridges Development Corporation of Kerala Limited</b>		
6	Construction of River Bridge at Station Kadavu for PWD awarded (May 2012) to Hope Constructions for ₹16.84 crore.	Failure of the sub-contractor to mobilise resources at site resulted in foreclosure of contract without any risk and cost to the sub-contractor. Retendering of balance work, despite objection from Finance Department resulted in cost increase of ₹6.44 crore.

### Conclusion

**KELTRON and SIDCO awarded work orders to their business partners on nomination basis and through tendering that was tailor-made to suit their business partners. Thus, a few firms viz., Mediatronix, RP Tech Net-X Technologies and SIPL managed to obtain major orders of GoK through KELTRON and SIDCO without complying with provisions of KFC, SPM and CVC guidelines. Besides, due to involvement of PSUs in the execution of works of GoK through private parties, GoK had to incur extra expenditure. In execution of civil works also, there was non-compliance with provisions of KFC, SPM and CVC directives.**

### Recommendation

- 1. GoK should dispense with the system of awarding works to PSUs on nomination basis.**
- 2. GoK should comply with the provisions of SPM and invite competitive tenders.**
- 3. PSUs which get work orders after participating in tenders should ensure that all the provisions of SPM and CVC guidelines are complied with.**

### 3.3 Corporate Social Responsibility of PSUs

#### Introduction

**3.3.1** Corporate Social Responsibility (CSR) refers to operating business in a manner that accounts for the social and environmental impact created by the business. Through CSR, companies give something back to society. CSR means and includes projects or programmes on eradication of hunger, poverty and malnutrition, promoting gender equality, promoting education, empowerment of women, ensuring environmental sustainability, protection of national heritage, etc. CSR is governed by provisions of the Companies Act, 2013 (Act) and Companies (Corporate Social Responsibility Policy) Rules, 2014 (CSR Rules).

According to Section 135 of the Act, companies with annual turnover of ₹1,000 crore or more or net worth of ₹500 crore or more or profit (before tax) of ₹5 crore or more in any of the three preceding financial years<sup>65</sup> have to spend at least two *per cent* of average profit<sup>66</sup> of such preceding financial years on CSR activities from 2014-15 onwards, giving preference to areas around their operation.

As of June 2016, 23 Public Sector Undertakings (PSUs) in Kerala came under the purview of CSR during 2014-15 to 2015-16. We assessed compliance of these PSUs with the provisions of the Act/ CSR Rules/ orders and notifications issued by Ministry of Corporate Affairs (MCA), Government of India (GoI), on CSR. Audit findings are discussed in the succeeding paragraphs.

## Audit Findings

### Formulation of CSR Policy and CSR spending

#### Non-constitution of CSR Committee and non-spending on CSR

3.3.2 As per Section 135(1) of the Act, each of the 23 PSUs was to constitute a CSR Committee consisting of three or more directors, out of which at least one director shall be an independent director. The CSR Committee was to formulate and recommend a CSR Policy and the amount of CSR expenditure to Board of Directors (BoD) and monitor the CSR Policy of the Company.

We noticed that out of the 23 PSUs, 13 PSUs (*Appendix 13*) did not constitute the CSR Committee or formulate the CSR Policy (as of June 2016). Among these 13 PSUs, three PSUs had negative average net profit during the three preceding financial years and hence, were not required to spend on CSR while balance 10 PSUs were required to spend on CSR.

Oil Palm India Limited and Kerala Agro Machinery Corporation Limited, though coming under the purview of CSR law, spent ₹0.33 crore (against the minimum requirement of ₹0.50 crore) for CSR activities without constituting a CSR Committee or formulating a CSR Policy. As the amount was spent without constituting CSR Committee or formulating a CSR Policy, the CSR spending of these two PSUs was irregular.

Similarly, eight PSUs were required to spend at least ₹7.93 crore on CSR during 2014-15 and 2015-16 as detailed in *Appendix 14*. But, they did not spend any amount on CSR during the above period.

GoK replied (October 2016) that Kerala State Power and Infrastructure Finance Corporation Limited (KSPIFC) had spent ₹0.25 crore in 2014-15 on a project for development of woman and child ward at Government Taluk Head Quarter Hospital, Nilambur and was eligible for including the same as CSR. The reply was not tenable as ₹0.25 crore spent during 2014-15 was part

<sup>65</sup>Vide Circular No: 21/2014 dated 18/06/2014 of Ministry of Corporate Affairs, Government of India.

<sup>66</sup>Average of profit made by them during the three immediately preceding financial years.

of ₹0.50 crore donation given to Government Taluk Head Quarter Hospital, Nilambur as per Government Order dated 27 July 2013 and not the amount earmarked for CSR during 2014-15.

State Farming Corporation of Kerala Limited replied (June 2016) that their profit before tax during 2014-15 was less than ₹5 crore and hence, they were not liable to spend on CSR. The reply was not acceptable as its annual profit before tax exceeded ₹5 crore during the preceding three years. Transformers and Electricals Kerala Limited replied (February 2017) that BoD decided not to spend for CSR activities since the Company was continuing in huge losses. Other five PSUs accepted the audit finding and assured compliance with CSR laws.

### **Non/ incorrect reporting on CSR activities**

**3.3.3** According to Section 135 (5) of the Act, in case of failure of a company to spend minimum 2 per cent of average profit on CSR, the BoD shall in its report<sup>67</sup> include the reasons for non-spending.

Out of the ten PSUs which did not spend the required minimum amount on CSR, three PSUs<sup>68</sup> did not report the reason for non-spending and three PSUs<sup>69</sup> wrongly reported that CSR Rules were not applicable to them. The remaining four PSUs were yet to publish their Annual Report as of June 2016.

KSPIFC replied (June 2016) that non-spending was not reported in the Directors' Report due to oversight and necessary disclosures would be made in the next year's report. Two PSUs<sup>70</sup> accepted the audit finding while Kerala Forest Development Corporation Limited replied (July 2016) that they were not aware of the circular dated 18 June 2014 of MCA and assured that the audit finding will be brought to the notice of BoD.

State Farming Corporation of Kerala Limited replied (June 2016) that the matter was reported correctly in the Annual Report 2014-15. The reply was not tenable as profit for the period 2011-12 and 2013-14 exceeded ₹5 crore and thus, the Company came under the purview of CSR law.

### **Deficiencies in spending on CSR**

**3.3.4** Ten out of the 23 PSUs covered in audit had constituted CSR committee as well as formulated a CSR policy and spent ₹10.74 crore (*Appendix 15*) on CSR activities during 2014-15 and 2015-16. The following deficiencies were noticed in the CSR expenditure incurred by these 10 PSUs.

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<sup>67</sup> Report attached to the financial statements laid before a company in general meeting as per Section 134 (O) (3) of the Act.

<sup>68</sup> Kerala State Power and Infrastructure Finance Corporation Limited, Transformers and Electricals Kerala Limited and Oil Palm India Limited.

<sup>69</sup> The State Farming Corporation of Kerala Limited, Kerala Forest Development Corporation Limited and Kerala Agro Machinery Corporation Limited.

<sup>70</sup> Kerala Agro Machinery Corporation Limited and Transformers and Electricals Kerala Limited.

### **Non-spending on CSR**

**3.3.4.1** Two PSUs<sup>71</sup> did not spend any amount on CSR during 2015-16 though they had to spend ₹0.67 crore as per the Act.

Rehabilitation Plantation Limited replied (July 2016) that they would spend the amount earmarked for CSR during 2016-17.

### **Non-display of CSR policy in website**

**3.3.4.2** Section 135 (4) (a) of the Act and Rule 9 of CSR Rules specify that the approved CSR Policy shall be displayed on the company's website. Four PSUs<sup>72</sup> did not display the CSR Policy on their website.

At our instance, three PSUs<sup>73</sup> agreed to display their CSR policy on their websites, while Malabar Cements Limited replied (August 2016) that they had displayed the schemes of assistance on their website. The reply is not tenable as this amounts to violation of Section 135 (4) (a) of the Act and Rule 9 of CSR Rules.

### **Inclusion of activities in the CSR Policy undertaken in pursuance of normal course of business**

**3.3.4.3** According to CSR Rules, a company shall undertake CSR activities as per its stated CSR Policy. Activities undertaken in pursuance of normal course of business of a company shall not be treated as part of CSR.

We observed that the CSR Policy (Item number-1) of Kerala State Backward Classes Development Corporation Limited (KSBCDC) (engaged in the upliftment of backward classes and minority communities by rendering financial assistance) states that where loanees are unable to repay loan due to fatal disease, accident, death, *etc.*, after ascertaining the position of the family, the principal, interest and compound interest would be partially or completely waived by including them under the Loanees Distress Relief Fund (LDRF) scheme. The LDRF is a fund set up to meet any future contingencies that may arise out of death or accidental disablement of the loanees. This is directly related to the business activity of KSBCDC and hence, item number-1 does not come under the purview of CSR.

GoK replied (January 2017) that if the LDRF scheme of the Company could not be counted under the ambit of CSR activity, necessary corrective action would be taken in future.

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<sup>71</sup> Rehabilitation Plantations Limited and Kerala Transport Development Finance Corporation Limited.

<sup>72</sup> Kerala State Backward Classes Development Corporation Limited (KSBCDC), Kerala Transport Development Finance Corporation Limited (KTDFC), The Pharmaceutical Corporation (Indian Medicines) Kerala Limited (TPCKL) and Malabar Cements Limited (MCL).

<sup>73</sup> Kerala State Backward Classes Development Corporation Limited (June 2016), Kerala Transport Development Finance Corporation Limited (May 2016) and The Pharmaceutical Corporation (Indian Medicines) Kerala Limited (July 2016).

### **CSR spending on inadmissible activities**

**3.3.4.4** Ministry of Corporate Affairs (MCA), GoI stipulated<sup>74</sup> that expenses incurred by companies for the fulfilment of any Act/ Statute or Regulations would not count as CSR expenditure under the Act. The Kerala Minerals and Metals Limited had spent an amount of ₹1.09 crore as part of CSR activity during 2014-15 and 2015-16, out of which ₹0.45 crore was spent as part of a legal obligation and financial assistance to Panmana panchayath for budget presentation, etc., which do not fall within the purview of the Act. Hence, the same could not be counted as CSR expenditure.

The Company replied (July 2016) that amount shown as CSR for the year 2014-15 and 2015-16 would be reviewed.

### **Contribution in kind for CSR activities**

**3.3.4.5** Section 135 (5) of the Act specifies that the BoD of every company shall ensure that the company spends, in every financial year, the required amount in pursuance of its CSR Policy. MCA reiterated (January 2016) that contribution in kind cannot be monetised to be shown as CSR expenditure.

During 2014-15 and 2015-16, Malabar Cements Limited (MCL) distributed cement in kind valuing ₹0.08 crore while the Pharmaceutical Corporation (Indian Medicines) Kerala Limited (TPCKL) distributed medicines valuing ₹0.19 crore and accounted for them as CSR activities.

TPCKL replied (August 2016) that they would take into consideration the audit findings when formulating a new CSR policy after the reconstitution of the BoD. MCL replied (August 2016) that cement was distributed after booking the expenses for CSR expenditure.

### **Contribution to State Government fund**

**3.3.4.6** According to Notification issued (27 February 2014) by MCA, contribution under CSR is permissible only to Prime Minister's National Relief fund or any other fund set up by Central Government. We, however, noticed that Kerala State Financial Enterprises Limited contributed (September 2015) an amount of ₹0.50 crore to Karunya Benevolent fund, a fund constituted by GoK.

GoK replied (December 2016) that the amount was contributed by the PSU on receiving letter from administrator of Karunya Benevolent fund with specific reference to make contribution under CSR. The reply was not tenable as contribution to funds set up by the State Governments was not permitted by MCA.

### **Absence of monitoring**

**3.3.4.7** Rule 5 (2) specifies that CSR Committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or

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<sup>74</sup>Vide Circular No. 21/2014 dated 18/06/2014.



programmes or activities undertaken by the company. We noticed instances of absence of monitoring of CSR as shown in *Appendix 16*.

### Conclusion

**Adherence of companies to the provisions of CSR was not satisfactory as 13 out of 23 companies did not constitute CSR Committee/ Policy. There were instances of non-spending and spending on inadmissible activities. GoK may, therefore, formulate appropriate monitoring mechanism for strict adherence to CSR laws.**

### Department of Tourism

#### 3.4 Lapses in empanelment of agencies and awarding of works

**Empanelment of agencies for promotion and marketing of tourism was marred by non-compliance to codal provisions leading to arbitrary selection of agencies and extra expenditure.**

**3.4.1** Department of Tourism (DoT), Government of Kerala (GoK) empanels agencies for promotion and marketing of tourism in Kerala. Director of Tourism requested (February 2013) Secretary, DoT, GoK for empanelment of new advertising/ marketing agencies for the period 2013-14 to 2015-16, as the tenure of the existing agencies was expiring in June 2013. The GoK accorded (March 2013) sanction for constitution of a Screening Committee<sup>75</sup> for the evaluation and selection of the agencies. Notification for empanelment of marketing agencies was issued (March 2013) for two categories namely, Marketing and Local Advertising.

There were 25 applicants under the first category and 27 applicants under the second category. Pre-bid meetings were held (June 2013) and 18 agencies were shortlisted in Marketing category and 23 agencies in Local Advertising category. Based on the evaluation<sup>76</sup> by the Screening Committee, seven agencies were empanelled under Marketing category and seven agencies under Local Advertising category for a period of three years.

We observed the following irregularities in the empanelment of agencies and award of works:

#### **Amendments of terms and conditions, post tender**

**3.4.2** Stores Purchase Manual of GoK and CVC guidelines prohibit amendments of terms and conditions, post tender.

We observed that after invitation of tender, the Marketing category was split into four broad categories namely, Branding and Advertising, International

<sup>75</sup>Comprising of Secretary, DoT; Secretary, Finance (Expenditure); Secretary, Planning and Economic Affairs Department; Managing Director of Kerala Tourism Development Corporation Limited and Director of Tourism.

<sup>76</sup> Ranking based on presentation, briefing and discussion.

Trade Fairs and Business to Business (B2B) activities, Domestic Trade Fairs and B2B activities and New media and Public Relations (PR) campaigns. As the sub-categorisation was not specified in the tender documents, prospective tenderers for the sub-categories were not able to participate in the tender process and already shortlisted agencies could not modify their bids. Though such sub-categorisation had been done during the previous empanelment process also, DoT failed to notify the sub-categories in the notice inviting tender.

We further observed that although three agencies were selected under the sub-category of Branding and Advertising, DoT further split the sub-category into two – Branding and Advertising within Kerala and Branding and Advertising outside Kerala. The act of sub-categorisation after calling the pre-bid meeting amounted to post-tender amendments.

### **Evaluation of agencies**

**3.4.3** According to the directions issued (September 2003) by CVC, pre-qualification criteria, performance criteria and evaluation criteria should be incorporated in the bid documents in clear and unambiguous terms. The detailed marking scheme for individual aspects/ parameters, i.e. financial capability, technical capability and experience, etc., on which the bid was to be evaluated was to be made available to the participating firms.

We observed that DoT had not prescribed any evaluation criteria for selection of agencies in the Tender Notification. Based on the decision of pre-bid meeting, company competence (20 marks), marketing strategy (30 marks), creativity and innovativeness (30 marks) and overall performance (20 marks) were made the criteria in the respective sub-categories. No yardstick was, however, prescribed for awarding marks nor was any qualification mark prefixed for selection of agencies. Further, number of agencies to be selected under each sub-category was also not specified in the Tender Notification/ pre-bid meeting. As a result, transparency in selection of agencies by the Screening Committee could not be ascertained.

Post tender amendments, as discussed in *Paragraph 3.4.2* coupled with absence of proper evaluation criteria led to the selection of Stark Communications Private Limited (Stark) as single agency for Branding and Advertising outside Kerala and for International Branding and B2B activities, which constituted the major chunk of marketing activities of DoT. Two agencies were selected for Branding and Advertising activities within Kerala, two for Domestic Trade fairs and B2B activities and three agencies for New media and PR campaigns as shown in *Table 3.12*.

**Table 3.12: Details of sub-categorisation**

Categories	Sub-categories	Number	Panel of Agencies
Marketing	Branding and Advertising outside Kerala	1	Stark Communications Private Limited
	Branding and Advertising within Kerala	1	MediaMate Advertising India Private Limited
		2	Maitri Advertising Works Private Limited
	International Trade Fairs and Business 2 Business (B2B) activities	1	Stark Communications Private Limited
	Domestic Trade Fairs and B2B activities	1	Crayons Advertising Limited
		2	AD- India Advertisers
	New media and PR campaigns	1	Draft FCB+ULKA Advertising Private Limited
		2	Stark Communications Private Limited
3		Span Communications, Kochi	
Local Advertising	For printing works	1	Breakthrough, Thiruvananthapuram
		2	Modern Graphics, Kochi
		3	Valappila Communications Private Limited
		4	H2O Spell
	For providing logistics support	1	Impresario Event Management India Limited
		2	AD-India Advertisers
		3	Chrysalis Communications Private Limited

Thus, selection of single agency/ fewer agencies was made despite there being two or more firms shortlisted for all categories.

GoK replied (August 2016) that the shortlisted agencies were informed about the evaluation criteria at the pre-bid meeting and the criteria were also mailed to each shortlisted agency. The reply was not acceptable since according to the directives of CVC, evaluation criteria for selection of agencies were to be specified in the Tender Notification itself and not in pre-bid meeting.

### **Non-invitation of financial bids**

**3.4.4** According to CVC guidelines (September 2003) and Stores Purchase Manual (SPM) of Government of Kerala (GoK), organisations should follow two-bid system, i.e. technical bid and financial bid for award of work. Article 173 of Kerala Financial Code further states that no work may be started before a proper estimate for it has been prepared and sanctioned by the competent authority.

We noticed that the empanelment of the agencies was done by way of evaluation of the technical bid only and the DoT failed to invite financial bids from among the empanelled agencies while awarding works. Rather, the work orders were issued on nomination basis to the empanelled agencies based on the estimate submitted by them. During 2013-14 to 2015-16, 81 work orders worth ₹56.82 crore were issued on nomination basis without inviting financial bids.

We also noticed that DoT awarded 18 work orders valuing ₹13.93 crore for conducting international fairs to Stark, the single empanelled agency, on nomination basis. Similarly, 40 work orders valuing ₹31.74 crore for conducting Branding and Advertising works outside Kerala were also awarded

to Stark on nomination basis. As DoT empanelled only one agency for these sub-categories, the reasonableness of the financial quote submitted by the agency could not be ensured by DoT.

In respect of Domestic Trade Fairs also, where there were two empanelled agencies<sup>77</sup> DoT did not obtain financial bids, despite having knowledge about tentative dates of domestic trade fairs. Work orders for 16 Domestic Trade Fairs, valuing ₹1.53 crore were issued on nomination basis to one agency (AD-India Advertisers). DoT, Karnataka had also participated in these Domestic Trade Fairs. On a comparison of the expenditure incurred by DoT, Kerala with DoT, Karnataka, we noticed that the cost per square metre (sq.m.) incurred by DoT, Kerala and DoT, Karnataka was ₹20,158<sup>78</sup> and ₹7,201<sup>79</sup> respectively.

GoK replied (August 2016) that single bid system helped in preventing unhealthy practice of cartelisation between the agencies in a category, which can lead to cost escalation and severe quality compromises. The GoK further replied that though the Directorate did not prepare estimates, the estimates submitted by the agencies were closely scrutinised before approval. The competitiveness of the estimates was also checked by comparing it with events of such nature in the past.

The reply was not acceptable since the practice followed by DoT was in violation of CVC guidelines and SPM. Invitation of competitive financial bids was the only method to break the nexus of cartelisation among bidders. In the absence of estimates, the past rates adopted for comparison were not obtained through competitive tenders but was the rate submitted by the empanelled agency selected on nomination basis.

### **Non-execution of agreement**

**3.4.5** As per Article 181 of Kerala Financial Code, no work which is to be executed under a contract should be started until the contractor has signed a formal written agreement. If no formal agreement is executed, there should at least be a written understanding specifying terms and conditions of the contract including prices and rates, etc.

We noticed that in violation of the above Article, GoK stipulated (August 2012) that the payment of all the items would be on the basis of actual costs based on bills and vouchers presented. We also noticed that the DoT did not enter into any agreement with the executing agency in respect of any of the works and made the payments to them based only on the bills submitted by the agencies without supporting vouchers.

GoK replied (August 2016) that due to procedural delays, budgetary constraints and treasury restrictions, DoT might not be able to fulfil obligations and an agreement might leave it vulnerable to the claims from agencies for additional payments and interest. The reply was not acceptable

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<sup>77</sup> Crayons Advertising Limited and AD- India Advertisers.

<sup>78</sup> DoT, Kerala spent ₹1.53 crore for conceptualisation works in 759 sq.m area occupied.

<sup>79</sup> DoT, Karnataka spent ₹0.79 crore for conceptualisation works in 1,097 sq. m area occupied.

since it was bound to comply with the provisions of Kerala Financial Code. Further, in the absence of formal written agreement, the DoT could not claim any loss due to non-execution of works by agencies.

### Conclusion

**The empanelment of agencies for marketing activities was beset with non-compliance to CVC guidelines and Stores Purchase Manual of Government of Kerala. Further, Department of Tourism failed to ensure competitiveness of rates for works executed due to award of works without obtaining financial bids.**

### Recommendation

1. **The Department of Tourism should avoid post tender amendments by incorporating pre-qualification criteria and evaluation criteria specifically for each sub-category of marketing activity.**
2. **Empanelment of single agency should also be dispensed with and financial bids should be obtained from among empanelled agencies.**

### 3.5 Irregular appointment of employees in PSUs, Forest and Public Works Departments

**Appointment of employees in violation of existing Government directions and irregular regularisation of temporary employees resulted in failure to ensure transparency and fairness in recruitment.**

**3.5.1** Public Sector Undertakings (PSUs) appoint employees on permanent and temporary basis. As per circular issued (5 September 1986) by Planning and Economic Affairs (Bureau of Public Enterprises) Department, Government of Kerala, all employees of PSUs, excluding workers (covered under the Factories Act) and supervisory or managerial personnel (whose basic starting salary exceeds ₹700<sup>80</sup>), are to be recruited through the Kerala Public Service Commission (KPSC). For this, the PSUs were to frame Staff Regulation/ Recruitment Rules and include the name of the PSU in the list of PSUs specified under sub rule (d) of rule 2, Kerala Public Service Commission (Consultation by Corporation and Companies) Rules, 1971.

We examined recruitment process in eight<sup>81</sup> PSUs, Forest and Public Works Departments. Audit findings are as follows:

#### **Irregular appointment of permanent employees**

**3.5.2** We noticed irregular appointment of 161 permanent employees in Kerala Small Industries Development Corporation Limited (SIDCO) and

<sup>80</sup> Salary as of September 1986 excluding Dearness Allowance, incentive bonus, annual bonus, etc.

<sup>81</sup> Kerala Small Industries Development Corporation Limited, Kerala Industrial Infrastructure Development Corporation, Kerala State Construction Corporation Limited, Indian Institute of Information Technology and Management, Kerala, The Kerala State Financial Enterprises Limited, Kerala State Industrial Enterprises Limited, Oil Palm India Limited and Kerala State Poultry Development Corporation Limited.

Indian Institute of Information Technology and Management, Kerala (IIITM-K) as discussed below.

- As per Staff Regulation of SIDCO, its Board of Directors (BoD) was empowered to recruit workers directly. Government of Kerala (GoK) had, while approving revision of pay for the employees of SIDCO, directed (February 2009) SIDCO not to appoint any employees, regular or temporary, without prior concurrence of Finance Department, GoK. Further, in view of the lack of transparency in direct appointment by PSUs, Industries Department, GoK ordered (August 2012) that Public Sector Reconstruction and Internal Audit Board (RIAB) shall scrutinise vacancies in PSUs, issue common advertisement and ensure transparent recruitment process.

SIDCO recruited (August 2015) 157 unskilled workers in 11 production units through KITCO<sup>82</sup>. Originally notified number of vacancies was 40. During the recruitment process, this was increased to 160 by converting peon posts (120) into worker category.

We observed that the recruitment to the post of peons was entrusted to KPSC as per the Staff Regulation of SIDCO. The Company, however, converted 120 peon posts into worker category without the concurrence of KPSC and made the recruitment directly. This was irregular. Further, the production units for which the recruitment was made, included three<sup>83</sup> defunct units with 43 converted posts of workers. These production units had not been functioning for a long time and there were no proposals to revive them. After recruitment, the recruited persons were posted in non-production units like, Marketing (49), Raw Material (25), Sales (19), Head Office (13), Estates (8), Construction (7) and others (20) though they were recruited against specific production posts with defined pay scale. These employees were paid average monthly emoluments amounting to ₹16,396 each. Thus, the additional annual financial commitment of ₹2.30 crore<sup>84</sup> due to recruiting excess staff without actual requirements and without following approved procedure was tantamount to irregular expenditure. The recruitment was also done without the concurrence of the Finance Department, GoK.

We also noticed that recruitment of 157 employees was not referred to RIAB in violation of the orders (August 2012) of Industries Department.

GoK stated (February 2017) that since the production units, for which the workers were recruited had been incurring loss, these employees were deployed to other divisions of SIDCO on working arrangement basis.

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<sup>82</sup> Formerly Kerala Industrial and Technical Consultancy Organisation Limited.

<sup>83</sup> SEC, Monvila, SIDCO Tiles, SIDCO Auto Engineering Unit.

<sup>84</sup> (Basic Pay of ₹2,560 + Variable Dearness Allowance ₹13,836) \* 117 employees (157-40) \* 12 months.

The reply was not acceptable as the reason for not obtaining concurrence of KPSC and prior approval of Finance Department, GoK for the appointments was not furnished.

- KPSC stipulated that if selection to a post is finalised by written test and interview, the maximum marks for interview shall be 20 *per cent* of the maximum marks for the written test. As per the directions of Industries Department, GoK, the interview board should comprise of nominees from Industries Department and RIAB.

We observed that not only there was gross irregularity of recruiting 157 unskilled workers against 40 vacancies by SIDCO, but also the maximum marks for Group Discussion (GD)/ Interview was fixed at 50 *per cent* of total marks. As a result, 16 candidates, who scored 80 *per cent* and above in the written test could not find a place in the selection list due to low marks awarded to them in the GD/ Interview whereas 14 candidates who scored 40 *per cent* and below in the written test were selected for appointment as they scored high marks in the GD/ Interview. Further, three out of four members of the Interview Board comprised officials from SIDCO without any nominees from RIAB.

GoK accepted (February 2017) the audit observations and stated that there was violation of directions of Government that the marks for interview shall not exceed 20 *per cent* of total marks. GoK also stated that a vigilance inquiry had been ordered to look into the entire recruitment process in SIDCO.

- IIITM-K, a PSU, did not frame Staff Regulation required to bring it under the Kerala Public Service Commission (Consultation by Corporation and Companies) Rules, 1971 for recruitment by KPSC. Therefore, recruitment in IIITM-K was made by the PSU itself. As per its interim Staff Guidelines, for appointment as Assistant Professors, candidates should possess doctorate degree with first class in the appropriate branch.

We observed that the Board of Directors of IIITM-K appointed (March 2013) four non-faculty staff as Assistant Professors with direction to acquire the required qualification within seven years of appointment. The appointment was made without advertising the vacancies for giving other eligible candidates an opportunity to apply for the post. The Staff Guidelines of IIITM-K were also not approved by GoK.

Government replied (January 2017) that appointments were made based on the recommendations of the Selection Committee constituted for the purpose and with the approval of Board of Directors. It was also stated that the appointments were done as per Staff Guidelines.

The reply is not tenable as appointment of staff with a condition to

acquire qualifications within seven years was in violation of Staff Guidelines. Opportunity was also not given to public and hence, the appointments were irregular.

### Irregular engagement of temporary staff

3.5.3 As per the provisions of the Employment Exchanges (Compulsory Notification of Vacancies) Act, 1959, vacancies<sup>85</sup> for contract employment exceeding three months were to be notified to the Employment Exchanges. Further, for such employment, Rules for Reservation in Government Service shall be applicable. According to Rule 14 of Rules for Reservation in Government Service, unit of appointment for the purpose of reservation shall be 20, out of which two shall be reserved for persons belonging to Scheduled Castes and Scheduled Tribes, eight for other backward classes and remaining 10 shall be from the open category. We observed that six<sup>86</sup> PSUs and one department engaged 1686 contract employees, without notifying the vacancies to Employment Exchanges as detailed in *Table 3.13*.

**Table-3.13: Engagement of temporary staff**

Sl. No.	Audit findings	Management/ Government Reply
1	<b>SIDCO</b> Managing Director, SIDCO appointed (2010-2016) 403 persons on temporary/ contract basis to various posts <sup>87</sup> on nomination basis with an annual financial commitment of ₹2.40 crore on the basis of unsolicited applications submitted by the prospective employees. The remuneration paid to the employees engaged on contract basis ranged from ₹5,000 (Sales Assistant, Peon, Accountant, etc.) to ₹37,500 (Executive Secretary to MD) per month. The appointments were irregular as reservation rules were not followed. There was no concurrence of GoK and was not as per approved staff pattern of SIDCO.	GoK stated (February 2017) that all the temporary employees had been relieved from service and a vigilance inquiry in the matter is underway.
2	<b>KSCC<sup>88</sup></b> Government had directed (March 2013) the Company to make appointments on contract/daily wages/temporary basis only against sanctioned posts. However, the Company appointed 60 employees on temporary basis in various cadres from March 2013 to June 2016, of which 32 were not against any sanctioned post.	Government replied (December 2016) that although sanctioned strength had been fixed, actual requirement would vary depending on the work on hand because the Company was a contracting company.  Reply of GoK was contrary to its own standing orders that contract appointments should be only against sanctioned posts.

<sup>85</sup> Does not apply to vacancies in relation to any employment to do unskilled office work.

<sup>86</sup> SIDCO, Kerala State Construction Corporation Limited, Kerala State Financial Enterprises Limited, Oil Palm India Limited, Kerala State Poultry Development Corporation Limited and Kerala State Industrial Enterprises Limited.

<sup>87</sup> Such as Accounts Executive, Co-ordinator, Assistant Public Relations Officer, HR Executive, Liaison Assistant, Audit Officer, Liaison Officer, etc.

<sup>88</sup> Kerala State Construction Corporation Limited.



Sl. No.	Audit findings	Management/ Government Reply
3	<b>PWD<sup>89</sup></b> The Department appointed 248 daily wage employees against 73 sanctioned posts, out of which only one person was engaged through Employment Exchange. The continuous engagement of employees other than through Employment Exchange is irregular.	Government replied (December 2016) that the daily wage employees were mainly engaged in Rest Houses when the regular staff availed leave and the posting was not permanent. Reply was, however, silent on appointment of workers in excess of sanctioned strength.
4	<b>KSFE<sup>90</sup></b> KSFE recruited 632 Assistants/ Attendants for a period of one year which was not against the sanctioned posts of the Company.	Government replied (January 2017) that all the 632 assistants/office attendants recruited were terminated from service.
5	<b>KEPCO<sup>91</sup></b> KEPCO appointed 230 employees in excess of the sanctioned strength for a period up to one year.	Government replied (November 2016) that as a growing organisation engagement of daily wages and contract employees as per requirement is essential.
6	<b>OPIL<sup>92</sup></b> Seven employees against four posts were appointed on contract/daily wage basis for which there were no sanctioned post.	OPIL replied (November 2016) that the temporary employees were engaged with the <i>bonafide</i> intention of running the rice mills at a low cost.
7	<b>KSIE<sup>93</sup></b> Managing Director (MD), KSIE appointed (October 2015 to June 2016) 106 employees on temporary basis either directly or through Labour Outsourcing Agency. In case of appointment through Labour Outsourcing Agency, the prospective employees would forward their applications to MD who would direct the Labour Outsourcing Agency to appoint the employees.  Based on its inspection (March 2016), Industries Department, GoK ordered (April 2016) to terminate all the appointments made by the MD. Instead of complying with Government directions, the MD appointed 25 more employees. Government replaced (June 2016) the MD. The new MD terminated (June 2016) all the irregularly appointed employees. An amount of ₹39.92 lakh had been disbursed as remuneration to the irregularly appointed employees.	Government replied (March 2017) that all employees who had been irregularly appointed had been terminated.

The replies were only partially acceptable as temporary appointment had to be made from Employment Exchange against sanctioned posts only thereby ensuring transparency, equal opportunity and reservation rules in appointments. Further, no recovery was effected from Managing Director,

<sup>89</sup> Public Works Department.

<sup>90</sup> The Kerala State Financial Enterprises Limited.

<sup>91</sup> Kerala State Poultry Development Corporation Limited.

<sup>92</sup> Oil Palm India Limited.

<sup>93</sup> Kerala State Industrial Enterprises Limited.

KSIE who illegally appointed the employees. GoK should initiate action to fix responsibility for such stark disregard to rules and causing undue huge financial burden on public exchequer.

### Irregular regularisation of contract employees

**3.5.4** The Hon'ble Supreme Court held (April 2006) in Umadevi Vs. State of Karnataka that 'regularisation' is not and cannot be a mode of recruitment by any State. It was also held that regularisation cannot give permanence to an employee whose services are *ad hoc* in nature.

As mandated under Article 14 and 16 of the Constitution, fair chances for all eligible candidates should be given in public appointment which can be achieved through public notice/ advertisement, a transparent selection procedure and adoption of reservation policy for weaker sections. When a person enters a temporary employment or gets engagement as a contractual or casual worker and the engagement is not based on a proper selection as recognised by the relevant rules or procedure, he is aware of the consequences of the appointment being temporary, casual or contractual in nature. Such a person cannot invoke the theory of legitimate expectation for being confirmed in the post when an appointment to the post could be made only by following a proper procedure for selection and in concerned cases, in consultation with the Public Service Commission. The passing of orders for continuance tends to defeat the very Constitutional scheme of public employment.

We observed that two PSUs and two departments regularised 476 employees as detailed in *Table 3.14*.

**Table-3.14: Details of temporary staff irregularly regularised**

Sl. No.	Name of PSU/Department	Temporary staff regularised	Month/Year in which regularised	Audit findings
1	Kerala Industrial Infrastructure Development Corporation	25	February 2016	Regularised with the approval of Industries Department, GoK. The past services of the employees were counted for pay fixation in violation of direction of GoK.
2	KSCC	62	March 2013	The employees were regularised considering long years of service and bleak opportunity for alternative appointment.
3	Forest Department	244	May 2015 to June 2016	Forest Department regularised 244 daily wage workers as Watchers/Part Time Sweeper/Lower Division Clerk as detailed in <i>Appendix 17</i> .

Sl. No.	Name of PSU/Department	Temporary staff regularised	Month/Year in which regularised	Audit findings
4	PWD	145	December 2011	PWD regularised 137 SLR workers <sup>94</sup> in worker category subject to conditional concurrence <sup>95</sup> of Finance Department. The conditional concurrence of Finance Department is a violation of Article 14 and 16 of the Constitution as fair chance to candidates through public advertisement and adoption of reservation rules was not followed.  PWD further regularised eight SLR workers on humanitarian grounds violating the conditional concurrence of Finance Department.
<b>Total</b>		<b>476</b>		

Government replied (November 2016) that the regularisations of employees of Forest Department were made as Government was convinced that the appointees deserved humanitarian and sympathetic consideration. It was also stated that the appointments were made with the approval of Cabinet and after consulting Finance Department.

Government also stated (December 2016) that in respect of KSCC, the appointments were made as there were bleak opportunities for further employment to the regularised employees. It was also replied that in respect of regularisation of 137 SLR workers out of 145 workers in PWD, the appointments were made with the concurrence of KPSC and Finance Department.

The replies are not acceptable as the regularisation of temporary employees is against decision of Hon'ble Supreme Court.

## **Kerala State Financial Enterprises Limited**

### **3.6 Payment of ineligible auction discount and prize money**

#### **Introduction**

**3.6.1** Kerala State Financial Enterprises Limited (Company) was incorporated in 1969 as a Miscellaneous Non-Banking Financial Company (MNBFC), fully owned by the Government of Kerala (GoK), with the object of operating chitty business and to protect the public from unscrupulous private chit fund operators. The activities of the Company are regulated by the Chit Funds Act, 1982.

A "chitty" is a contract between an organisation/ a person and subscribers in which each subscriber agrees to remit monthly a fixed amount of money

<sup>94</sup> SLR Workers – Seasonal Labour Roll Workers, working in all the seasons in a particular scale of pay and not in the regular service.

<sup>95</sup> SLR workers should commence their service after 4 July 1983, should have completed 500 days of service, should be in service as on 1 January 2011 and should not have crossed the age of 55 as on 1 January 2011.

during the duration of the chitty. Total of the monthly subscriptions, called the chitty amount, will be given out each month as prize money to the subscriber who bids for the maximum reduction in the prize money<sup>96</sup>, subject to a maximum of 25 per cent. Amount foregone by the successful bidder in the monthly auction is equally shared among all the subscribers as “auction discount”. Eligibility of subscribers to participate in the auction for prize money and share of auction discount<sup>97</sup> was contingent upon payment of monthly subscription within due date.

In order to assess the transparency and fairness in distribution of prize money and auction discount, we examined transactions during 2011-12 to 2015-16 in nine branches<sup>98</sup> of the Company and noticed instances of irregular payment of auction discount and prize money as discussed in succeeding paragraphs.

## Audit Findings

### Irregular payment of auction discount

**3.6.2** According to Paragraph 13.1 of the Manual of Procedure (MoP)<sup>99</sup> of the Company, subscribers of chitty can pay monthly subscriptions in cash, demand draft, money order or cheque. As per Circular No.33/2009 dated 3 April 2009 issued by the Managing Director of Company, cheques received from subscribers are to be deposited into the bank on the very next day of receipt and if the cheques are not cleared within three days (seven days in case of outstation cheques), the Company should get back the cheques from the bank and pass cancellation entries against the accounts of these subscribers. According to Paragraph 13.4(b) of the MoP, in case of dishonour of cheques remitted by subscribers, cancellation entries against the accounts of these subscribers had to be passed.

We noticed that 4,050 prized subscribers in nine branches of the Company had remitted monthly subscriptions in respect of 43,352 instalments by cheque within due date and availed the benefit of auction discount amounting to ₹10.68 crore. But, there was delay in realisation of cheques ranging up to 1105 days<sup>100</sup> with average abnormal delay<sup>101</sup> of 27 days. In spite of the delay, these prized subscribers were allowed auction discount of ₹10.68 crore (**Appendix 18**) due to the failure of the Company to link auction discount to prized subscribers with the realisation of cheques.

The reasons for undue delay in realisation of cheques submitted by the prized subscribers were not on record. We selected 59 cases and requested banks to

<sup>96</sup>If more than one subscriber bids for the maximum reduction, prize money would be given to one subscriber through draw of lots.

<sup>97</sup> In the case of prized subscribers (prized subscribers are those subscribers who have won the prize money) only. Non-prized subscribers are eligible for auction discount irrespective of payment of subscription within due date.

<sup>98</sup> Alappuzha II, Cherthala I, Cherthala II, Karunagappally I, Parasala, Perumbavoor I, Palakkad, Thalayolaparambu and Thamarassery.

<sup>99</sup> Manual of Procedure of the Company prescribes the procedures to be followed for conduct of chitty business.

<sup>100</sup>We noticed that cheques were shown as cleared in the records even after validity period. This was done by remitting the dues in cash directly to the Bank Account of the Company.

<sup>101</sup> Delay of more than seven days is considered as abnormal delay.

furnish the details of such cases. Scrutiny of the details revealed that delay in realisation was due to delay in presentation of cheques to banks (26 cases), insufficient funds in the accounts of the subscribers (18 cases) and delay on the part of the banks (15 cases). Collusion between the employees of the Company and chitty subscribers in such cases could not be ruled out. We noticed some such instances as discussed below:

### **Issue of cheques by officials of the Company in favour of subscribers**

**3.6.3** According to Paragraph 3.22 of MoP of the Company, officials of the Company are not to issue cheques in favour of subscribers towards payment of monthly subscriptions. We noticed that 20 cheques for a total amount of ₹6.92 lakh were issued by two staff of Alappuzha II Branch and their relatives against 115 instalments of 76 subscribers.

Thus, misappropriation of cash received towards chitty subscriptions by the Company staff and issuing of cheques in favour of subscribers in lieu of cash received could not be ruled out. Some instances of suspicious transactions are given in *Appendix 19*.

### **Non-initiation of action on dishonoured cheques**

**3.6.4** According to Section 138 of the Negotiable Instruments Act, 1881, in case of dishonour of cheques due to insufficiency of funds, drawer of cheque shall be punished with imprisonment for a term which may extend to two years, or with fine which may extend to twice the amount of the cheque, or with both. Further, according to Paragraph 13.4(b) of the MoP, in case of dishonour of cheques remitted by subscribers, cancellation entries against the accounts of these subscribers had to be passed. We noticed that:

- 59 cheques for an amount of ₹29.57 lakh received in respect of 92 instalments of 62 subscribers in Alappuzha II Branch during 2010-11 to 2014-15 were dishonoured due to insufficiency of funds. Dishonour of these cheques was not, however, recorded in the books of accounts. Instead of passing reversal entry in respect of these dishonoured cheques or taking action under Section 138 of the Negotiable Instruments Act, 1881, the branch allowed the subscribers to deposit cash directly into the bank account of the Company after delays ranging up to 91 days. Through this fraudulent process, the subscribers were granted ineligible auction discount of ₹98,426.

We also noticed that some of the dishonoured cheques were issued by employees of the Company in Alappuzha II Branch as given in *Appendix 20*.

- Similarly, 58 cheques for ₹8.59 lakh issued by subscribers in Alappuzha II Branch during 2010-11 to 2014-15 were dishonoured. Dishonour of these cheques was also not accounted for in the books of accounts of the Company by reversing the entry at the time of receipt of cheques. The accounts of these subscribers were closed without realising dues of ₹8.59 lakh.

### **Irregular payment of prize money**

**3.6.5** In accordance with Rule 14 of the Kerala Chit Funds Rules, 2012, a subscriber who has defaulted in payment of monthly subscriptions shall not be entitled to participate in the auction for prize money.

We noticed that:

- In respect of 14 high value chitties in five branches, 12 defaulting subscribers had remitted monthly subscriptions amounting to ₹39 lakh through cheques and were allowed to participate in auction before realisation of dues as shown in *Appendix 21*.

It can be seen from the *Appendix 21* that two subscribers obtained prize money of ₹62.40 lakh before the Company had realised the dues.

We also noticed that Shri. Ayoobkhan, a chitty subscriber against Chitty No. 44/2012<sup>102</sup> was allowed to participate in the auction (November 2012) and won the prize money before the realisation of the cheque submitted by him for second and third instalments. The cheque submitted was dishonoured and the next four instalments were also defaulted upon. The Company released the prize money of ₹23 lakh to him on 19 March 2013 and allowed him to remit the defaulted (2<sup>nd</sup> to 7<sup>th</sup>) instalments of ₹6 lakh on the same day out of the prize money.

We further noticed that the subscriber again defaulted on the subsequent 23 instalments. The Company referred this case to the Revenue Authority in July 2014 for collection of ₹23 lakh. The amount was not collected till July 2016.

Favouring of a few defaulters resulted in genuine subscribers losing their legitimate chance of getting the prize money.

The Company replied that appropriate action would be taken to ensure that defaulting subscribers were not allowed to participate in chitty auction in future.

### **Non-collection of interest on delayed realisation of cheque**

**3.6.6** According to clause 18 of the Chitty agreement with subscribers, in case of delay in payment of monthly subscriptions, interest at the rate of 14 per cent per annum shall be payable by prized subscribers<sup>103</sup> and at the rate of 12 per cent per annum by non-prized subscribers<sup>104</sup>. Payment of interest was in addition to disallowance of auction discount (prized subscribers) and ineligibility to participate in the auction for prize money (non-prized subscribers).

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<sup>102</sup> Commenced in September 2012, instalment amount-₹1 lakh and duration- 30 months.

<sup>103</sup> Members who have won prize money.

<sup>104</sup> Members who have not won prize money.

We noticed that during 2011-12 to 2015-16, nine branches of the Company had allowed auction discount (prized subscribers) and right to participate in auction (non-prized subscribers) on receipt of 63,659 cheques towards monthly subscriptions of ₹259.15 crore. Though these cheques were not realised within the prescribed seven days, interest of ₹1.23 crore was not charged.

### **Failure of internal control mechanism**

**3.6.7** All cheques received were entered into the system software and cheque deposit slips generated. In respect of cheques dishonoured and which could not be revalidated due to expiry, cash was remitted by subscribers directly into banks and the receipt earlier accounted for against the cheque was set off against the cash remittance by entering the cash payment date into the system software at the time of preparation of Bank Reconciliation Statement.

Since the Company accounts for monthly chitty subscriptions on receipt of cheques without waiting for realisation of cheques, delay in realisation can be watched only through preparation of monthly Bank Reconciliation Statement.

We noticed that the Company did not prepare monthly Bank Reconciliation Statements regularly. Internal Auditors and Statutory Auditors failed to notice and report the practice of irregular withholding of cheques of subscribers and consequent delay in realisation. Thus, through this fraudulent way of receipt of cheques within due dates and their delayed realisation with the possible connivance of officials of the Company, chitty subscribers were allowed ineligible auction discount and right to participate in the auction for prize money, besides extending undue benefit by way of non-levy of interest for delayed realisation of monthly subscriptions.

Accepting all the audit observations, the GoK replied (December 2016) that the Company had since implemented a control system in order to plug any loopholes and revenue leakage. They also stated that in all the cases where officials were involved, appropriate action would be taken to recover loss from the officials concerned.

### **Conclusion**

**System of realisation of cheques against monthly subscription of chitty is marred by undue delays and possible collusion between officials and subscribers leading to payment of ineligible auction discount besides, ineligible subscribers being allowed to participate in auction for prize money. Cheques issued against chitty instalments were dishonoured but no action was initiated against such dishonour of cheques.**

**It is recommended that the Company should streamline the process by linking eligibility for auction discount and prize money to realisation of cheques.**

**Kerala Tourism Development Corporation Limited**

**3.7 Non-obtaining of environmental clearance**

**Decision of the Company to procure boats before obtaining clearances from Ministry of Environment and Forest, Government of India resulted in non-realisation of potential revenue of ₹1.45 crore per annum.**

According to Section 2 of the Forest (Conservation) Act, 1980, prior approval of the Ministry of Environment and Forest (MoEF), Government of India (GoI) is necessary for use of reserve forest for non-forest purpose. Further, according to the guidelines issued (October 2012) by the National Tiger Conservation Authority under clause (c) of sub-section (1) of Section 38-O of the Wild Life (Protection) Act, 1972, all tourist facilities in tiger reserves must adhere to all environmental clearances.

Kerala Tourism Development Corporation Limited (Company) is engaged in tourism activities in Kerala. In June 2012, the Company decided to purchase one 120-seater catamaran<sup>105</sup> boat to meet increasing demand from tourists for boating on the Periyar Lake (a reserve forest area) and obtained (August 2012) the sanction of GoK for the same. While according sanction for the amount of ₹1.50 crore for the procurement of the catamaran, GoK directed the Company to comply with all procedural formalities. Thereafter, based on the recommendation of Chief Engineer, the Company decided to buy one more catamaran boat using the Company's own fund. The anticipated revenue from introduction of the two catamaran boats was ₹1.45 crore per annum.

The Company invited (December 2012) tender for supply of two 120-seater catamaran boats at an estimated cost of ₹2.40 crore. The Company awarded (March 2013) the work to Praga Marine Private Limited (PMPL), the only qualified bidder at ₹2.30 crore<sup>106</sup>. GoK released (May 2014) a grant of ₹1.50 crore for the same. The boats to be delivered within three months (June 2013) were ready for despatch in November 2014, but the Company could not take possession yet (December 2016) as mandatory forest clearance for the operation of boats was not obtained.

We noticed the following:

- The Company invited (December 2012) tenders before obtaining clearances/ permissions from MoEF, GoI and Department of Forest, GoK. Application for forest clearance from MoEF was submitted only in September 2016. Consequently, although PMPL intimated (November 2014) readiness for delivery of boats, the Company had not taken possession of the boats so far (December 2016). Further, the online application submitted by the Company (September 2016) was returned (September 2016) by Forest Department, GoK for correcting shortcomings, it was still pending (December 2016). As a result, the Company could not tap the anticipated revenue through provision of

<sup>105</sup>A catamaran is a multi-hulled watercraft featuring two parallel hulls of equal size.

<sup>106</sup> ₹1.15 crore each.



increased boating facilities to tourists.

- Though the agreement between the Company and the contractor did not stipulate any advance payment for supply of boats, the Company paid (June 2013) interest free advance of ₹0.46 crore to the contractor, which is still pending for settlement.

The GoK replied (November 2016) that approval had been sought (September 2016) from the MoEF, GoI for launching the boats. The reply was not acceptable since clearance from MoEF was to be obtained beforehand. Hence, due to delay and inaction on the part of the Company in getting clearance from MoEF, delivery of the boats to the Company had not yet taken place (December 2016) which resulted in non-realisation of potential revenue of ₹1.45 crore per annum and blocking up of ₹0.46 crore since June 2013.

### **Kerala Small Industries Development Corporation Limited**

#### **3.8 Avoidable financial commitment**

#### **The Company entered into a business activity without assessing its feasibility resulting in financial liability of ₹3.01 crore.**

Kerala Small Industries Development Corporation Limited (SIDCO) appointed (March 2015) Shri. Suresh Babu as Consultant/Economic Advisor based on his voluntary offer to develop SIDCO's business activities. The consultant brought (8 May 2015) to the notice of SIDCO a tender floated (22 April 2015) by Uttar Pradesh Co-operative Federation Limited (UPCF) for the supply of three lakh MT of Di-Ammonium Phosphate (DAP). SIDCO participated in the tender and was selected as L1 with the rate of USD 478 (₹30,382<sup>107</sup>) per metric tonne (MT). Accordingly, an agreement was executed (28 May 2015) between UPCF and SIDCO. Since SIDCO was not a producer of DAP, it floated a global tender (27 May 2015) with Probable Amount of Contract of ₹950 crore to identify suppliers for the same. The approval of Board of Directors (BoD) was obtained (3 June 2015) wherein BoD authorised MD, SIDCO to carry out all necessary actions to implement the decisions of the BoD.

M/s Ram Online Services (P) Ltd. which was selected as L1 in the global tender (out of five technically qualified bids) reduced their rate to USD 474 (₹29,862<sup>108</sup>) per MT after negotiation and thus, the margin of SIDCO was USD 4 per MT (₹252). Considering the huge quantity of three lakh MT and seasonal requirement of the fertilizer, SIDCO requested (30 June 2015) the other four bidders<sup>109</sup> to supply at the L1 rate with the intention of supplying the entire quantity to UPCF in time. Accordingly, agreements were executed (July 2015) with all the five bidders. As per the agreement, the suppliers were

<sup>107</sup> Calculated on the basis of Exchange Rate on 16 May 2015 (last date of tender) (478 \* ₹63.56)

<sup>108</sup> Calculated on the basis of Exchange Rate ₹63.

<sup>109</sup> El Joun United Company for General Trading and Contracting, Kuwait, M/s Obar Middle East Oil Field Services WLL, Kuwait, Nasser Al-Hussainan Electric & Electronic Appliances Est, Kuwait and M/s Quartet Industries Solution (P) Limited, Kochi, Kerala.

required to furnish Performance Bank Guarantee (BG) of 2 per cent for the value of Letter of Credit to be established by SIDCO. However, BG was released by only two suppliers<sup>110</sup> to SIDCO.

As per the terms and conditions of agreement between SIDCO and UPCF, SIDCO had to furnish a performance guarantee of 1 per cent (₹9.11 crore) of the contract value (₹911.45 crore<sup>111</sup>). Due to lack of funds, the BG furnished (14 July 2015) for USD 4,78,000 (₹3.01 crore) by M/s El Joun United Company for General Trading and Contracting, Kuwait (M/s El Joun) was reassigned (28 July 2015) in favour of UPCF for executing the trial order of 30,000 MT by AGM, Information Technology & Telecommunications (IT &TC) without authorisation. UPCF issued (22 August 2015) Letter of Credit for ₹92 crore towards the cost for the initial shipment of 30,000 MT, out of the total quantity of 3 lakh MT of DAP in favour of SIDCO with the last date of shipment being 30 September 2015. However, SIDCO could not open letter of credit in favour of any of its suppliers due to lack of funds and hence, it failed to fulfil the obligation of supply of DAP to UPCF within the time limit.

Due to non-supply of DAP by SIDCO within the stipulated period, UPCF terminated (10 December 2015) the agreement and encashed the BG. The arbitrator appointed by M/s El Joun issued notice to SIDCO for realising the loss sustained by them due to SIDCO's failure to open Letter of Credit violating the terms and conditions of the contract entered into between them.

In this connection, we observed the following:

- The Company was established with the objective of promotion of small scale industries (SSI) in Kerala. Hence, the decision of the Company to enter into a transaction which had no connection to its stated objective was irregular.
- As per Central Vigilance Commission (CVC) guidelines, the selection of consultants should be made in a transparent manner through competitive bidding. The scope of work and role of consultants should be clearly defined and the contract should incorporate clauses having adequate provisions for penalising the consultants in case of defaults by them at any stage of the project including delays attributable to the consultants. The MD appointed the consultant/Economic Advisor without following a transparent selection procedure.
- The BG of USD 4,78,000 (₹3.01 crore) provided by M/s El Joun was unauthorisedly endorsed by the AGM (IT&TC) of SIDCO in favour of UPCF. However, no action was initiated against the employee who endorsed the BG.

Thus, the decision of the MD, SIDCO to enter into a new venture amounting to ₹950 crore outside its core activity based on the advice of a consultant

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<sup>110</sup> M/s Obar Middle East Oil Field Services WLL, Kuwait (USD 2,50,000, not reassigned by SIDCO to UPCF), El Joun United Company for General Trading and Contracting, Kuwait (USD 4,78,000).

<sup>111</sup> 3,00,000 MT \* USD 478 = USD 14,34,00,000 \*Exchange Rate for USD ₹63.56 (last date of tender).

without analysing its financial position had resulted in financial commitment of USD 4,78,000 (₹3.01 crore).

Government stated (November 2016) that the matter has been referred to Vigilance Department and further action would be proceeded based on the findings of Vigilance Department.

### 3.9 Undue benefit to suppliers

**Payment of advances in violation of tender/agreement conditions resulted in undue benefit to suppliers and potential loss of ₹6.01 crore to the Company.**

As per Rule 12.16 of Stores Purchase Manual (SPM), ordinarily, payments for supplies made or services rendered should be released to the supplier only after the supplies have been made or services have been rendered. Rule 12.17 states that the Departments may, in consultation with Finance Department, relax the ceilings mentioned in Rule 12.16. However, while making any such advance payment, adequate safeguards in the form of bank guarantee, etc., should be obtained from the supplier.

Kerala Small Industries Development Corporation Limited (SIDCO) constituted (May 2012) a trading division which focuses mainly on supporting MSME manufacturers by helping them to market their products under the brand name of SIDCO. The total purchases by the trading division amounted to ₹18.31 crore during the period 2012-13 to 2015-16. We noticed irregularities in granting of advances to suppliers in violation of tender conditions and provisions of SPM which resulted in undue favour to suppliers and potential loss of ₹6.01 crore as detailed in *Table 3.15*.

**Table 3.15: Details of deviation from tender/ agreement condition and SPM.**

Item	Name of Supplier/ Agreement date	Tender/Agreement Condition	Violation
Cement Blocks	PRR Bricks, Mavelikkara/ April 2015	As per Clause 7 of terms and conditions of Notice Inviting Tender “No advance payment shall be made for the above work”. Further, as per Clause 6 of agreement conditions the supplier shall supply the products on credit for 15 days from the date of invoice, the payment to which shall be released only on submission of the concerned purchase bills along with the acceptance certificates.	Managing Director (MD) released (May 2015) an advance of ₹50 lakh without interest violating tender/agreement condition. The supplier had supplied cement blocks amounting to ₹0.91 lakh and the balance ₹49.09 lakh and supply is still pending (December 2016).

Item	Name of Supplier/ Agreement date	Tender/Agreement Condition	Violation
Sand	SSTPL <sup>112</sup> / January 2015	As per Clause 13 of the agreement, advance payment amounting to value of sand dredged in five days, up to a maximum quantity of 5,000 cu.m (₹1.14 crore) for first two consignments would be made by SIDCO to SSTPL subject to the condition that advance would have to be settled against subsequent trade of sand.	As per the agreement conditions, SSTPL dredges sand from Kayamkulam lake which was to be supplied to SIDCO. SSTPL informed (24 January 2015) that 10,000 cu.m sand was ready for delivery and requested for advance payment. MD, SIDCO released an advance of ₹70 lakh (January/June/July 2015). Out of this, SIDCO had first advanced ₹50 lakh in January 2015 upon the condition that advance shall be settled towards supply of dredged sand within a period of two months from the date of execution of agreement. In spite of non-supply of any material against this advance by SSTPL, SIDCO paid further advances of ₹10 lakh each in June and July 2015. We cross verified the data available with Kerala Irrigation Infrastructure Development Corporation Limited who had awarded the work to SSTPL. We found that SSTPL had dredged only 3,111 cu.m sand (September 2015). SSTPL had not supplied any sand so far and the amount of ₹70 lakh is still pending as advance with the supplier (December 2016).
Revolving Chairs	Indigo Life Style, Thrissur/ Agreement not signed	There was no provision in the tender conditions for payment of advances.	Audit observed that an amount of ₹45 lakh was disbursed (April to May 2013) before inviting (September 2013) tender. This was irregular and needs investigation. The supplies valuing ₹1.10 crore made were neither of specified quality nor manufactured by SSI units. The sales outlets of SIDCO have reported that the revolving chairs supplied were unsaleable.
Sand from other States	Link Land Traders, Ernakulam/ October 2014	As per Clause 5 of the agreement SIDCO shall establish an irrevocable, transferable, Inland Letter of Credit (LC). 95 per cent of payment shall be made against shipping documents.	SIDCO had not complied with Clause 5 and 6 of the agreement conditions. The amount of ₹2 crore was credited to Dhanlaxmi Bank Limited to open an LC. LC was issued against purchase order and the amount was credited (April 2015) to the supplier against the purchase order. This amounted to providing advance to the supplier which was not envisaged in the agreement. The supplier had neither refunded the advance nor supplied material.

<sup>112</sup> M/s Sukrithakaran Software Technologies Private Limited, Thiruvananthapuram.

Item	Name of Supplier/ Agreement date	Tender/Agreement Condition	Violation
Packaged drinking water, coconut oil and soda & drinks	M/s Hebron Aqua and Foods (India) Pvt. Ltd, Ernakulam/ January 2013	There was no provision in the agreement regarding payment of advances. As per Clause 5 of the agreement, at the time of taking delivery of the consignments, the buyer shall make payment to the manufacturer the full value of products supplied to them.	An amount of ₹3.40 crore was released (November 2013 to January 2015) as advances. The supplier had stopped (December 2015) supplying the products. An amount of ₹1.67 crore is still pending as advance with the supplier (December 2016).
Washing Soap	Chetak India Soaps and Detergents, Cherthala/ January 2013	There was no provision in the agreement regarding payment of advances. As per Clause 5 of the agreement, at the time of taking delivery of the consignments, the buyer shall make full payment to the manufacturer.	An amount of ₹50 lakh was released (February to July 2013) as advances. The amount was adjusted against supplies and ₹5.10 lakh is pending (December 2016) with the supplier.

Thus, the granting of irregular interest free advances without safeguarding the financial interest of SIDCO (such as by obtaining bank guarantees for the advances) had resulted in undue advantage to the suppliers to the extent of ₹6.01 crore (including interest loss<sup>113</sup> of ₹0.55 crore).

Government stated (January 2017) that a vigilance inquiry had been initiated considering the gravity of the matter.

### Steel and Industrial Forgings Limited

#### 3.10 Idling of rejected products

**Bulk production and supply of Cam Shaft gear without rectifying the defects pointed out by DMW on the samples supplied resulted in loss of ₹8.48 lakh and idling of rejected products worth ₹2.13 crore.**

Steel and Industrial Forgings Limited (Company), a PSU, engaged in manufacturing and marketing of forgings, received (October 2013) an order for supply of 1,198 ‘SIFL 263 M Cam Shaft gear ready to hob’ (Cam Shaft gear) from Diesel Loco Modernisation Works, Patiala, (DMW), Ministry of Railways, at an all inclusive rate of ₹43,438.30<sup>114</sup> each for a total value of ₹5,20,39,078. As per the conditions of the bid, the Company was to submit three samples to DMW within 45 days (November 2013) from the date of order and commence bulk supply after receipt of approval from DMW. The Company supplied three samples on 04 November 2013. Samples were cleared (December 2013) by DMW subject to the condition that future supply should be conforming to the specified dimensions and also as per the drawings No.10142691 Alt “NIL”.

<sup>113</sup> Calculated on amount blocked up on cement block, sand and river sand from other States at 10 per cent.

<sup>114</sup> Basic price ₹36,818.98 plus Excise Duty (ED) 12 per cent plus Cess 3 per cent on ED and Central Sales Tax at the rate of 5 per cent.

Subsequently, 350 gears were to be delivered by February 2014 and the remaining 845 by 31 August 2014 at the rate of 150 items per month. Accordingly, Company supplied 943 gears up to January 2016, of which only 262 gears (28 per cent) were accepted by DMW and 681 gears (72 per cent) were rejected due to deviation from the ordered specifications for the product. The scheduled delivery date and quantity, actual delivery date and quantity, date of rejection and quantity and reason for rejection are given in *Appendix 22*.

The Company requested (April 2016) for extension of delivery period up to December 2016 which was agreed to by DMW subject to reduction in price as per DMW's latest buying rate from the originally accepted basic price of ₹36,819 to ₹26,159 (April 2016). The reasons for rejection were deviation from the required specifications such as bore over size, run out, parallelism, etc. The Company took up (June 2014) the huge rejection of the gears with DMW stating that the method of inspection was not mentioned in the drawings. But their argument was rejected by DMW explaining that the method of checking was shown to the Company many times earlier, bore checking had already been mentioned in the drawings and inspection chart was available in the drawings. Hence, the Company had to take back the rejected gears by incurring an expenditure of ₹7.87 lakh. The Company also made arrangements with M/s Parthasarathy CNC Technology Pvt. Ltd., Coimbatore (M/s Parthasarathy) for rectifying the defects pointed out by DMW.

We observed that:

- The product was not an entirely new item. The Company had been regularly supplying Cam Shaft gears to DMW. But, this tender was considered as a fresh entry in the market because the Cam Shaft gears required further machining to get them into 'ready to hob condition' compared to the previously supplied gears. However, the Company had not procured the equipment needed for the finishing operations such as gear shaping, heat treatment and inspection before quoting for the tender, due to non-availability of sufficient funds.
- In the absence of finishing equipment, the components were forged in the factory of the Company at Athani, heat treatment was carried out by the Company's outsourced vendors and machining to ready to hob condition was carried out at their own Machining Unit at Shornur and at MS Engineering Unit, a vendor of the Company, at Coimbatore. The products machined both at its own Unit and at vendors' Unit did not meet the specifications stipulated by DMW.
- The Company could not rectify the defects of the 681 rejected gears even after a lapse 36 months (January 2017) of its rejection in May 2014.
- The actual variable cost for production of Cam Shaft gear worked out to ₹31,287.56 per unit. But the Company had to accept reduced rates for 938 gears even below the variable cost due to its failure to supply the items as per the specifications within the scheduled delivery period.

The decision to quote in the bid without ensuring its competence and capacity to supply the product as per the specifications stipulated by DMW and production in bulk quantity without rectifying the defects pointed out by DMW, resulted in loss of ₹8.48 lakh<sup>115</sup> and idling of rejected products valuing ₹2.13 crore<sup>116</sup>.

Management replied (August 2016) that the Company supplied the gears as DMW was insisting for immediate supply even though they had not received any feedback for the already supplied gears. It was also stated that since DMW was making payment against “R” Note (Goods Received Note), the Company was under the impression that supplies were accepted.

The reply of the Company is not acceptable as DMW had already clarified (June 2014) that the method of checking was shown to the Company many times earlier. Further, even though the Company identified M/s Parthasarathy in December 2015 for re-working the rejected gears, the Company could not supply any of the rejected gears after rectification till date (January 2017).

The matter was referred (July 2016) to Government and their reply was awaited (February 2017).

## Statutory Corporations

### Kerala State Road Transport Corporation

#### 3.11 Infusion of buses into fleet

##### Introduction

**3.11.1** Kerala State Road Transport Corporation (KSRTC) provides public transport to 32 lakh commuters daily through its 94 Depots, Sub Depots and Operating Centres. KSRTC had a fleet strength of 5,686 buses as on 31 March 2016. In order to augment/ replace its fleet, KSRTC procures chassis<sup>117</sup> from manufacturers through open tenders and thereafter, carries out bus body building at its central and four regional workshops<sup>118</sup>.

We examined the procurement of chassis, bus body building and infusion of buses into the fleet during 2011-12 to 2015-16 to see whether KSRTC had planned and procured chassis in an efficient and timely manner, was able to build and infuse buses into fleet timely and could generate adequate revenue by infusing new buses.

<sup>115</sup> (Transportation cost ₹7.87 lakh + contribution loss (selling price- variable cost) on 262 items sold ₹0.61 lakh).

<sup>116</sup> 681 gears \* ₹31,287.56.

<sup>117</sup> The base frame of a bus.

<sup>118</sup> Central workshop at Pappanamcode and regional workshops at Mavelikkara, Aluva, Edappal and Kozhikode.

## Audit Findings

3.11.2 Audit findings are discussed below:

### Procurement

#### Shortfall in procurement of new chassis

3.11.3 As per its own norms, KSRTC is required to replace buses after 10 years of commissioning or after operation of 10 lakh kilometres (km) distance, whichever is earlier. Further, according to Rule 260A of the Kerala Motor Vehicle Rules, 1989 (KMVR), KSRTC is required to replace stage carriages<sup>119</sup> older than five years in Super Class<sup>120</sup> services with new ones.

We noticed that though KSRTC had to infuse 3,578 buses during 2011-12 to 2015-16 as per the above norms, it had infused only 1,845 buses as shown in Table 3.16.

**Table 3.16: Details of requirement of chassis as per norms during 2011-12 to 2015-16**

Sl. No.	Particulars	2011-12	2012-13	2013-14	2014-15	2015-16	Total
1	Number of new chassis required <sup>121</sup>	1,919	269	489	601	300	3,578
2	Purchase order quantity	625	325	60	1,215	285	2,510 <sup>122</sup>
3	New buses infused	215	486	332	203	609	1,845 <sup>123</sup>
4	Shortfall in infusion (1- 3)	1,704	(-) 217	157	398	(-) 309	1,733
5	Cumulative shortfall in infusion <sup>124</sup>	1,704	1,487	1,644	2,042	1,733	1,733

Source: Data compiled from vehicle data provided by EDP Centre of KSRTC.

The main reasons for the shortfall were:

- As against the norm of 10 years, KSRTC replaced buses which were 13 to 15 years old. As a result, 1,068 buses<sup>125</sup> were not considered for replacement.
- Though KSRTC placed 16 Purchase Orders for procuring 2,500 chassis during the period 2011-12 to 2015-16, it received 2,241 chassis and built 1,835 buses. The shortfall of 665 buses<sup>126</sup> was due to delay in procurement of chassis, body building and final releasing of buses to

<sup>119</sup> Stage carriage means a motor vehicle constructed or adapted to carry more than six passengers, excluding the driver, for hire or reward at separate fares paid by or for individual passengers, either for the whole journey or for stages of the journey.

<sup>120</sup> Fast, Super Fast, Super Express, Super Deluxe, etc.

<sup>121</sup> This includes buses required for replacement of old buses and buses required for introducing new schedules after adjusting the number of buses replaced from Super Class services.

<sup>122</sup> Including 10 fully built AC buses.

<sup>123</sup> Including 10 fully built AC buses.

<sup>124</sup> Shortfall of current year plus shortfall of previous years.

<sup>125</sup> 3,578 buses - 2,510 (No. of chassis plus 10 buses actually received).

<sup>126</sup> 2,510 buses - 1,845 buses = 665 buses.



Depots as discussed in *Paragraphs 3.11.4 and 3.11.5*. During the period 2011-12 to 2013-14, KSRTC availed loan of ₹120 crore from HUDCO<sup>127</sup> for procurement of 825 buses and received fund of ₹87 crore from Government of Kerala (GoK) for procurement of 466 buses. KSRTC, however, procured only 1,000 buses<sup>128</sup> against the required number of 1,291 leaving a shortage of 291 buses. We observed that the balance fund was not utilised for the procurement of chassis and instead diverted for working capital purposes.

Accepting the audit observation, GoK stated (March 2017) that the balance available fund had been utilised for meeting working capital requirements due to paucity of sufficient fund.

### **Delay in procurement of chassis**

**3.11.4** KSRTC did not prepare annual plans to assess the requirements for addition of new buses in place of scrapped/ withdrawn buses, for commencing new schedules, etc. Instead, KSRTC assessed its requirement of buses to be procured over a period including backlog at irregular intervals.

During the five year period, KSRTC had processed Purchase Orders (PO) for two bulk<sup>129</sup> procurements consisting of 1,000 chassis (March 2011) and 1,500 chassis (December 2013).

We noticed in this connection that:

- According to Stores Purchase Manual (SPM) of GoK, the time allowed to bidders for submission of bids is one month from date of the invitation of tender and maximum validity period of bid is three months. Thus, a normal time of four months is required for invitation and finalisation of tender. Since the chassis procured are to be used for body building from the beginning of the financial year, KSRTC should initiate the procurement process during the last quarter of the previous year.

In the case of procurement of 1,000 chassis, we observed that the Board of Directors (BoD) accorded its approval for procurement in March 2011, tenders were invited in July 2011 and POs placed by September 2011. The delay in inviting tender was due to delay in arranging finance for the procurement. Delivery of chassis against the POs was started only at the end of October 2011. Thus, there was no stock of bare chassis at body building units during the period April 2011 to October 2011. KSRTC could infuse only 215 buses during the year 2011-12 against 338 buses required for replacement of scrapped buses<sup>130</sup> and operation of new services<sup>131</sup>. Had KSRTC carried out the procurement in time, it could have built more buses and avoided the position of shortage of 123 buses in the year 2011-12.

<sup>127</sup> Housing and Urban Development Corporation Limited.

<sup>128</sup> Included in 1,845 buses.

<sup>129</sup> In which 16 POs were placed.

<sup>130</sup> 215 buses.

<sup>131</sup> 123 new services.

Further, the PO price in the above tender was valid up to 24 August 2012. However, after procuring 625 chassis, the BoD invited fresh tender (February 2012) to procure the remaining 375 chassis<sup>132</sup>. Since the lowest unit rate (L1) for conventional chassis obtained in the new tender was ₹1.20 lakh higher than the existing price, KSRTC placed (August 2012) POs for 325 conventional chassis<sup>133</sup> at the existing price of ₹10.20 lakh per unit with applicable variation in statutory duties and taxes. The suppliers did not accept the POs at the existing rates initially but, accepted (December 2012) after a lapse of four months. Due to delay in acceptance, the delivery schedule of September 2012 to November 2012 in the POs was amended as January 2013 to April 2013.

We observed that the invitation of a new tender during the validity of the existing PO price was unwarranted as KSRTC did not foresee lower market price. Thus, due to its injudicious decision to invite a new tender, KSRTC lost 11 months (February 2012 to December 2012). We further observed that during the period from November 2012 to January 2013, there was no body building of buses owing to the stock out position of chassis. KSRTC could infuse only 486 buses against 759 buses<sup>134</sup> required for replacement of scrapped buses and operation of new services for the year 2012-13. Had KSRTC placed POs at the existing rate without inviting fresh tender, it could have avoided the stock out position of chassis and consequent loss of body building of 125 buses<sup>135</sup>.

GoK admitted (March 2017) that there was no specific yearly purchase plans for chassis/ buses. With regard to invitation of tender in February 2012 for 375 chassis, GoK stated that the tender was invited in order to obtain more competitive rates but, seeing the fresh rates on the higher side, Purchase Orders were placed at the old rates. The reply is not acceptable because invitation of fresh tender in February 2012 was not to obtain more competitive rates and the delay had resulted in stock-out position of chassis and consequent production loss of buses.

- In the second case, KSRTC invited (February 2014) tender for procurement of 1,500 chassis<sup>136</sup>. It, however, had to retender twice owing to technical problems faced by participants in e-tendering procedures. Meanwhile, the Model Code of Conduct for the General Election 2014 came into force in March 2014 due to which tender proceedings were stalled. KSRTC placed (October 2014) POs for 1,350 conventional chassis at the L1 rate of ₹10.42 lakh per chassis obtained in the re-tender (August 2014).

We observed that there was a requirement of 656 new buses<sup>137</sup> to replace scrapped buses and to operate new services for the year 2013-14. As a normal time of four months was required for invitation and finalisation of tender, KSRTC should have initiated the procurement process in the last

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<sup>132</sup> 325 conventional chassis and 50 air suspension chassis.

<sup>133</sup> Since there was no valid rate available for Rear Air Front Weveller Suspension chassis, the BoD decided to go for retender in respect of 50 air suspension chassis.

<sup>134</sup> Replacement for 468 buses scrapped plus 168 new services plus back log of 123 buses.

<sup>135</sup> (3 months(October 2012 to December 2012) \* Average production of 46 buses per month) – Actual production of 13 buses = 125 buses.

<sup>136</sup> 1,350 conventional and 150 air suspension chassis.

<sup>137</sup> Replacement for 283 buses scrapped plus 100 new services plus back log of 273 buses.

quarter of 2012 or procured more quantity in the previous procurement to meet the requirement of buses in the beginning of the year 2013-14. KSRTC, however, initiated the process in December 2013. Due to the delay, supply of chassis got delayed leading to stock out position of chassis during the period October 2013 to October 2014<sup>138</sup> and consequent production loss of 480<sup>139</sup> buses. Against the requirement of 656 buses, KSRTC commissioned 332 buses leading to a shortfall of 324 buses.

We further noticed that there was a four *per cent* concession<sup>140</sup> in rate of excise duty on bus chassis during February 2014 to December 2014. However, due to the delayed purchase, KSRTC lost the opportunity of availing concessional excise duty. The savings on account of concessional rate of excise duty and VAT foregone due to the delay in purchase of 414 chassis<sup>141</sup> during the period from February 2014 to October 2014 worked out to ₹1.61 crore<sup>142</sup>.

GoK stated (March 2017) that the delay in initiation of the procurement of 1,500 chassis was unavoidable due to declaration of General Election and litigation due to disqualification of bidders. The reply was not acceptable in view of the fact that procurement process to be initiated by December 2013 was unduly delayed up to February 2014. Declaration of General Election in March 2014 impacted the procurement process because the initiation of process was delayed up to February 2014.

### Bus Body Building

**3.11.5** After procurement, the chassis are issued to five workshops of KSRTC for bus body building. As per the production plan, time required for body building of a bus is 30 days and thereafter, five<sup>143</sup> days are required for registration before issuing them to Depots for operation.

We noticed delays in bus body building and putting the completed buses into operation as shown in *Table 3.17*.

**Table 3.17: Details of delay in production and operation of buses**

Particulars	Normal time	Number of buses which were infused into operation with delay			
		Delay 1 to 10 days	Delay 11 to 25 days	Above 25 days	Total
Delay in body building	30	315	139	160	614
Delay in releasing of buses	5	814	279	40	1133
Delay in operation of schedules.	2	14	0	1	15

Source: Compiled from data provided by KSRTC

<sup>138</sup> In Central workshop from December 2013 to October 2014.

<sup>139</sup> (11 months \* Average monthly production of 46 buses) – Actual production 26 buses = 480 buses.

<sup>140</sup> From 14 *per cent* to 10 *per cent*.

<sup>141</sup> Based on average monthly production @ 46 buses for 9 months period from February 2014 to October 2014

<sup>142</sup> 414 buses \* [ ₹10,80,879 (price at 14 *per cent* excise duty) - ₹10,42,000 (price at 10 *per cent* excise duty)] = ₹1.61crore.

<sup>143</sup> A norm of five days was adopted since KSRTC could complete the formalities in five days as observed in 712 cases.

The issues noticed in bus production are brought out in the subsequent paragraphs.

### Underutilisation of production capacity

**3.11.5.1** The sanctioned strength of employees, monthly production capacity, average number of workers employed, production target set and actual production during October 2014 to April 2016 at the five body building units of KSRTC are shown in *Table 3.18*.

**Table-3.18: Unit-wise sanctioned strength, production capacity, target, etc.**

Name of body building unit	Sanctioned strength	Monthly production capacity (buses)	Average workers employed	Production	
				Target <sup>144</sup>	Achieved
Pappanamcode	754	70	400	825	340
Mavelikkara	126	10	60	136	106
Aluva	126	10	100	136	123
Edappal	252	20	85	254	121
Kozhikode	126	10	78	135	125
<b>Total</b>	<b>1,384</b>	<b>120</b>	<b>723</b>	<b>1,486</b>	<b>815</b>

Source: Compiled from data provided by KSRTC

We noticed that KSRTC took 41 days to 272 days for building and releasing buses as against a normal time of 35 days<sup>145</sup>. The major reasons for the inordinate time taken for building buses and putting them into operation are discussed below.

- Total production capacity at body building units of KSRTC based on the sanctioned strength was 120 buses per month. We noticed that delivery schedules of chassis were not drawn in line with the above production capacity. Stock in yard ranged up to 397 chassis due to receipts in successive lots over and above the monthly production capacity of workshops. Out of 2,241 chassis received during 2011-12 to 2015-16, around 51 per cent (1,146 chassis) were held in the open yard for more than 50 days before being taken for body building. Since the workshops also failed to meet their production targets, successive receipts of chassis before exhausting the available stock resulted in accumulation and long holding of chassis in the open yard for periods ranging up to 246 days. As the chassis were procured out of the loan provided by HUDCO, idling of the same entailed avoidable interest burden of ₹2.99 crore<sup>146</sup> on the capital locked up for such period. The situation could have been avoided had the POs been placed in advance of requirement and delivery of chassis were made in a phased manner in line with the production capacity of the workshops. At the close of the year 2015-16, a total of 397 bare chassis costing around ₹43.70 crore<sup>147</sup> were lying in the open yards of the five workshops.

<sup>144</sup> Production target set (September 2014) for body building of 1,500 chassis for the period from October 2014 to April 2016.

<sup>145</sup> 30 days for production plus 5 days for registration related formalities.

<sup>146</sup> Interest was worked out for the period over and above the 30 days from the date of receipt of chassis till the date of commencement of production.

<sup>147</sup> ₹11,00,685 \* 397 chassis = ₹43.70 crore.

KSRTC stated (November 2016) that accumulation of stock was due to bulk purchase for availing concessional excise duty.

The reply was not acceptable since while going in for bulk procurement of chassis, KSRTC did not reckon the aspect of concessional excise duty. The bulk procurement of chassis was, in fact, to meet the backlog of chassis requirement.

- As per the work norms in vogue, mandays prescribed for body building of Ordinary and Fast Passenger (FP) buses were 325 and that for Super Fast (SF) buses were 340. We observed that the work norms were fixed not on the basis of any scientific work study but on the basis of bi-lateral settlement with labour unions. KSRTC introduced pneumatic doors<sup>148</sup> in new buses to be built from November 2014 which required additional mandays. We, however, observed that KSRTC did not update the work norms to incorporate the above change.
- The Chief Office of KSRTC set (September 2014) the production targets, directing the body building units to make necessary arrangement for employing required number of workers up to the maximum of the sanctioned strength to achieve the target. The units, however, could not engage the required number of workers as there was Court's Stay Order on engaging temporary workers and therefore, failed to achieve the target. Total number of buses produced in all the units during the period October 2014 to March 2016 was 815 buses against the production target of 1,486 buses (up to March 2016). We observed that in the last five years, KSRTC did not recruit workers<sup>149</sup> on permanent basis to fill the vacancies in permanent posts in body building units but employed temporary hands as and when required. Thus, non-recruitment of sufficient number of permanent workers against the vacancies existing in the body building units and dependence on temporary workers led to under achievement of the production target.

Accepting the audit observation, GoK stated (March 2017) that the body building was delayed due to shortage of staff in workshops.

- As per the production plan, time required for production of buses was a maximum of 30 days. We, however, noticed that time taken for completion of body building of buses ranged between 31 days and 121 days in 614 out of 1,835 cases. The delay in completion of body building was due to non-availability of material in time and shortage of workers. We observed stock out position of essential material at various points of time and the workshops had to keep waiting for the material to complete the production process. The heads of the body building units also stated the same reasons for the delay as observed by Audit.

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<sup>148</sup> Driver operated automatic door system.

<sup>149</sup> Through Kerala Public Service Commission.

Considering 30 days required for body building of a bus, 11,271 bus days were lost due to excess production time leading to probable revenue loss of ₹11.47 crore<sup>150</sup>.

GoK admitted (March 2017) that there was delay in production during certain periods due to shortage of material.

The reply was not acceptable as availability of material can be ensured through better planning at the time of placement of purchase order for chassis.

### Operation of buses

**3.11.6** We noticed inordinate delay in infusion of vehicles into the fleet after these were ready for operation due to delay in arranging insurance, delay in registration, etc., as discussed below:

#### Loss of vehicle days due to delay in arranging insurance

**3.11.6.1** The process of registration of vehicles and obtaining certificate of fitness, insurance, etc. of buses produced in the workshops was being done at the Chief Office of KSRTC. After completion of body building, the buses were measured and inspected by the Regional Transport Authorities (RTA) and reports thereon forwarded to the Transport Authority at Thiruvananthapuram, who issued Registration Certificate and Certificate of Fitness (CF) based on such field inspection reports. After obtaining CF, the Chief Office of KSRTC obtained temporary permits valid for four months and insurance for the new buses before allotting them to Depots.

We noticed that out of 1,845 buses commissioned during the period 2011-12 to 2015-16, 1,133 buses were released to Depots after delay ranging up to 65 days<sup>151</sup>. Total vehicle days lost on account of the delay worked out to 9,943 days. The delay was mainly attributable to the delay in insuring the vehicles. The delay in releasing the vehicles to Depots resulted in loss of revenue of ₹10.12 crore worked out at average Earning Per Bus per day (EPB) of ₹10,179.

Further, according to the circular<sup>152</sup> issued by GoK, all general insurance transactions of Public Sector Undertakings should be carried out only through Kerala State Insurance Department. KSRTC, however, insured its buses with New India Insurance Company Limited in violation of the circular issued by the GoK.

GoK replied (March 2017) that the delays in arranging the insurance happened due to poor financial position of KSRTC. The reply is not acceptable because the amount of loan provided by HUDCO for the procurement of buses included the cost of insurance also.

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<sup>150</sup> Worked out at average Earnings Per Bus (EPB) of ₹10,179 per day of the five year period.

<sup>151</sup> A norm of five days was adopted since KSRTC could complete the formalities in five days as observed in 712 cases.

<sup>152</sup> No.16/14/Fin. dated 21/02/2014.

### Loss of vehicle days due to delay in putting the new buses into operation

**3.11.6.2** The Chief Office of KSRTC, after completing the formalities related to registration, certificate of fitness, permit and insurance allotted the newly commissioned buses to Depots. Depots, on receipt of new buses were to press them immediately into scheduled operations.

We noticed that out of the 658 buses released to 11 Depots<sup>153</sup>, operation of service in respect of 15 buses<sup>154</sup> commenced after delay (after considering minimum two days for allotting the buses for operation) ranging between 1 and 32 days, mainly due to shortage of crew. Total vehicle days and revenue lost due to the delay was 74 days and ₹7.53 lakh<sup>155</sup> respectively.

### Loss of vehicle days due to delay in replacement of scrapped buses

**3.11.6.3** During 2011-12 to 2015-16, KSRTC had scrapped 1,951 buses. Against this, KSRTC had infused 1,845 buses into the fleet during the same period. Thus, 106 buses were short replaced. Shortage of buses for want of replacement ranged between 33 (July 2014) and 194 (December 2014) which stood at 106 as on 31 March 2016 as given in *Table 3.19*.

**Table 3.19: Details of buses scrapped and shortage in replacement**

Period	Buses scrapped	Buses commissioned	Shortage in replacement
	(Number)		
April 2011 to October 2011	82	33	49
July 2014 to March 2016	917	811	106

The delay in replacement of scrapped buses which was in turn due to delay in procurement of chassis, bus body building and final release of buses to Depots, affected scheduled operations causing loss of 1,01,771 vehicle days during the period from April 2011 to October 2011 and July 2014 to March 2016 with a revenue loss of ₹103.59 crore<sup>156</sup>.

Further, due to non-availability of new buses for replacing 303 five year old buses in Super Class services, KSRTC had to seek exemption<sup>157</sup> from the State Government for plying the same 5 years old vehicles for another 3 to 6 months. Thus, KSRTC had to retain old buses resulting in the denial of high quality vehicles to passengers of Super Class services.

GoK replied (March 2017) that during the audit period KSRTC held 5,984 buses against 5,040 schedules and the delay in replacing buses in Super Class services were due to the delay in procurement of buses caused due to

<sup>153</sup> Thiruvananthapuram Central, Vizhinjam, Chathannoor, Kollam, Kottayam, Pala, Thiruvalla, Ernakulam, Thrissur, Palakkad and Kasargod.

<sup>154</sup> Mentioned in *Table 3.17*.

<sup>155</sup> Calculated at average EPB for the five year period of ₹10,179 \* 74 vehicle days = ₹7.53 lakh.

<sup>156</sup> Calculated at average EPB for the five year period of ₹10,179 \* 1,01,771 vehicle days = ₹103.59 crore.

<sup>157</sup> The Government had granted (June 2014) exemption for six months to 119 buses whose 5 years' life had expired between April and July 2014 and to another 184 buses for three months whose 5 years' life had expired between August and December 2014.

imposition of Code of Conduct for Parliament Election and litigation by bidders.

The reply is not correct in view of the fact that during the five year period, in place of 1,951 buses scrapped, KSRTC infused only 1,845 buses. Further, 5,040 schedules as stated in the reply was calculated without considering new schedules added (560) during the audit period and schedules cancelled due to non-availability of buses.

### **Non-operation of schedules taken over from private operators**

**3.11.6.4** GoK had approved a scheme as per which Super Class services all over the State shall be run and operated by the State Transport Undertaking i.e., KSRTC. Accordingly, as of March 2016, KSRTC had taken over 214 Super Class services operated in the State by private stage carriages.

We observed that out of the 49 Super Class services taken over in 11 Depots, nine services commenced belatedly due to shortage of buses. In Palakkad and Kottayam Depots, three<sup>158</sup> and one taken-over services respectively were stopped for want of new buses. Similarly, in Kasargod Depot, due to non-allotment of buses, two schedules have not yet (July 2016) started. Thus, KSRTC had taken over Super Class services, but was unable to operate them for want of buses.

We also observed that operation of 15 taken-over schedules was not feasible as the revenue collections from these schedules were below the revenue generation criteria set for the respective service. The Depot authorities stated that the poor collection from these schedules was due to the continued operation of private stage carriages on these routes. Though Kasargod Depot had lodged complaints with RTA/ Police, no effective action was taken by RTA/Police to curb illegal/unauthorised operation by private stage carriages.

GoK admitted (March 2017) that the delay in operation and non-operation of taken-over services were due to shortage of buses.

### **Low collection from operation of new buses**

**3.11.7** The Executive Director (Operations) developed (November 2012) criteria for ascertaining the profitability of different services. Accordingly, Earnings Per Bus per day (EPB) for Ordinary, Fast Past Passenger, Super Fast and Super Deluxe were set as ₹12,700, ₹14,700, ₹17,000 and ₹20,000 respectively. If the EPB falls below ₹7,500, ₹9,500, ₹12,000 and ₹14,500 in the cases of Ordinary, Fast Past Passenger, Super Fast and Super Deluxe respectively, the schedule should be stopped. We carried out bus wise revenue analysis by checking the revenue collections of schedules in which the new buses were operated. We noticed that of the 658 buses allotted to the 11 Depots selected in audit, EPB were less than the criteria set in 59 cases. Reasons for non-achievement of criteria were wrong selection of schedules, wrong timing of schedules, etc. KSRTC had not taken any action either to

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<sup>158</sup> One from August 2015, one from November 2015 and one from February 2016.



cancel these schedules or to improve the collection from the schedules.

GoK replied (March 2017) that steps had been taken to rearrange the low earning schedules to improve revenue collection.

### Conclusion

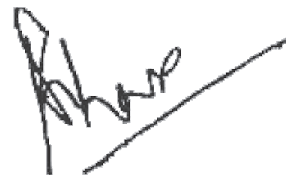
**Kerala State Road Transport Corporation (KSRTC) failed to comply with the norms of replacement of buses and as a result, it could not infuse required number of buses into the fleet during the five year period which led to shortage of buses for operations. Initiation of purchases was delayed and consequently body building and fleet addition were also delayed. Due to delayed procurement process, KSRTC failed to avail the benefits of concessional rate of excise duty. Though KSRTC had sufficient body building capacity to meet the demand for new buses during the period, it could not utilise body building capacity optimally due to non-engagement of sufficient manpower, lapses in material management, etc. Release of newly commissioned vehicles to Depots was delayed due to delay in completing registration formalities and arranging insurance. Further, after receipt of new buses in Depots, there was delay in pressing the buses into operation.**



Thiruvananthapuram,  
The 28 April 2017

(AMAR PATNAIK)  
Principal Accountant General  
(Economic & Revenue Sector Audit)  
Kerala

Countersigned



New Delhi,  
The 05 May 2017

(SHASHI KANT SHARMA)  
Comptroller and Auditor General of India