

Chapter 1

Introduction

The Sugar Industry

1.1 The sugar industry is one of the oldest agriculture based industries in the world. Sugar is produced in over 122 countries across the world. India is the second largest sugar producer in the world after Brazil and is also the largest sugar consumer.

Annual average sugar production in India during 2005-06 to 2009-10 was 21488 thousand tonne.

It is estimated that the world sugar production would be around 167 million metric tonne in the 2010-11 International Sugar Season (October-September).

India contributes approximately 14.68 *per cent* of the total sugar production in the world. Uttar Pradesh is the second largest producer of sugar in the country after Maharashtra. The production of sugar in the country during the years from 2005-06 to 2009-10 and the contribution of Uttar Pradesh is given below:

(In thousand tonne)

Year	2005-06	2006-07	2007-08	2008-09	2009-10
All India production of sugar	19267	28364	26357	14539	18912
Contribution of Maharashtra	5197	9100	9075	4578	7067
Contribution of Uttar Pradesh	5784	8475	7319	4064	5179

(Source: Sugar India Year Book 2011)

The details of total number of installed sugar factories in the country and in two top sugar producing states in 2009-10, were as follows:

Particulars	Public	Private	Cooperative	Total
All India	62	269	320	651
Maharashtra	--	35	166	201
Uttar Pradesh	33	95	28	156

(Source: Sugar India Year Book 2011)

The Companies

1.2 Uttar Pradesh State Sugar Corporation Limited (UPSSCL) was established in the year 1971 as a wholly owned undertaking of Government of Uttar Pradesh (GoUP) under the Companies Act, 1956 to run private sugar mills acquired by the State Government under the Uttar Pradesh Sugar Undertakings (Acquisition) Act, 1971.

- During the year 1971 to 1989, 28 mills¹ were acquired and one mill (Pipraich) was purchased (1974) in open auction.
- Six mills² were established during 1974 to 1988
- Of these 35 mills, five mills were placed under the management of four subsidiaries of UPSSCL viz. Kichha Sugar Company Limited (formed in 1974), Nandganj-Sihori Sugar Company Limited (two mills) and Chhata Sugar Company Limited (both formed in 1975) and Ghatampur

¹ 1971(12 mills): Amroha, Barabanki, Bhatni, Bijnore, Bhurwal, Jarwal Road, Khadda, Laxmiganj, Mohiduinpur, Ramkola, Rampur and Sakoti Tanda; 1984 (12 mills) Bareilly, Bulandsahar, Chhitauni, Doiwala, Ghughli, Hardoi, Maholi, Meerut, Munderwa, Rohankalan, Saharnpur and Siswa Bazar; 1989 (four mills) Baitalpur, Deoria, Nawabganj and Shahganj.

² 1974 (one mill): Kichha; 1978 (two mills): Chandpur and Chhata; 1978 and 1979 (two mills): Raibareilly and Nandganj; 1988 (one mill) Ghatampur.

Sugar Company Limited (formed in 1986). Remaining 30 mills were under the direct management of UPSSCL (up to 2002).

The acquired sugar mills had capacity of 711 tonne crushing per day (TCD) to 2200 TCD. Capacity of nine operating mills (except Rohankalan) were increased up to 1600 TCD to 3000 TCD in upgradation work undertaken by UPSSCL during 1986-87 to 1997-98 with a resultant improved performance.

1.2.1 The GoUP formulated a policy of Privatisation/ Disinvestment of PSUs in June 1994 which provided for review for privatisation of enterprises whose annual loss was more than ₹ 10.00 crore and eroded net worth by 50 per cent or more.

The net worth of UPSSCL eroded due to continued losses and in May 1995,

In July 2001, BIFR sanctioned a rehabilitation scheme for UPSSCL which resulted in placement of the 35 mills as below:

- UPSSCL retaining 11 potentially healthy (operating) mills;
- Ten³ already closed mills and eight⁴ unviable mills were transferred to a newly formed subsidiary (May 2002) Uttar Pradesh Rajya Chini Evam Ganna Vikas Nigam Limited (UPRCGVNL);
- Doiwala and Kichha sugar mills of UPSSCL were transferred to Government of Uttarakhand in the year 2002.
- Four mills⁵ remained with the other three subsidiaries of UPSSCL.

UPSSCL was referred to Board for Industrial and Financial Reconstruction (BIFR) under the provision of Sick Industrial Companies (Special Provisions) Act, 1985 (SICA). In August 1995 BIFR

declared UPSSCL a sick company and directed the operating agency (IFCI) to finalise a suitable rehabilitation package.

1.2.2 The Department of Infrastructure Development (DID), GoUP issued (June 2007) Guidelines for selection of Consultants/Advisors, Developers for Public Private Partnership (PPP) Projects and Private Partners for Disinvestment in Uttar Pradesh. The Guidelines provide for formation of various Committees, process to be followed for disinvestment, appointment and functions of Lead Advisor, Legal Advisor, Accounting Advisors, Asset Valuers and also the procedure to be followed for bidding and methodologies of valuation of enterprise.

In June 2007, the Government decided to privatise/ sell the sugar mills of UPSSCL including all the sugar mill of its subsidiaries and directed UPSSCL to submit a proposal for privatization /sale of sugar mills. The 'in-principle' consent of the Board of Directors for the privatization/ sale of its 33 sugar mills was conveyed by UPSSCL to the Government in June 2007.

As provided in the Guidelines, the GoUP specified (June 2007) the Pradeshiya Industrial Investment Corporation of Uttar Pradesh (PICUP) as Government Nodal Agency. The GoUP appointed (June 2007 to January 2008) Lead Advisor and constituted Core Group of Secretaries on Disinvestment (CGD)⁶, Consultative Evaluation Committee (CEC) and Consultative Monitoring

³ Barabanki, Bareilly, Chhituni, Ghugli, Hardoi, Maholi, Meerut, Munderwa, Nawabganj and Rampur (all closed during 1998-2000).

⁴ Bhatni, Bhurwal, Deoria, Ramkola and Shahganj (all closed during 2007-08) Baitalpur, Laxmiganj and Piparaich (all closed during 2008-09).

⁵ Nandganj (closed in 1998-99), Chhata, Ghatampur and Raibareilly mills (all closed during 2009-10).

⁶ The Management stated (November 2011) that Cabinet Committee on Disinvestment (CCD) was not constituted and CGD directly recommended to the State Cabinet for approval as prescribed in Chapter-1 of Guidelines.

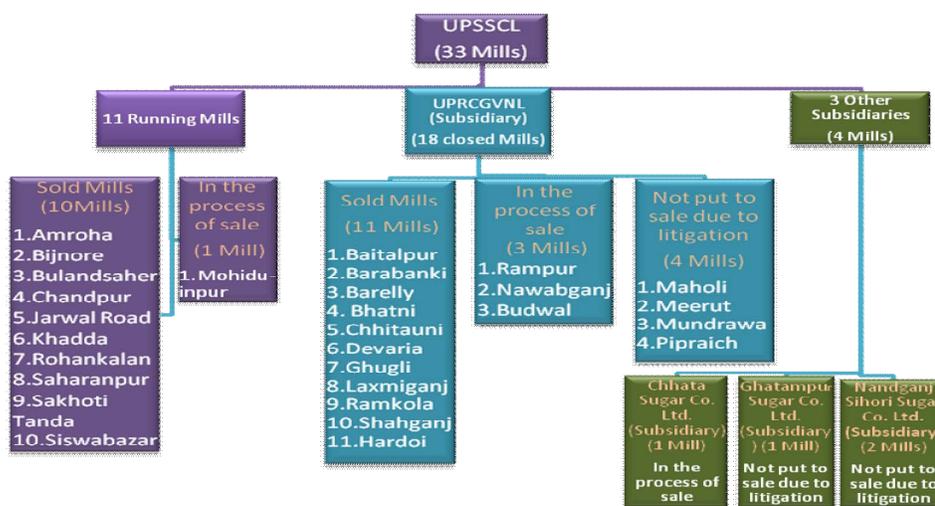
Committee (CMC) to carry out the process of disinvestment of sugar mills. In May 2008, the GoUP nominated the UPSSCL as Nodal Agency for Disinvestment process on sale of sugar mills.

Scope of audit

1.3 As per direction from CGD, the management of UPSSCL, UPRCGVNL and Chhata Sugar Company Limited advertised (June 2009 and June 2010) for sale of 11 mills, 14 mills and one mill (Chhata) respectively. Of these, sale of ten mills of UPSSCL and 11 mills of UPRCGVNL were finalized in July 2010-October 2010 and January 2011-March 2011 respectively. Sale process of one mill (Mohiuddinpur) of UPSSCL, three mills of UPRCGVNL and the mill of Chhata Sugar Company Limited had not been finalized so far (November 2011) as the process of sale/ disinvestment was annulled on 30 June 2011, i.e. before the last date of submission of Expression of Interest cum Request For Qualification and Request For Proposal (22 July 2011). Sale process in respect of remaining seven mills had not been initiated (November 2011) by the management because of litigation in the Courts and proceedings in BIFR.

The following chart depicts position of mills with UPSSCL and its subsidiaries at the start of sale process in June 2007.

Position of mills of UPSSCL



The profile of ten operating sugar mills of UPSSCL and 11 closed sugar mills of UPRCGVNL is given in *Annexure 1 and 2*.

1.3.1 Our examination conducted during March 2011 to April 2011 and July 2011 to August 2011 was confined to ten operating mills of UPSSCL and 11 closed mills of UPRCGVNL sold between July-October 2010 and January-March 2011.

Before actual commencement of the Audit of the Sale of sugar mills, we held (10 March 2010) an Entry Conference with Senior Management of UPSSCL to discuss the Audit Objectives, Audit Criteria and Audit Methodology to be adopted for the Audit and to elicit the cooperation and assistance required for conduct of audit. Our Audit involved scrutiny of records and documents made available to us by the Management of UPSSCL relating to Disinvestment Process. The Audit Inspection Report on sale of operating sugar mills of UPSSCL was issued to the Management on 18 July 2011. The Management of

UPSSCL submitted (23 August 2011) the reply. The reply has been suitably incorporated in our Report and discussed in the relevant paragraphs.

1.3.2 As the sale of 11 closed sugar mills of Uttar Pradesh Rajya Chini Evam Ganna Vikas Nigam Limited (UPRCGVNL) also took place in January 2011-March 2011, we continued the audit subsequently and the combined final Report (UPSSCL and UPRCGVNL) was sent to the Company (UPSSCL) and the Government on 17 October 2011.

The Management, while replying to audit observation in the Report *inter-alia* stated (17 November 2011) that issues related to the policy of the Government and hence it would be appropriate for the State Government to respond to those matters.

Response of the Government of Uttar Pradesh

1.3.3 The State Government in reply to Draft Audit Report, stated (16 November 2011) as follows:

“While reserving the right to give complete reply, your attention is invited on following points:

1. Section 16,17,18,19 and 19(A) of Comptroller and Auditor General (Duties, Powers and Conditions of Service) Act-1971 provide for the audit of Government companies.
2. Section 619 of Companies Act, 1956 provides the audit of Government Companies etc.
3. Under the Article 164(2) of the Constitution of India following is the provision in respect of Hon’ble Council of Ministers:

The Council of Ministers shall be collectively responsible to the Legislative Assembly of the State.

In this regard it is stated that the approval of Hon’ble Council of Ministers has been obtained on all points in respect of disinvestment process of Sugar Corporation. Following are the points in respect of which approval of the Hon’ble Council of Ministers has been obtained:

1. Decision of sale/privatization of all the 33 units of the Nigam, vide Government Order dated 04.06.2007, after getting approval of the Hon’ble Council of Ministers.
2. Approval on the appointment of Disinvestment Consultant and Legal Consultant on 26.06.2009.
3. Approval on the appointment of valuers on 26.08.2009.
4. Approval for sale of 11 Sugar Mills on the basis of slump Sale, Selection of Investors, EOI cum RFQ, RFP and slump Sale Agreement on 26.08.2009.
5. Approval of short-listed bidders on the basis of RFQ on 26.08.2009.
6. Approval of finalization of principles of valuation and finalization of expected price of 11 operating sugar mills and its information to be made available to tenderers and of final RFP and slump sale agreement on 26.08.2009.
7. Approval for re-fixation of expected price and final RFP and slump sale agreement in respect of 11 operating sugar mills on 13.05.2010.
8. Approval for sale of 04 operating sugar mills to selected buyers on highest financial bids on 01.07.2010.

9. In respect of 06 operating sugar mills approval of selected buyers on the basis of maximum financial bid under SCM. Permission to selected buyers to make SPV and approval for payment of additional fees to disinvestment advisors on 17.09.2010.
10. The following approvals have been taken on 29.12.2010 in respect of 15 closed sugar mills:
 1. Sale of closed sugar mills on slump sale basis
 2. Approval of 4 EOI cum RFQs for selection of investors and on 4 RFP and slump sale agreements.
 3. Approval for formation of SPV by selected purchasers.
 4. Approval on the selection of valuers. Approval on the fixation of expected price with 10% discount after adjustment of amount of VRS , contingent liabilities, TDC and stamp duty, which the buyers would bear in order to obtain real market sale value of mill units. Approval on informing selected bidders of the expected price prior to issue of RFP, final RFP and slump sale agreement
 5. Approval of the short listed bidders on the basis of received RFQs
 6. Approval on forfeiture of security deposits of H-1 bidders who declined to purchase 07 sugar mills and approval for sale to highest bidders under SCM.
 7. Approval for sale of 03 sugar mills to highest bidder H-1.
 8. Approval for sale of one sugar mill to challenger-1 under SCM.

It is clear that every step of disinvestment process of sugar mills has been approved by the Hon'ble Council of Ministers. The decisions of the Hon'ble Council of Ministers are beyond the audit jurisdiction of the Accountant General".

The reply of the State Government is, however, not tenable in view of the fact that the Gazette Notification dated 25 April 2003 of the State Government states that the Comptroller and Auditor General of India is empowered to audit the entire Disinvestment Process. Further, we have not commented on the policy decision of the State Cabinet to sell the sugar mills. The Report highlights the deficiencies and irregularities in implementation of the said policy decision by the Core Group of Secretaries on Disinvestment/Consultative Evaluation Committee at various stages of the process including the valuation and bidding processes, finalization of the Request for Proposal, fixation and irregular disclosure of the Expected Price to Bidders before bidding, Selection of Bidders, transfer of possession of mills etc. These decisions of the Core Group of Secretaries on Disinvestment/Consultative Evaluation Committee have been subsequently approved by the Cabinet.

In view of the response of the Government, the Exit Conference, which was rescheduled twice on the request of the Management, was not held.

Audit objectives

- 1.4 The objectives of our Audit were to assess whether;
 - ❖ the procedure as laid down in the State Government Guidelines on disinvestment was adhered to,

- ❖ the valuation methodologies adopted for sale were consistent with the Guidelines and
- ❖ the Company ensured that the procedure of disinvestment had generated adequate competition so as to obtain the best value.

Audit criteria

1.5 The audit criteria adopted for assessing the achievement of the Audit Objectives were:

- Disinvestment policy of GoUP,
- Guidelines issued by the GoUP for selection of Consultants/ Advisors, Developers for Public Private Partnership (PPP) projects and Private Partners for Disinvestment in Uttar Pradesh.
- Public documents in respect of Companies, available on website of Ministry of Corporate Affairs ; and
- Information/ Documents in respect of Companies required to be filed with Registrar of Companies, Uttar Pradesh and Uttarakhand.

Audit methodology

1.6 The methodology adopted for attaining the audit objectives with reference to audit criteria consisted of explaining audit objectives to the Management of UPSSCL during an Entry Conference held on 10 March 2011, scrutiny of minutes of meetings of Core Group of Secretaries on Disinvestment (CGD), Consultative Evaluation Committee (CEC), Consultative Monitoring Committee (CMC), Board of Directors of the two Companies, Reports of Legal Advisor and Accounting Advisors and recommendations of Lead Advisor, Annual Accounts of the Companies, inter-action with personnel of the Companies and analysis of information.

A Glossary of the various terms and abbreviations used in this Report along with the brief definitions of the terms is placed at the end of this Report.

Acknowledgement

We place on record our sincere appreciation for the co-operation of Management of UPSSCL in facilitating our audit. We also place on record our sincere appreciation to Registrar of Companies, Kanpur for facilitating the collection of desired information.