

## CHAPTER II: MINISTRY OF CIVIL AVIATION

### Airports Authority of India

#### **2.1 Lack of appropriate action by AAI led to loss of its revenue and undue benefit to contractor**

**Airports Authority of India extended undue benefit by allowing credit facilities violating the terms of contract which had resulted in non-recovery of dues. Further, by not issuing notice for vacating advertising sites after the contract period was over, the Authority had suffered a loss of revenue amounting to ₹41.68 crore.**

Airports Authority of India (AAI) awarded (October 2007) a license for indoor and outdoor advertisement at Netaji Subhas Chandra Bose International Airport (NSCBI), Kolkata to TDI International India Ltd (TDI) for a period of five years from 19 October 2007 to 18 October 2012. As per the terms of the license, TDI would pay ₹1.26 crore per month (plus applicable taxes) as license fee for the first year, with a 10 *per cent* escalation for each subsequent year. TDI would also submit a security deposit of ₹13.95 crore to AAI against license fee and electricity charges in the form of a Bank Guarantee (BG).

Though the TDI was irregular in payments to AAI and despite dispute between AAI and TDI, the Authority extended credit facility to the TDI and continued to extend the term of the license as indicated below:

- TDI had been irregular with payment of license fee since the beginning and had stopped paying license fee from May 2009. AAI (June 2009) allowed TDI six months' credit facility which was later extended (February 2010) to a year, upto June 2010. At the same time (February 2010), AAI extended the term of the license by six months (upto April 2013). The rationale for extending the term of license, two and a half years before its intended completion date (October 2012) in the face of delayed payments by the licensee was not evident. It is pertinent to note that the formal agreement for the license arrangement was yet to be signed at this stage (February 2010), the contract being actually signed in August 2010.
- In April 2013, TDI initiated arbitration proceedings against AAI, disputing its dues of ₹13.44 crore, citing loss of business, non-availability of sites due to relocation and levy of higher interest rate. The arbitrator was appointed in December 2013. AAI, meanwhile, instead of inviting a fresh tender, continued to extend the agreement with TDI (the agreement was extended in January 2013 and again in March 2014), even as the dispute continued. The extended period of the agreement ended on 18 October 2014. By then, the arbitrator had passed an interim order (August 2014) restraining AAI from invoking BG submitted by TDI. The outstanding dues for the entire contract period (2007 to 2014), as on October 2014, were ₹23.43 crores. The final award of arbitration was still awaited (November 2016).

On 9 October 2014 (just before the end date of the extended agreement on 18 October 2014), TDI informed AAI that they were not agreeable to extend the contract on existing

terms and conditions. AAI, however, continued to negotiate with TDI for extending the contractual period. The negotiations continued for over a year (from October 2014 to December 2015) with no tangible result. In December 2015, AAI issued a notice to TDI to stop display and remove advertisements from AAI sites.

During the interim period of 14 months (from 18 October 2014 when the agreement term formally ended and December 2015 when TDI was asked to stop display), TDI continued to display advertisements on AAI sites to which AAI did not object. No formal agreement was entered into with TDI for use of AAI sites during this period to safeguard the interests of AAI. When AAI (October 2015) raised a claim on TDI for using AAI sites for advertisement post October 2014, TDI (November 2015) refused to honour it, citing the absence of any contractual obligation for the period. The revenue loss to AAI on this account was ₹41.68 crore. Besides, AAI paid ₹4.82 crore in service tax on the bill raised on TDI for the period of October 2014 to December 2015 which could not be recovered when TDI refused to make payments.

Even by December 2015, AAI had not taken appropriate steps for initiating a fresh tender. As such, when AAI issued the notice to TDI for vacating their sites (December 2015), they were un-prepared for a fresh long term arrangement. Hence, AAI resorted to temporary advertisement arrangement which yielded a meagre amount of ₹0.39 crore (over January to July 2016). Compared to the license rates agreed in October 2007, the monthly revenue loss to AAI during this period was ₹0.87 crore<sup>1</sup>.

The Management stated (March 2016) that

- All the due payments for the effective contract period till 18 October 2014 had been realised except those specifically stayed by an Arbitral Tribunal and ₹7 crore which TDI had requested for internal adjustment from other airports, where they had a credit balance.
- AAI had benefitted by retaining the contractor up to 18 October 2014 on already concluded terms and conditions. In the call for tenders for long term concession in January-February 2016, there had been no response.

The Ministry (April 2016) endorsed the views of the Management.

The reply of the Management / Ministry is not acceptable on account of the following:

- As per the Joint Reconciliation statement between AAI and TDI (December 2015), the total outstanding dues for the contract period (17 October 2007 to 18 October 2014) was ₹23.43 crore. The scope for internal adjustment appears to be remote as TDI (in its meeting with AAI on 23 December 2015) had agreed to adjustment of only ₹0.98 crore which was grossly insufficient for the proposed internal adjustment.
- The lack of response to the tender issued in January– February 2016 was on account of the high rates fixed by AAI for the advertising sites which were pointed

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<sup>1</sup> ₹1.26 crore – ₹0.39 crore = ₹0.87 crore

out at the vendors' meet. Besides, the response to a tender in 2016 cannot be the rationale for extending the contract from October 2012 to October 2014 without resorting to competitive bidding.

- Besides the prospects of recovery of ₹41.68 crore from TDI for the period October 2014 to December 2015 appears to be remote in the absence of a formal contractual agreement during the period. TDI has already rejected the claim citing the lack of legal and contractual basis for raising such claims.

Thus, AAI failed to take appropriate action to protect its own interests and extended continued undue benefits to the TDI. Deferred payment facilities were allowed for a year, contract period was extended even as the licensee initiated a dispute on payment and dues amounting to ₹23.43 crore for the contract period (October 2007 to October 2014) remained un-realised. Even after the contract period ended, AAI did not issue a notice for vacating the sites leading to TDI using these sites for another 14 months (October 2014 to December 2015) resulting in revenue loss of ₹41.68 crore to AAI, as TDI did not acknowledge any dues in the absence of a contractual obligation.

## **2.2 Loss of revenue due to non-inclusion of land in lease agreement**

**Airports Authority of India allotted (April 2007), a built up space at Bijwasan, to Delhi International Airport Limited (DIAL) for the purpose of providing dormitory accommodation for CISF personnel deployed at Indira Gandhi International Airport (IGIA), New Delhi. While signing the agreement, AAI did not include in the lease agreement (March 2008), the area of land along with the built up space and the lease rent payable for the same. On it being pointed out by Audit in July 2014, AAI raised (January 2015) invoices for lease rent towards land measuring 19,525 sqm, however, DIAL refused payment on the ground that there was no agreement to charge rent for such land. Thus, AAI sustained loss of ₹28.67 crore.**

Airports Authority of India (AAI) handed over (April 2007) built up space measuring 13,067 square meter (sqm) (at Bijwasan in Delhi) to Delhi International Airport Limited (DIAL) for providing dormitory accommodation for Central Industrial Security Force (CISF) personnel deployed at Indira Gandhi International Airport (IGIA), New Delhi. A lease agreement for a period of three years, with effect from April 2007, was signed between AAI and DIAL in March 2008 in respect of the aforesaid built up space. The lease agreement was extended (October 2010) for further period of three years with effect from 04 April 2010. The agreement for the period beyond 03 April 2013 was yet to be signed by DIAL. In the meantime, at the request of DIAL, AAI constructed the second floor of the leased building covering an area of 6,562.54 sqm at a cost of ₹5.43 crore and handed over its possession to DIAL in four phases<sup>1</sup>.

Audit noticed that while forwarding the initial lease agreement to DIAL for execution, the Commercial Directorate of AAI had requested (October 2007) the Land Management Department, Northern Region of AAI to identify the land being used exclusively by DIAL and to take further necessary action for charging the rent for the land from DIAL. However, Land Management Department of AAI did not take any action to measure the

<sup>1</sup> 22.8.2012, 17.10.2012, 19.11.2012 and 17.04.2014

land. Ultimately, in the joint measurement of the land and building space, carried out by AAI and DIAL, it was revealed that DIAL was using 13,999.50 sqm of built up space (as against 13,067 sqm mentioned in the lease agreement) and 19,525 sqm of unpaved land since April 2007.

On it being pointed out by Audit in July 2014, AAI raised invoices on DIAL amounting to ₹2.27 crore on 30 October 2014 towards lease rent for excess built up space of 932.5 sqm and ₹28.67 crore (excluding service tax) on 10 January 2015 towards lease rent for unpaved land space of 19,525 sqm being used by DIAL since April 2007. DIAL paid the lease rent for excess built up space in November 2014. However, DIAL refused payment for land stating (April 2015) that land had never been part of any rent agreement since inception *i.e.*, April 2007, hence demand for payment of lease rent, either for the past or for the future period, was not acceptable to them.

Audit observed as under:

- (i) AAI did not get the area of open land space measured and included in the lease agreement which was signed 11 months after allotment of built up space to DIAL. In the absence of such a clause in the agreement, the amount of lease rent amounting to ₹32.21 crore could not be recovered from DIAL. This has resulted in revenue loss of ₹28.67 crore (excluding service tax of ₹3.54 crore) to AAI (up to 31 March 2015).
- (ii) Commercial Manual of AAI {Clause 2(c) of Chapter-2} provides that in case of remote buildings not falling within the airport area and where rentals are likely to be different from the Terminal Buildings, then the commercial rent prevalent in the vicinity of the area should be ascertained by a Committee through market survey. The Manual further provided that rate to be applied should be approved by the Corporate Head Quarters.

Audit noticed that AAI did not conduct any market survey before agreeing for the rate of lease rent with DIAL for the aforesaid built up space. Audit was, therefore, unable to make an assessment whether the rate of lease rent agreed with DIAL was at par with the rate prevalent for a similar commercial property located in the Bijwasan area.

The Management in its reply (December 2014) stated that the space rentals being charged from DIAL for CISF complex at Bijwasan were as per approved rates.

The reply of the Management is not acceptable as due to non-inclusion of a suitable provision in the lease agreement with regard to land measuring 19,525 sqm, AAI sustained revenue loss of ₹28.67 crore.

The matter was reported to the Ministry in August 2016; their reply was awaited (January 2017).

### 2.3 *Idling of civil enclaves due to absence of realistic assessment of their requirement*

**AAI did not carry out a realistic assessment of the requirement of Civil Enclaves at Jaisalmer, Bhatinda and Bikaner, due to which investment of ₹100.59 crore on creation of facilities at these Civil Enclaves remained idle since their operationalisation. AAI also incurred a recurring loss in the form of depreciation charges amounting to ₹40.06 crore.**

Airports Authority of India (AAI) manages 125 airports in the country including 26 Civil Enclaves<sup>1</sup>. Audit test checked upgradation/creation of facilities by AAI at three Civil Enclaves at Jaisalmer, Bhatinda and Bikaner with reference to the policy of Government of India on Airports Infrastructure, 1997 and other relevant guidelines. Ministry of Civil Aviation (MoCA) issued (December 1997) a policy on airports infrastructure. The Policy stated that AAI would invest only in projects with demonstrated economic viability and positive rate of return. Further, wherever Government of India compelled AAI to invest in non-viable projects for the fulfilment of social objectives, the initial capital cost of the project and the recurring annual loss sustained by the AAI on this account would be reimbursed. Further, as per paragraph 7.8 of Report on Committee on Infrastructure (June 2006), if AAI was to take up any project with Internal Rate of Return (IRR) below 8 *per cent*, then AAI could ask the respective State Government to bridge the gap funding. As per the provision of 'Norms and Standards for Determining the Capacity of Airport Terminals 2009' issued by Ministry of Civil Aviation in case of smaller airports and green field airports origin destination surveys and market surveys were required to be conducted for arriving at the traffic forecast.

Audit observed the following:

#### *(a) Civil Enclave, Jaisalmer*

AAI maintained a Civil Enclave comprising of old terminal building capable of handling 50 passengers at a time, at Jaisalmer airport of Indian Air Force (IAF). There was no civil apron. Considering that the existing civil enclave was quite away from the Air Force operational area, subjecting passengers to grave security risks and adverse weather conditions and also continued demand from IAF for development of a separate parking apron/enclave in the close vicinity, AAI approved in-principle (July 2001) construction of a new Civil Enclave with a terminal building capacity of 250 passengers, new civil apron, taxiway and other ancillary facilities. The land required for the new enclave, approach road etc. was provided in July 2003, free of cost, by the State Government to AAI. The Board of AAI in its 118 meeting held on 25 February, 2008, approved construction of a New Civil Enclave at Jaisalmer at a cost of ₹81 crore. Accordingly, construction of Civil Enclave was completed in May 2013 at a total cost of ₹63.27 crore. However, since operationalisation, there has been no passenger and flight movements at Civil Enclave, Jaisalmer.

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<sup>1</sup> *A civil enclave is an area allotted for the use of civil aircraft and civil aviation related services at an airport belonging to the Armed Forces.*

**(b) Civil Enclave, Bhatinda**

In pursuance to the directives issued from the Prime Minister's Office during a meeting held on 05 September, 2007 under the Chairmanship of Principal Secretary to the Prime Minister, development of various airports in Punjab was discussed. AAI agreed to consider the request of State Government of Punjab (GoP) for commencement of civilian flights from Bhatinda airport of IAF, to meet the demand arising from the upcoming refinery. Ministry of Defence issued (February 2008) 'No Objection Certificate' (NOC) to AAI for a maximum of two civil flights. GoP provided (June 2009) around 39 acre of land for construction of Civil Enclave to AAI. Accordingly, AAI approved (November 2010) construction of a low cost terminal at Bhatinda airport of IAF, to accommodate 100 passengers with car park, a civil apron to park two ATR type of aircrafts, taxi track etc. at a total cost of ₹26.15 crore. The work was completed in March 2013 at a total cost of ₹23.66 crore. However, the facilities created were remaining idle since their operationalisation, as passenger and flight movement at Bhatinda had been nil.

**(c) Civil Enclave, Bikaner**

AAI approved in-principle (March 2009), up-gradation of the small Civil Enclave that existed at Bikaner airport of IAF, with a New Civil Enclave comprising of civil apron, car park, link taxiway etc. at an estimated amount of ₹11 crore. The work was completed and operationalised in May 2014 at a total cost of ₹13.66 crore. However, the facilities created were lying idle as passenger and flight movement had been nil.

Audit further observed that:

- (a)** AAI did not conduct Origin-Destination survey and Market surveys as stipulated in the 'Norms and Standards for Determining the Capacity of Airport Terminals 2009', to ascertain the growth rate for traffic projections. However, such survey was not conducted for all the three Civil Enclaves even though historical data for the Jaisalmer, Bhatinda and Bikaner Civil Enclaves was not available.
- (b)** If AAI was to take up any project with IRR below 8 per cent, it could ask respective State Government to bridge the gap funding as provided in the report on Committee on Infrastructure (June 2006). However, in case of Jaisalmer, AAI calculated the IRR at 14 per cent<sup>1</sup> on the basis of Jodhpur Airport, which is located more than 280 km away. Thus the presumptive IRR calculation deprived AAI from raising a claim on the State Government of Rajasthan for the gap funding as per the above provisions.

In case of Bhatinda and Bikaner, Audit did not find on record any IRR calculations done by AAI to determine the economic viability of the project. As Civil Enclave at Bhatinda was constructed at the request of the State Government of Punjab, AAI was entitled to get reimbursement of initial cost as well as recurring cost incurred by it from GoP, as per provisions of Infrastructure Policy. However, AAI did not approach the GoP for reimbursement of expenses and thus had to bear the entire expenditure out of its own resources.

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<sup>1</sup> Considering the incremental cash flow at 16 per cent for 2009-14 and 12 per cent for 2015-24

- (c) AAI had no firm commitment from the airlines to start operations from these Civil Enclaves.

The Management in its reply (September 2016) stated that the investment by AAI in these Civil enclaves was justified on strategic, socio-economic and disaster management considerations. The Management further stated that National Civil Aviation Policy-2016 (NCAP), allowed AAI to take up projects which were financially viable with non-zero IRR.

The reply given by the Management was not acceptable as these projects were conceived and completed before adoption of NCAP-2016. Further, the Management contention that these Civil Enclaves were upgraded/constructed for strategic and disaster management considerations is an afterthought, as these reasons were not considered at the approval stages of these projects.

Thus, due to failure to carry out a realistic assessment of the requirement of the above Civil Enclaves by AAI, investment of ₹100.59 crore in creating facilities at these Civil Enclaves remained infructuous (March 2016). AAI also incurred revenue expenditure in the form of depreciation amounting to ₹40.06 crore till March 2016.

The matter was reported to the Ministry in December 2016; their reply was awaited (January 2017).

#### **Air India Limited**

#### **2.4 Non-realisation of potential rental income**

**Inordinate delay in taking decision on renting out two properties coupled with delay in granting approval for renovation of a property, resulted in non-realisation of potential rental income of nearly HKD 66.75 lakh (₹4.96 crore).**

Air India Limited<sup>1</sup>, Hong Kong (Station) has in their possession two residential properties in Hong Kong, one at Woodland Heights {2,486 square feet(sqft.)} and the other at Villa Monte Rosa (2,580 sqft.). The properties were originally used as official residences of Regional Executive Director and Manager posted in Hong Kong. Consequent to withdrawal of the post of Manager, the property at Woodland Heights fell vacant and was let out on a long lease for a period of 9 to 10 years till termination of the lease in May 2009. The other property at Villa Monte Rosa also fell vacant in May 2010 after the post of Regional Executive Director was transferred to Mumbai.

In July 2009, Air India Limited, Mumbai (Headquarters) sought from the Station, a model for revenue generation from the available immovable properties, as part of its financial restructuring plan. Although the Station suggested for renting out one of the properties and selling the other, the Board of Directors decided (October 2009) to dispose off both the properties. As the procedure for disposing off the properties was likely to take time, the Station approached Headquarters in November 2009 to rent out the property at Woodland Heights at least for a period of one year, and again in January 2010 to rent out both the

<sup>1</sup> *Air India was changed to Air India Limited in 1994; Air India Limited was again changed to National Aviation Company of India Limited (NACIL) in 2007; NACIL was once again changed to Air India Limited in 2010.*

properties<sup>1</sup> at least for a period of one year, after repair/renovations. The Station also stated that the cost of repairs/renovations could be offset with two month's rental income from both the properties. However, Headquarters did not accede to this request.

Based on Headquarters' direction, the Station initiated the process of disposing off the properties in February 2010, by appointing a consultant. In June 2010, the legal representative of a prospective buyer of Woodland Heights pointed out to the Station that the title deeds of the properties were in the name of 'Air India'<sup>2</sup> and were not transferred to 'Air India Limited' when the name of the company was changed in 1994, and thus could not be sold without changing the title deeds. However, the Land Registry Office in Hong Kong was not amenable to a change of name in the title deed as Air India was no more in existence. To resolve the issue, the Station approached several consultants for legal opinion as well as the Consulate General of India Hong Kong, but the issue remained unresolved till date.

After these developments, the Station once again approached Headquarters (May 2011) to rent out the properties at approximately HKD 60,000 to 70,000 per month after renovating them. However, no response was received from Headquarters. It was only in June 2012 after another proposal (June 2012) from the Station and a delay of more than one year, that the proposal to rent out properties in Hong Kong was finally given 'in-principle' approval. In the meanwhile, the Station had rented out the property at Woodland Heights on ad-hoc basis for a period of 6 months from 15 February 2012 at a monthly rent of HKD 65,000 (*i.e.*, ₹4,82,950)<sup>3</sup>.

After approval of Headquarters, the property at Woodland Heights was rented out from November 2012 at a monthly rental of HKD 75,000, after carrying out minor repair works. However, the other property at Villa Monte Rosa could not be rented out as the property required major renovation works for which approval of Headquarters was pending. It was only in January 2015 after a lapse of two and half years, that approval was given for renovating the property at Villa Monte Rosa. The renovation was completed in May/June 2015 at a cost of HKD 11.12 lakh (*i.e.*, ₹82.62 lakh). The property was finally rented out in November 2015 at a monthly rent of HKD 88,000 (*i.e.*, ₹6,53,840).

Delays resulted in potential revenue loss in the form of rental income. Had Headquarters given approval for renting out the properties in November 2009 itself on being approached by the Station for the first time, the Station could have realised a revenue of at least HKD 66.75 lakh, *i.e.*, ₹4.96 crore by way of rental income as detailed in **Annexure I**. It would also be pertinent to mention that the Station has incurred an expenditure of HKD 12.48 lakh towards mandatory charges such as property tax, management fee and annual rent for these properties during the period April 2009 to March 2016. Moreover, it was also seen that the Station hired two residential apartments for accommodating India based officers posted in Hong Kong and incurred an expenditure of HKD 31.09 lakh (*i.e.*, ₹2.31 crore) towards rent for the period from April 2009 to March 2016.

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<sup>1</sup> *As the property at Villa Monte Rosa was likely to fall vacant as the Executive Regional Director was under orders of transfer.*

<sup>2</sup> *Name of Air India Limited prior to 1994*

<sup>3</sup> *Rate of Exchange of 1 HKD = ₹7.43 being the average Rate of Exchange of November 2009 and March 2016 has been adopted.*

On being highlighted on earlier occasion (November 2012), the Ministry had stated (May 2014) that the apartment were not put up for rental as the Station was anticipating sorting out the title issue within a few months, while the normal terms of rentals in Hong Kong is two years with one year fixed period.

The reply of the Ministry is not acceptable as the Station had approached Headquarters on various occasions (November 2009, January 2010, May 2011 and June 2012) as mentioned above for renting out the properties for short duration, which was not acceded to by Headquarters. The legal issue regarding title deeds was also noticed as early as June 2010 based on which, the Station once again approached Headquarters in May 2011 for renting out the properties, which was also not acceded to. Moreover, even after 'in-principle' approval of Headquarters for renting out the properties was received in June 2012, the Station could not rent out one of the properties as the approval for renovation of the property was received only in January 2015, after a lapse of two and half years.

The Station, while confirming the facts and figures, stated (June 2016) that the Country Manager was posted to Hong Kong in August 2008 when both the properties were occupied and hence, the Country Manager could not be accommodated in one of these properties. As the apartment rented out for the Country Manager was for a period of three years, the Country Manager could not be shifted to Woodland Heights, when it fell vacant in May 2009. Thereafter, a decision was taken to dispose off the properties in October 2009 and hence no India Based Officer was accommodated in these properties for smooth disposal.

However, the reply does not address the issue of delay in approval for renting out the properties and for renovation of one of the properties, which resulted in revenue loss. The reply also does not indicate the reasons for not accommodating the India Based Officers in these properties, once the legal issue regarding title deeds were noticed in June 2010.

### ***2.5 Short coming in tendering process in renewal of Aviation Insurance resulting in a loss of USD 30,89,959 to Air India Limited***

**Air India awarded the contract for Aviation Insurance Policies for the year 2009-10 to a consortium led by Reliance General Insurance Company Limited (RGICL). After awarding the contract but before commencement of the Policy an aircraft of AIL caught fire at Mumbai. Considering this as additional risk RGICL demanded additional premium of USD 30,89,959, and deducted the same from the claim relating to subsequent incidence of an aircraft crash at Mangalore. This resulted in additional expenditure of ₹14.40 crore (USD 30,89,959).**

Air India Limited (AIL)<sup>1</sup> invited technical bids (March 2009) for renewal of Aviation Insurance Policies for the year 2009-10. In response, two bids were received from: (i) a Consortium of 4 Public Sector Undertaking (PSU) insurance companies, led by The New India Assurance Company Limited (TNIACL)<sup>2</sup> and (ii) Consortium of 4 private insurance companies<sup>3</sup> led by ICICI-Lombard General Insurance Company Limited (ICICI - LGICL).

<sup>1</sup> *Erstwhile National Aviation Company of India Limited (NACIL)*

<sup>2</sup> *National Insurance Company Limited (NICL), The Oriental Insurance Company Limited (TOICL) and United India Insurance Company Limited (UIICL)*

<sup>3</sup> *With three other Companies viz. RGICL, BAGICL & IFFCO-TGICL*

However, on suggestion of the private sector insurance companies<sup>1</sup>, AIL invited fresh tender (June 2009) inviting bids on standalone basis to get more competitive rates. Five private insurance companies<sup>2</sup> submitted their bids individually, on standalone basis, whereas the consortium of PSUs under the leadership of TNIACL bid as a consortium which was accepted by AIL. After submission of bids, Reliance General Insurance Company Ltd. (RGICL) requested for an opportunity to quote a joint bid with other three private companies<sup>3</sup>, which was allowed (24 June 2009) by AIL.

The three bidders *i.e.*, (i) consortium of private insurance companies led by RGICL, (ii) consortium of PSUs led by TNIACL and (iii) ICICI-LGICL (standalone bidder) were invited (31 July 2009) to submit their commercial/ price bids by the Evaluation Committee. On comparison of rates quoted, the consortium led by RGICL emerged as lowest bidder by quoting a premium of USD 2,42,38,414.69. On 9 September 2009 the aviation insurance policy of AIL for the policy year from 1 October 2009 to 30 September 2010 was awarded to consortium led by RGICL and they confirmed their acceptance on the same date.

In the meanwhile, an incidence of fuel leakage and fire at the engine of AIL's Aircraft VT-ESM occurred on 4 September 2009 at Mumbai Airport. The consortium led by RGCIL vide their letter dated 16 September 2009 raised the issue of new loss based on this incident and subsequently (September 2009) demanded an estimated Additional Premium (AP) of USD 35,00,000, on the ground that they had marketed the risk to reinsurance, based on the information provided by AIL under Clause 11(f) of the tender, taking into consideration the market conditions and strength of AIL, as projected in the AIL's current Insurance booklet and thus the new loss information would constitute a material change in the loss position following submission of their commercial bid and that the reinsurers would want to revise their terms in light of this new information. The consortium led by RGICL, also reported (23 September 2009) that as per the information from market, the loss to the VT-ESM Aircraft was estimated to be in the range of USD 18 million. AIL (24 September 2009) confirmed that the loss was estimated to be in the range of USD 18 to 20 million.

Subsequently (March 2010) RGICL demanded USD 29,10,857 plus applicable taxes, if the loss amount was more than USD 11 million. The AP was not required to be paid in case the loss amount was below USD 11 million. This threshold limit of USD 11 million was fixed by the consortium led by RGCIL after being aware of the estimated loss in the range of USD 18 to 20 million. Further, no basis for determining the limit of USD 11 million was intimated to AIL.

In June 2010 TNIACL, who were the existing insurers of the fleet for the period upto 30 September 2009, settled the claim relating to Aircraft VT-ESM at USD 14.5 million. The claim settlement amount against Aircraft VT-ESM exceeded the thresh hold limit of USD 11 million as set by RGICL. RGICL informed that non-payment of AP by 30 April 2010 would result in cancellation / withdrawal of cover.

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<sup>1</sup> *RGICL, BAGICL & IFFCO-TGICL*

<sup>2</sup> *ICICI-LGICL, RGICL, BAGICL, IFFCO-TGICL and HDFC Ergo General Insurance Company Limited (HDFC-EGICL)*

<sup>3</sup> *(i) BAGICL (ii) IFFCO-TGICL and (iii) HDFC-EGICL*

In May 2010, another aircraft (VT-AXV) crashed at Mangalore. RGICL informed that the markets had made it clear that unless the AP issue was settled, there would be difficulty in making a cash call on the money under the policy from the reinsurance markets to satisfy the hull, passenger and third party claims in respect of crash of aircraft at Mangalore. RGICL informed (12 July 2010) that if the loss AP was not settled, the reinsurers would issue the 'notice of cancellation'. AIL conceded the demand of RGICL and advised (6 August 2010) RGICL to adjust the AP against the balance proceeds of the Hull claim VT-AXV and settle the balance amount. The funds were transferred (12 August 2010) by RGICL after deducting AP of USD 30,89,959.

The recovery of AP by RGICL from the amount of Hull Claim of VT-AXV had thus resulted in excess expenditure of USD 30,89,959<sup>1</sup> (Premium USD 28,01,413 + Service Tax USD 2,88,546) to AIL. Besides, though the initial bid (March 2009) did not restrict the bidders to submit the bids on standalone basis, AIL considered the suggestion of the private sector insurance companies and re-tendered to obtain single bids to enhance competition. However, after submission of bids on standalone basis, RGICL was again allowed to submit their bid in consortium. The decision of AIL to accept the financial bids from consortia contradicted the very purpose of re-tendering. AIL also followed a non-transparent mechanism to allow the change in compositions of the bidders, after submission of bids.

The Management in its reply (September 2016) stated:

1. AIL had permitted (15 June 2009) PSU insurance companies to submit their bid as a consortium. During the course of presentation, private insurance companies excluding ICICI - LGICL stated that they would like to form a consortium with RGICL as their leader. With a view to give fair and equal treatment to all bidders and to have a common level playing field, AIL had agreed to the request of the private insurance companies.
2. RGICL's demand for AP had been protested vehemently by AIL from the beginning. RGICL, however, finally adjusted the premium out of the insurance proceeds paid on account of hull loss and if AIL had not agreed to this, RGICL could have withdrawn the cover since the underwriters had given 7 days cancellation notice which would have grounded the fleet and caused disruption in services, besides bad publicity in India as well as abroad. Further, claims under crash of aircraft at Mangalore would have remained unsettled and legal action initiated against AIL. Since the matter was not settled *in toto*, AIL was not in a position to take any legal steps against RGICL to avoid inconvenience to the suffering families of passengers who had lost their lives.
3. In the event of a major loss between the submission of the bid and the placement, either globally or with the insured, the underwriters had right to revise the bid.

The Ministry of Civil Aviation in its reply (December 2016) further added that:

- (i) The reason for re tendering was mainly on account of the arguments put forth by one of the brokers that AIL was not securing best rates in the market; consortium bidding would be advantageous to AIL; and there was no basis of tendering as pointed out by Audit.

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<sup>1</sup> USD 30,89,959 x ₹46.7865 per USD as on 12-08-2010 = ₹14,45,68,367

(ii) The incident of VT-ESM occurred on 4 September 2009 which was after the submission of technical and financial bids and the RGICL consortium stated that it was a material fact which has not been taken into account while submitting the bid. Price Protection Clause is not possible under the insurance contracts wherein there is time gap between the submission of bids and the actual payment of the policy. It was further stated that if there is a major event between the date of the submission of the bid and the actual placement of the policy, the underwriters usually reserve the right at the time of submission of the bid to revise their quotes to take into account the major event.

(iii) AIL had two options, one to accept the lower figure of USD 10 million for the VT-ESM claim and not pay any Additional Premium or accept a claim higher than 10 million, when the AP of USD 3.09 million would become payable. As such any settlement of the VT-ESM claim about USD 13.09 million was beneficial to AIL. As AIL got the net settlement of USD 14.5 million, the second option was beneficial and chosen.

The reply is not acceptable in view of the following reasons:

1. The initial bid (March 2009) invited by AIL did not restrict the bidders to submit the bids on standalone basis. The private insurance Companies did not avail the opportunity to submit bids on standalone basis and after submitting bids in consortium, requested AIL to re-invite bids on standalone basis. Further after giving opportunity to submit bids on standalone basis, RGICL again requested for opportunity to submit the bid in consortium. The decision of AIL to accept the financial bids from consortia contradicted the very purpose of re-tendering.

2. The Consortium led by RGICL on 9 September 2009 had confirmed the acceptance of the AIL placement of policy at the Premium rate of USD 2,42,38,414.69. Thus, the acceptance of the offer was binding and legally enforceable contract under the Indian Contract Act, 1872. Therefore, subsequent revision of the terms of payment of the policy amounted to breach of Contract. No legal action against RGICL was initiated by AIL to get back the amount of excess premium paid to the insurer.

3. The Ministry's contention that if there is a major event between the date of the submission of the bid and the actual placement of the policy, the underwriters usually reserve the right at the time of submission of the bid to revise their quotes to take into account the major event should be viewed in the light of the fact that in the note dated 24 March 2010 submitted by the Executive Director (Finance) to the Chairman and Managing Director it has been brought out that the practice in the international market is that, if there is a major catastrophic incidence, like that of World Trade Center, then only AP becomes payable and it applies to all Airlines worldwide. The note also states that this fact has also been confirmed by lead insurance brokers like Wills, JLT and Avon. Besides the impact of the claim/claim history will be considered by reinsurer, at the time of negotiations of subsequent renewal of the policy in 2010-11. The insurance contract is valid, once offer of the insured is accepted as per the provisions of India Contract Act, 1872. As such, the claim of AP was not valid.

4. The consortium led by RGICL, in their letter dated 24 August 2009 had confirmed that as assured by them, that 100 *per cent* claim of AIL would be settled irrespective of failure to pay by insurer/consortium partners. Thus, though the underwriters wanted to

revise their terms in the light of loss to the VT-ESM Aircraft and were not ready to accept the reinsurance, Consortium led by RIGCL was bound to pay the entire claim relating to Hull claim of VT-AXV aircraft at the premium agreed by them at the time of accepting the offer of AIL without charging any additional premium.

Thus, the demand for additional premium was against the spirit of the award of contract by AIL and acceptance thereof and assurance given by the consortium led by RIGCL and has resulted in excess expenditure of USD 30,89,959 (₹14.40 crore) to AIL.

## **2.6 Irregular award of Contract**

**Award of contract to M/s. IBM India Private Limited, at a cost of ₹155.70 crore, on nomination basis for SAP ERP Implementation, Application Management and Maintenance Services and Supply of Hardware and Software in violation of the conditions applicable for awarding contracts on the basis of Rate Contracts of DGS&D and guidelines issued by the Central Vigilance Commission.**

Air India Limited (AIL) proposed (July 2009) to implement System Application Program - Enterprise Resource Planning (SAP-ERP). M/s. SAP India Private Limited (SAP) was selected (September 2010) on nomination basis for the supply of SAP software licenses and based on the recommendation of SAP, M/s. IBM India Private Limited (IBM) was nominated (September 2010) as Implementation Partner for the SAP ERP Project.

SAP submitted their initial financial proposal on 27 September 2010 at a cost of ₹33 crore for SAP Licenses and 22 *per cent* per annum on the license fees, towards SAP Enterprise Support (ES). Again, on 28 September 2010, SAP submitted a fresh proposal for a total estimated project cost of ₹225 crore plus taxes and duties for implementation in 2 years and enterprise support for 5 years. Though IBM was not a partner under the existing Director General of Supplies and Disposal (DGS&D) rate contract, awarded to M/s. Resseaux Tech Private Limited, the proposal was approved (28 September 2010) by the Board of Directors (BOD) of AIL in its 34<sup>th</sup> Meeting. Further, the Board authorised the Management to finalise the scoping study and conclude the contract within three weeks of issuing the Letter of Intent (LoI) on mutually agreed terms and conditions.

AIL issued (20 October 2010) an LoI on SAP (₹69.30 crore) for supply of SAP software and software support and another LoI on IBM (₹155.70 crore) for SAP Implementation services, SAP Application Management Services, supply of Hardware for ERP Project and supply of software as required for integration/ interfacing for the ERP Project.

On 6 January 2011, an End User License Agreement (EULA) was entered into with SAP for Software Licenses and Enterprise Support and another agreement was entered into with IBM for (a) Supply of Hardware, Software and SAP Implementation and Support and (b) Statement of Work.

On account of the financial constraints faced by the Company, M/s. IBM Global Finance (IGF), offered (November 2010) a financing agreement for the Project (excluding AMCs) amounting to ₹156.63 crore (including Bank Guarantee charges payable by AIL) at interest charges of 7.8 *per cent* (Internal rate of return), in association with Standard

Chartered Bank<sup>1</sup>. The payment was scheduled to be spread over 22 months with an initial moratorium of 3 months.

The Go-Live of the SAP-ERP Project was on 31 January 2013. Out of the total project cost of ₹225 crore, payment amounting to ₹211.43 crore had been made (December 2016) to SAP and IBM.

Audit observed the following deficiencies in the process of award of contract:

- The rate contract was awarded by DGS&D to M/s. Reseaux Tech Private Limited with M/s. Arteria Technologies Private Limited as the consortium partner and SAP India Ltd. as the Original Equipment Manufacturer (OEM). IBM was not a partner under the existing DGS&D rate contract. The contract under the approved DGS&D Rate Contract should have been awarded to M/s. Reseaux Tech Private Limited with M/s. Arteria Technologies Private Limited as the consortium partner and SAP India Ltd. as manufacturer. However in violation of the DGS&D guidelines, and Provisions contained in the Manual<sup>2</sup> on Policies and Procedures for purchase of goods, issued (August 2006) by the Ministry of Finance, Department of Expenditure, Air India awarded the contract for implementation to M/s. IBM on nomination basis on the recommendations of M/s. SAP India Ltd.
- The amount of ₹155 crore payable to IBM was based on (4 October 2010) the man-months computed by IBM under the Implementation Plan (1,392 man-months) and Annual Maintenance Services for a period of 5 years (1,668 man-months). Audit noticed that the estimated project cost submitted to the Board on 28 September 2010 was not supported by a cost analysis carried out by AIL. The actual cost quoted by IBM against their Implementation Plan submitted on 4 October 2010 did not deviate from this estimate. Audit did not receive evidence of the price justification carried out by AIL, except the fact that the rates for man-days were identical to those in the DGS&D rate contract. The requirement of man-days was also not made a part of the agreement with IBM to enforce actual availability of manpower.

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<sup>1</sup> *They provided the Bank Guarantee to AIL*

<sup>2</sup> *The Manual on Policies and Procedures for purchase of goods and services, issued (August 2006) by the Ministry of Finance, Department of Expenditure, stipulates that if an organisation directly procures DGS&D rate contracted goods from the suppliers, the prices to be paid for such goods shall not exceed those stipulated in the rate contract and other salient terms and conditions of the purchase should be in line with those specified in the rate contract.*

- In contravention of the guidelines<sup>1</sup> of Central Vigilance Commission (CVC), communicated vide office order of July 2007, the additional works (₹1.87 crore) for setting up of SAP ERP Data Centre at New Delhi was also awarded to IBM, on nomination basis.

The Management in its reply (December 2016) stated as follows:

- As per provisions of Material Management Department (MMD) Manual, Material Management Administrative Order (MMAO) 684, if Rate Contract of DGS&D rate is followed there is no need for a tender procedure. The SAP licenses were on Rate Contract of DGS&D and this was duly checked from DGS&D website and confirmed. Further, during the 34<sup>th</sup> Board Meeting, the need to have the implementation carried out on nomination basis by M/s. IBM was clearly brought out. As regards award of contract to IBM on nomination basis, the reply added that though AIL was not aware of the existence of CVC guidelines, contract to carry out implementation part was awarded to IBM on nomination basis, on account of their experience in SAP implementation with other airlines in India. No cost analysis to assess and justify the reasonableness of the price quoted by SAP and IBM was considered necessary since they were in line with the rates in Rate Contract of DGS&D.
- The entire process for putting in place an ERP system in Air India started with a presentation to the Committee of Secretaries in July 2009. Draft Request for Proposal (RFP) for appointing ERP Consultant was circulated (6 April 2009) and discussed but not issued. Instead the finalised RFP document for implementation of SAP-ERP was released on 23 March 2010. In addition, there were several deliberations before the Group of Ministers; as well as extensive deliberation within Air India before implementation of SAP-ERP was decided in February 2010. SAP India contacted Air India for the first time and enumerated various benefits that ERP implementation would provide to Air India. The hardware from IBM as procured based on the specific recommendation from M/s. SAP India Ltd., as well as the implementation costs claimed by IBM were as per the

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<sup>1</sup> *CVC in its Office Order dated 5 July 2007 had communicated the necessity to resort to tendering process as basic requirements for the award of contract by any government agency, as any other method, especially award of contract on nomination basis, would amount to a breach of Article 14 of the Constitution guaranteeing right to equality, which implies right to equality to all interested parties. As per the Hon'ble Supreme Court judgement [arising out of SLP (Civil) No.10174 of 2006] "The law is well settled that contracts by the State, its corporations, instrumentalities and agencies must be normally granted through public auction/public tender by inviting tenders from eligible persons and the notification of the public auction or inviting tenders should be advertised in well-known dailies having wide circulation in the locality with all relevant details such as date, time and place of auction, subject matter of auction technical specifications, estimated cost, earnest money deposits etc. The award of government contracts through public auction/tender is to ensure transparency in public procurement, to maximize economy and efficiency in government procurement to promote healthy competition among the tenderers, to provide for fair and equitable treatment of all tenders and to eliminate irregularities interference and corrupt practices by the authorities concerned. This is required by Article 14 of the Constitution.*

*However, under rare exceptional circumstances such as natural calamities and emergencies declared by the government; where the procurement is possible from a single source only; where the supplier or contractor has exclusive rights in respect of goods or services and no reasonable alternative or substitute exists; where the auction was held on several dates but there were no bidders or the bids offered were too low, etc. this normal rule may be departed from and such contracts may be awarded through private negotiations."*

DGS&D rate contracts. There is a categorical assertion by IBM to this effect which were verified by AIL. Within the same overall implementation costs, IBM have also given the hardware and the software to run this hardware. It may be noted that in case IBM had not provided this hardware and the system free of cost, AI would have had to incur additional costs in procuring the same.

- The decision to create a Data Centre at EDP Palam by IBM on nomination basis was discussed with the then Director Finance (DF) and ED-IT and approved in a meeting of Vertical Heads chaired by CMD during an IT Review Meeting held in New Delhi on 1st March, 2011. From the Minutes of Meeting held on 1 March, 2011 it is seen that the ED-Projects (SAP ERP) had highlighted the need to get the Data Centre ready for housing in Computer Centre, the deadline to meet various project timelines being 31 March 2011. In view of the urgency of the ERP Project, CMD advised ED (IT) and DF to process the proposal in this regard and get the work expedited through IBM for creation of the Data Centre to fast track the project clearance. It is not clear from the records available why the Data Centre requirement was not built into the original proposal for procurement/implementation of the SAP-ERP system.

The reply is not acceptable in view of the following:-

- While there is no requirement to invite bids in case the orders are placed on the Rate Contract holder of DGS&D, the fact remains that IBM who were the implementing agency, was not a rate contract holder. Besides, the provisions of Clause 29 of MMAO of Manual of MMD of AIL state that the purchase order should be placed on the DGS&D contracted supplier. The contract was awarded to IBM, who were not such a supplier under the DGS&D Rate Contract.
- Even under the DGS&D Rate Contract awarded to M/s. Resseaux Tech Private Ltd., as per Remarks 3 below item 5 (b) of Schedule A of this contract, estimation of the number of mandays for any project was to be done along with the user department who had the option of choosing the optimum number of professionals in the team. There was no cost analysis of the man-days required and the total estimated project cost, in the submission to the Board at the time of approval in its 34th meeting. The fact that the estimate submitted to the Board without cost analysis did not vary from the final contract amount, is in the opinion of Audit indicative of the absence of detailed analysis of man-days requirement by AIL.
- While envisaging the project, the requirement of Data Centre (₹1.87 crore) was neither contemplated by AIL nor informed by SAP and IBM. Moreover, award of the contract for Data Center, on nomination basis, was not brought to the notice of the Board.

Thus award of contract to M/s IBM at a cost of ₹155.70 crore for implementation of SAP and ₹1.87 crore for data center were in violation of guidelines issued by CVC and terms and conditions of Rate Contract of DGS&D.

The matter was reported to the Ministry in January 2017; their reply was awaited (January 2017).