Chapter 6 – Stores

The Stores department is headed by Member (Mechanical) at Railway Board level and by Controller of Stores at the Zonal level. The department is responsible for ascertaining the needs of the Zonal Railways in the matter of materials & stores and of arranging for the supply of such materials & stores in the most efficient, economical and expeditious manner possible. It is also responsible for their receipt, inspection and distribution to the various stores depots. The Controller of Stores of a Railway was in-charge of inventory control.

The total expenditure of the Stores Department during the year 2009-10 was ₹ 10,458.47 crore. During the year, apart from regular audit of vouchers and tenders etc., 184 offices of the Stores Department were inspected.

This chapter includes major audit findings dealing with issues of assessment, procurement policies/decision and utilization of stores. Issues regarding non-adherence/non-implementation of rules contained in the Codes for Stores Department and other rules/orders issued by Railway Board are also covered.

6.1 Railway Board: Manufacture and supply of "L" type composition brake blocks- Undue benefits to M/s Escorts Limited of ₹1.66 crore and loss of ₹ 1.23 crore due to inability to exercise option clause

Failure of the Railway Board to insist that the "composition brake blocks" supplier passes on the benefit of excise duty concession resulted in extending undue benefit of `1.66 crore to M/s Escorts. Further, in the absence of a standard clause in the contract to reduce the ordered quantity by 30 per cent, the Railways could not exercise the minus option clause in a falling market and avail financial benefit of ` 1.06 crore

A. Railway Board floated (December 2006) a tender for procurement of Composition Brake Blocks (CBBs) for freight and coaching stock required for the period 2007-08. During the technical evaluation of the 13 offers by RDSO, 5 offers (main Part 1 suppliers) were considered as eligible for bulk orders. All 5 suppliers quoted the same all inclusive (basic + ED+ ST) rate of ₹ 488.73 per CBB leading to suspicion of cartel formation. The Tender Committee recommended for placing the order by splitting the quantity equally among the five suppliers at their lowest negotiated bids. On subsequent negotiations, all firms accepted Railways' counter offered rate of ₹ 420 per CBB and orders were issued to M/s Rane Brake, M/s Pioneer Friction, M/s Escorts Ltd., M/s Allied Nippon and M/s Industrial Laminates for supply of 1,50,817 CBBs each and development order on M/s BIC Auto and M/s Bony Polymers for supply of 66,537 CBBs each.

M/s Escorts in their offer had quoted an all inclusive rate to be supplied from their Faridabad /Rudrapur Plants. The Executive Director, Finance (Stores) in his proposal had recommended that in the case of supply from the Rudrapur Plant in Uttarakhand State which was exempted from payment of excise duty, the benefit should be passed on to the Railways. M/s Escorts however, did not agree to pass on the duty / tax benefits for the Rurdapur plant to the Railways. However, it was noticed that the counter offer was issued to M/s Escorts with the place of manufacture as Faridabad only. Subsequently, M/s Escorts represented that during their discussion with Officer on Special Duty/ Minister of Railways it was agreed that the firm would be allowed to supply CBBs from both the plants at the same landed cost. The contract was finally placed on M/s. Escorts for supply from both the Plants. As no negotiation was held with any of the suppliers at this stage, it was not clear how M/s Escorts was allowed to discuss the tender issue with OSD/ MR which violated the CVC guidelines on tender finalisation and therefore needed to be investigated.

A review by Audit revealed that M/s Escorts had supplied 1,96,057 CBBs at a basic rate of ₹ 420 from its Rudrapur plant, which had been exempted from payment of excise duty. As the firm had not paid any excise duty on these supplies, there was no justification in allowing the duty element in the all inclusive rate of ₹ 420 per CBB. The undue benefit thus passed on to M/s Escorts in this contract amounted to ₹ 1,02,89,071.

Against a subsequent tender for 2008-09 (2007/RS (I)/951/1/TC), a similar contract was placed at the same all inclusive rate of ₹ 420 per CBB for Part I suppliers including M/s Escorts and ₹ 350 per CBB for Part II (developmental) suppliers. Against this contract also, M/s Escorts supplied 1,19,905 CBBs from its Rudrapur Plant which did not attract any excise duty. Similar undue benefit was passed on to M/s Escorts on these supplies amounting to ₹.62,92,614.

Thus the failure of the Railway Board to insist that the supplier pass on the benefit of excise duty concession resulted in extending an undue benefit of ₹ 1,65,84,467 to M/s Escorts.

B. The standard quantity variation clause in Railway contracts for procurement of stores entitled the Zonal Railways to increase or decrease the ordered quantity by 30 per cent of the tendered quantity during the currency of contracts. However, the quantity variation clause in the above two contracts for brake blocks referred above contained provision only for increasing the quantity by 30 per cent and not for reduction. No recorded reasons were given for deviating from the standard clause.

In the tender no. 2008/RS(I)/951/1(TC) floated for 2009-10 for CBBs opened on 20 April 2009, the rate obtained was ₹ 396.24 and ₹ 298 per CBB for Part 1 supplier and Part II suppliers respectively which was reduced to ₹342 and ₹288 per CBB during negotiation. In the absence of a clause to reduce the quantity by 30 per cent in a falling market, the Railways could not exercise the minus option clause and avail financial benefit of ₹ 1,05,67,450 on 127238 CBBs remaining to be supplied as at the end of May 2009(limited to 30 per cent of the order quantity).

The matter was taken up with the Ministry of Railways in October 2010 who stated in their reply that the tender had already been finalized with the approval of the tender accepting authority (Minister of Railways) on 10 September 2007 and counter offer issued to the firm on 14 September 2007. M/s Escorts in their letter dated 29 October 2007 claim to the alleged meeting as having held on 29 October 2007 and hence CVC guidelines were not violated. It was also stated that M/s Escorts had quoted all inclusive rate Ex-Rudrapur/ Faridabad, after taking into consideration the duty benefits available at Rudrapur and hence not offered differential rates. The condition of supply from Faridabad was made by Railway in their counter offer which the firm was free to accept or reject.

The contention of the Ministry of Railway's was not tenable in view of the following:

The counter offer of the Railways was accepted by the firms only during October 2007 and the contract was finalized on 22 November 2007. According to the CVC guidelines on tendering process, counter offer was tantamount to negotiations and should be treated at par with negotiation. The acceptance of the counter offer by the bidders should have been unconditional. However, M/s Escorts was allowed to have further meetings regarding supply from both the plants and this was tantamount to post tender negotiations thereby violating the CVC guidelines. The final proposal was approved by only two members of the Tender Committee and also not approved by the tender acceptance authority. Further, the counter offer was made to the firms at an all inclusive (Basic+ED+ST/VAT) rate of ₹420, hence M/s Escorts was not eligible to claim the ED component which was never paid by it on the supplies from the Rudrapur Plant. This conferred unintended benefits to M/s Escorts when compared to the other suppliers on whom orders were placed at the same rate. Further, absence of a minus option clause led to financial loss of ₹1.06 crore.

6.2 Railway Board : Loss of ₹ 2.47 crore due to injudicious exercise of Option Clause at the time of placement of original purchase order

Railway Board exercised the plus 30 per cent option clause while placing the purchase order for finished BOX-N wagon axles enhancing the ordered quantity from 8000 to 10400 axles. With a decline in price the Railways lost the opportunity of reducing the quantity to 5600 axles while exercising the minus 30 per cent option clause resulting in loss of ₹2.47 crore

The quantity variation clause in Railway contracts for procurement of stores entitled the Railways to increase or decrease the ordered quantity by 30 per cent of the tendered quantity during the currency of contracts.

The Railway Board floated (March 2008) a global tender no. WTA-441 for supply of 8000 finished BOX-N wagon axles. The tender was opened in May 2008 and evaluated by the Tender Committee (TC) in January 2009 eight months after opening of the tender. As the lowest offer was found to be technically unsuitable, the TC recommended negotiations with the second lowest tenderer, M/s. Jinan Railway Vehicle Equipment Co. Ltd, China whose offer (US $1010 per axle) was higher than the last purchase rate by 31.51 per cent. After two rounds of negotiations, the firm reduced the price to US $950 per axle which was found to be reasonable by the TC and recommended for acceptance (June 2009). The TC further recommended that the 30 per cent option clause for increasing the tendered quantity may also be exercised at the time of placement of the Purchase Order thereby increasing the quantity to 10,400 axles. The recommendations were accepted by the Railway Board and a purchase order was issued in July 2009 to the above firm for 10,400 axles at the rate of US $950 per axle.

Railway Board in November 2009 observed that the price of this axle had come down substantially and in Global Tender No. WTA–453 opened in August 2009, the lowest rate received was US $740 which was lower than the existing contract rate by US $210 per axle. Therefore it was decided to exercise the minus option clause available in the contract. However, the firm offered to supply the quantity at the lower rate of US $740 which was accepted by Railway Board. Thus, the Railways procured 8000 axles at the rate of US $950 per axle between September 2009 and January 2010 and 2400 axles at the rate of US $740 per axle during March 2010. In this connection Audit observed the following:

(i). The TC while evaluating the offers received, observed in January 2009 that the shortfall of 8000 axles was calculated on the basis of a wagon production target of 20,000 during 2008-09, whereas the actual wagon production was much lower, hence 8000 axles would not be required in 2008-09. However, they recommended increasing in the quantity ordered from 8000 to 10400 Nos. by exercising the plus 30 per cent option clause at the time of placement of orders which was unwarranted.

(ii). While recommending second round of negotiation of rates, the TC observed (March 2009) that the prices of raw materials since opening of the tender in May 2008 had shown a substantial decline in subsequent months. The international steel prices had started falling since July 2008 and by May 2009 were 55 per cent lower than the prevailing price of July 2008. Considering the fact that the new tender had already been floated, the Railway Board could have even discharged the tender and expedited the finalization of the new tender to avail the financial benefit of reduction in price.

(iii). Had the option clause not been exercised at the time of issue of the purchase order, the Railway Board would have had the option of reducing the quantity ordered from 8,000 to 5,600 axles, instead of from 10,400 to 8,000 axles. Thus, the Zonal Railways incurred a loss of ₹2.47

crore due to injudicious exercise of option clause at the time of issue of the purchase order.

The matter was taken up with the Ministry of Railways in August 2010 who stated in their reply that the plus 30 per cent option was exercised at the time of placement of purchase order to meet the immediate requirement of 14000 axles by Rail Wheel Factory (RWF). It was also stated that on receipt of lower rate of US $ 740 per axle in the next tender, the lower rate was applied to the 30 per cent option quantity of 2400 axles.

The contention of the Ministry of Railways was not tenable in view of the following:

Urgency of requirement of axles as the reason for exercising the option clause at the initial stage was questionable as the TC met for the first time after eight months of opening the tender and the purchase order was finally issued in July 2009, thirteen months after the tender was opened. It was further noticed that out of 14,000 axles requested by the RWF in May 2009, only 4,311 axles pertained to this tender and the rest was to be sourced against two other existing contracts. This indicated that there was no urgency for placement of order for additional 30 per cent axles. Much before the opening of the next tender, the TC itself was aware (March 2009) of the declining trend in the price of raw materials. It was, therefore, not prudent to order the increased quantity at the time of placing the purchase order. By ordering the quantity of 10400 axles instead of 8000, the Railways lost the opportunity of reducing the quantity to 5600 axles and procuring the balance 4800 at US $740 per axle. Though the Railways purchased 2400 axles at the rate of US $740 per axle, they could not avoid the loss of ₹2.47 crore.