Report of the
Comptroller and Auditor General of India

Union Government (Commercial)
No. 21 of 2015
(Compliance Audit Observations)

Volume I

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for the year ended March 2014

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PREFACE

1. The accounts of Government Companies set up under the provisions of the Companies Act (including Companies deemed to be Government Companies as per the provisions of the Companies Act) are audited by the Comptroller and Auditor General of India (CAG) under the provisions of Section 619 of the Companies Act, 1956. The accounts certified by the Statutory Auditors (Chartered Accountants) appointed by the CAG under the Companies Act are subject to the supplementary audit by CAG whose comments supplement the reports of the Statutory Auditors. In addition, these companies are also subject to test audit by CAG.

2. The statutes governing some Corporations and Authorities require their accounts to be audited by CAG. In respect of five such Corporations viz. Airport Authority of India, National Highways Authority of India, Inland Waterways Authority of India, Food Corporation of India and Damodar Valley Corporation, the relevant statutes designate CAG as their sole auditor. In respect of one Corporation viz. Central Warehousing Corporation, CAG has the right to conduct supplementary and test audit after audit has been conducted by the Chartered Accountants appointed under the statute governing the Corporation.

3. Reports in relation to the accounts of a Government Company or Corporation are submitted to the Government by CAG under the provisions of Section 19-A of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971, as amended in 1984.

4. The Audit Report for the year ended 31 March 2014 has been prepared in two volumes. This is Volume I of the Audit Report and contains 31 individual audit observations relating to 28 PSUs under the control of seven Ministries/Departments. Volume II contains 37 individual audit observations pertaining to 18 PSUs under the control of seven Ministries/Departments. Instances mentioned in this Report are among those which came to notice in the course of audit during 2013-14 as well as those which came to notice in earlier years. Results of audit of transactions subsequent to March 2014 in a few cases have also been mentioned.

5. All references to 'Companies/Corporations or PSUs' in this Report may be construed to refer to 'Central Government Companies/Corporations' unless the context suggests otherwise.

6. The audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.

EXECUTIVE SUMMARY

I Introduction

1. This Report includes important audit findings noticed as a result of test check of accounts of records of Central Government Companies and Corporations conducted by the officers of the Comptroller and Auditor General of India under Section 619(3) of the Companies Act, 1956 or the statutes governing the particular Corporations.

2. The Report contains 31 individual observations relating to 28 PSUs under 7 Ministries/Departments. The draft observations were forwarded to the Secretaries of the concerned Ministries/Departments under whose administrative control the PSUs are working to give them an opportunity to furnish their replies/comments in each case within a period of six weeks. Replies to 15 observations were not received even as this Report was being finalised. Earlier, the draft observations were sent to the Managements of the PSUs concerned, whose replies have been suitable incorporated in the report.

3. The paragraphs included in this Report relate to the PSUs under the administrative control of the following Ministries/Departments of the Government of India:

Ministry/Department (Number of PSUs involved	Number of paragraphs	Number of paragraphs in respect of which Ministry/Department's reply was awaited
1. Atomic Energy (BHAVINI, NPCIL and UCIL)	3	1
2. Civil Aviation (AAI, AICL, ACIL and AIL)	8	7
3. Coal (BCCL and SECL)	3	1
4. Commerce and Industry (NINL, MMTC, PEC, STC and STCL)	5	1
5. Consumer Affairs, Food and Public Distribution (CWC and FCI)	5	1
6. Development of North Eastern Region (NERAMAC)	1	0
7. Finance (IIFCL, MCX-SX, NIAC and SPMCIL)	4	2

8. Irregularities in payment of entitlements by CPSEs (CIL, MCL, ECL, NCL, WCL, CCL and CMPDIL)	2	2
Total	**31**	**15**

4. Total financial implication of audit observations is ₹ 6,179.35 crore.

5. Individual Audit observations in this Report are broadly of the following nature:

- ❖ Non-compliance with rules, directives, procedure, terms and conditions of the contract etc. involving ₹ 4,931.56 crore in 16 paras.
- ❖ Non safeguarding of financial interest of organisations involving ₹ 808.29 crore in nine paras.
- ❖ Defective/deficient planning involving ₹ 432.37 crore in three paras.
- ❖ Inadequate/deficient monitoring involving ₹ 1.41 lakh in one para.
- ❖ Non-realisation/partial realisation of objectives involving ₹ 7.13 crore in two paras.

6. The Report also contains a para relating to recoveries of ₹ 56.60 crore made by seven PSUs at the instance of Audit.

II Highlights of some significant paras included in the Report are given below:

Ministry of Civil Aviation (MoCA) and Airports Authority of India (AAI) failed to bring to the notice of Airports Economic Regulatory Authority (AERA) the provisions of Shareholders Agreement which mandated affirmative vote of AAI till AAI held 10 *per cent* equity shares in Delhi International Airport Limited (DIAL), in respect of special resolution under the Companies Act, 1956 and Reserved Board Matters. This led to levy of Development Fee by DIAL, resulting in additional burden on the travelling public of ₹ 3,415.35 crore out of which an amount of ₹ 2,841 crore has been collected upto March 2014 and the balance will be collected upto April 2016.

(Para 2.2)

Trade in agro commodities by the State Trading Corporation of India Limited (STC), PEC Limited and MMTC Limited highlighted mismanagement, possible fraud, negligence and absence of financial prudence. As the entire activity of identifying supplier, buyer, storage, arranging for shipment, etc. was performed by the associates which are private parties, it is a moot point whether these would qualify to be termed as 'trading activity'. In fact, the three CPSEs failed to assess credit worthiness of associates and have been involved in providing finance to risky ventures without adequate safeguards. Resultantly, they suffered losses because of inadequate security against the amount financed and they were also not able to secure the pledged stock safely. Inordinate delays in disposal of un-lifted material and in taking decision to invoke the 'risk sale' clause as also release of stock on the basis of PDCs indicated culpability on the part of the Management. Though each CPSE has Government nominees on the Board of Directors, nothing came to notice to show that they had effectively protected the interests of the Government by insisting on adequate safeguards.

(Para 4.1)

The MCX Stock Exchange Limited (the Company) was incorporated on 14 August, 2008. Multi Commodity Exchange of India Limited (MCX) and Financial Technologies (India) Limited (FTIL) were its promoters. The Company had entered into long term agreements with its related party FTIL that entailed various restrictive clauses as well as high costs. Further, the PSU Banks had 67 *per cent* shareholding as on 31 March 2010 and had their nominees on the Board of the Company during 30 April 2010 to 20 September 2012. These nominees of PSU banks on the Board of the Company did not review these unfavourable agreements and failed to protect the interests of the banks they represented. Despite present action by new management, by way of suspension of various agreements with FTIL, the liability due to restrictive clauses in these agreements would continue as only interim action to suspend only a few agreements has been taken (January 2015).

(Para 7.2)

India Infrastructure Finance Company Limited (Company) conducted its operations of borrowing funds and lending the same for various infrastructure projects under SIFTI.

Audit observed that funds borrowed by the Company were not based on detailed working of requirements and resulted in excess borrowings. Moreover, funds were borrowed at higher cost upto ₹ 37.56 crore by issuing bonds for 25 years' tenor[1] instead of 15 years' and 20 years' tenor. Besides, the borrowing from LIC was done at higher than prevailing market rates incurring extra cost of ₹ 21.57 crore.

Audit further observed that under lending operations the Company

- Compromised on compliance of guidelines regarding appraisal of the loan proposal by the lead bank, obtaining guarantee for recovery of loan from lead bank and failed to protect its financial interests.
- Was likely to suffer a loss of ₹ 8.11 crore due to absence of standard operating procedures to safeguard its interests against quitting of lead/other lenders of the consortium.
- Lost business opportunity to the extent of ₹ 1,064.94 crore in 13 loans by not agreeing to finance the cost overruns, though the loans were restructured by the Company after having ensured their financial viability.

Despite having been modified a number of times, both the Refinance scheme and the Takeout finance scheme remained unattractive.

(Para 7.1)

Air India Charters Limited (Company) renewed dry lease of four aircraft disregarding the rationale for acquisition of 18 new aircraft, shortage of crew and loss making routes which led to unfruitful expenditure of ₹ 405.83 crore between March 2011 and May 2014 towards lease related charges.

(Para 2.5)

Lapses in implementation of post shipment finance scheme by STC led to non-recovery of dues of ₹ 347.70 crore. Discounting of export documents of dubious legality conceded by EXIM Bank, were also noticed besides infructuous expenditure on insurance premium of ₹ 17.07 crore.

(Para 4.4)

AAI did not take action as per its credit policy and allowed M/s Kingfisher Airlines Limited to continue its operations on credit basis even after withdrawal of the credit facility. AAI also did not act timely on the advice of MoCA to take all legal means beside encashing bank guarantee of the airlines. This resulted in loss of revenue of ₹ 172.69 crore apart from loss of interest of ₹ 117.03 crore (up to February 2014).

(Para 2.3)

There was inordinate delay in formulation of a policy regarding levy of airport charges and allotment of land to flying clubs and the attempt of framing policy in 2007, did not bear any result even till August 2014. In the absence of timely action and mechanism to verify the eligibility under Category I or II flying clubs, which were involved in other commercial activities and also otherwise not entitled to avail the benefits of concessional rates, these continued to enjoy the same. Further, in the absence of any agreement with the parties, most of the flying clubs raised disputes regarding rates and did not clear their

[1] ***Implies tenure or period of loan or bond as used by the Company in its records.***

dues. Moreover, AAI suffered losses due to delay in identification of sites and issue of required clearances.

(Para 2.1)

Dankuni Coal Complex (DCC) was established at a cost of ₹ 147 crore in 1990 as a unit of Coal India Limited (CIL) based on the recommendations of the Fuel Policy Committee, 1974 of Government of India (GOI), and the Working Group Nos. 9 and 10 of the Planning Commission (1974). Later, CIL handed over DCC to South Eastern Coalfields Limited (SECL) for running the plant on operating lease basis in April 1995 and renewed the lease subsequently at an annual lease rent of ₹ 7.50 crore followed by further renewal of lease w.e.f. 1 April 2010 at ₹ 1 per annum.

Audit observed that DCC did not operate efficiently since inception so as to achieve financial viability. DCC did not take effective measures to control environmental pollution. The Unit has been sustaining substantial loss (₹ 650.97 crore as on 31 March 2014). Audit examination revealed:-

- Operation far below installed capacity as there was no capital infusion for revival/capital rehabilitation of the plant
- Outdated technology
- Poor offtake of gas by customer
- Non-remunerative price obtained from customer
- Poor sale of by-products
- Absence of marketing strategy.

Neither DCC, nor SECL or CIL took any coordinated and productive steps to address the core issues pointed out above which would have helped DCC to get its financial health restored.

(Para 3.3)

Audit reviewed activities and other matters relating to execution of purchase orders in Bharatiya Nabhikiya Vidyut Nigam Limited (BHAVINI). Audit examination revealed that:

- As BHAVINI had entrusted (December 2003) all the activities to CMM, NPCIL pertaining to its procurement contracts, it had paid ₹ 46.07 crore till March 2014, as service charges excluding taxes.
- BHAVINI had not formulated an independent procurement manual so far (November 2014) and procurement manual of NPCIL was being followed on the grounds that the same was found adequate and comprehensive.
- No timeline was prescribed for various stages of the procurement processes such as for placement of purchase orders after receipt of indents and for receipt of materials after placement of purchase orders. There was delay in the placement of 100 purchase orders (76 *per* cent) out of a sample of 131 Purchase orders selected for audit. The delay ranged from one day to 1092 days with a median delay of 158 days.
- Norms with regard to mode of tendering were not strictly followed. Out of 131 purchase orders, in 125 purchase orders the value exceeded ₹ 50 lakh each for

which only public tenders were to be called. However, public tenders were called only in 71 cases (57 *per cent*).

- Though BHAVINI had set up its own CMM division in May 2004, the same had not yet taken over the activities from NPCIL due to lack of in-house expertise in the matter.

(Para 1.1)

Audit reviewed the policy framework of Uranium Corporation of India Limited (UCIL) for managing different types of contracts, the tendering system and the post-contract management. Audit observed that:

- UCIL had no works contract manual for contract finalization, delegation of powers, post-contract management, etc.
- UCIL was required to commence e-procurement in respect of all procurements in excess of ₹ 10 lakh from the month of May 2013. The Company went about implementation of e-procurement in a haphazard manner with inadequate preparatory work and assigned (April 2014) the job to M/s ITI which was in progress (January 2015).
- There were delays at various stages of purchase order finalisation process as compared to the time limits prescribed in its purchase manual. Delay was noticed in 59 to 83 *per cent* cases selected for audit which was in the range of one to 768 days.
- Though UCIL had prescribed a norm of 180 days in its purchase manual for finalising public tender, it did not lay down any timeline for finalisation of works contracts. Audit observed that there were delays ranging from 12 to 541 days in finalisation of 16 out of 29 works contracts selected for Audit.
- UCIL evaluated performance of vendors and classified them as 'Excellent', 'Very Good' and 'Good'. However, there was no ‘Poor’ rating. Further, the entire exercise of vendor rating proved futile as these were not considered at the time of placement of purchase orders.

(Para 1.2)

A review of procurement contracts in Nuclear Power Corporation of India Limited (NPCIL) revealed that it did not:

- make proper assessment of the available material before floating tenders for manufacture of steam generators for Kakrapar Atomic Power Project - 3&4. As a result, material valuing ₹ 17.51 crore, which could be issued to the suppliers as free issue material (FIM), remained blocked in its inventory;
- ensure economy in the tendering process as it had incurred additional expenditure of ₹6.01 crore due to non-consideration of the impact of local taxes during evaluation of bids and non-placement of purchase order on a supplier within the validity period of his price bid and subsequent placement of order on a different supplier at a higher price; and
- prescribe any time frame for completion of tendering procedure after receipt of an indent due to which the completion dates stipulated in the contracts did not match with the desired dates of delivery given in the indents.

(Para 1.3)

There are co-insurance arrangements between the PSU insurance companies and the private insurance companies. Under co-insurance, one Company (known as the "lead insurer") underwrites the insurance business and shares a part of that business with other public/private insurance business.

Significant audit findings in the Co-insurance arrangements entered into by New India Assurance Company with the private insurance companies are as under:

- Company has no specific policy or guidelines for co-insurance business where role of the lead insurance Company and that of the client are significant in determining the terms and conditions of the insurance contract.
- The Company assumed risk without recording the most vital information like Incurred Claims Ratio and details of the risk such as location of the risk, total exposure, break up of Sum Insured etc.
- Risk inspection was not carried out by the Company nor was the Inspection report of the lead insurer obtained before acceptance of the risk. The Company paid an amount of ₹ 21.78 crore in settlement of 6 out of 25 such claims.
- Justification notes with the approval of the Competent Authority, for the acceptance of the risk, were not available in 38 cases reviewed by Audit and 12 out of them were having Sum Insured (SI) exceeding ₹ 500 crore.
- Co-insurance risk was accepted at a rate lower than that quoted by the Company at the time of participation in the tender for 100 *per cent* share in nine out of 38 cases. The difference in premium amounted to ₹ 2.02 crore and the Company settled 3 claims for ₹ 2.27 crore.

(Para 7.4)

Review of implementation of Passenger Reservation and inventory system in Air India Limited, Mumbai revealed the following:-

- Lack of (i) integrated single IT platform and (ii) required linking to Finance Module with manual interventions due to absence of automated interfaces resulting in the underlying risk to data integrity.
- Pricing, despite being the key element of Passenger Reservation System, was out of scope of the system. The risk of manual errors (either intentional or un-intentional) could not be ruled out.
- System design deficiencies and lacunae in customization resulted in un-reconciled revenue of ₹ 136.84 crore and long outstanding debts of ₹ 113.94 crore.
- Lack of in-built relational integrity between related data resulted in a situation whereby the system allowed purchases without proper user requests, purchase quantity exceeding the requirement and materials received before placing orders.
- Non mapping of business rules in the system resulted in accounting ₹ 5.35 crore as revenue contrary to its Accounting Policy and blocking of bookings under higher priced tickets in companion free scheme.

(Para 2.7)

10 CPSEs did not adhere to the DPE guidelines with respect to payment of allowances and perks to its employees by restricting the same within the maximum ceiling of 50 *per cent* and made irregular payment of ₹ 573.10 crore for the years 2007-08 to 2013-14.

(Para 8.1)

CHAPTER I: DEPARTMENT OF ATOMIC ENERGY

Bharatiya Nabhikiya Vidyut Nigam Limited

1.1 Procurement contracts

1.1.1 Introduction

The Government of India (GOI) approved (September 2003) setting up of a Prototype Fast Breeder Reactor (PFBR) at Kalpakkam, Tamil Nadu at an estimated cost of ₹ 3492 crore. The GOI also approved (September 2003) formation of a Special Purpose Vehicle (SPV) under the Companies Act, 1956 for implementation of the PFBR project. Accordingly, Bharatiya Nabhikiya Vidyut Nigam Limited (BHAVINI) was formed (October 2003) by the Department of Atomic Energy (DAE) as a public limited company for constructing the PFBR with a capacity of 500 megawatt electrical (MWe).

1.1.2 Procurement system in BHAVINI

All the activities pertaining to purchase contracts, namely, processing of indents, tendering, commercial evaluation of the bids, finalisation and placement of purchase orders and all other matters pertaining to execution of purchase contracts had been entrusted by BHAVINI to Contract and Material Management unit of Nuclear Power Corporation of India Limited (CMM, NPCIL). The services of CMM, NPCIL for processing of all large value purchase contracts for PFBR had been availed on service charges at the rate of 1.75 *per cent* up to a cumulative total purchase order value of not more than ₹ 1,000 crore and at one *per cent* of the value thereafter, *plus* service tax and other statutory levies as applicable. The terms of payment of the service charges stipulated payment of 50 *per cent* of services charges upon placement of purchase order and that of remaining 50 *per cent* upon receipt of items.

1.1.3 Audit scope, objectives and methodology

The procurement activities of BHAVINI were reviewed to assess whether:

- BHAVINI was able to develop necessary expertise to carry out procurement activities independently;
- the procurement system had laid down appropriate timelines for completing various stages of procurement in order to ensure timely placement of purchase orders and receipt of materials; and
- the prescribed guidelines for tendering and procurement were duly adhered to by BHAVINI.

Out of a total of 4,647 purchase orders placed by BHAVINI up to 31 March 2013, 131 purchase orders valuing ₹ 2,259.99 crore were selected for audit which represented 73 *per cent* of the total purchase orders value (₹ 3,110.59 crore) up to March 2014. The audit was conducted during July 2013 to September 2013 and covered the period up to 2012-13. Subsequently, audit observations were further updated during 2014.

1.1.4 Audit findings

The PFBR project was to be completed within seven years of sanction i.e., by September 2010 at an estimated cost of ₹ 3,492 crore. However, the project could not be completed on time and therefore, the GOI approved (April 2012) extension of completion schedule of the project by four years up to September 2014 with date of commencement of commercial operations as 31 March 2015. Besides, the GOI also approved (April 2012) proposal (May 2009) of BHAVINI for revision in cost of the project to ₹ 5,677 crore. The reasons for time and cost overruns in the project were attributed by the Management to factors such as delay in obtaining Government sanctions, damages due to tsunami, significant increases in prices of raw materials and labour rates, changes in designs and specifications, impact of taxes and duties, etc. Audit, however, observed that in addition to the aforesaid factors, inability of BHAVINI to develop in-house expertise for undertaking procurement activities independently and deficiencies in the existing procurement system and procedures of BHAVINI were also responsible for delay in completion of the project and cost overruns. These deficiencies are discussed in the succeeding paragraphs.

1.1.4.1 Over-dependence on NPCIL for procurement

(a) Outsourcing of procurement function to NPCIL

BHAVINI had entrusted (December 2003) all the activities pertaining to its procurement contracts to the Contracts and Material Management (CMM) division of NPCIL. Further, BHAVINI approved (July 2004 and August 2005) a proposal for payment of service charges to CMM, NPCIL for processing of various purchase contracts for PFBR components at 1.75 *per cent* of the purchase order value up to a cumulative total value of ₹ 1,000 crore and one *per cent* of the purchase order value thereafter, exclusive of service tax and statutory levies, as applicable. BHAVINI had paid ₹ 46.07 crore to CMM, NPCIL till March 2014, as service charges excluding taxes, on purchase orders valuing ₹ 2,759.16 crore. Audit observed that though BHAVINI had set up its own CMM division in May 2004, the same had not yet taken over the activities from NPCIL due to lack of in-house expertise in the matter.

The Management stated (October 2013) that service contract was placed with NPCIL to process high value contracts as NPCIL had an established set up in the nuclear sector. All decisions of procurement were taken by competent authorities in BHAVINI and CMM, NPCIL was working only as an executing agency.

The fact, however, remains that by entrusting NPCIL with the entire gamut of activities relating to procurement such as processing of indents, tendering, evaluation of bids, price negotiations, placement of orders, etc., BHAVINI virtually transferred full control to NPCIL and decision-making by BHAVINI in procurement related matters became a mere formality.

DAE stated (December 2013) that BHAVINI had created its own CMM wing and all purchase orders were being placed internally which was evident from the fact that out of 4647 orders up to 31.03.2013, 4528 orders were placed by BHAVINI internally without taking assistance of NPCIL. Only 119 orders were placed by NPCIL.

The reply is not acceptable as out of total 4647 purchase orders valuing ₹ 3,110.59 crore placed by BHAVINI up to March 2013, 4528 orders amounting to ₹ 526.81 crore (17 *per cent*) only were processed by BHAVINI itself. This indicates that BHAVINI processed only small value orders and was entirely dependent on NPCIL for high value procurement.

(b) Adoption of procurement manual of NPCIL

BHAVINI has not formulated an independent procurement manual so far (November 2014). Instead, the procurement manual of NPCIL was followed by BHAVINI on the grounds that the same was found adequate and comprehensive. Audit, however, observed that as BHAVINI was formed as a Special Purpose Vehicle for fast breeder reactor projects, it needed to develop its own procurement manual.

DAE stated (December 2013) that a committee had already been constituted (June 2013) to review the procurement manual and BHAVINI would soon have its own manual for procurement. However, the Management confirmed (December 2014) that the manual was still under finalisation.

1.1.4.2 Deficiencies in procurement system

(a) Absence of timeframe for different procurement stages

Audit observed that no timeline was prescribed for various stages of the procurement process such as for placement of purchase orders after receipt of indents and for receipt of materials after placement of purchase orders. As a result, there were undue delays in placement of orders and receipt of materials. In absence of any laid down timeline in NPCIL procurement manual for placement of orders, Audit made an assessment of delay in placement of purchase orders with reference to the time frame[♣] of 180 days, 90 days and 60 days in case of public, limited and single tenders respectively. The result of the audit assessment is summarised in the following table:

Table 1

Delay in placement of purchase orders

Mode of tender	Total cases selected for audit	Number of cases where delay in placement of POs was observed	Percentage of cases where delay in placement of POs was observed	Range of delay (days)	Median delay (days)
Public	75	60	80	3 to 1092	213
Limited	33	26	79	1 to 826	115
Single	23	14	61	4 to 350	130
Total	**131**	**100**	**76**	**1 to 1092**	**158**

[♣] ***The time limits of 180 days, 90 days and 60 days for placement of purchase orders in case of public tender, limited tender and single tender respectively as prescribed in the purchase manual of Uranium Corporation of India Limited, which is also in the administrative control of the DAE, were adopted.***

As may be seen from the above table, out of 131 purchase orders selected for audit, there was a delay in the placement of 100 purchase orders (76 *per* cent). The delay ranged from one day to 1092 days with a median delay of 158 days. The median delay in case of public, limited and single tenders worked out to 213 days, 115 days and 130 days respectively.

Audit observed that no uniform timeline had been prescribed for receipt of materials after placement of purchase orders. Instead, different delivery periods were fixed in different purchase orders. However, actual receipt of materials did not conform to the delivery period mentioned in the purchase orders. Test check of 25 purchase orders revealed that there was a delay ranging from 5 months to 55 months in receipt of ordered materials/components.

While accepting the audit observation, the Management stated (October 2013) that delays were taking place from tender to supply of material due to complexities involved in the first of its kind reactor, technical deliberations and price negotiations. DAE endorsed (December 2013) the reply of the Management.

(b) Non-adherence to prescribed mode of tendering

BHAVINI had outsourced (December 2003) its major procurement activities to NPCIL. Besides, BHAVINI had also developed its own CMM group and adopted procurement manual of NPCIL for undertaking procurement activities. Audit observed that norms laid down in the procurement manual of NPCIL with regard to mode of tendering were not strictly followed by BHAVINI. As per norms laid down in the procurement manual, in case of purchase order valuing more than ₹ 50 lakh, open/public tender was to be called. The mode could be changed with proper justification into limited tender with approval from competent authority. However, it was observed that even for high value purchases valuing more than ₹ 50 crore, public tenders were not called and instead limited tenders and even single tenders were invited. The mode of tendering adopted for procurement in the 131 cases selected for audit was as shown in table 2 below:

Table 2

Mode of tendering adopted by BHAVINI

(₹ in crore)

Value of purchase order	**Public tender**		**Limited tender**		**Single tender**		**Total**	
	No.	**Value**	**No.**	**Value**	**No.**	**Value**	**No.**	**Value**
Above ₹ 50 crore	6	882.55	2	162.26	3	411.31	11	1456.12
₹ 5 crore to ₹ 50 crore	22	339.96	13	237.70	7	90.65	42	668.31
₹1 crore to ₹5 crore	21	73.82	0	0	6	26.27	27	100.09
₹ 50 lakh to ₹ 1 crore	22	16.88	17	12.16	6	5.11	45	34.15
Sub-total (A)	**71**	**1313.21**	**32**	**412.12**	**22**	**533.34**	**125**	**2258.67**
Below ₹ 50 lakh (B)	4	0.78	1	0.11	1	0.43	6	1.32
Grand total (A+B)	**75**	**1313.99**	**33**	**412.23**	**23**	**533.77**	**131**	**2259.99**

As may be seen from the above table, out of 131 purchase orders, in 125 orders the value exceeded ₹ 50 lakh each for which only public tenders were to be called. However, public tenders were called only in 71 cases (57 *per cent*) and limited and single tenders were called in 54 cases (43 *per cent*). On the contrary, out of 6 purchase orders valuing less than ₹ 50 lakh, public tenders were called in 4 cases (67 *per cent*) and limited and single tenders were called in 2 cases (33 *per cent*). This indicates that the tendering was done in an arbitrary manner without giving consideration to the guidelines laid down in the procurement manual. Thus, the tendering system failed to ensure transparency and effective competition.

The Management stated (October 2013) that limited tender was primarily followed for complex components owing to limited skilled industry available in the country. It was felt scientifically prudent to go with the time-tested experienced players as most of the nuclear and reactor components were being done for the first time. Public tender had been adopted for all components in the conventional system. Single tender was resorted to for specific jobs which could not be made in a competitive bidding method and where there was only single source.

The reply is not acceptable as the guidelines given in the procurement manual had classified the mode of tendering on the basis of value of purchase order and not on the type of items to be purchased. BHAVINI needed to carry out extensive market research to locate new vendors and to bring in competition instead of awarding the contracts to known suppliers only.

While endorsing the reply of the Management, DAE stated (December 2013) that the decisions on mode of tender had been taken by the appropriate authority as defined in the manual. Public tender dispensation had been given in all the tenders wherever the estimated value of indent was more than ₹ 50 lakh, by the respective approving authority. Thereby, the guidelines of procurement manual were followed in all cases.

The reply is not acceptable as deviations from the prescribed mode of tender on the basis of approval by the competent authority needed to be an exception and not common occurrences. However, the reply of DAE and the above audit analysis indicate that the guidelines given in the procurement manual on the mode of tendering were frequently violated.

Conclusion

NPCIL was associated with the construction, commissioning and operation of Fast Breeder Reactor Project at Kalpakkam on the directive of the Government of India. However, BHAVINI had outsourced all the activities pertaining to the procurement contracts to NPCIL against payment of service charges. Though BHAVINI had set-up its own CMM division in May 2004, the same had not yet taken over the activities from NPCIL due to lack of in-house expertise in the matter. Besides, BHAVINI did not formulate its own procurement manual and followed the manual of NPCIL. No timelines were prescribed in the procurement manual for various stages in the procurement process due to which there were delays ranging up to 1092 days in the placement of purchase orders after receipt of indents. The guidelines prescribed in the procurement manual in respect of the mode of tendering were not strictly adhered to which prevented BHAVINI from ensuring transparency and competition in the tendering process.

Audit recommendations and responses of DAE

Recommendations of Audit	*Response of DAE*
In view of the aforesaid findings, it is recommended that BHAVINI may consider:	***The recommendations given by Audit are solicited.***
➢ ***developing in-house expertise for undertaking procurement activities independently in an efficient and cost-effective manner.***	➢ ***In-house expertise has been developed to take up the future projects.***
➢ ***formulating its own procurement manual and laying down norms for each stage of procurement.***	➢ ***Separate procurement manual will be made for BHAVINI. A committee has been constituted for this purpose in June 2013 and working on it actively.***
➢ ***adhering strictly to the guidelines framed in the procurement manual in order to minimise time and cost overruns.***	➢ ***BHAVINI will continue to make all out efforts to adhere to the guidelines in the procurement manual.***

DAE has accepted the second and third recommendation made by Audit. In respect of the first recommendation, the response of DAE is not acceptable in view of the fact that BHAVINI processed only small value orders and was entirely dependent on NPCIL for high value procurement (refer para 4.1.1), which indicates that development of in-house expertise to carry out procurement activities independently was yet to be achieved.

Uranium Corporation of India Limited

1.2 Contract Management

1.2.1 Introduction

Uranium Corporation of India Limited (UCIL/Company) was incorporated on 4 October 1967 as a public sector enterprise under the administrative control of the Department of Atomic Energy (DAE) with the objectives of mining ore and processing the same for production of Uranium concentrate. The entire production of Uranium concentrate by the Company is purchased by the DAE. The Company has its Corporate office at Jaduguda, District East Singbhum, Jharkhand. It has seven mines and two processing plants in Jharkhand State.

1.2.2 Scope of audit

Audit examined the procedures governing finalization of works/procurement contracts by the Company, tendering process, placement of purchase orders and execution of contracts. A period of four years from 2010-11 to 2013-14 was covered in audit.

1.2.3 Audit objectives

Audit was conducted to assess whether:

- the Company had a well-defined policy framework for managing different types of contracts and the same was duly adhered to;

- the tendering system was transparent and ensured efficiency, economy, effectiveness and fair competition; and
- the post-contract management was effective so as to ensure compliance to the agreed terms and conditions of the contracts.

1.2.4 Audit criteria

Audit criteria were derived from the following:

- Purchase manual of the Company;
- Terms and conditions of the contracts/ purchase orders; and
- Minutes of the meetings of Board of Directors and its sub-committees.

1.2.5 Audit methodology and sample size

Audit was conducted on the basis of examination of records relating to works/procurement contracts entered into by the Company, collection of information through questionnaires and audit requisitions, verification of replies of the Management to the preliminary audit enquiries and discussion with the Management. The purchase orders and works contracts finalised during 2010-11 to 2013-14 for the activities in Jharkhand State were selected for audit.

Out of the 18001 purchase orders (POs) and 1921 works contracts valuing ₹ 1308.63 crore finalized by the Company during the period 2010-11 to 2013-14, a sample of 160 POs/contracts (131 POs and 29 works contracts) with aggregate value of ₹ 494.81 crore was selected for audit. The sample was selected on the basis of stratified random sampling method and consisted of 18 contracts/POs valuing more than ₹ 5 crore, 46 contracts/POs from those valuing in the range of ₹1 crore to ₹ 5 crore and 96 contracts/POs from those valuing less than ₹ one crore. The selected sample thus represented 37.8 *per cent* of the total contract value.

1.2.6 Audit findings

1.2.6.1 Policy framework for Contract Management

(a) Absence of works contract manual

The activities of the Company have increased manifold since its incorporation in 1967, yet no 'Works Contract Manual' was prepared to lay down the guidelines for contract finalisation and execution, delegation of powers, post-contract management, etc. in order to ensure that the best practices, system and procedures were followed uniformly by all the units of the Company.

While accepting the audit observation, the Management stated (May 2014/January 2015) that the review of the manual was at final stage and it was likely to be placed in the Board of Directors' meeting to be held during fourth quarter of 2014-15.

(b) Delay in commencement of e-procurement

The Ministry of Finance instructed (March 2012) that all the Ministries/ Departments of the Central Government, their attached and subordinate offices may commence e-procurement in respect of all procurements with estimated value of ₹ 10 lakh or more in a phased manner. As per the time schedule prescribed by the Ministry of Finance, the Department of Atomic Energy (DAE) and its attached subordinate offices were required to commence e-procurement from the month of December 2012 and May 2013 respectively. The Board of Directors (BOD) of the Company decided (December 2012) to float public tender for awarding the contract for implementation of e-procurement. The purchase department of the Company, however, issued (January 2013) limited tender enquiry to three vendors without making any assessment of the scope and specifications of work. Due to incomplete details, response to the limited tender enquiry was received only from one vendor. The Company, therefore, decided (July 2013) to cancel the limited tender and float public tender containing full details in order to ensure better participation. While the procedural formalities for public tendering were in progress, the Company decided (November 2013) to explore the possibility of adopting e-tendering and e-procurement services offered by another agency, namely, M/s ITI which was already offering its services to DAE. Accordingly, the Company assigned (April 2014) the job of implementation of e-procurement which was in progress (January 2015).

Audit observed that non-assessment of the requirements and specifications of work and issue of limited tender enquiry delayed the commencement of implementation of e-procurement besides violating the decision of the BOD to float public tender in the beginning itself.

While accepting the audit observation, Management stated (January 2015) that many of the units/ departments under DAE had availed services of ITI in implementing e-procurement to maintain uniformity.

The fact, however, remains that the Company went about the implementation of e-procurement in a haphazard manner with inadequate preparatory work leading to inordinate delay as against the targeted time of implementation i.e. May 2013.

(c) Non-adherence to time schedule for finalising purchase orders

Audit observed delays at various stages of purchase order finalisation process as compared to the time limits prescribed in its purchase manual. The following table depicts the time taken by the Company in issuing purchase enquiries and placing purchase orders after receipt of purchase requisitions during the period 2010-11 to 2013-14:

Stage of procurement	Mode of tender	Time limit (days)	No. of cases examined	No. of delayed cases	Percentage of delayed cases	Delay range (days)	Median Delay (days)
Time taken for placement of purchase orders after receipt of	Public tender	180	47	39	83	1 to 768	121
	Limited Tender	90	67	57	85	8 to 522	73

purchase requisition	Single Tender	60	17	10	59	11 to 116	54
Time taken for the issue of purchase enquiries after receipt of purchase requisition	Public tender	30	47	30	64	4 to 757	60
	Limited Tender	15	67	52	78	1 to 280	55

As may be seen from the table, there was a median delay of 60 days and 55 days in issue of purchase enquiries for public tender and limited tender respectively. Further, the median delay in placement of purchase orders in case of public, limited and single tender was 121 days, 73 days and 54 days respectively.

Thus, out of the sample of 131 purchase orders selected for audit, there was delay in placement of 106 purchase orders with a median delay of 80 days. Audit observed that the delays in consolidation of purchase requisition, deciding the mode of tender, opening of bids and negotiations with the suppliers contributed to the overall delay in the placement of purchase orders by the Company.

Management stated (May 2014/January 2015) that efforts were being made to achieve placement of purchase orders as per the time schedule prescribed in the purchase manual.

(d) Absence of norms for finalization of works contracts

In order to avoid time and cost overrun, it is necessary that the contracts are finalized within reasonable time. To this end, a definite time schedule needs to be followed for completion of different stages in the finalisation of contracts. Audit observed that though the Company had prescribed a norm of 180 days in its purchase manual for finalising public tender, it did not lay down any timelines for finalisation of works contracts. Considering the norm of 180 days prescribed for finalising public tender, Audit observed that there was a delay ranging from 12 days to 541 days in finalisation of 16 out of 29 work contracts selected for Audit. The major reasons for the delay were revisions in cost estimates and scope of work, delayed provision of budget for works, refloating of tenders due to poor response, repeated changes in notice inviting tenders (NIT) before issue, etc.

Management stated (July 2013/May 2014 and January 2015) that the timelines for finalisation of the tender would be covered in the Works Contract Manual which was under draft stage and likely to be adopted soon.

(e) Non-realisation of EPF dues from contractors

As per Section 30(2) and (3) of the Employees Provident Fund Scheme, 1952, the contractors are required to pay to the principal employer (viz. Company) Employees Provident Fund (EPF) dues recovered from the employees engaged by him together with an equal amount of his contribution and administrative charges. Upon receipt of the EPF contributions from the contractors, the principal employer has to remit the same to the Regional Provident Fund Commissioner. Further, as per section 36-B of the Scheme, every contractor shall, within seven days of the close of every month, submit to the principal employer a statement showing the recoveries of contributions in respect of employees employed by or through him. For ensuring necessary compliance in this regard, the work orders issued by the Company to the contractors also contained a clause to this effect.

A test check of the running account bills in case of 8 work orders revealed that the contractors did not remit the EPF dues amounting to ₹1.34 crore to the Company. However, the Company neither deducted the EPF dues from the contractors' bills nor obtained from them any proof of payment of EPF dues to the Regional Provident Fund Commissioner.

Management stated (May 2014) that instructions had been issued (May 2014) to the concerned officers for ensuring compliance to the statutory regulations. The Management further stated that in larger contracts, the Company was ensuring deposit of EPF with the statutory agency and was collecting the necessary documents.

The fact, however, remains that in case of the 8 works orders commented upon by Audit, the Company did not ensure deposit of EPF dues. Besides, compliance to statutory provisions was required in all cases of contracts irrespective of their value.

(f) Redundant exercise of vendor rating

The Company evaluated the performance of vendors on the basis of three parameters viz. right quality, right quantity and right delivery and accordingly assigned a numerical rating to the vendors. Based on the numerical ratings, the vendors were classified as Excellent, Very good and Good. Audit, however, observed that there was no 'Poor' rating for unsatisfactory performance and the vendors with zero numerical rating were also classified as 'Good'. Besides, the vendor ratings were done separately by each unit of the Company due to which vendors for the same item were evaluated differently by different units. Further, the entire exercise of vendor rating was futile as the ratings were not considered at the time of placement of purchase orders. Audit also observed that different vendors existed for the same items at different units due to absence of common codification in the vendor database of the Company.

Management stated (July 2013) that the vendor evaluation system developed by Tata Consultancy Services was adopted (April 2012) on trial and the system would be updated/corrected in due course of time based on the experience of this trial. Management further stated (January 2015) that the efforts to develop common codification of material were underway which would also effect vendor codification thereby improving the vendor rating system.

1.2.6.2 Tendering system

(a) Non-monitoring of credentials of the bidders

The Company issued (October 2010) a public tender for purchase of High carbon steel grinding rod. Only two bidders viz. M/s Chandi Steel Industries Limited and M/s Balaji Ispat Udyog submitted their offers. Audit observed that these two parties were associates of each other and were having their registered offices at the same place. As the two bidders were inter-related parties, this was practically a single bidder submitting two bids and therefore the tender should have been cancelled and re-floated. However, the Company evaluated the bids separately which indicates that there was lack of monitoring in respect of the credentials of the bidders by the Company.

Management stated (May 2014/January 2015) that the procurement had been done from the lowest bidder through public tendering and as per the records available with the Company, the bidders were two different companies having separate registration and licences.

The reply is not acceptable as the financial statements of the bidders clearly indicated that the two bidders were inter-related. The Company, therefore, needed to exercise due diligence before awarding the contract.

(b) Excess expenditure on advertisement at higher than prescribed rates

As per clause 3 of the New Advertisement Policy (effective from 2 October 2007) of the Directorate of Advertising and Visual Publicity (DAVP), all Central Government Ministries/ Departments/attached and subordinate offices/field offices shall route their advertisements through DAVP. PSUs, Autonomous bodies and Societies of Government of India may issue all advertisements directly at DAVP rates to empanelled newspapers.

Audit, however, observed that the Company did not ask the newspaper publishers to accept DAVP rates for printing its advertisements/NITs. Instead, the Company violated the above directions and got its advertisements published through M/s Ridge Advertising and Marketing Consultants, Ranchi at commercial rates which were much higher than the DAVP rates. This resulted in extra expenditure of ₹ 6.22 crore on publishing of advertisements during the period February 2012 to October 2013.

Management stated (May 2014/January 2015) that clause 3 of the new Advertisement Policy of DAVP did not make it mandatory for the PSUs to rely solely on DAVP. Further, DAVP rates for advertisements were not made available to the PSUs by the Media House owners as the Indian Newspaper Society (INS) had issued (August 2005 and July 2006) circulars communicating that the advertisements from PSUs would be accepted only on commercial rates and not on DAVP rates.

The reply is not acceptable since it was mandatory, as per the new Advertisement Policy, for all PSUs to issue advertisements to the empanelled newspapers at DAVP rates. As the Advertisement Policy of DAVP did not mention about any exemption to the PSUs in this regard, the contention of Management is not tenable. Further, the New Advertisement Policy was effective from October 2007 i.e. after the issue of the above stated circulars by INS and therefore the policy had an overriding effect on these circulars. Moreover, the sixth Rate Structure Committee, taking cognizance of the non-compliance of new Advertisement Policy by many PSUs, recommended that the Government may issue a communication to all Ministries to advise PSUs, Autonomous Bodies and Societies under their administrative control to release their advertisements at the rate which is not higher than the DAVP rates.

1.2.6.3 Post-contract management

(a) Non-invoking of risk purchase clause

As per clause 11.3 of the purchase manual of the Company, any delay in effecting supplies by the supplier would call for invoking the penalty clause, procurement of those materials at the cost of the defaulting party and cancellation of the order ultimately with the approval of the competent authority. Audit, however, observed that in case of following two purchase orders where the supplier had defaulted in supplies of common salt at Jaduguda and Turamdih units of the Company, the aforesaid provisions were not adhered to by the Company:

Sl. No.	PO Number	PO Date	Name of the supplier	Quantity ordered (MT)	Quantity supplied (MT)
1.	2084	07.02.2012	M/s Mangalam Enterprises	2500	288.83
2.	9701	07.02.2012	M/s Mangalam Enterprises	2500	Nil

Audit further observed that the defaulted quantity of 4711.17 MT was procured from three other suppliers at an extra cost of ₹ 28.44 lakh. However, the cost was not recovered from the defaulting supplier in terms of the above clause of the purchase manual.

While accepting the audit observation, the Management stated (July 2013) that a proposal had been initiated for forfeiture of security deposit against order of Jaduguda which was likely to be finalized soon. As the party had neither deposited security deposit nor made any supply against order for Turamdih, the Company did not have any recovery measure against the default made by the supplier. An effective system to monitor purchase orders and implementation of post contract penalties would be kept in the revised version of purchase manual.

Though the Company forfeited (October 2013) security deposit of ₹ 3.41 lakh, however, no action was taken by the Management as per the risk purchase clause to recover balance amount of ₹ 25.03 lakh.

Conclusion

The Company had not prepared a works contract manual even after 47 years of its formation to lay down the guidelines for contract finalisation and execution. There were delays with a median delay of 80 days in placement of purchase orders after receipt of purchase requisitions. The Company, though, had a system for assessing performance of vendors and rating them accordingly but this was not being done in a centralised manner leading to different ratings for the same item. Besides, vendor ratings were not considered at the time of placement of purchase orders. The clause in the purchase manual with regard to risk purchase was also not strictly followed by the Company.

The implementation of the audit observations which have been accepted by the Management will be followed up in subsequent audit.

Recommendations of audit and response of the Management

In view of the aforesaid findings, it is recommended that the Company may consider:

Recommendations of Audit	*Reply of the Management (January 2015)*
➢ ***Formulating a comprehensive works contract manual laying down guidelines and time schedule for various activities in contract finalisation and execution.***	➢ ***The works contract manual has been formulated by the Company and is under finalisation for putting up before the Board of Directors.***
➢ ***Developing a centralised vendor rating system for assessment of performance of vendors and utilizing such information for deciding on the award of future contracts.***	➢ ***The vendor rating system is under trial stage and once the rationalization of uniform material coding is introduced, the assessment of performance of vendor will be done uniformly.***
➢ ***Adhering strictly to the timelines prescribed for placement of purchase orders and other provisions of the purchase manual.***	➢ ***Efforts are being made to adhere to the timeline prescribed in the purchase manual for placement of purchase order in most practicable manner.***

The matter was reported to the Department of Atomic Energy in December 2014; their reply was awaited (March 2015).

Nuclear Power Corporation of India Limited

1.3 Procurement Contracts

1.3.1 Introduction

Nuclear Power Corporation of India Limited (Company) is a wholly owned Central Government Company incorporated on 17 September 1987 under the administrative control of Department of Atomic Energy (DAE) with the objective of operating atomic power stations and implementing the atomic power projects for generation of electricity in pursuance of the schemes and programmes of the Government of India under the Atomic Energy Act, 1962. The Company is responsible for design, construction, commissioning and operation of nuclear power reactors. The mission of the Company is to develop nuclear power technology and to produce nuclear power as a safe, environmentally benign and economically viable source of electrical energy to meet the increasing electricity needs of the country. The Company is presently operating 20 nuclear power plants under seven atomic power stations with a total installed capacity of 5680 mega-watt electrical (MWe).

1.3.2 Organisational set-up for procurement activities

NPCIL has a separate unit under the control of Executive Director, Contract and Materials Management (C&MM) which is responsible for catering to the needs of operating stations and also of ongoing projects in terms of procurement of machinery, materials and equipments based on requirements by sites/stations and Procurement Directorate. High value contracts (₹ 5 crore and above) for procurement including those for major power projects are entered into by C&MM, Mumbai unit. The C&MM units located at seven♦ sites also enter into contracts as per financial powers delegated to them under NPCIL Headquarters instructions (July 2011). The Company does not have a manual on Contract Management. However, the codified instructions on procedures to be followed for entering into procurement contracts have been prescribed by NPCIL Headquarters through delegation of financial powers issued from time to time.

1.3.3 Audit Objectives

The audit was conducted during July 2013 to September 2013 to assess whether:

- the requirements were properly assessed before floating the tenders;
- tendering process ensured transparency, economy and competitiveness; and
- contractual terms and conditions were duly complied with and the contracts were executed within the schedule time.

1.3.4 Audit criteria

Audit criteria were derived from the following:

- Circulars/ instructions of NPCIL Headquarters on procurement of materials;
- Terms and conditions of tender documents and purchase orders/contracts;
- Delegation of financial powers;
- Milestones projected in the detailed project reports for major projects; and
- Policy/directions of Government of India on mega power projects.

1.3.5 Scope of Audit and sample size

Audit assessed the adequacy of the procurement systems and procedures in ensuring economy, transparency and competitiveness in procurement of materials. Audit also examined the extent of compliance to the instructions/guidelines laid down by the Company for procurement activities and fulfillment of contractual obligations by the Company. The records maintained by the CMM unit at Mumbai were examined in audit. Out of a total of 177 contracts entered into by the Company upto the year 2012-13, a sample of 33 contracts was selected on the basis of stratified random sampling method as detailed below:

Particulars	Range of value of contracts	Number of contracts		Money value of contracts (₹ in crore)		Percentage of Selection of contracts in terms of	
		Total	Selected	Total	Selected	Number	Value
Ongoing contracts including	Less than ₹ 30 crore	78	8	1173.79	181.46	10	15
	₹ 30 crore to	24	2	937.79	88.96	8	9

♦ ***Tarapur (Maharashtra), Rawatbhata (Rajasthan), Kalpakkam (Tamil Nadu), Narora (Uttar Pradesh), Kakrapar (Gujarat), Kaiga (Karnataka) and Kudankulam (Tamil Nadu)***

contracts entered into prior to 2010-11	₹ 50 crore						
	More than ₹ 50 crore	56	17	14969.70	6829.28	30	46
Contracts completed during 2010-11 to 2012-13	Less than ₹ 30 crore	14	1	221.56	12.47	7	6
	₹ 30 crore to ₹ 50 crore	1	1	30.00	30.00	100	100
	More than ₹ 50 crore	4	4	360.07	360.07	100	100
Total		**177**	**33**	**17692.91**	**7502.24**	**19**	**42**

The selection of contracts for audit was done with a view to ensure greater coverage of contracts having relatively high value and of those which were completed during the three years ended on 31 March 2013. The selected contracts were entered in respect of four ongoing projects viz. Kakrapar Atomic Power Project- units 3 and 4, Gujarat (KAPP 3 & 4) and Rajasthan Atomic Power Project-units 7 and 8, Rajasthan (RAPP 7 & 8); and four completed projects viz. Rajasthan Atomic Power Project- units 5 and 6, Rajasthan (RAPP 5 & 6) and Kaiga Atomic Power Project-units 3 and 4, Karnataka (Kaiga 3 & 4).

1.3.6 Audit findings

The audit findings have been classified under three major heads viz. Pre-tendering requirements, tendering and award of contracts, and execution of contracts, as discussed in succeeding paragraphs.

1.3.6.1 Pre-tendering requirements

(a) Improper estimation of requirement of materials

The Company placed (March 2009) purchase orders on M/s Larsen & Toubro Limited (L&T) and Bharat Heavy Electricals Limited (BHEL) for manufacture and supply of four steam generators each for KAPP 3 and KAPP 4 respectively. The value of purchase orders for each of the two manufacturers was ₹ 345 crore. Besides, the Company also supplied free issue material (FIM♥) valuing ₹ 16.65 crore to each of them.

Both the manufacturers expressed (March 2010) difficulties in procuring certain materials and welding consumables required for fabrication of the steam generators and they had requested the Company to issue those items so that the work could be expedited. Accordingly, the CMM wing forwarded (March 2010) the list of 75 items that could be issued as additional FIM from its stores to the manufacturers and requested them to intimate their requirements. The Contractors, M/s L&T and M/s BHEL intimated (March/April 2010) the requirement of 40 items and 26 items respectively to the Company and requested for issue of these items as additional FIM. However, the wing eventually decided (July 2010) to issue only three items to each of them and the remaining material valuing ₹ 17.51 crore was retained by the Company in its stores. The

♥ ***Free issue material (FIM) is the surplus material remaining in the inventory of NPCIL from the previous procurements and is issued to the contractors in the subsequent purchase orders by adjusting their cost in the value of purchase orders.***

reasons for issue of only three items each to the two manufacturers against their requirements of 40 and 26 items were not found on record.

Audit observed that as per the Company's instructions (July 2004) the indenting officer should refer to the list of usable surplus stock items for their possible use before raising an indent. Though the Company had issued certain items as FIM while placing the purchase orders on the parties, the aforesaid instructions were not followed scrupulously as significant quantity of certain other items were also available with the Company which were neither included in the list of original FIM nor were given as additional FIM even after being demanded by the manufacturers. This resulted in unwarranted blocking of material worth ₹17.51 crore in the inventory which also entailed increased carrying cost.

The Management stated (October 2013) that as the tender was divided between BHEL and L&T, it was a considered decision that the items/materials that could be issued equally to both the manufacturers were included in the list of FIM while preparing the estimates for the tender. As majority of the items pointed out by Audit were not sufficient to be divided equally between the two manufacturers, the same were not included in the list of FIM.

The reply of the Management is not acceptable as it was evident from the list of surplus items not included in the tender, that these were available in sufficient numbers and could have been divided between the two bidders. Moreover, the instructions of the Company's Headquarters (about referring to the list of surplus items before raising indent) did not put any restrictions in case of division of order. Thus, it was not binding on the Company to divide the surplus items equally between the two manufacturers.

The Management further stated (January 2015) that though the Company's instructions did not put any restrictions in case of division of order, the indenting officer while deciding the items to be issued as FIM at tender stage considered equal availability of items for Steam Generator before giving it to the manufacturers. Further, additional FIM demanded by the manufacturers could not be issued as it was not feasible to ascertain the market prices of these materials. These materials would be considered for issue as FIM in future projects with due consideration to economy.

The reply confirms the audit observation that whole of the surplus material was not considered for FIM at the tender stage in contravention to the Company's instructions (July 2004). Further, the contention of the Management that additional FIM could not be issued due to non-feasibility of ascertaining their market price is not acceptable since cost of additional FIM was fixed by the Company after considering the market price and the same was duly intimated to the parties at the time of offering (March 2010) the list of additional FIM.

1.3.6.2 Tendering and award of contracts

(a) Non-consideration of tax element during evaluation of bids

The Company floated (July 2009) a two-part public tender for manufacture and supply of End shield assemblies and components for KAPP 3 & 4 and RAPP 7. In respect of KAPP-4, two bidders, viz. M/s Larsen & Toubro Limited (L&T) and M/s Walchandnagar Industries Limited (WIL) were found (December 2009) to be qualified after technocommercial evaluation. After evaluation of price bids, the Company placed (March 2010) the purchase order on L&T who had been found to be the L1 bidder.

Audit observed that of the two technically qualified bidders, L&T was subject to higher Value Added Tax rate of 12.5 *per cent* as both the KAPP site as well as L&T's unit at Hazira were situated in Gujarat, whereas WIL was subject to a lower rate of 2 *per cent* on account of Central Sales Tax. Audit further observed that though the basic price inclusive of transportation (₹ 60.25 crore) quoted by L&T was lesser than that quoted by WIL (₹ 62.50 crore), the price inclusive of taxes quoted by L&T (₹ 68.36 crore) was higher than that quoted by WIL (₹ 63.84 crore). However, while evaluating the price bids of the two bidders, the Company did not consider tax element for comparison of prices. The non-inclusion of tax element in price bid evaluation resulted in selection of L&T as L1 bidder and consequent placement of purchase order with additional commitment of ₹ 4.52 crore (₹ 68.36 crore minus ₹ 63.84 crore).

The Management stated (February 2012) that in case of project procurement, where fiscal concessions are applicable, bid evaluation criteria were indicated in tender documents which provided that the price bid evaluation would be done on the total of summary prices (i.e., ex-works price, transportation and transit insurance). The Management also added (May 2012) that as per instructions (May 1999) of the Ministry of Power, sales tax, local levies and octroi shall not be considered for the purpose of evaluation of bids for capital goods supplied to Mega Power Projects under deemed export status.

The Management further stated (January 2015) that in case of nuclear power projects, the deemed export benefits are available in case of competitive bidding as opposed to International competitive bidding (ICB) vide paras 8.2(j) and 8.4.7 of Foreign Trade Policy 2009-14.

The reply of the management is not acceptable as the Foreign Trade Policy 2009-14 extended the status of Deemed Exports to the supply of goods to nuclear power projects through competitive bidding also as opposed to ICB provided the goods were manufactured in India. Benefits listed under the Foreign Trade Policy 2009-14 to be extended under the deemed exports were (a) Advance Authorization, (b) Deemed Export Drawback, and (c) Exemption from terminal excise duty. Further, as per the Ministry of Power's instructions (May 1999) read with DPE guidelines (August 1997), sales tax, local levies and octroi shall not be considered for the purpose of evaluation of bids only in respect of international competitive bidding. Since the tender was floated for manufacture and supply of End Shield assemblies inviting domestic manufacturers to bid, extending benefits under the Ministry of Power's Office Memorandum of May 1999 applicable to international competitive bidding was not justified.

(b) Failure to place purchase order within price validity period

The Company floated (May 2010) a two part public tender for procurement of 2000 modules of Phosphor Bronze Wire Mesh♦ for use in KAPP 3 & 4 and RAPP 7 & 8

♦ ***Phosphor Bronze Wire Mesh is used as internal packing material for distillation columns in nuclear power projects. Distillation columns are required for upgradation of isotopic purity of heavy water (used in nuclear reactor) from the downgraded heavy water.***

projects. In response to the tender, the Company received bids from five bidders. Based on the technical evaluation (July 2010), all the five bidders were found technically qualified, but they were capable of meeting only part of the requirement of the above projects. Therefore, based on the recommendations of the evaluation committee, all the five bidders were technically approved (July 2010) to deliver the quantity as per their assessed capacities, as shown below:

Sl. No.	Name of the Bidders	Price per module quoted by the bidder (₹)	Position of the bidder	Number of modules recommended to be ordered
1	M/s Haver Standard India Private. Limited (HSIL)	80,000	L1	1000
2	M/s Evergreen Technologies Private. Limited, Mumbai (ETPL)	1,00,884	L2	500
3	M/s Paper Machine Wire Industries (PAMWI)	1,02,500	L3	600
4	M/s Three Gee Engineers Private. Limited	1,33,525	L4	250
5	M/s Champion Manufacturing Company, Hyderabad	2,10,000	L5	250

It was further decided that the order would be placed on L1 bidder for their maximum proposed quantity followed by L2 and so on till the total requirement was met. During price bid evaluation (September 2010), M/s HSIL which had quoted the price of ₹ 80,000 per module emerged as L1 bidder. As L1 was eligible for only 1000 modules against the total requirement of 2000 modules, the Company asked L2 and L3 bidders to match the price of L1. M/s ETPL (L2) expressed their inability to match L1 price but agreed to reduce their quoted price of ₹ 1,00,884 per module to ₹ 90,796 per module. M/s PAMWI (L3) agreed to match L1 price of ₹ 80,000 per module. A committee meeting was held (September 2010) wherein it was recommended to place the purchase orders (PO) for the first 1500 modules on M/s HSIL (L1) and M/s PAMWI (L3) at L1 price and to include an option in their purchase orders for increasing the PO quantity by the remaining quantity (500 modules) after one year on the same unit rate and other commercial terms and conditions prevailing in their POs, if their performance was found satisfactory during one year. Further, if the above condition was not acceptable to the parties, order would be placed on M/s ETPL for the remaining 500 Modules at their negotiated price.

Accordingly, POs were placed (October 2010) on M/s HSIL (1000 modules) and M/s PAMWI (500 modules) at a price of ₹ 80,000 per module. Subsequent to the placement of POs, the Company requested (25 October 2010) the bidders to inform whether they agreed for supplying additional quantity of 500 modules after one year at the price of ₹ 80,000 per module. The replies from the parties were received by the Company on 8 November 2010 wherein they had expressed their inability to supply additional quantities at the same rate. On 30 November 2010, the Company requested M/s ETPL to extend the validity of their offer upto 20 December 2010, though the same had already expired on 29 November 2010. However, M/s ETPL refused (2 December 2010) to extend the validity of their offer. The Company, therefore, issued (January 2011) a single part limited tender to the above five bidders and based on the evaluation of bids, placed (May 2011) an order on M/s Three Gee Engineers (L1) for supply of the balance 500 modules at a price of ₹ 1,06,525 per module.

Audit observed that though the Company had received intimations from M/s HSIL and M/s PAMWI on 8 November 2010 regarding their inability to supply additional 500 modules, the Company did not place the PO on M/s ETPL within the price validity period viz., upto 29 November 2010 at their negotiated price of ₹ 90,796 per module. Thus, the non-placement of PO within the price validity period at the lower price of ₹ 90,796 per module and subsequent placement at a higher price of ₹ 1,06,525 per module resulted in additional expenditure to the extent of ₹ 1.49 crore (including taxes, duties and transportation).

The Management stated (October 2013/January 2015) that the time taken was only for correspondence with M/s HSIL and M/s PAMWI to get additional supplies at the same price. Upon refusal by both the parties, option to place the order for balance quantity on M/s ETPL was exercised and letter dated 30 November 2010 was sent seeking extension of the validity of their offers at the negotiated price to which they did not agree.

The reply was not tenable as M/s HSIL and M/s PAMWI had conveyed their inability to supply the additional quantity at the same rate on 8 November 2010. Therefore, considering the fact that the offer of M/s ETPL was valid only up to 29 November 2010, timely action should have been taken to place the order for the balance 500 modules on M/s ETPL instead of placing it at a higher rate on M/s Three Gee Engineers.

(c) Time limit for completion of tendering procedure not laid down

Audit observed that the Company did not prescribe any time limit for completion of tendering procedure and placement of purchase order after receipt of an indent. A review of the time taken in finalisation of contracts revealed that the time gap from the date of indent to the date of award of contract ranged between 3 months to 20 months due to which the completion dates stipulated in the contracts awarded did not conform to the desired dates of delivery as given in the indents.

The Management stated (January 2015) that recommendations for time limits of different activities involved from receipt of indent to placement of purchase order had been submitted to competent authority and were under process for approval.

(d) High variance between cost estimates and actual value of contracts

As per NPCIL instructions (July 2011) on 'Delegation of Financial Powers', while working out the estimated cost of an item all prevailing cost elements thereof as well as market conditions such as inflation, recession, competition etc. as on the date of indent should be taken into consideration so that the estimated cost so worked out is comparable with the market price, with the given specification/quality of product.

A review of the 33 contracts selected for audit revealed that there was wide variation in estimates made and the final values of the contracts entered into by the Company. The variance of actual values as against the estimates ranged from 0.28 *per cent* to 78 *per cent* on the lower side and 6 *per cent* to 71 *per cent* on the higher side. Thus, the purpose of the estimation of costs was not fully achieved.

The Management stated (November 2013) that estimates were made on the basis of engineering judgment, variation in the market, segment bidders, type of industry and many other factors. Due to those factors, a variation of 10 *per cent* to 20 *per cent* was expected with respect to estimated cost.

However, as the variation in 16 cases was more than 20 *per cent*, Audit is of the view that the cost estimation needs to be more realistic.

In response, the Management further stated (January 2015) that the concerned sections had been advised to take due care while preparing estimates.

1.3.6.3 Execution of contracts

(a) Avoidable payment of compensation due to non-release of work front

The Company placed (September 2002) four purchase orders on the erstwhile M/s BSES (now M/s Reliance Infrastructure Limited (RIL)) for supply, erection and commissioning of electrical system package for KAIGA 3 & 4 and RAPP 5 & 6 as per the following details:

Sl. No.	PO No	Project	Item	Value (₹)	Contractual date of completion
1	6043	KAIGA- 3&4	Supply	95,34,48,652	KAIGA-3 - 30.06.2006 KAIGA-4 - 31.12.2006
2	6044	KAIGA- 3&4	Erection & Commissioning	10,19,13,173	
3	6039	RAPP- 5&6	Supply	86,17,42,223	RAPP-5 - 30.03.2007 RAPP-6 - 30.09.2007
4	6040	RAPP- 5&6	Erection & Commissioning	9,54,82,289	

The work in respect of all the four projects was delayed as the Company could not release the work front to M/s RIL on time. Besides, the delay was also caused by non-availability of adequate manpower and other inputs by the Company. As the delay was entirely attributable to the Company, the Board of Directors (BOD) decided (March 2009) to extend the delivery dates in respect of KAIGA-3 and KAIGA-4 upto 6 May 2007 and 31 October 2008 respectively without levy of liquidated damages. Further, the BOD also approved (March 2009) payment of ₹ 1.60 crore to M/s RIL as compensation towards extended stay at work site for a period of 10 months and bank commission charges and insurance premium for the same period. Similarly, the BOD approved (February 2011) extension in delivery period for RAPP 5 and RAPP 6 upto 15 January 2009 and 12 October 2009 without levy of liquidated damages and also approved payment of ₹ 1.75 crore to M/s RIL as compensation for extended stay, bank charges and insurance premium. Thus, due to non-release of work front in time and non-supply of adequate manpower and other inputs, the Company incurred avoidable expenditure of ₹ 3.35 crore towards compensation paid to M/s RIL.

While accepting the audit observation, the Management stated (November 2013) that delay in release of the work fronts was due to delay in civil works. As the delays were attributable to the Company, the review committee recommended the compensation payable to M/s RIL. The Management further stated (January 2015) that the concerned sections had been advised to take appropriate action in this regard in future.

(b) Delay in execution of contracts and consequential effect on completion of projects

The detailed project reports (DPRs) approved for RAPP 7 & 8 (December 2008) and KAPP 3 & 4 (January 2009) projected the milestones for completion of various stages of the projects. As against the milestones projected, the actual/expected time for completion of significant stages of the projects was as follows:

Milestone	Completion date as per DPR				Actual/ expected date of completion*			
	KAPP3	KAPP4#	RAPP7	RAPP8^	KAPP3	KAPP4#	RAPP7	RAPP8^
First pour of concrete	December 2009	June 2010	December 2010	June 2011	November 2010	March 2011	July 2011	September 2011
Reactor first criticality	December 2014	June 2015	December 2015	June 2016	November 2015	March 2016	July 2016	September 2016
Commencement of commercial operation	June 2015	December 2015	June 2016	December 2016	May 2016	September 2016	January 2017	March 2017

**** Date of first pour of concrete is the actual date. Dates for subsequent stages are expected dates worked out on the basis of date of first pour of concrete.***

 # As per DPR, the activities of KAPP 4 would follow with a phasing of six months from those of KAPP 3.

^ As per DPR, the activities of RAPP 8 would follow with a phasing of six months from those of RAPP 7.

A review of 27 ongoing procurement contracts pertaining to the under-construction KAPP 3 & 4 and RAPP 7 & 8 projects revealed that in respect of 17 contracts, there was a delay ranging from 2 months to 24 months as compared to the contractual dates of completion. The delay in execution of the contracts would adversely affect the completion of the project with resultant loss of revenue.

The Management furnished (October 2013) the purchase order-wise reasons for the delay. It was observed from the reply that the project schedule of KAPP 3 & 4 would be delayed by 18 to 23 months and that of RAPP 7 & 8 by 15 to 20 months on account of delay in supply of End shields with reference to the contractual delivery dates (CDD) and the Master Control Network (MCN). It was also observed that in some cases, the Management justified the delay by stating that the delays in case of individual POs were expected to be lesser than project delay.

Audit, however, is of the view that as the delays in completion of the contracts would result in not only cost overrun but delayed generation of electricity and also loss of revenue. Vigorous efforts are required to be made by the Management to analyse the reasons for the delays and take remedial action promptly to ensure timely completion of the projects.

In response, the Management stated (January 2015) that the concerned sections had been advised to take appropriate action in this matter for future.

The Department of Atomic Energy endorsed (February 2015) the views of the Management.

Conclusion

The Company did not make proper assessment of available material before floating tenders for manufacture of steam generators for KAPP 3&4 projects. As a result, material valuing ₹17.51 crore, which could be issued to the suppliers as free issue material (FIM), remained unutilised in the inventory with consequential increased carrying cost. The Company did not ensure economy in the tendering process as it did not take into consideration the impact of local taxes during evaluation of bids which resulted in additional expenditure of ₹4.52 crore. Further, non-placement of purchase order on a supplier within the validity period of price bid and subsequent release of order on a different supplier at a higher price resulted in extra expenditure of ₹ 1.49 crore. The Company had not prescribed any time frame for completion of tendering procedure after receipt of an indent which led to mis-match between the desired dates of delivery given in the indents and the completion dates stipulated in the contracts. Besides, delays ranging from 2 months to 24 months were noticed in the execution of 27 ongoing procurement contracts selected for audit.

Recommendations of Audit and response of the Management

In view of the aforesaid audit findings, the recommendations made by Audit and the response received from the Management are as follows:

Audit Recommendations	***Response of the Management***
➢ ***The Company should make proper assessments of materials available in the inventory before floating the tenders and supply such materials to the contractors with due consideration to economy.***	➢ ***The usable materials will be considered for issue as fresh issue material in future projects with due consideration to economy.***
➢ ***The Company should lay down a specific time frame for completion of each stage in the tendering process after receipt of an indent.***	➢ ***The recommendations for time limits of different activities involved from receipt of indent to placement of purchase order have been submitted to competent authority and are under the process of approval.***
➢ ***The Company should ensure strict compliance to the terms and conditions of the contracts.***	➢ ***The concerned sections in NPCIL have been advised to take appropriate action in this matter in future.***

CHAPTER II: MINISTRY OF CIVIL AVIATION

Airports Authority of India

2.1 Allotment of land for setting up and operations of flying clubs

2.1.1 Introduction

Airports Authority of India (AAI) was formed by merger of International Airports Authority of India and National Airports Authority and came into existence on 1 April 1995 with the enactment of the Airports Authority of India Act, 1994. Section 11 of the Act envisaged that AAI in the discharge of its functions under the Act shall act on business principles. Till formation of AAI, Director General of Civil Aviation (DGCA) allotted land and hangar spaces to various flying schools/clubs/academies to impart training and other aviation related activities. This work was taken over by AAI from 1995.

Till 2007, AAI did not have a defined policy for levying charges on flying schools/ flying clubs. In February 2007, AAI decided to classify flying clubs into two categories which are as follows:

Category I: - Flying clubs/flying training organization registered as educational societies and operating on 'no profit no loss' basis to be charged nominal rates i.e. @ 10 *per cent* of the normal rates.

Category II: - All other flying clubs/institutions to be charged at normal AAI rates for various services.

There were 32 flying clubs/schools situated at various airports, under the control of AAI, in India (March 2014). The scope of audit was limited to the review of records at the AAI Corporate Office and examination of records at five regional headquarters Chennai (Southern), Mumbai (Western), Delhi (Northern), Kolkata (Eastern and North Eastern) and Hyderabad for a period of three years ended 31 March 2013; however, the data given in the para has been updated upto 31 March 2014.

Audit was carried out with the objective to assess efficiency of AAI in framing and reviewing policy for fixation of charges to be levied on flying clubs and its effective implementation.

2.1.2 Audit Findings

2.1.2.1 Failure to allot land for setting-up of flying clubs:

Board of Directors (Board) of AAI accorded (21 February 2007) 'in principle' approval for allotment of land for setting up of Flying Schools/ Aircraft Maintenance Workshops at different airports by calling Expression of Interest (EOI) subject to availability of land. In

March 2007, AAI invited 'Expression of Interest' for setting up of flying schools/aircraft maintenance workshops at 31 airports after confirmation from the Regional Offices regarding availability of requisite area of land. A committee was constituted which invited tenders in phases for setting up of flying schools. The AAI Board accorded (November 2007) its approval to allot minimum one acre and at the most 2.5 acres of land subject to availability at each of the airports. Some of the important bidding parameters were as follows:

(i) Not more than one site will be allotted to a successful bidder even if the bidder becomes successful at more than one airport.

(ii) In case either or both of the sites are not available at a particular airport, due to any reason whatsoever, the successful bidder shall have no right for any claim.

(iii) The lease of land shall be for a period of 5 years extendable by another 5 years on mutually agreed terms and conditions.

Audit observed lapses in allotment of land for setting up of flying clubs in the following cases:

(a) Ludhiana Airport: The successful bidder M/s. Bird Consultancy Services Private Limited (BCS) quoted a minimum guaranteed royalty of ₹ 23.25 crore for five years apart from the required license fee. The bidder was offered (November 2007) a choice between two sites, measuring 1 acre each. Based on their requirement, M/s BCS requested (November 2007) AAI for an allotment of 2.5 acres of land. AAI, therefore, offered (December 2007) two sites one of 2.5 acres (approx) and the other of 1 acre, with the condition that M/s BCS would relocate the flying club at their own cost if it became necessary to do so for the envisaged development of Ludhiana Airport. In response M/s. BCS requested (January 2008) AAI to make an alternate arrangement for land allotment. AAI, however, without considering the same, allotted (July 2009) land measuring approx. 2.5 acres to M/s BCS. M/s BCS, however, turned down the conditional offer and final award of tender did not take place. As of August, 2014 the envisaged development of Ludhiana airport has not materialized. Thus, allotment of land to the successful bidder on a condition not acceptable to the bidder resulted in loss of opportunity to AAI to earn revenue in the form of minimum guaranteed royalty amounting to ₹ 23.25 crore apart from the license fee.

(b) Nadirgul Airport: Due to delay on the part of AAI to identify suitable land, the successful bidder (July 2007) M/s Guru Nanak Educational Trust could be allotted land only in July 2009. The party, however, declined to accept the allotment due to undue delay. Thus non identification of the site before calling bids and inordinate delay in allotment of land to successful bidder resulted in revenue loss of ₹ 2.44 crore to AAI in the form of minimum guaranteed royalty apart from the license fee.

The Management confirmed the facts (December 2013) relating to non-allotment of land at Ludhiana and Nadirgul airports and stated that policy on flying schools was under formulation which would take care of all these issues in future. The above said policy is yet to be formulated (August 2014).

(c) Behala Airport: Due to delay in identification of the site by AAI, the successful bidder M/s Trans Bharat Aviation (P) Limited (TBA) was allotted land in June 2009 i.e. after six months from the date of selection (December 2008). The no objection certificate (NOC) for construction of hangar was issued by AAI only in July 2010 by which time the approval obtained by TBA from DGCA for setting up of flying institute was on the verge of expiry (August 2010). As DGCA denied further extension to TBA, the flying institute could not be set up. This resulted in revenue loss of ₹ 4.21 crore to AAI in the form of minimum guaranteed royalty quoted by TBA apart from the license fee.

Though the Management confirmed the facts (November 2013), no comments were offered for delay in issuance of NOC.

(d) Khajuraho Airport: M/s. Falcon Aviation Academy (FAA) was given formal allotment letter in November 2009 i.e. after a lapse of almost one year after the date of selection (December 2008). M/s. FAA expressed its inability to complete the formalities till 21 January 2010. The AAI, however, decided to forfeit the EMD of the party and to call for fresh tenders. So far (March 2014), the land has not been allotted to any flying club. Thus, due to an inordinate delay in issuing formal allotment letter, AAI lost an opportunity to earn revenue of ₹ 1.65 crore for five years in the form of minimum guaranteed royalty quoted by FAA apart from the license fee.

The Management confirmed the facts (November 2013); however, no comments were offered on delay in identification of the site by AAI.

It emerges from the above mentioned cases that AAI did not have an efficient system in place for identification of sites before inviting bids for setting up flying schools at various airports. There were unreasonable delays in allotment of land to successful bidders leading to loss of revenue for AAI both in the form of royalty quoted by bidders and the license fee which could have been earned from these flying schools.

2.1.2.2 Absence of monitoring credentials of flying clubs

Pursuant to AAI's decision of February 2007 regarding charges to be recovered from flying clubs, a list of 28 flying clubs falling under category I and 13 under category II was circulated to all airports in April 2007. All flying clubs covered under category I were required to produce a current valid certificate in support of their credentials for availing the benefits of levy of nominal rates, failing which, following course of action was to be taken:

- 90 days notice to be issued to such flying clubs to stop operations and surrender land and hangar space occupied by them after clearing outstanding dues.
- License fee be charged from such flying club on normal rates plus 13 *per cent* of the gross turnover (GTO) for all activities carried out by them at the respective airport.
- In case of non compliance with the above, occupation of land and hangar space by the flying clubs was to be treated as unauthorized and necessary action was to be taken for eviction.

Audit observed that AAI initiated, only in January 2010, the process of verification of the credentials for eligibility of category I, though the categorization of the clubs was decided in February 2007. Thus, due to delay on the part of AAI in executing its decisions, the following four Flying Clubs were able to evade normal rates for AAI services which resulted in revenue loss to AAI:

(a) Delhi Flying Club (DFC): DFC was established in 1957 at Safdarjung Airport and placed (February 2007) in category I. Last agreement with DFC was entered in 1982 for a period of five years, i.e. up to 31 March 1987. Thereafter, the agreement was not renewed. DFC was not carrying out any flying training/flying related activity since January 2002. Further, in compliance of instructions issued by AAI in January 2010 for verification of the credentials for eligibility of category I, DFC also failed to furnish any credentials in support of their categorization under category I. AAI was also aware that since October 2007 DFC was letting out allotted land/buildings for commercial purposes such as, operating IGNOU study centre, conducting interviews for air hostesses and religious/marriage functions etc.

Audit scrutiny revealed that no bills were raised by AAI to charge applicable license fee plus 13 *per cent* of Gross Turn Over (penal rates) and neither any eviction proceedings were initiated against DFC which had not paid even its outstanding dues as per category I rates and an amount of ₹ 7.54 crore was recoverable as of March 2014. Had AAI raised bills as per normal rates, the outstanding amount would have increased to ₹ 19.26 crore (February 2007 to March 2014).

(b) Bombay Flying Club (BFC): BFC established at Juhu Airport, Mumbai in 1931 and was placed in category I by AAI. BFC which was a company under the Companies Act, 1913 till March 2011, was carrying out commercial activities other than flying training and was also not operating on 'no profit no loss' basis. In March 2011, BFC was converted to a society registered under Societies Act, 1860. However, AAI took no action to verify and ensure whether BFC was eligible for privileges under category I and whether the Club was operating on 'no profit no loss' basis. Moreover, from 2008-09 onwards BFC had not paid its outstanding dues even as per category I rates and an amount of ₹ 3.60 crore was recoverable as of March 2014. BFC filed Writ Petition No. 858 of 2012 before High Court, Bombay, against levy of charges by AAI. The Court in its interim order directed BFC to pay ₹ 2.50 lakh per month with effect from 01-4-2012.

AAI informed (February 2014) Audit that in compliance with court order, BFC paid three installments totaling ₹ 7.50 lakh and thereafter, in compliance with MoCA instructions (09 October 2012), AAI decided (November 2012) to keep the order of recovery of outstanding dues from Category-I Flying Club in abeyance till further orders. Audit is of view that had AAI raised bills as per normal rates, the outstanding amount would have increased to ₹ 36.86 crore (February 2007 to March 2014).

(c) Madhya Pradesh flying club (MPFC), Bhopal: MPFC was established at Bhopal Airport in 1986 and was placed in category I by AAI. MPFC utilized the premises allotted to them for commercial purposes such as parking/maintenance of aircraft of private agencies. Audit observed that AAI neither raised bills at penal rates nor did they initiate eviction proceedings against MPFC. Resultantly AAI failed to raise bills amounting to ₹ 0.81 crore (from 2008-09 to 2013-14) on account of differential between normal and nominal rates.

(d) Madhya Pradesh flying club (MPFC), Indore: MPFC was established at Indore Airport in 1961 and was placed in category I by AAI. Audit observed that the club, which was registered as a company under the Companies Act 1913, was carrying out commercial activities other than flight training and hence was not eligible to be placed in category I. However, neither bills at penal rates were raised by AAI nor eviction proceedings initiated against MPFC, Indore. MPFC, Indore had not paid even its outstanding dues as per category I rates and an amount of ₹ 0.80 crore was recoverable from it as of March 2014. Had AAI raised the bills as per normal rates outstanding amount would have increased to ₹ 9.10 crore (from 2008-09 to 2013-14).

2.1.2.3 Non realization of dues.

(a) Due to absence of any agreement with flying clubs

AAI issued a circular (May 2007) to all its Airport Directors to review and renew 'land license' agreements with flying clubs and clarified that any occupation beyond the valid agreement period would amount to unauthorized occupation, which was to be dealt with as per penal provisions. It was incumbent upon AAI to enter into fresh agreements with the parties occupying land/space at various AAI airports, but no such efforts were made by AAI. In the absence of agreements, realization of dues outstanding against such parties could not be enforced. Airport Directors/Regional Offices had not taken action to renew the land license agreements. Details of outstanding dues from flying clubs at various AAI airports, not realized in absence of a legally binding agreement were as follows:

Airport	Name of the Party	Date of Land Allotment	Last Agreement entered	Amount due as on March 2014
Safdarjung	Delhi Flying Club	April 1957	1982 for 5 years	₹ 7.54 crore
Begumpet	M/s Andhra Pradesh Aviation Academy	August 1969	1982 for 5 years	₹ 2.24 crore
Amritsar	Amritsar Aviation Club	1962	Up to 1994	₹ 0.37 crore
Jaipur	Rajasthan Flying Club	April 1966	1966	₹ 5.77 crore
Guwahati	Assam Flying Club	May 1958	No agreement till date	₹ 1.11 crore
Kanpur	U. P Flying Training Instt. (upto April 2012, as party surrendered the land without clearing dues).	1952	No records available	₹ 9.57 crore

Ministry of Civil Aviation (MoCA) advised (09 October 2012) AAI to place the issue of recovery of dues from category-I flying clubs before AAI Board and keep the order of recovery of charges in terms of AAI Board resolution of 2007 in abeyance, till finalization of the policy of the Ministry regarding prescribing the eligibility criteria for flying clubs for availing facility of nominal rates for various charges payable to AAI. Accordingly, AAI instructed (November 2012) all airports to keep recoveries from category I flying clubs in abeyance till further orders. Audit scrutiny revealed that as of August 2014, the said policy has not been finalized by MoCA.

Audit also observed that due to lapses on the part of AAI in renewal of land license agreements, some flying clubs were in occupation of land in excess of allotment as follows:

Airport	**Name of the Party**	**Area (in sq. mtrs.)**		
		Allotted	**Actually occupied**	**Unauthorized occupation**
Safdarjung	Delhi Flying Club	3124	6168.33	3044.33
Begumpet	M/s Andhra Pradesh Aviation Academy	454.42	5593.32	5138.90

(b) Salem Airport

(i) M/s International Aviation Academy Private Limited (IAAP) was allotted land in July 2009 at Salem airport and paid the license fee for the first and second year and royalty for the first year in advance. However, due to delay in commencement of operations in view of pending approval from DGCA, it could not clear its dues thereafter. IAAP also did not honour the interim orders (December 2011) of Madras High Court to deposit an amount of ₹ 50 lakh within a period of six weeks. IAAP started flying activities from 2012. Audit observed that neither was IAAP evicted nor the dues realized and an amount of ₹ 11.71 crore was outstanding (March 2014) against the club.

(ii) M/s. Kohinoor Educational Services Private Limited (KESP) was allotted land at Salem airport in March 2009 and started flying activities from June 2010. KESP, did not meet its contractual obligations in terms of payments. However, no action to realize dues from KESP was taken nor any eviction orders issued by AAI. An amount of ₹ 11.76 crore was outstanding (March 2014) against KESP.

The Management while confirming the above facts (November 2013 & March 2014) stated that eviction proceedings had been started against both clubs.

The fact, however, remains that both clubs continue to occupy AAI land without clearing their dues.

(c) Kolkata Airport

M/s Multiple Manpower Development Private Limited (MMDPL), Kolkata was allotted hangar space (510.20 sqm.), built up space (42.73 sqm) and paved land (2700 sqm) for a period of one year from 5 December 2006 for flying training activities at Behala civil aerodrome. The above contract was extended up to 31 December 2008 on the same terms and conditions, except royalty, which was enhanced from 12 to 13 *per cent* of the total revenue proceeds.

Notice Inviting Tender (NIT) was called for by AAI (November 2008) for establishing flying schools on AAI airports. As per the NIT, "those private flying clubs on AAI land whose license had expired and those whose license is still valid may be allowed to take part in the tender and in the event of their not being successful in the tender they would have to vacate the existing premises and hand over the same to AAI". MMDPL did not participate in the bid but requested (June 2009) that their contract may be extended for a period of 5 years. MMDPL also agreed to pay royalty equivalent to that quoted by the successful bidder and license fee for the space under their occupation. Accordingly, AAI allotted (January 2009) the area to MMDPL for a period of five years. MMDPL, however, disputed the calculation of license fee at a higher rate and refused to enter into an agreement and continued to occupy the space unauthorisedly without making any payment.

AAI initiated (February 2011) eviction proceedings and passed an eviction order (July 2011) directing MMDPL to pay arrears for the period December 2006 to December 2010 amounting to ₹ 2.46 crore. Thereafter, MMDPL approached the Airport Appellate Tribunal which dismissed the appeal (February 2013). MMDPL finally approached (July 2013) AAI for execution of fresh agreement and waiver of arrears of license fee and royalty from 01.01.2009. Later on, AAI initiated legal action against MMDPL in June 2014. An amount of ₹ 8.43 crore was outstanding (May 2014) against MMDPL.

(d) Safdarjung Airport, New Delhi

DGCA had allotted land measuring 825.25 sqm to M/s Delhi Gliding Club at Safdarjung Airport, New Delhi. However, records relating to allotment were not available with AAI and no agreement in this regards was found on record. Flying activities were closed at Safdarjung airport since January 2002.

Audit observed that though Delhi Gliding Club had closed glider flying activities more than 11 years ago, AAI did not take action to realize outstanding dues amounting to ₹ 2.48 crore (March 2014) or to get the premises vacated by the club.

2.1.2.4 Aero Club of India

Aero Club of India (ACI), an apex body of over 22 flying/ gliding clubs and other aero sports organizations was allotted (1984) land measuring 1617.10 sqm at Safdarjung Airport for a period of 30 years with effect from 19 September 1983 at a nominal license fee of ₹ 1/- per annum. As per terms of agreement (December 1984) the land license fee was subject to revision. Though AAI raised the bills at revised rates (2007) retrospectively from 1986 onwards, it could not realize dues and ₹ 2.77 crore were outstanding against ACI as on 31 March 2014. However, AAI did not take action either to realize dues or to evict ACI from the premises.

As lease of ACI expired on 18 September 2013, ACI requested (July 2013) MoCA to extend the lease for another 99 years on the existing terms and conditions. Though such extension was not in line with the policy of AAI, MoCA proposed to approve extension of lease period by another 30 years from 19 September 2013 at a license fee of ₹ 1/- per annum and forwarded the case to AAI. Board of AAI in 157th meeting (December 2013) accorded approval to the proposal of MoCA, considering it as a special case and forwarded (February 2014 the case to MoCA for obtaining approval of the competent authority. ACI was still in unauthorized occupation of the space without clearing the dues (August 2014).

Conclusion

There was inordinate delay in formulation of a policy regarding levy of airport charges and allotment of land to flying clubs and the attempt of framing policy in 2007, did not bear any result even till August 2014. In the absence of timely action and mechanism to verify the eligibility under Category I or II, flying clubs which were involved in other commercial activities and also otherwise not entitled to avail the benefits of concessional rates continued to enjoy the same. Further, in absence of any agreement with the parties, most of the flying clubs raised disputes regarding rates and did not clear their dues. Moreover, AAI suffered losses due to delay in identification of sites and issuance of required clearances.

The matter was reported to the Ministry in January 2014; their reply was awaited (March 2015).

2.2 Disregard of provisions of Shareholders Agreement by MoCA and AAI resulted in additional burden on the travelling public in the form of Development Fee in IGI Airport, Delhi

MoCA and AAI failed to bring to the notice of AERA the provisions of Shareholders Agreement which mandated affirmative vote of AAI till such time AAI held 10 *per cent* equity shares in DIAL, in respect of special resolution under the Companies Act, 1956 and Reserved Board Matters. This led to levy of Development Fee by DIAL, resulting in additional burden on the travelling public of ₹ 3415.35 crore.

The Government of India (GoI), in its Order dated 9 February 2009, granted approval to Delhi International Airport Private Limited (DIAL)[♥] for levy of Development Fee (DF) at the rate of ₹ 200 per embarking domestic passenger and ₹ 1300 per embarking international passenger, inclusive of all applicable taxes under section 22 A of the AAI Act, 1994, purely on an ad-hoc basis, for a period of 36 months with effect from 1 March 2009. One of the conditions of approval was that the final determination of the levy be made by GoI/Regulator after adequate consultation with users.

The Regulator (Airports Economic Regulatory Authority of India–AERA) after taking into consideration the revised final project cost informed by DIAL as ₹ 12,857 crore (as against ₹ 8,975 crore projected to the Ministry in October 2009), sought responses from stakeholders in its Consultation Paper of 21 April 2011. Airports Authority of India (AAI) in their submission dated 12 May 2011 before AERA stated that it was not in a position to make any further contribution towards equity. Further, DIAL too represented to AERA that as AAI have expressed inability to contribute further equity, it will not be possible to raise further equity without diluting the equity of AAI /breach of the trigger Debt-Equity Ratio.

Considering the above, the AERA permitted (14 November 2011) DIAL to levy DF at the rate of ₹ 200 per embarking domestic passenger and ₹ 1300 per embarking international

[♥] ***A Joint Venture Company (JVC) incorporated under the Companies Act, 1956.***

passenger (exclusive of statutory levies, if any) to bridge the funding gap. The levy commenced with effect from 1 December 2011.

While determining the levy of DF, AERA observed "Clause 3.3.1 read with clause 3.3.3.3 of the Shareholders Agreement (SHA) would seem to indicate that the private participants are obliged to acquire the equity shares, offered to AAI at the time of further capitalization and which it does not subscribe". AERA also stated, "however, irrespective of the position whether other promoters can bring in further equity or not, in case they are presumed to be able to bring such equity, the same will lead to reduction in equity stake of AAI below the current 26 *per cent* level. Keeping in view of the provisions of the Companies Act, it will fundamentally alter the special position of AAI in the JVC, i.e. DIAL. The Authority feels that such fundamental alteration, at least at this stage, does not appear to be in public interest in as much as AAI is lessor of the airport and ought to have a special position in DIAL".

Audit observed that AAI/MoCA* did not bring to the notice of AERA, clause 6.1.1 as also clause 5.11.1, 5.12.1 and 5.13.2 of the SHA, emphasising the rights of AAI with respect to Reserved Board Matters and Reserved Shareholders Matters even when it holds at least 10 *per cent* of the equity capital of DIAL, thereby affirming AAI's rights in respect of special resolution under the Companies Act, 1956 and Reserved Board Matters.

Clause 5.13.2 and clause 6.1.1 of the SHA are reproduced below:

Clause 5.13.2: A resolution of the Board of Directors shall be adopted by the affirmative vote of the simple majority of the Directors present at a meeting at which a quorum of the Board of Directors is present. Provided, however, that as long as AAI along with the AAI Nominees, in the aggregate, holds not less than ten (10) *per cent* of equity share of the JVC, any decision in relation to the Reserved Board Matters shall be considered as passed by a majority vote necessarily requiring the affirmative vote of the Directors nominated by AAI.

Clause 6.1.1: till such time as AAI along with AAI Nominees, in the aggregate hold at least ten (10) *per cent* Equity Shares in the JVC, the JVC (or any of its Directors, officers, agents or representatives) shall not give effect to any decision or resolution in respect of the Reserved Shareholders Matters, unless the same is approved by the affirmative vote of AAI.

The SHA defines 'Reserved Shareholders Matters' as "any shareholder resolution requiring the consent of not less than three-fourths (75 *per cent*) of the shareholders voting (special resolution) under the provisions of the Companies Act". Therefore, it is seen that the SHA specifically protects the special position of AAI in the JVC till such point as AAI holds at least 10 *per cent* of the equity shares of DIAL and as such the rights of AAI would not be affected to any extent as per the provisions of the Companies Act even in case its equity was brought below 26 *per cent*. Similarly, clause 5.11.1, 5.12.1 and 5.13.2 further strengthen the position of AAI in the JVC by way of making it necessary for AAI nominee to be present to constitute quorum for Board meetings, bestowing upon AAI the right to nominate a member on any committee/sub-committee constituted by the

* ***Ministry of Civil Aviation***

Board and making it mandatory for any decision in relation to 'Reserved Board Matters' to require the affirmative vote of AAI nominee Directors on the Board till such time as AAI holds 10 *per cent* of the equity in the JVC.

As the equity contribution of AAI in DIAL was ₹ 637 crore, by pegging AAI share holding at 10 *per cent* the other shareholders of DIAL could have contributed capital to the extent of ₹ 5733 crore (90 *per cent* of total paid up capital of ₹ 6370 crore) without affecting any of the rights of AAI either under the provisions of Companies Act 1956 or under the SHA. As the other shareholders of DIAL had contributed only ₹ 1813 crore towards the share capital of DIAL, the said shareholders could have brought in additional capital of ₹ 3920 crore to maintain the required debt-equity ratio and bridge the funding gap, thereby obviating the need to levy DF on the travelling public.

The Ministry of Civil Aviation (MoCA) is responsible for formulation of national policies and programmes for the development and regulation of the Civil Aviation sector in the country and it exercises administrative control over affiliated Public Sector Undertakings such as the Airports Authority of India. As per MoCA, its Vision is to "enable the people to have access to safe, secure, sustainable and affordable air connectivity services with World-Class Civil Aviation Infrastructure". As such, MoCA/AAI are responsible for protecting the interest of the public at large and in this capacity, it was incumbent upon them to bring to the notice of AERA, the relevant provisions of SHA which would have provided for infusion of equity by the shareholders other than AAI to bridge the funding gap.

This failure on the part of MoCA/AAI led to levy of Development Fee amounting to ₹ 3415.35 crore out of which ₹ 2841 crore has been collected upto March 2014 and the balance amount will be collected upto April 2016.

MoCA replied (May 2014) as under:

(a) AAI required funds for execution of projects at Chennai and Kolkata airports and upgradation of various facilities at select airports, as such it informed AERA about its inability to make any further contribution towards equity. AAI also indicated that the JVC i.e. DIAL could still maintain the trigger debt-equity ratio in terms of clause 3.3.1 of the Shareholders Agreement by way of infusion of funds in such form and quantity by the private participants without diluting equity shareholding.

(b) AERA, while determining DF had considered all other means of bridging the funding gap for the Delhi airport project and had felt that it was not in public interest that the lessor of the Delhi airport, i.e. AAI, should have its shareholding reduced below 26 *per cent*. It was also felt by AERA that being a public sector undertaking, AAI would ensure greater support passenger interest. Hence, in order to have a balance between passengers interest safeguarding, the AERA had determined the amount of DF in respect of DIAL, keeping the AAI's equity share at 26 *per cent*.

(c) While determining DF, AERA had a reference to OMDA as well as the Shareholders Agreement in respect of DIAL. The Reserved Shareholders Matters mentioned in clause 6.1.1 of SHA and detailed under Schedule-4, did not cover many matters of operational as well financial nature and significance.

(d) Prior to issue of order in the matter of review of levy of DF at Delhi airport, AERA had enquired from the private participants as well as AAI regarding the amount of equity/any other means of finance that they plan to employ for bridging the funding gap. At that stage the DIAL expressed its inability to infuse any further equity. AAI indicated that it was in a position to infuse ₹ 93 crore in the JVC. Infusion of additional equity by a shareholder can be done upon a cash call by the Company. However, DIAL has not made any cash call till date (May 2014).

(e) While determining aeronautical tariffs in respect of Delhi airport, the amount of DF gets reduced from the Regulatory Asset Base (RAB[♦]). Thus the asset value on which DIAL is entitled for a fair rate of return stands diminished by the amount of DF. AERA has not allowed any depreciation on such DF funded assets. Hence, to that extent, burden on the travelling public through aeronautical tariffs, has been reduced permanently for all times to come through reduction of RAB on account of DF.

(f) If AERA had not determined any DF and in case DIAL was also unable to infuse any additional equity, then there would have remained a funding gap for the project which would have impacted the timely investment in improvement of infrastructure/facilities in respect of Delhi airport and would also have resulted in the airport becoming economically unviable.

Reply of the Ministry is not acceptable in view of the following:

(a) Proposal of AAI was contradictory as infusion of debt would have affected the debt-equity ratio while infusion of equity would have diluted the equity shareholding. As such the proposal of AAI was practicably not feasible.

(b) Reply confirms that Ministry/AAI did not take cognizance of clause 6.1.1 of SHA which stipulates that AAI's affirmative vote is the deciding factor for all 'Reserved Shareholders Matters' irrespective of the quorum present and voting. Thus as per clause 6.1.1 till AAI holds 10 *per cent* of the equity in the JVC no decision or resolution on 'Reserved Shareholders Matters' can be given effect to unless it is approved by the affirmative vote of AAI. Effectively, this ensures all the rights and privileges of a shareholder holding 26 *per cent* or more equity. AAI/Ministry failed to bring up before the AERA the special protection given to AAI by clause 6.1.1of SHA.

[♦] ***Regulatory Asset Base (RAB) refers to aeronautical assets and any investments made for the performance of Reserved Activities, owned by JVC but does not include CWIP, working capital, penalties, Liquidated Damages.***

Further, as per Clause 3.3.3.1 of SHA, AAI shall have option to subscribe for any subsequent capitalisation of JVC or otherwise. Clause 3.3.3.3 of SHA binds/ obliges the private participants to acquire/subscribe for the shares not opted by AAI. Thus decision of AAI /MoCA not allowing dilution of equity below 26 *per cent* gave opportunity to the private participant to escape their obligation/responsibility under the SHA to raise additional equity/debt for the project.

(c) The Ministry's reply while making mention of *'many matters of operational as well financial nature'* does not spell out such matters in specific terms. However, matters requiring Special Resolution as per Companies Act 1956 are exhaustive and cover all aspects of operational and financial nature. Therefore, Schedule 3 and 4 of SHA indicating Reserved Board Matters and Reserved Shareholders Matters (both require Special Resolution), respectively, and matters requiring Special Resolution as per Companies Act 1956 provide complete protection to AAI in financial, operational as also all important matters relating to the JVC. Hence reply is not acceptable.

(d) DIAL's expressing inability to infuse any further equity indicated its intention of running the airport with minimal ownership funds. However, no action has been taken by MoCA/AAI on DIAL for non compliance to clause 3.3.1 and 3.3.2 of SHA.

(e) MoCA did not provide any details or calculations to support their contention that burden on the travelling public through aeronautical tariffs, has been reduced permanently for all times to come through reduction of RAB on account of DF. The AERA, in their tariff order No. 3/2012-13 dated 24-4-2012 has worked out Net Target Aero Revenue of ₹ 7660.90 crore for Ist control period of five years (2010 to 2014) considering the element of DF reduced from the RAB. Audit worked out the Net Target Aero Revenue of ₹ 8638.06 crore approx. by using the same data as used by AERA but without considering the element of DF. It may be seen that if no DF would have been levied, the additional burden (during Ist control period) on the travelling public through aeronautical tariff would have been an increase of ₹ 977.16 crore approx. (₹ 8638.06 crore minus ₹ 7660.90 crore) i.e. ₹ 195.43 crore approx. per year. With passenger traffic at about 35 million during 2011-12, per passenger increase in aeronautical charges would be around ₹ 55 approx. only as against the DF of ₹ 100/ ₹ 600 being levied presently[♦]. With the increase in traffic in the coming years the burden on this account would have been negligible (projected traffic at 37 million for 2013-14).

The reply of the Ministry is at variance with its Press Note dated 16 October 2012, which stated that if funding gap was met in terms of equity infusion and proportionate raising of loans by the airport promoter including AAI, the Airport Development Fee could stand abolished.

[♦]AERA revised with effect from 01.01.2013 the rate of Development Fee in respectof IGI Airport, New Delhi as ₹ 100/- per embarking domestic passenger and ₹ 600/- per embarking international passenger vide Order No. 30/2012-13 dated 28.12.2012

(f) The fact that the special position of AAI in the JVC would remain unchanged even if its equity was diluted to 10 *per cent* was never brought to the notice of AERA by MoCA/ AAI.

2.3 Loss due to failure in taking timely action as per approved credit policy

AAI did not take action as per credit policy and allowed M/s Kingfisher Airlines Limited to continue its operations on credit basis even after withdrawal of the credit facility. AAI also did not act timely on the advice of MoCA to take all legal means beside encashing bank guarantee of the airline. This resulted in loss of revenue of ₹ 172.69 crore apart from loss of interest of ₹ 117.03 crore (up to February 2014).

Airports Authority of India (AAI) provides aeronautical[1] and non-aeronautical[2] services at various civil airports in the country for which it charges fees and rent from an airline availing such services. As per credit policy of AAI, approved in 2007, bills are raised on fortnightly basis, and a credit period of 15 days, from the date of receipt of bills, is allowed to an airline subject to a security deposit equivalent to two months' billing of the airline. The credit policy further stipulated levy of interest at the rate of 12 *per cent* per annum on delayed payments.

M/s Kingfisher Airlines Limited (KFA) informed (13 April 2005) AAI, that they were scheduled to commence operations from 9 May 2005 and requested for grant of credit facilities for Route Navigation Facility Charges (RNFC), Terminal Navigation Landing Charges (TNLC), Landing and Parking Charges, Passenger Service Fees and other charges levied by AAI from time to time. AAI conveyed (28 April 2005) approval of credit facility to KFA subject to submission of a bank guarantee of ₹ five crore from a scheduled bank, in favour of AAI, towards security deposit. KFA deposited on 5 May 2005, the requisite bank guarantee and commenced its operations with effect from 9 May 2005.

KFA was persistently defaulting in making payments to AAI. Dues from the airline accumulated to ₹ 4.81 crore (against security deposit of ₹ 5 crore) up to 31 December 2005. The position of outstanding dues worsened after KFA took over, in June 2007, another airline, viz. Deccan Aviation. AAI took up the issue of pending recovery with KFA from time to time but the position did not improve. AAI informed (02 August 2007) MoCA that against guarantees of ₹ 25.70 crore available with them, outstanding dues against KFA had reached ₹ 36 crore. Ministry in response (5 September 2007) advised AAI to resort to all legal means beside encashing the bank guarantee (BG) of KFA. MoCA gave identical directions in August 2008 and October 2008, but AAI continued the credit facility to KFA till 31 May 2011, when the bank guarantee of ₹ 100 crore was encashed and AAI put operations of KFA on Cash & Carry basis with effect from 1 June 2011. Even after adjusting the proceeds of the BG, an amount of ₹ 217.31 crore remained outstanding as on 31 May 2011. In the meantime, the outstanding dues against KFA remained always in excess of the amount of security deposit held by AAI.

[1] ***Aeronautical services means the facilities and services necessary for safe and efficient operations of the airport, movement and parking of aircrafts etc.***

[2] ***Non-aeronautical services are related to passenger services at an airport.***

Inspite of repeated commitments, KFA failed to clear the outstanding dues. AAI filed a suit against KFA in April 2012, at 63rd Court, Andheri, Mumbai, under Negotiable Instruments Act, 1881, for bouncing of cheques amounting to ₹ 136.22 crore. Director General of Civil Aviation (DGCA) initially suspended (October 2012) the license for operations of KFA and thereafter, cancelled the same in December 2012. Considering that the probability of recovery of dues was very low because of (i) stopping of commercial operations by KFA due to withdrawal of its flying permit/license by DGCA and (ii) in case of winding up of KFA, priority for payment would be last since AAI's debts were unsecured; AAI had written off, during year 2013-14, dues of KFA amounting to ₹ 172.69 crore. AAI had also filed (March 2014) a civil recovery suit before the High Court of Bombay for an amount of ₹ 294.57 crore (including interest up to 28 February 2014).

Audit examination revealed that:

(a) AAI failed to take timely action against KFA for not adhering to the credit policy. KFA continuously defaulted in making timely payments and the amount of outstanding dues was more than the available security deposit during majority of the period of operations of KFA. AAI, however, encashed (May 2011) the available BG and put (with effect from 1 June 2011) KFA's operations on cash and carry basis, only after more than 5 years of default. Even after withdrawal of credit facility with effect from 1 June 2011, KFA was allowed to operate on credit basis leading to accumulation of huge outstanding dues against KFA.

(b) MoCA failed to enforce execution of its own directions by AAI. Chairman, AAI had turned down the request made by CEO, KFA, in a meeting held on 18 November 2008, for allowing a considerable time for settlement of overdues, on the ground that all other private airlines were settling their dues, and special treatment only for Kingfisher Airlines was not possible. Scrutiny of minutes of 146th meeting of Board of Directors (which included representative/s from MoCA) held on 15 December 2011, however, revealed that:

   (i) Contrary to the aforesaid stand taken by Chairman, AAI, MoCA/AAI, accepted the commitments made by CEO, KFA, for payment of overdues and allowed, as a very special case, KFA to continue the operations of the airline. Subsequently, the KFA failed to fulfill their commitments.

   (ii) On the proposal to file a suit in the Court of Law for recovery of dues and for attachment of aircrafts of KFA for recovery of outstanding dues, no specific directions were given by the Board of AAI.

Thus, despite being aware that KFA was a willful defaulter, MoCA and AAI, both allowed the operations of the airlines to continue even beyond withdrawal of credit facility and did not take timely action to recover the mounting dues.

AAI replied (October 2014) that they had exercised all measures and controls along with invoking all legal aspects to realise the dues. It further stated, that MoCA was also informed of the process of liquidation of outstanding dues from time to time and various measures as suggested were also taken to realise the dues.

Reply does not absolve AAI of its failure in taking action as per provisions of credit policy and allowing KFA to continue its operations even after withdrawal of the credit facility. AAI also did not take timely action as advised by MoCA. This amounted to extending undue favour to KFA which resulted in loss of revenue of ₹ 172.69 crore apart from loss of interest of ₹ 117.03 crore (up to February 2014). Further, MoCA also failed to enforce its directives and diluted its stand by allowing KFA to continue operations.

The matter was reported to the Ministry in December 2014; their reply was awaited (March 2015).

2.4 Non-recovery of cost of manpower and absence of provision to safeguard AAI's interests

As per JV agreement signed with Maharashtra Airport Development Company Limited (MADC), AAI deployed its manpower at Multi Modal International Passenger and Cargo Hub Airport at Nagpur (MIHAN) for Operation Support Period (OSP) of five years from 2009-10 to 2013-14 against payment of manpower cost by MIHAN India Limited (MIL). Against manpower cost of ₹ 64.99 crore incurred by AAI, MIL has paid an amount of ₹ 9.09 crore so far (January 2015). AAI also did not include any clause in the JV agreement to mitigate the financial risk in the event of non-absorption of AAI employees by the JV partner.

Airports Authority of India (AAI) signed (18 December 2006) a Memorandum of Understanding with Maharashtra Airport Development Company (MADC) to establish a Joint Venture Company (JVC), MIHAN India Limited (MIL♠) for development and operation of Nagpur International Airport for a period of 30 years. The MoU inter alia contained a provision that "the terms and conditions of the AAI staff working with the JVC shall be same as is being done in the case of Mumbai and Delhi Airports. The arrangement will be for five years and at the end of this period, the JVC shall absorb 100 *per cent* of the staff ". The Memorandum of Understanding (MoU) was ratified by the Board of Directors of AAI and subsequently, Ministry of Civil Aviation (MoCA) approved transfer of Dr. Babasaheb Ambedkar International Airport, Nagpur to the JVC.

As per Clause 15.2 of the Joint Venture Agreement "as on date of transfer of Nagpur Airport to the JVC, all employees working at Nagpur airport (except the CNS/ATM personnel and related support staff) would be placed at the disposal of the JVC for a period of five years on the same terms & conditions of employment with AAI. At the end of the five years' period, all such employees shall be absorbed by the JVC on such terms & conditions which shall not be inferior to their existing terms & conditions which they are already enjoying as employees of AAI". After expiry of initial period of five years on 6 August 2014, the period was further extended up to 30 November 2014 and thereafter up to 31 March 2015.

Audit observed that:

(i) With airport operations being handed over to a JV, AAI employees became surplus. With a view to mitigate such situation, AAI had inserted a provision in

♠ ***Multi Modal International Passenger and Cargo Hub Airport at Nagpur managed by MIHAN India Limited wherein AAI and MADC were having 49 per cent and 51 per cent equity, respectively.***

the OMDA whereby DIAL/MIAL had committed to pay retirement compensation in case AAI employees were not absorbed by the new operators. It was noticed that no such obligation was placed on MIL in the absence of which AAI would be burdened with the liability of employees who do not get absorbed under MIL.

(ii) As on the date of transfer of Airport to MIL, 155 employees were at disposal of MIL. These employees are working presently with MIL but till date (March 2015) MIL has not finalized its HR Policy and Rules and Regulations for inviting offer of absorption. In absence of an offer from MIL, AAI was not in a position to obtain willingness of its employees to get absorbed in MIL.

(iii) AAI has incurred an expenditure of ₹ 64.99 crore towards staff cost for the employees who are with MIL, for the period from August 2009 to January 2015. An amount of ₹ 55.90 crore (January 2015) is still outstanding against MIL on this account.

AAI stated (April 2014) that the outstanding dues were being consistently pursued with MIL. It further stated (March 2015) that MIL was finalising its HR policy which would be available soon and further action in the matter would be taken only on receipt of proposal from MIL.

The reply has to be viewed in the context of a meagre reimbursement of staff cost of ₹ 9.09 crore (March 2015) by MIL. AAI is silent on the issue as to how it proposes to deal with the financial liability of employees in the event of their non-absorption in MIL.

The matter was reported to the Ministry in November 2014; their reply was awaited (March 2015).

Air India Charters Limited

2.5 Unfruitful expenditure due to imprudent acquisition of aircraft on dry lease

Air India Charters Limited renewed dry lease[1] of four aircraft disregarding the rationale for acquisition of 18 new aircraft, shortage of crew and loss making routes which led to unfruitful expenditure of ₹ 405.83 crore between March 2011 to May 2014 towards lease related charges.

Air India Charters Limited (Company) launched low cost operations in April 2005 with a fleet of three aircraft obtained (April 2005) on dry lease for a period of five years expiring by April - July 2010. Subsequently, the Company acquired 18 aircraft (new aircraft) between December 2006 and December 2009 on finance lease[2] backed by a guarantee by the Government of India (GOI). During the same period (2006-07 to 2009-10), AICL also

[1] *Dry lease: A dry lease is a cancellable lease at the discretion of lessor; the lessee being allowed to use the asset during the lease period by paying lease rental and maintenance reserve as per the lease agreement. The asset in case of dry lease should be returned to the lessor in the agreed working condition.*

[2] *Finance lease: Finance lease is essentially a financial loan to own the assets and lessee has the right to utilize the asset throughout its useful life while the lessor retains only legal rights over it during the lease period.*

acquired four more aircraft on dry lease expiring by March – May 2011. As on March 2010, the Company, thus, had a fleet of 25 aircraft.

The Company returned the three aircraft taken on dry lease in April 2005 on expiry of their lease term in April-July 2010. Besides, an aircraft of the Company was lost in an accident in May 2010. Thus, by August 2010, the Company had a fleet of 21 aircraft. The dry lease of another four aircraft was also due for expiry in March – May 2011. While deliberating the proposal for renewal of lease these four aircraft, the Board of Directors of Company (Board) felt (October 2010) that returning the aircraft might be a better option in view of aircraft utilisation of 10 hours per day against 12 to 14 hours per day expected from the brand new fleet, cancellation of flights due to non-availability of crew, loss making routes and idling of 4 out of 21 aircraft for maintenance/stand by. Hence, the Company felt that returning the dry leased aircraft would enable better utilisation of remaining flights and savings on cost.

However, the Company approved (January 2011) renewal of dry lease of the four aircraft on the ground of (i) critical reviews from the local press on withdrawal of flights from Kerala, (ii) demand from elected representatives from Kerala, (iii) upward trend in airline industry and (iv) proposed aircraft utilization of 10.9 hours/day and 11.2 hours/day in Winter 2011 and Summer 2012 respectively along with operating surplus. Accordingly, dry lease of the four aircraft was continued for three more years up to March/May 2014. Subsequently, the lease was not renewed and presently (January 2015) AICL has a fleet of 17 aircraft.

With regard to dry lease of four aircraft in 2006-10 and their continuation for additional three years during 2011-14, Audit observed the following:

- Acquisition of 18 aircraft was approved (June 2004) by the Company and the Ministry of Civil Aviation (December 2005) to replace the aircraft taken on dry lease. In fact, the Company/Ministry had decided that in case Boeing was able to commence deliveries of aircraft earlier than winter 2006/07, the number of aircraft to be taken on dry lease would be reduced accordingly. Hence, dry lease of four aircraft should have been terminated in tandem with receipt of aircraft on finance lease and certainly on expiry of the lease period in March - May 2011. This was also supported by the minutes of Board, which recognised (October 2010) the economy of issues against renewal of dry lease and proposed for return.

- The project report for acquisition of 18 aircraft had been approved (June 2004/December 2005) with a condition to achieve increased aircraft utilisation of 12.7 hours per aircraft per day. This utilisation level was not achieved by the Company. After approval to the renewal of dry lease for four aircraft in January 2011, significantly lower flight utilization of 10.5 to 11.0 hour per day was targeted by the Company in March 2011. The average daily utilization of flight hours/ block time {(ADU (FH)[1] and ADU (BT)}[2] was around 8.53 hours/ 9.85 hours during 2009-10. This reduced to 8.03 hours/ 9.25 hours in 2010-11 and further reduced to 7.73 hours/8.75 hours by 2013-14. Thus, even the reduced

[1] ***ADU(FH): Average Daily Utilisation (Flight Hours)***

[2] ***ADU(BT): Average Daily Utilisation (Block Time)***

targets for aircraft utilisation as envisaged by the Company in March 2011 were not achieved. In fact, the utilisation levels fell consistently bringing to question the rationale for continuance of dry lease of the four aircraft after the expiry of their lease period in March 2011 even as the low level of aircraft utilisation added to the losses of the Company.

Thus, renewal of dry lease of four aircraft till May 2014 without factoring in shortage of crew, loss making routes and pay-load restrictions was against the rationale of acquisition of 18 new aircraft and led to unfruitful expenditure of USD 76.39 million[1] (₹ 405.83 crore) between March 2011 and May 2014 towards lease rentals, contribution to maintenance reserves and re-delivery charges.

The Company, in reply, attributed (October 2014) the under utilisation of aircraft to non-availability of pilots due to (i) resignation of expatriate pilots during 2011-12; (ii) implementation of Civil Aviation Requirement (CAR) on Flight and Duty Time Limitations for crew effective from February 2012; (iii) pilot 'strike' during May 2012; and (iv) difficulty in recruiting fresh pilots due to unattractive salary and base of operation being non-metro stations.

The reply is not tenable in view of the following:

- The Board felt (October 2010) that in order to achieve better utilisation, returning the aircraft might be a better option in the prevalent situation such as shortage of crew, loss making routes, payload restrictions etc. The Company was well aware of the crisis of crew shortage but it still went ahead with the renewal of lease which was not only against normal prudence but also violated the objective of acquiring the new aircraft as envisaged in the feasibility report for acquisition of the new aircraft.
- As regards time limitations imposed under CAR effective from February 2012, ADU (FH)/ ADU (BT) during 2012-13 was 6.53/7.43 hours respectively. However, this could have been better managed had the Company not renewed the dry lease of four aircraft. After discontinuance of dry lease of the four aircraft between March and May 2014, ADU (FH)/ADU (BT) during from April 2014 to December 2014 improved from 7.73/8.75 hours in 2013-14 to 9.31 hours/10.58 hours during 2014-15 (upto December 2014).
- Further RASK[2] and CASK[3], the key performance indicators for operations during 2012-13 to 2014-15 (upto December 2014) of AICL are tabulated below:

Year	RASK	CASK
2012-13	₹ 2.51	₹ 2.48
2013-14	₹ 2.80	₹ 2.45
2014-15 (upto December 2014)	₹ 3.24	₹ 2.14

[1] ***Includes Lease rentals for the period April 2010 to May 2014 - USD 64.38 million, Contribution to Maintenance Reserve, net of actual expenditure recouped – USD 4.51 million and Redelivery charges on termination of lease – USD 7.50 million.***

[2] ***RASK – Revenue per available seat kilometre.***

[3] ***CASK – Cost per available seat kilometre.***

As can be seen from the table above, revenue earned per kilometre rose sharply even as the operating cost per kilometre fell during 2014-15. This was on account of, *inter alia*, reduction in number of aircraft.

Thus, the Company ended up incurring unfruitful expenditure of ₹ 405.83 crore between March 2011 and May 2014 on lease related charges on account of improper renewal of dry lease of four aircraft.

The matter was reported to the Ministry in December 2014; their reply was awaited (March 2015).

2.6 Avoidable expenditure on ferry flights to Mumbai for maintenance

Air India Charters Limited (AICL) delayed establishment of hangar project at Thiruvananthapuram and consequently performed the flight maintenance at Mumbai, resulting in avoidable expenditure of ₹ 18.07 crore.

With a view to (a) overcoming constraint of space and difficulties relating to ground movement of aircraft at Mumbai and (b) reducing expenditure on ferrying 'maintenance flights' to Mumbai, Air India Limited (AIL) decided in November 2004 to establish a hangar at Thiruvananthapuram for carrying out major 'C' checks, structural repairs of B-737 aircraft to be operated by its subsidiary *viz.* Air India Charters Limited (AICL) and other narrow body aircraft owned by AIL as well as undertaking third party maintenance work at the facility. AIL had anticipated that engine overhaul, replacement of landing gears, APU overhaul, structural repair of aircraft and components would continue to be carried out at Mumbai for which estimated three flights per week to and from Mumbai would continue and, thus, establishment of hangar at Thiruvananthapuram would reduce number of 'maintenance flights' from 18 to three per week.

AICL launched a low cost airline with B-737 aircraft in 2005 under the brand name Air India Express. It operates its flights from Southern India. As no maintenance facility was available in the South, it had to ferry flights to Mumbai for maintenance of its fleet.

As per internal arrangement between AIL and AICL, it was decided (2008) that civil construction work for the hangar would be done by AIL and equipment would be procured and commissioned by AICL. Land for the hangar was allotted free of cost to AIL by the Kerala State Government in November 2005 subject to the condition that AIL should start physical construction before November 2006. However, construction works were delayed due to delayed payment to contractors resulting in repeated demobilization and remobilization of work force and inter-dependence of works of multiple contractors as against the initial idea of having a single contractor for most of the work.

The civil construction work was finally completed by AIL in June 2012 after incurring an expenditure of ₹ 78.16 crore. Clearances/approvals from Thiruvananthapuram Municipal Corporation for occupancy, Pollution Board, Department of Factories and Boilers, Fire Department, *etc.* necessary for full-fledged operation of the hangar were obtained only by September 2012.

The cost of the equipment required for the hangar was estimated by AICL at ₹ 21 crore[1], against which procurement activity was initiated as early as 2008. Against this, equipment (58 items) worth ₹ 4.99 crore only has been procured till date (January 2015). AICL did not place orders for equipment valuing ₹ 10 crore[2](149 items) due to delay in construction of the hangar and space constraints. AICL decided to stop purchasing further equipment till the hangar jobs were completed. AICL has not procured the remaining equipment till January 2015.

The hangar was partially commissioned in January 2013 to carry out 'C'-checks and phase checks. The shop activities (wheel shop, brake shop, pressure vessel shop and structural repair facility) except battery shop had been partially commissioned by May 2014.

Audit observed the following:

- The intended equipment (estimated cost of ₹ 21 crore) had not been procured by the Company. Equipment worth ₹ 4.99 crore alone were purchased with which some shops were partially operated.
- Even among the equipment valued at ₹ 4.99 crore, equipment (32 items) worth ₹ 2.72 crore had been commissioned since 2012, 19 items worth ₹ 1.12 crore (pertaining to wheel, brake and pressure vessel shops were commissioned only in May 2014) and 7 items worth ₹ 1.15 crore (pertaining to hot bonding and system shops) were either not commissioned or were to be transferred to Thiruvananthapuram from Mumbai.
- Even after incurring an expenditure of ₹ 83.14 crore on the hangar project by AIL and AICL over 2007-14, AICL had to ferry all 'maintenance flights' to Mumbai till January 2013 owing to tardy implementation of the hangar facilities.
- Despite partial commissioning, the number of 'maintenance flights' to Mumbai registered an increase of 12 *per cent* in 2013-14[3], defeating the very objective of establishing the hangar at Thiruvananthapuram in order to overcome the constraint of space and difficulties relating to ground movement of aircraft at Mumbai.
- The Company ferried 2522 flights to Mumbai for maintenance during October 2011 to September 2014 (2011-12: 671 flights, 2012-13: 771 flights, 2013-14: 866 flights and 2014-15: 214 flights) against envisaged ferrying of 468 flights (156 flights per year) to Mumbai for major maintenance.
- Most of the shops so far commissioned were partial and the desired objective of setting up the hangar could not be achieved. The avoidable operating cost incurred on account of ferrying maintenance flights to Mumbai from October 2011[4] worked out to ₹ 18.07 crore considering the operating cost, revenue earned

[1] ***Estimates were based on 2007 prices***

[2] ***Hot bonding shop (30 items), Structural Shop (77 items), Welding Shop (13 items) and Machine Shop (29 items) and the remaining amounts was required for development, modification of different shops.***

[3]***From 771 in 2012-13 to 866 in 2013-14.***

[4] ***As parallel taxi was ready from September 2011, the loss worked out from October 2011.***

including cargo and excess baggage• and scheduled maintenance of 3 flights per week to Mumbai during October 2011 to September 2014.

Thus, even after incurring an expenditure of ₹ 83.14 crore on the hangar project by AIL and AICL over 2007-14, the Company had to ferry all 'maintenance flights' to Mumbai till March 2013 thereby incurring a loss of ₹ 18.07 crore.

AICL stated (October 2014) that:

The delay in commissioning the hangar was attributable to delays caused in vacating the plot *i.e.* rubber factory, boundary dispute with Airports Authority of India (AAI), obtaining approvals from various authorities and delay in executing the work by the contractors. AICL added that there was greater potential to generate traffic in longer routes than operating in shorter routes within Southern region which commenced subsequent to implementation of the hangar at Thiruvananthapuram.

Reply of AICL is not acceptable in view of the following:

- There was no mention of hindrances by AICL when its representatives visited the site in March 2005. Soon after laying the foundation stone (November 2006), the Company undertook the construction work, which indicated that hindrances did not impact the construction work.
- The defunct rubber factory was outside the allotted land and the boundary dispute with AAI towards construction of taxi track did not affect the hangar construction as is evident from internal notes (April 2008) of AIL Project Committee, which stated that the construction work at the project site was proceeding as per plan. Furthermore, pending settlement of boundary dispute and compensation of land, the project was declared as 'completed' by the project committee in February 2012.
- The fact remains that it was AIL's inability to efficiently plan and execute the work through a single contractor by providing necessary resources on time and ready the site as planned that contributed to the delays.

The matter was reported to the Ministry in November 2014; their reply was awaited (March 2015).

Air India Limited

2.7 Review of implementation of Passenger Reservation System and RAMCO Inventory System

2.7.1 Introduction

Passenger Reservation System and RAMCO inventory system are two of the significant information systems in use in Air India Limited (Company). Both information systems are presently functional (PRS since February 2011 and RAMCO since May/ November 2012).

• *Five per cent of Total passenger revenue of ₹239.93 crore.*

Passenger Reservation System: Passenger Reservation System (PRS), end-to-end software, is outsourced to the 'Society for Information Telecommunication Agency' (SITA) and the servers (main and backup) are located at Atlanta, USA. The estimated cost of the project was US$ 185.925 million (₹ 860 crore) spread over 10 years. The system was implemented in February 2011.

The PRS system aims at automating the reservation, ticketing, boarding and baggage functions for Air India. It consists of the following three major functions:

- ***Reservation system*** which covers booking of tickets through various modes (Website, authorized agents, AI's booking windows or through other portals)
- ***Departure Control system*** (DCS) which covers activities related to baggage and boarding.
- ***Frequent Flier Program*** (FFP) which is a reward programme for passengers.

***RAMCO*:** Implementation of RAMCO system for Maintenance, Repair and Overhaul (MRO) activities was initiated (May 2010) at a cost of ₹ 50 crore to meet primary requirements of quality control and technical services, line maintenance, inventory management of the combined fleets for the Company and its subsidiaries. The system was implemented in May and November 2012 in Mumbai and New Delhi respectively. It covers the following activities:

- ***Procurement process*** *including planning, purchase, receipt of material and settlement of bills.*
- ***Inventory Management*** *which comprises of classification, issue, receipt, return and adjustments of inventory, physical verification.*
- ***Repairs and maintenance*** *based on MRO requirements.*

Besides being core functional areas, the information from PRS and RAMCO systems are incorporated into the SAP system for financial accounting.

2.7.2 Audit Objectives and scope

Audit was conducted to review performance of the Company in implementing PRS and RAMCO systems to seek assurance on the following:

- Whether objectives of the two information systems have been achieved;
- Whether the business rules of the Company have been effectively mapped in two information systems; and
- Whether the two information systems have been efficiently integrated with SAP financials.

Transactions for the period 2011-12 to 2013-14 were covered in the audit.

2.7.3 Audit Criteria

Audit criteria was derived from Corporate Rules, Government guidelines, amendment parameters, best practices and System Controls envisaged in the systems in the respective agreements with Vendors.

2.7.4 Audit findings

2.7.4.1 Passenger Reservation System (PRS) - Non finalisation of service level agreement (SLA) with vendor

The vendor (SITA) had agreed to a Service Level Agreement (SLA) for monitoring the system performance in its bid. However, the SLA is yet to be finalized and adopted (June 2014) on account of difference between the Company and SITA regarding methodology for measuring performance. Pending resolution of this dispute, the vendor, SITA reports on key performance parameters (uptime and response time) as per its proposed SLA using its own methodology for Passenger Service System (PSS), Internet Booking Engine (IBE) and Frequent Flyer Programme (FFP).

Audit noticed that while response time of 1.50 seconds has been achieved, the system availability and uptime, as worked out by the vendor, has been consistently below the SLA benchmark of 99.97 *per cent*; the service availability at times went down to 99.35 *per cent* in 2011-12, 99.16 *per cent* in 2012-13 and 99.41 *per cent* in 2013-14.

The Company agreed with the observation. In the Exit Conference (12 November 2014), the Company informed that penalties were being levied on the vendor in line with the agreement for disruptions and outages.

The Company needs to take necessary steps to improve the uptime of PSS as this not only impacted its revenue but also affected its reputation.

2.7.4.2 Delay in uploading pricing decisions

For booking and ticketing through PRS, information on pricing, flight schedules, routes and seats availability are essential inputs. While routes and flight schedules were fed into the system by the Company directly, the pricing information was worked out manually by the Company and transmitted to a vendor. The vendor codified these changes and uploaded it into the Airline Tariff Publishing Company's (ATPCO) system (a common system for all airlines) which made it available globally. The PRS got the pricing input from ATPCO.

The agreement with the vendor codifying and uploading prices stipulated that requests with priority '1', being TOP PRIORITY, should be distributed within 4 hours, those with priority '2' should be distributed within 8 hours and requests with priority level '3' should be distributed within 24 hours.

During April 2012 to May 2014, the Company made 5,017 price revision requests to the vendor. Audit noticed delays of more than one day in 1,876 price revisions (37 *per cent* cases). Delay of more than 30 days was noticed in 19 cases including a delay of 82 days in a single case. Of the 1,876 cases of delay, 100 were Priority 1 cases, *i.e.* where the time period prescribed for uploading the revised prices was 4 hours. Even here, around 30 *per cent* requests were delayed by more than 5 days.

The Company is a price follower in the market and reacts to the market in fixing its price and giving special fare offers. Unless such changes in fares were quickly implemented, they would not have the desired impact on revenue, as by then prospective customers might have already booked with competitors. The delay in uploading the pricing decisions would be detrimental to the airline's business.

It was noticed that PRS had a tool which allowed uploading of pricing information directly rather than be routed through a vendor. This had not been acquired by the Company. Manual intervention by a third party (the vendor) also increased the risk of errors in data entry. Audit noticed an instance of incorrect data entry by the vendor in uploading the price revision. The fuel component in the pricing was incorrectly discontinued for an hour on 19 February 2013. The omission resulted in a loss of ₹ 34.48 lakh for the single hour. Thus, the manual intervention exposed the Company to an additional degree of risk.

The Company replied (November 2014) that a Committee was being constituted to evaluate acquisition of 'Pricing Tool'. In the Exit Conference, the Company accepted the concern and replied that the process was on for acquiring PRS pricing tool, to rectify this problem.

While appreciating the efforts of the Company for expediting price changes and ensuring accuracy, the critical concern regarding errors and delays in manual intervention would remain so long as the key element of pricing remains outside the scope of PRS.

2.7.4.3 Non adherence to credit policy led to accumulation of outstanding dues

The Company offered credit sales to various agents and entered into agreements with them for promoting regional sales. The Company had a policy of terminating the contracts for credit sales with the defaulting agents, at any time on expiry of 30 days after the Company issued notice to the defaulter. The process of appointment and termination of credit contracts, sales reporting and monitoring of the remittance were not under the purview of PRS. The Company manually performed these functions and transmitted the termination requests appropriately to the vendor.

Audit found that there was an accumulation of outstanding dues of ₹ 113.94 crore from various agents for a period exceeding three years. No action had been initiated to block these defaulting agencies or to realize these amounts from defaulting agents. The defaulters continued to sell tickets through PRS, thereby further adding to the dues.

The Company replied (November 2014) that necessary action had been initiated to collect the dues. Alongside efforts to collect outstanding dues, action should also be taken to map the management policy correctly in PRS, thereby blocking further transactions from defaulting agents.

2.7.4.4 Incomplete mapping of Business policy on Companion Free Scheme

There were three classes of travel - the first, business and economy class. Within each class, however, there were various classification of tickets based on 'Reservation Booking Designator' (RBD). Typically there were three RBDs in first class, six RBDs in business class and 16 RBDs in economy class. The fare difference in tickets of different RBDs within the same class could be considerable (for example, the fare in 'Z' RBD in business class for AI 101-Mumbai-New York on 6 February, 2015 was 63 *per cent* of 'C' RBD in the same class).

The Company offered 'Companion Free Scheme' as a promotional measure valid on full IATA fares on all Ex-India international points (except SAARC) wherein the companion of the passenger was allowed to travel free of cost[1], if the passenger had booked tickets under IATA full fare. The scheme specified RBDs for companion ticket depending on the RBD of the paid ticket in each class of travel.

The information on passenger travels availing CFS from January 2012 to December 2013 was reviewed and it was observed that in all 42 cases, the RBD of the free ticket was higher than the RBD specified in the scheme. This resulted in higher RBDs being blocked for sale, thereby decreasing potential for revenue sale.

The Company replied (November 2014) that there was no provision in PRS to restrict the RBD for CFS tickets.

The contention of the Company that PRS did not have the provision of booking tickets in specific RBDs was incorrect. At present all staff tickets were booked in specific RBDs and, therefore, it would be technically possible to restrict RBDs for CFS cases also which would safeguard the revenue interests of the Company.

2.7.4.5 Irregularities in Departure Control Services of PRS

As per the IATA requirements, boarding passes should be issued to passengers during check-in before boarding, with unique consecutive numbers for the leg of travel and in accordance with aircraft capacity. These boarding passes should also be linked to PNR and ticket numbers. It was, however, observed that boarding passes without numbers and without reference to PNR and ticket numbers were being generated by the PRS. Though PRS could block issuance of such boarding passes, this control had not been activated by the Company.

The Company informed that such boarding passes were meant for the crew in order to facilitate their entry into the aircraft, when their regular entry passes were unavailable.

Audit is of the opinion that this practice engendered a significant degree of risk to airport security and had a potential for misuse. As the system allowed printing of boarding passes without reference to PNR/ticket numbers, any intentional manipulation to allow boarding for unauthorised person, could not be ruled out. There had been media reports[2] on seizure

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[1] ***Excluding duties and taxes***
[2] ***Times of India of 22 August 2013 titled, "CBI to probe fake LTC claims racket involving govt, PSUs."***

of blank boarding passes in the LTC scam. Such risks could have been avoided by employing stringent validation controls in the PRS system.

The Company replied (November 2014) that DCS had now been modified to disable acceptance of passengers without associating PNR and e-tickets. The compliance would be watched in audit.

2.7.4.6 Incomplete controls to block violation of Free Baggage Allowance (FBA) policy

The Company offered FBA based on travelling sector and class of journey. The rules in this regard were amended by the Company from time to time as mandated by IATA. As per the baggage policy, in domestic sector, 35 kgs of FBA was allowed for passengers travelling in Executive class and 20-15 kgs is available for Economy class.

In order to ensure mapping of the appropriate baggage rules in PRS, Audit analysed the data for one year (2013-14) on Delhi-Mumbai route in the domestic sector. It was noticed that out of 20,735 passengers who travelled during this period in this sector by AI 605 flight, baggage in excess of norms was allowed for 2,055 passengers. It was seen that in one instance, baggage upto 201 kgs was allowed against a single ticket, without noting it as excess.

Similar uncharged/ unreported excess baggage was noted on international route Delhi - New York also during test check. The system accepted baggage of upto 224 kgs against a single ticket without noting it as excess baggage. The baggage report generated from the system for the flight for the month of May 2014 also did not report any excess baggage.

The PRS system had the provision for building in the control regarding baggage limits which had not been activated by the Company. Implementation of the business rule, thus, was left to the discretion of the booking counter staff, who manually confirmed FBA based on number of passengers under same check-in and charged for the excess baggage if any.

The Company agreed with audit concern and stated (November 2014) that 'automated baggage rule' was under implementation.

2.7.4.7 Contact details of FFP members

For maintaining customer relationship, vital contact details of members, such as mail address, business/home address, contact numbers, should be obtained by the Company from the members. However, audit analysis of data on frequent flyer members, revealed incomplete information in some crucial fields like contact numbers (1,04,129 cases), Home and Business address (9,545 cases) and e-mail address (13,498 cases) with the Company. This stymied the efforts of the Company in providing services to its FFP members.

The Company replied (November 2014) that improvements to data capture are in progress and the system is being upgraded. Further progress will be watched in audit.

2.7.4.8 Non-automation of Frequent Flyer miles updation

An analysis of implementation of FFP policy by the Company indicated that there were instances where the mileage points earned were not automatically updated into the PRS. This resulted in missing miles, resulting in dissatisfaction to the customers and members constantly approaching the Company for updating the missing mileage points.

While this could be due to omission or incorrect membership identity provided by the passenger, it was frequently on account of slippages by the airline:

- incorrect entry made by the airline staff at reservation or check-in level;
- omission in closing the flight preventing entries from departure control system into FFP; and
- non-matching of names between FFP membership and tickets.

The Company replied (November 2014) that onus to provide correct information was with members and also claimed that the success rate of automatic credits into the system was 85 *per cent*.

Reply is not convincing as success rate of automatic credits claimed by the Company was limited to the data which DCS could pass into FFP and not on the overall FFP miles earned.

2.7.5 RAMCO inventory system

2.7.5.1 Planning and acquisition of RAMCO system

(a) Delay in implementation

The Company's Board approved (November 2007) the capital expenditure of ₹ 27 crore towards implementation of RAMCO systems for MRO with a plan to complete the implementation in 18 months. There was a delay of more than 2 years in the tendering procedure. Owing to non-adherence of commercial procedure, the Company had to re-tender after CVC adversely commented on the tendering process.

Board re-approved (May 2010) the revised capital expenditure of ₹ 50 crore with anticipated completion by November 2011 resulting in additional cost of ₹ 23 crore. The system was implemented only in May 2012 (in Mumbai) and November 2012 (in New Delhi) with a delay of 6 months to 1 year.

(b) Incomplete implementation

Despite pending application changes on shop and line maintenance, Engineering change management, Hangar maintenance and shop maintenance, the 'Go live' was declared. This necessitated additional payment of ₹ 69.18 lakh (which was likely to increase further with future expenditure till the completion of agreed tasks) to the vendor for further changes in the system. Further, the vendor had committed for integration with Oracle Financials in its bidding document. With implementation of SAP Financials, the requirement was now for integration with SAP. However, integration of RAMCO and SAP systems is not covered in the contracted scope of work. The integration of RAMCO with SAP has not been achieved till date (January 2015).

The Company stated (November 2014) that the roll out into production was on hold due to taxation issues[♣] in RAMCO. The reply is not tenable in view of the fact that 'Go live' was declared before completion resulting in payment for any subsequent changes/implementation thereof. Moreover, the current RAMCO version implemented in the Company does not support integration with SAP. The Company would have to implement a higher version involving additional cost to achieve such integration.

2.7.5.2 Lack of segregation of duties

(a) Purchase orders (PO) and repair orders (RO)

Purchase Orders and Repair Orders issued from RAMCO system from May 2012 till June 2014 were analyzed in Audit. It was observed that out of 44,178 orders worth ₹ 5,449.21 crore issued during this period, 7,171 orders constituting 16 *per cent* of the orders, amounting to ₹ 136.04 crore, were created and approved by same user. It was also noticed that the system allows the same user who initiated and approved the order to receive the material. Four such instances where a single user initiated, approved and received the materials were noticed in Audit. Lack of segregation of duties and responsibilities left the system vulnerable besides rendering it non-compliant to the business rules of the Company as recorded in their Purchase Procedure manual.

The Company replied (November 2014) that user roles and authorizations were well defined in the system but due to shortage of staff the same had not been implemented completely.

Audit is of the opinion that circumventing segregation of duties in a computerized system due to shortage of staff compromised internal controls and suitable corrective steps were needed to be taken by the Company.

(b) Stock corrections

Stock corrections (changes in quantity or attributes of the material) were made in RAMCO inventory system manually based on periodical physical verification as well as changes in classification of the inventories. The related accounting entries (debit or credit adjustment entries) in the inventory register were carried out automatically by RAMCO system.

Audit analysis of the stock corrections for the period May 2012 to June 2014 revealed that a total 18,471 correction entries had been entered manually or passed automatically in the system. These corrections led to reduction in stock worth ₹ 50.19 crore in the inventory register. Out of these 18,471 corrections, 16,378 corrections were carried out manually during this period based on physical verification. Ninety-eight *per cent* of these corrections (16,152 corrections) had been initiated and authorized by the same user identity in contravention of the duties and responsibilities as stipulated in the Company's manuals.

♣ ***Taxation issue due to establishment of Air India Engineering Services Limited (AIESL) as a separate entity and any inventory movement across the Company and its subsidiaries attracts taxes***

RAMCO system had made 2,093 automatic corrections in the inventory register during the same period. Variances were observed between the manual changes entered and their corresponding debit/credit adjustments passed by the system, indicating lacunae in the in-built system logic.

The incorrect assignment of segregation of duties coupled with the faulty system logic were the kind of significant risks that need to be addressed. An incorrect correction entry passed in the system affects the stock position, impacts inventory valuation and could result in wasteful procurement despite availability of stock.

The Company replied (November 2014) that the system had the capability to define authorization levels as per financial delegation and it was being implemented now. The corrective steps taken by the Company would be watched in Audit.

2.7.5.3 Inventory purchased in excess of the requirement

The Purchase Procedure manual and policy guidelines of the Company described the sequence of events for procurement. Effective control over procurement would imply that the material(s) ordered were in line with the requirement and that the material(s) received were as per order. Undue purchases as well as short receipts compromise the financial interests of the Company.

Audit analyzed all the 27,485 PRs and their subsequent POs placed during the period May 2012 to June 2014 and found that in 10 *per cent* (2,835) of POs, the quantity ordered by the purchase department was more than the quantity requested by the user department.

The Company (November 2014) attributed it to minimum order quantity (MOQ), to avail price benefits and for combining multiple requests into a single order. It is, however, noticed that RAMCO system did not document MOQ for materials nor was the consolidation of multiple requests apparent in the system. Maintenance of a master file with MOQ details, reorder levels *etc.*, and linking it with actual procurement would enable the Company to better reap the benefits of automation. Besides, linking cases where purchase requests have been combined would improve the transparency of the system.

2.7.5.4 Discrepancies in intra stock transfers and receipts

RAMCO inventory system was a combined system for the Company and its subsidiaries. Intra and Inter Company transfer of stock, therefore, was inbuilt into the system. Such transfers should be carried out with appropriate accounting of the stock movement and stock closing, to enable proper accounting of the same.

Audit analyzed the stock transfers during May 2012 to August 2012 and noticed that 3,547 stock transfer orders were issued for transferring 22,394 units of inventory worth ₹ 36.55 crore. Stock transfer orders, stock issued and received did not match as seen below:

Stock transfer orders	**Stock issued**	**Stock received**
22,394 units	21,628 units	18,366 units

As the above recorded status related to December 2014, *i.e.* after two years of issue of transfer orders and subsequent actions in May-August 2012, stock was not expected to be in transit. The significant difference (15 *per cent*), between the stock issued and received, was a matter of concern. The differences occurred in 208 stock transfer orders with the quantity transferred recorded as 3,364 units by the transferor unit while the corresponding quantity received was only 102 units, raising doubts on the location of the balance 3,262 units transferred during the limited three month period alone.

Audit also noticed that in case of 95 stock transfer orders issued during May – August 2012, the order had been treated differently by the transferor and the transferee. While the order had been designated 'closed' at the transferring end signifying its completion, the corresponding status recorded at the receiving end was either 'partially received' or 'not received'. The opposite situation was also noticed where only partial transfer had been recorded at the transferring end while the receiving end depicted the material as having been 'Completely Received'. This raises doubts on the integrity of the inventory register and left scope for the possibility of additional un-authorized transfers.

The Company replied (December 2014) that the audit analysis pertained to the migration period. The Company further stated that the stock transfers were three dimensional with three variables such as stock transfer order, stock transfer issues and stock transfer receipts, and hence, the transactions should be viewed with keeping transfer order and issue constant and receipts as variable.

Reply is not acceptable since audit analysis of the stock transfers during September 2013 also revealed similar discrepancies.

Suitable corrective steps are needed to be taken by the Company as these discrepancies could significantly affect the inventory accounting of the Company.

2.7.5.5 Improper inventory valuation

During migration of inventory from earlier inventory systems of Air India and erstwhile Indian Airlines Limited, inventory held in stock, serviceable (₹ 256.46 crore) and unserviceable (₹ 527.37 crore), without applicable weighted average cost in the earlier system were migrated with the latest weighted average costs. Similarly, old inventory (₹ 57.76 crore) was brought back to stock by adopting latest weighted average rate. This altered the inventory position following migration. This had also been commented by the Statutory Auditors while auditing the accounts of 2012-13.

The Company replied (November 2014) that though the legacy data was updated and cleansed to some extent, it was not completed and to certain extent necessary correction entries were carried out during 2013-14. The reply is not tenable since this had resulted in overvaluation of inventory, contrary to the Accounting Policy of the Company as well as Accountant Standard 2.

2.7.5.6 Incomplete inventory migration

During migration, the system was programmed to take the date of migration as date of last movement for opening balances, thereby impacting classification of inventory as non-moving/ slow moving. This resulted in continued dependency on the legacy system.

The Company stated (November 2014) that due to lack of fields to capture last movement date, RAMCO had updated the non-moving flag based on legacy data.

The reply confirmed the Company's continued dependence on the legacy system.

2.7.5.7 Improper stock position of Companies

The Company implemented a single inventory system (RAMCO) to optimally utilize the inventory across the Company and its subsidiaries. There was a mis-match between the physical stock of spares inventory held in RAMCO against the Company and against its subsidiaries vis-a-vis the closing stock inventory accounted for as on 31 March 2013, in the books of respective companies, as given below:

(₹ in crore)

Company	RAMCO	Accounts	variation
Air India NB	716.42	740.96	24.54
Air India WB	447.11	421.26	-25.85
AICL	74.56	76.17	1.61
CD	9.54	9.23	-0.31
		TOTAL	**-0.01**

The Company stated (October/November, 2014) that precision of accounting was being maintained on a global basis and attributed the variation to changes in the part account group.

Reply is not acceptable as the part account group was coded for aircraft model, the type of inventory and were uniquely identifiable with the corresponding company through the company code available in the system. During any movement of inventory among the companies, the system should automatically update the concerned fields. Non-reconciliation of company-wise (Holding Company and the Subsidiaries) inventory indicated that the segregation possible through unique company codes had not been utilised by the Company.

The Company, agreeing with the observation, replied (November 2014) that the vendor had been approached to provide system executable accounting reports for finalizing the accounts for the year 2013-14 and also to provide monthly accounting entries tallying with the year-end summary. However, the issue was yet to be addressed as was evident from the continuance of discrepancies in the 2013-14 accounts:-

(₹ in crore)

Company	Inventory system	Accounts	variation
Air India NB	1995.72	1971.07	-24.65
Air India WB	775.03	790.19	15.16
AICL	177.18	186.75	9.57
CD	30.85	31.31	0.46
		TOTAL	**-0.54**

Suitable remedial action is needed to be taken by the Company to ensure that correct inventory position against the respective companies could be depicted, thus maintaining the integrity of accounts of the Company as well as its subsidiaries.

2.7.6 Integration issues

2.7.6.1 Non-integration of PRS and RAMCO with financial accounting system

Both PRS and RAMCO systems provided essential data for preparing the financial statements of the Company. However, they did not have a direct interface with SAP Financials.

PRS generated the revenue information on passenger reservations and departures which was the major component of revenue of the Company. PRS system, however, did not have a direct interface with the SAP financial module and the information was transmitted from PRS via Kale revenue accounting system. Significant problems regarding functioning of Kale revenue accounting system had been noticed which impacted the financial statements of the airlines.

RAMCO provides the inventory details which needed to be incorporated in SAP for financial accounting. In the absence of an automatic interface with SAP, information was manually entered into SAP. During the year 2012-13 alone, 82,630 manual entries to the extent of ₹ 1,14,747.76 crore were passed into SAP Financials impacting several accounting heads such as inventory and its related provisions (₹ 974.73 crore), Fixed Assets and Depreciation (₹ 250.99 crore), Revenue From Cargo, Passenger, Mail, GSA (₹ 125.26 crore) and Travel Expenditure, Passenger Amenities and Hire Charges (₹ 1082.60 crore). Such large volumes of manual entries into SAP enhanced risk of errors and omissions.

The Company, agreeing (November 2014) with the audit observation, stated that non-integration of systems necessitated passing of manual entries in the system, apart from rectifications which necessarily needed to be passed manually. The Company also assured Audit that integration of RAMCO with SAP would be carried out in the next phase.

While the progress would be watched in Audit, the Company could have avoided such integration by implementing an integrated system from the start as such a system was available even then.

2.7.6.2 Interface of passenger revenue with Financial Accounting

Accounting Policy of the Company on revenue recognition was in line with Accounting Standard 9 which stipulated that passenger revenue was to be recognised when transportation service was provided *i.e.* on flown basis during an accounting year.

The data relating to passenger revenue processed by Kale consultants and reservations made for the month of March 2013 was analysed in Audit. It was observed that in 5,804 cases, date of travel was either prior to or subsequent to the accounting year 2012-13 and, hence, ought not to have been considered for revenue accounting for 2012-13. Besides, date of travel recorded in the revenue data processed by Kale consultants was inconsistent with the ticket details as well as the actual flight details recorded in the PRS (as confirmed through a test check of some cases vis-à-vis the PRS system).

Audit noticed that the discrepancy occurred due to an error of Kale consultants. While Kale consultants had sourced the data from PRS, they had wrongly used the date field from the 'remarks' column rather than the 'date flown'. As a result, SAP Financials overstated the revenue for 2012-13 by ₹ 5.37 crore• for travel beyond the accounting period, contrary to the policy of the Company.

The Company replied (July 2014) that as per standard industry practice, revenue was recognized based on the actual date of travel, considering the start of such flights that may cover more than a day. The Company also stated that the difference in travel dates were due to change of travel date by the passenger.

The argument of journeys starting on more than a day is not acceptable as Audit observed difference of more than 6 months in travel dates. In 926 instances the difference between the two dates was more than 2 days and went upto 365 days.

What is of concern is that the discrepancy had continued to affect revenue accounting even in 2013-14 as Kale consultants continued to use incorrect dates of travel. In 1305 cases, the date of travel was prior to date of issue of tickets indicated a flaw in revenue accounting.

2.7.6.3 Inconsistency in Revenue Accounting reports

The Company was dependent on Kale Consultants for its revenue accounting as well as for generating MIS reports. Considerable differences were observed in the information received as MIS vis-à-vis revenue accounting information. The revenue recognized in the SAP Financials, as sourced from Kale consultants, for the year 2012-13 was ₹ 12,557.15 crore. During the same period, MIS reports provided by the same agency indicated a much lower revenue earned as ₹ 12,420.31 crore.

The difference of ₹ 136.84 crore generated from the two systems had not been reconciled. It is pertinent to note that amount of revenue earned as per MIS reports was lower than the final revenue recognized even though the MIS reports included an element of provisional revenue to cater to omission of any bookings 'not flown' into revenue accounting during the generation of MIS reports. The inconsistency in revenue earnings between the MIS reports and SAP accounting needed to be corrected.

Reply of the Company was still awaited (March 2015).

2.7.6.4 Retrieval of sales data – Productivity Linked Bonus (PLB)

Productivity Linked Bonus (PLB) is paid by the Company to eligible agents based on international flown revenue generated by them. The Company depends upon Kale Consultants for this information as the PRS does not have necessary provisions for data

• ***Against the total revenue of ₹ 12,557.15 crore*** extraction. Based on the data provided by Kale Consultants, qualified agents were offered PLB for 2012-13 by the Company.

Subsequently (October 2012), the Company realized that the data provided by the Consultant included tickets issued by them on other carriers as well. The revised data revealed that 22 agents earlier qualified were ineligible for PLB as they had not achieved the minimum productivity slabs.

The Company replied (November 2014) that since no reports were available in PRS, PLB was paid based on the reports obtained from outsourced vendor and assured that due care would be taken to randomly check the data to safeguard its financial interests.

Conclusion

Failure on the part of the Company to design and activate necessary controls in the Passenger Reservation System and the Inventory System, inappropriate customization, lack of validations in line with business processes and improper data migration resulted in the Company not achieving the full potential of the automated systems. The Company resorted to manual interventions and had a high degree of dependence on multiple vendors. Lack of an integrated system coupled with the manual interventions and weak security controls exposed the system to the risk of manipulations, unauthorized use and unreliability of data.

Air India Limited and Air India Charters Limited

2.8 Avoidable expenditure due to under-utilisation of own simulators

Air India Limited and its subsidiary viz. Air India Charters Limited failed to optimally utilize its own simulators for want of proper planning and maintenance, which resulted in avoidable expenditure of ₹ 8.47 crore during July 2009 to March 2014 on purchase of simulator slots at third parties' simulators for training the pilots.

As a part of the aircraft purchase agreements entered into by Air India Limited (AIL) and its subsidiary Air India Charters Limited (AICL) with M/s Boeing, USA in January 2009, the supplier (M/s Boeing, USA) agreed to provide simulators for B-777 aircraft to AIL and B-737-800 aircraft to AICL for training the pilots. The market price of the B-777 and B-737-800 simulators provided free of cost was ₹ 64.43 crore and ₹ 44 crore respectively. While the simulator for B-737-800 aircraft was installed in February 2007, simulator for B-777 aircraft was installed in December 2009.

AIL and AICL had been purchasing slots on B-777 and B-737-800 simulators from third parties for training their pilots for these aircraft. With the installation of own simulators, it was expected that the airlines would not be required to purchase simulator slots from third parties, thereby saving on costs and also hire out the spare capacity of simulators to third parties for earning revenue.

As per AIL, a simulator can be used optimally for 20 hours a day. Normally, a simulator session lasts for four hours and five sessions can be planned in a day. The remaining four hours are kept for preventive maintenance. Thus, available hours on a simulator in a year are 7300.

Audit examination revealed that:

(i) Both the airlines planned utilization of lesser number of hours than the available capacity of the simulator. Actual utilisation was even less than the planned number of hours. Due to the gap between available capacity and actual utilisation, coupled with time lost in breakdown of the simulators (apart from the allowance of four hours per day for their maintenance), both the companies resorted to purchase of simulator slots from third parties. The available, planned, utilised and number of hours for which the simulators of third parties were hired by both the airlines during 2009-10 to 2013-14 is tabulated below:

Year	Available capacity (Hours) at the rate of 20 hours per day	Planned (Hours)	Percentage of available capacity planned	Utilised Hours	Percentage of available capacity utilised	Usage of simulator of third parties (Hours)
B-777 of AIL						
2009-10*	1800	856	48	826	46	230
2010-11	7300	5739	79	5196	71	939
2011-12	7320	6627	91	5884	80	730
2012-13	7300	6124	84	5039	69	1224
2013-14	7300	5146	70	4286	83	36
Total:	31020	24492	-	21231	-	3159

B-737-800 of AICL						
2009-10#	5680	3803	67	3597	63	361
2010-11	7300	5402	74	4616	63	418
2011-12	7320	6281	86	5437	74	20
2012-13	7300	5349	73	4076	56	0
2013-14	7300	4998	68	4389	88	0
Total:	34900	25833	-	22115	-	799

**** January 2010 to March 2010*** ***#July 2009 to March 2010***

Thus, the simulators were never planned for utilization for more than 91 *per cent* of their available capacity. While actual utilisation remained consistently lower than plan, the highest utilisation being 88 *per cent* of plan.

(ii) Considering an allowance of 6,204 hours♠ for preventive maintenance, AIL should have planned the simulators for 31,020 hours from January 2010 to March 2014. However, the airline planned it for 24,558 hours. Thus, there was significant gap of 6,462 hours between available and planned capacity of the simulators. Actual utilisation was further less by 3,363 hours than the planned hours. The gap was mainly due to unserviceable simulator, 'pull out'/ 'no show' of crew/instructors, which indicated deficient preventive maintenance during the inbuilt allowance for 6,204 hours, defective planning and management on the part of the airline. As a result of reduction in number of B-777 aircraft from 20 in (2009-10) to 15 (2013-14) due to sale and grounding of aircraft, the

♠ ***At the rate of 4 hours per day.***

training requirement for the related crew had reduced which increased the prospects of hiring out the simulator to other parties for earning revenue. However, AIL failed to take any initiative for hiring out the spare capacity (6,462 hours) to third parties.

(iii) Similarly, in the case of simulator available with AICL, the airline planned its simulator's utilisation for 25,833 hours, against the available hours of 34,900, thus, leaving a gap of 9,067 hours, in addition to 6,980 hours available for maintenance during July 2009 to March 2014. The airlines actually utilised the simulator for 22,115 hours with a further gap of 3,718 hours. In addition to 6,980 hours available for repairs/maintenance of the simulator, it remained unserviceable for 2,734 hours. For the gap of 9,067 hours between the available and planned capacity of the simulator, AICL also did not explore possibility of hiring out the simulator to third parties for earning revenue.

(iv) Instead of utilising the optimum capacity of their own simulators, both the airlines had purchased simulator slots for 3,958 hours from third parties *viz.* Jet Airways in Mumbai, Egypt Air Training Centre in Cairo and Emirates CAE Flight Training in Bangaluru during the same period (2009-10 to 2013-14) by incurring an avoidable expenditure of ₹ 8.47 crore.

AIL replied (February and November 2014) that:

- Available hours on the simulator cannot be utilised unless the requirement of the training days equals the same. This requires careful scheduling of crew and training of officers. If for any reason, any one of the above is 'out of sync', it will result in non-utilisation and the hours would lapse on that count.
- Mostly urgency for time bound refresher course and training for pilot proficiency check/instrument rating was dictated by Director General of Civil Aviation (DGCA).
- Induction of new aircraft and launch of line-operations puts immense strain on the training department. A total of 20 (Nos.) B-777 aircraft were inducted between 2007 and 2010. To ensure adequate utilisation of aircraft, it was considered better to train pilots at a higher and quicker rate using other simulator facilities. Also due to induction of B-787 aircraft, replacement pilots had to be trained.
- In house infrastructure, including simulators should be utilised to optimum capacity to ensure minimum cost of training. However, this also should be supported by adequate number of instructors. In the absence of sufficient numbers of instructors, it would not be possible to train large number of pilots within a limited period of time. Also AIL's attempts to recruit instructors have borne limited success.
- It was not financially viable to keep a large pool of instructors employed, since training was a cyclical phenomenon. That was also the reason that during peak times, it was prudent to hire outside simulators and complete training tasks within restricted time frames.

The reply is not acceptable in view of the following:

- The contention that induction of 20 B-777 aircraft put the AIL's training department under pressure and it led to outsourcing of training is not convincing as the very purpose of installing B-777 simulator in December 2009 at Mumbai was to impart training on regular basis to B-777 pilots as AIL was going to procure these aircraft.
- The argument of inadequate instructors is not established as AIL deployed its own instructors on Jet Airways simulator for training its pilots.
- Though the requirements of training as well as vacancies in 'flight instructor' cadre were well known to AIL, these posts were advertised for recruitment during April 2009 to January 2013. The airline advertised only 6 posts in February 2013, out of the shortfall of 74.
- In an airline such as AIL operating several types of aircraft, training is an ongoing process and not cyclical. Durations for Conversion Training[1], Recurrency Training[2] and Line Training[3] are well defined by DGCA and fully within the knowledge of the AIL and, therefore, could be planned in advance.
- Outside simulator facility was used continuously and not exceptionally. Inability to coordinate between its own departments to ensure optimal utilisation of own simulator facility for fulfilling training requirements indicated the need for improvement in planning and management of training needs.

AICL replied (November 2014) that:

Under-utilisation of B-737-800 simulator was due to shortage of instructors and un-serviceability of the simulator due to various factors such as computer problems, shortage of spares, maintenance of air-conditioner, power fluctuations. AICL added that while the simulator was under service, training at outsourced party was resorted to, since training of pilots is a continuous critical function and non-adherence to it would lead to idling of pilots as well as under utilisation of aircraft. However, AICL assured that all efforts were being made to cut down on the use of outside simulator.

Reply of AICL substantiates the audit concern that simulators were not maintained properly for optimal utilisation despite an allowance of four hours per day towards preventive maintenance. Moreover, in contradiction to the reply regarding cutting down external simulator usage, audit observed that a tender had been floated on 27 October 2014 to invite bids from parties offering their simulators for wet/dry B-737-800 simulator for imparting training to AICL's pilots, which indicated that AICL was again planning for outsourcing simulator training.

Replies of AIL and AICL did not state specific reasons for planning the simulators for substantially less number of hours than their available capacity and raise serious concerns about the entire planning process for acquiring the simulators.

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[1] ***For imparting training to pilots on a particular aircraft type.***
[2] ***For validation of licences of pilots.***
[3] ***For imparting training to qualified pilots on flying mode.***

Thus, while their own simulators of the two airlines remained under-utilised due to lack of proper planning and maintenance, simulator slots were being purchased and the pilots were being sent for training to third party simulators which resulted in avoidable expenditure of ₹ 8.47 crore.

The matter was reported to the Ministry in December 2014; their reply was awaited (March 2015).

CHAPTER III: MINISTRY OF COAL

Bharat Coking Coal Limited

3.1 Avoidable payment of penal interest

Bharat Coking Coal Limited repeatedly failed to pay the deployment charges of Central Industrial Security Force in time and consequently incurred avoidable payment of penal interest to the tune of ₹ 16.84 crore for delayed payment of dues for the period March 2005 to July 2013.

Bharat Coking Coal Limited (BCCL), a subsidiary of Coal India Limited (CIL) is a Central Public Sector Undertaking engaged in mining of coal and allied activities. BCCL deploys Central Industrial Security Force (CISF - a Central Para Military Force under the Ministry of Home Affairs, Government of India), on payment of deployment charges which include salary, allowances and other expenses**,** to meet the security requirement of its various coal mining projects located in Jharkhand and West Bengal. The deployment of CISF is governed by the guidelines of Ministry of Home Affairs (MHA), CISF Induction and Policy Manual 2000 and Memorandum of Understanding (MOU) signed between CISF and BCCL from time to time.

MHA issued guidelines in May 2005 underlining the need for timely payment and recovery of cost of induction of CISF in PSUs. As per the above guidelines, penal interest would be levied if a PSU defaulted in payment of monthly dues by more than one month at the rate of 2 *per cent* above the Prime Lending Rate (PLR) as decided by Reserve Bank of India from time to time. The interest would be levied with effect from 1 April 2005 on PSUs where CISF had been inducted and also in cases where existing strength of CISF was augmented on or after 20 August 1993. In case of PSUs where induction/ augmentation had taken place prior to 20 August 1993, interest at the above rate would be charged with effect from 1 April 2005, if they failed to clear the outstanding dues accumulated upto March 2005 within three months from the date of notice for payment. These guidelines were brought to the notice of all concerned for recovery of interest in case of default in payment.

Audit examination (July 2014) revealed that BCCL repeatedly defaulted in making payment of monthly dues towards salaries and other expenses of CISF personnel deployed at various locations. Delays in payment after due date ranged between 1 and 415 days. Consequently, through demand letters between August 2009 and October 2013, CISF made a claim of ₹ 16.84 crore as penal interest for delayed payment of monthly dues to its personnel for the period March 2005 to July 2013. However, BCCL did not agree to make such payment and represented (August 2013) to MHA for waiver of the above claim of CISF. Representation of BCCL was turned down by MHA in November 2013 on the ground that "the charging of penal interest in case of default/delayed payment was an integrated part of the terms and conditions of CISF deployment and hence, it was not possible to exempt the penal interest." The Board of Directors of BCCL finally decided (January 2014) to make the payment of penal interest and accordingly, BCCL made a payment of ₹ 16.84 crore as penal interest to CISF in March 2014.

While accepting the audit contentions, BCCL stated (December 2014) that:

- Salaries and other expenses of CISF were based upon the MOU signed between BCCL and CISF from time to time and the same was a contractual liability of the Company.

- The then BCCL Management had managed their funds judiciously when there was financial crisis for discharging its liabilities.

- Being a BIFR company, BCCL had to move as per BIFR plan and only statutory payment, and expenditure which was the most important component to maintain the production level and to avoid industrial unrest, got priority.

- Since BCCL operated in a highly accident prone mining condition, in the event of occurrence of any such contingencies as well as precautionary measures, the fixed deposits of the Company were kept intact to meet such contingent requirement.

The contention of BCCL was not convincing as:

- The representation of BCCL for waiver of penal interest was duly considered and rejected by MHA. Further, safeguarding property of the Company through CISF was a critical issue for the organization and as such expenses on CISF should have been considered an obligatory expenditure of BCCL.

- Salaries and wages of BCCL's own employees which stood in the range of ₹ 1751.52 crore and ₹ 4465.65 crore during 2005-06 to 2013-14 were never defaulted.

- Except suffering loss in 2007-08 and 2008-09, BCCL made an annual average profit of ₹868.98 crore during the same period and was also regular in making repayment of loan to CIL at the rate of ₹ 20 crore per month.

- At the request of BCCL, CIL had provided assistance of ₹ 60 crore as interest bearing loan @ 6.5 *per cent* for meeting CISF dues of BCCL in March 2005. However, no further persuasion thereafter for seeking assistance of CIL (carrying lower rate of interest) was made by BCCL.

Thus, due to delayed payment of CISF dues by BCCL without adhering to the guidelines of MHA resulted in an avoidable outgo of funds on account of penal interest to the tune of ₹16.84 crore for the period from March 2005 to July 2013 to CISF.

The matter was reported to the Ministry in January 2015; their reply was awaited (March 2015).

3.2 Wasteful expenditure on procurement of Two Road Header Machines

Bharat Coking Coal Limited had made payment to a foreign supplier for procurement of two Road Header machines which were not in conformity with NIT specifications. The machines were not approved by DGMS for operation in the coal mines though the same were under field trials for a considerable period. Expenditure incurred on procurement amounting to ₹ 11.16 crore became wasteful.

Road Header machine is used in the underground mines of coal companies for excavation of coal and development of roads for the purpose of preparation of panel in mining. Specifications of the machine should conform to the mining conditions for operation in underground mines. Approval of Director General of Mine Safety (DGMS) is mandatory for safe mining which is accorded to supplier on successful completion of field trial and satisfactory performance reports of the machine during field tests in actual mining conditions monitored by DGMS.

Bharat Coking Coal Limited (BCCL) invited (June 2006) a Global Tender for procurement of two Road Header machines for its Moonidih Project of Western Jharia Area. In response, four firms submitted their offer but none of them was found technically qualified. A fresh tender was invited in April 2008. As per the pre-bid meeting (March 2008) held with the prospective bidders, some modifications were made in NIT which, inter alia, included that the machine should be approved by DGMS, India and if any bidder had neither valid DGMS approval nor field trial permission, they had to obtain field trial permission for use of the machine in the mines of BCCL well in advance before despatch of the same. Further, in case of imported supplies, 80 *per cent* value of each machine would be paid against Letter of Credit (LC) which would be opened after receipt of authenticated copy of valid approval or field trial permission accorded by DGMS along with the relevant despatch documents.

In response to the above NIT (April 2008), only two offers were received, out of which one offer was not qualified for technical scrutiny which was thus, carried out for only one offer received from a foreign firm (Supplier). During evaluation of the offer, the Supplier categorically stated (October 2008) that the main equipment did not have DGMS approval for use in underground mines in India and it was assured that they would take necessary DGMS approval before its use and also necessary field trial permission would be obtained before despatch from the country of origin. Based on the clarifications received, the offer of the Supplier was accepted by the Tender Committee and the same was approved (July 2009) by BCCL Board on single tender basis for ₹ 22.94 crore[1] . As per the supply orders issued (July 2009), the two Road Header machines were received and unloaded at Moonidih Project on 28 July 2011 and BCCL made a payment of ₹ 11.16 crore[2] during the period July 2011 to September 2012 for procurement of the two machines, out of which ₹ 8.49 crore was paid to the Supplier and its agent on 11 July 2011 and 21 July 2011 respectively.

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[1] *comprising value of two machines, agency commission, spares cost for three years, duties and taxes, commission, installation and training charges including service tax*

[2] *included 80per cent value of two machines and agency commission of ₹ 7.79 crore and ₹ 0.70 crore respectively, custom duty of ₹ 2.52 crore, ocean freight of ₹ 0.12 crore and ₹ 0.03 crore for escort charges, bedding charges, handling charges and insurance.*

Examination in audit revealed that:

- At the time of commissioning of the Road Header machines, the General Manager of Moonidih project refused (December 2011) to accept the machines on the ground that the height of the Road Header machines was not as per the specification of supply orders; this fact was also established during joint inspection carried out (December 2011) in presence of the Supplier.

- The Supplier admitted (April 2012) that if the machines were not found acceptable, the same should be sent back to their workshop at China at the cost of BCCL for making suitable modification to the height but obtaining DGMS approval thereafter would be the sole responsibility of BCCL. However, the conditions imposed by the Supplier were not found acceptable to the Committee constituted (April 2012) for the purpose in BCCL to settle the dispute.

- The Committee finally opined that if the Supplier ensured suitability of the machine for operation in mines where the seam thickness ranged from 1.9 metre to 2.9 metre, the payment already made to the Supplier would not go waste. Though the Supplier agreed to the above condition, the Road Header machines were yet to obtain DGMS approval and were under field trial till date (July 2014) despite lapse of three years since their receipt in Moonidih Project.

- As per clause No. 17 of NIT, BCCL had the option to conduct inspection and test at the premises of the Supplier at the point of delivery before shipment to detect non-compliance of any specification. The above clause also permitted the purchaser to conduct inspection on arrival at site which would be considered 'final'. As BCCL had not conducted pre-inspection at Supplier's end, it lost the opportunity to detect non-compliance of height specification before despatch and consequently to avoid release of payment of 80 *per cent* of the value of the two machines, agency commission and related expenditure which was made prior to delivery of machines at project site. Major payment on FOB[♦] value of the machines had already been made to the Supplier and hence inspection at Moonidih Project and detection of defects afterwards did not protect the financial interest of BCCL. It was a situation of fait accompli for BCCL to accept the defective machines.

- Though the Supplier agreed to take back the machines to their workshop at China for necessary modification, BCCL did not succeed in pursuing the Supplier to make necessary arrangements to meet specification requirements, free of cost, as per the conditions under Clause No. 17 of NIT.

- Performance bank guarantee of ₹ 2.29 crore accepted from the Supplier was not sufficient to recover the amount (₹ 11.16 crore) which was paid before the delivery of the two Road Header machines, which subsequently found defective.

♦ ***Free on Board - indicates the passing of ownership and risks to the buyer at the port of shipment upon payment for the cost of goods which includes marine freight transport, insurance, unloading and cost of transportation from the arrival port to the final destination etc.***

- Experiencing the above, BCCL Board had decided that in future purchases, a clause relating to submission of additional bank guarantee equivalent to LC payment before opening the LC would be incorporated in NIT so that in case of any rejection, cost of LC opening amount could be recovered immediately. This decision was dictated by hindsight.

While accepting the audit observations, BCCL stated (April 2014) that:

- The advertised Global Tender was floated for procurement of two Road Header machines from proven manufacturers, i.e., the machine produced by the manufacturer was already put in use either in India or abroad with satisfactory performance. Payment terms in NIT were made on the basis of provisions of purchase manual of Coal India Limited taking into consideration the proven-ness of the manufactured goods. In case of procurement of plant and machinery from manufacturer of proven nature, inspection is done after commissioning of the same at site. Pre-despatch inspection at manufacturer's site was not mandatory as per NIT and supply order.

- Since DGMS approval was mandatory for use of such machines in underground coal mines in India, clause relating to "Field Trial permission of DGMS" was incorporated before delivery of the machines from foreign port for safeguarding the interest of BCCL.

- Ownership of machines was transferred to BCCL immediately as they were shipped on FOB basis. Had the request of the Supplier to send the machine back to their workshop at China been agreed to, the ownership of the Road Headers was required to be re-transferred in the name of the Supplier and in that case BCCL would have been at much higher risk as 80 *per cent* of the FOB price of the machines (₹ 11.16 crore) had already been paid and also goods not being in the custody of BCCL, it would have resulted into unavoidable situations.

- The terms of NIT and bank guarantee stipulation were made as per the purchase manual. Since such instances were not experienced in the past and the issue did not emerge during pre-bid meeting, provision of bank guarantee equivalent to 80 *per cent* of FOB value in the contract was not conceived.

Ministry re-iterated (December 2014) the views of the management furnished in April 2014.

The contention of BCCL/Ministry is not acceptable in view of the following:

- As per chapter – IX, clause 9.3 of the Purchase Manual of Coal India Limited, 80 *per cent* payment may be considered for supply of equipment for the suppliers whose equipment were considered proven for supplies to CIL and its subsidiaries and to be accepted only for regular supply orders placed for the proven equipment. The Road Header machines supplied by the foreign firm were only having the field trial permission which was provisional in nature and did not have final approval of DGMS for operation in the coal mines in India. As such, the interpretation of 'proven manufacturer' made by the BCCL in the instant case was not appropriate. Proper and timely due diligence in framing terms and conditions of the NIT would have avoided the incident.

- Though final approval of DGMS was mandatory for use of machine in the mines, the terms and conditions set in NIT for payment to Supplier without ensuring DGMS approval were against the financial interest of BCCL. Release of 80 *per cent* payment to the Supplier based on the field trial permission was thus imprudent.

- BCCL had itself admitted that the ownership of the machines was transferred to it as soon as machines were shipped on FOB basis and there was risk in sending the machines back to Supplier. It is obvious that pre-despatch inspection and adequate provision of bank guarantee equivalent to 80 *per cent* of FOB value could have protected the financial interests of BCCL.

- The fact remains that Road Header machines were still lying inoperative (November 2014) since May/June 2013 for want of compliance with various observations of DGMS. The machines were under field trial even after a lapse of three years since their receipt.

Thus due to inept contract management, BCCL had to incur a wasteful expenditure of ₹ 11.16 crore on procurement of two Road Header machines that were lying idle for more than 3 years with little prospects of their gainful utilization.

South Eastern Coalfields Limited

3.3 Operational Performance of Dankuni Coal Complex

3.3.1 The Dankuni Coal Complex (DCC) was established at a cost of ₹ 147 crore in 1990 as a unit of Coal India Limited (CIL) based on the recommendations of the Fuel Policy Committee, 1974 of Government of India (GOI), and the Working Group No. 9 and 10 of the Planning Commission (1974). Later, CIL handed over DCC to South Eastern Coalfields Limited (SECL) for running the plant on operating lease basis in April 1995 and renewed lease subsequently at an annual lease rent of ₹ 7.50 crore followed by further renewal of lease w.e.f. 01.04.2010 at Re. 1 per annum.

3.3.1.2 The objective of setting up DCC, a low temperature carbonization (LTC) plant, was to produce environment friendly coal gas[1]/coke/tar and other coal derived by-product chemicals from non-coking coal for domestic and industrial use. The Plant includes Coal Handling Plant for crushing and screening coal into coal fines and obtaining sized coal, Retort Plant for heating up coal to produce coal gas, Gas Cleaning Plant for cleaning coal gas and separating tar, light oil and other impurities from the gas and a Gas Holder for storing gas. There are other utilities like the Gas Compressor for compressing and cooling the gas for taking out further impurities and the Effluent Treatment Plant (ETP[2]) for treatment of the toxic effluents.

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[1] ***Coal gas/town gas is a flammable gaseous fuel made by the destructive distillation of coal.***

[2] ***ETP is a plant designed to treat the effluent coming from different areas of the plant out of production process.***

3.3.1.3 An attempt was made in Audit to assess whether the Unit operated efficiently and economically while fulfilling the objective for which the Unit was established and included an examination whether:

- the targeted level of production was achieved;
- the equipment was properly maintained and utilised;
- effective marketing mechanism existed;
- proper pricing of products was ensured;
- regular review of the state of the plant was done; and
- environmental requirements were fulfilled.

3.3.1.4 Audit reviewed the accounts and records of DCC pertaining to last five years ie. from 2009-10 to 2013-14. Recommendations of the Fuel Policy Committee (1974) of GOI, recommendations from the Working Group No. 9 and 10 of the Planning Commission (1974), projections in the Feasibility Study on the unit, revised cost estimate for the unit, decisions of the Boards of CIL and SECL for the approval of various agenda items w.r.t. functioning of DCC, and reports submitted by external agencies on various functional areas of the unit were studied in Audit.

3.3.2 Audit Findings

3.3.2.1 Analysis of the operating results of DCC for the five years ended 31 March 2014 **(Annexure-I)** revealed that contributions from operations were in the range of only 18 *per cent* to 27 *per cent* of the income from sales proceeds. This could recover the fixed cost to the extent, at an average of 70 *per cent* only. As a result, contribution failed to recover even the fixed cost of the unit, approximately in the range of ₹ 5 crore to ₹ 31 crore during 2009-10 to 2013-14, which led to enhancement of operating loss to the equal extent during the same period.

3.3.2.2 The expenditure of DCC for the period 2009-10 to 2013-14 relating to pay and allowances, maintenance charges, plant running expenses and town administration expenses was as depicted under:

(₹ In Lakh)

Year	**Pay and allowances**		**Maintenance Charges**		**Plant running Exp.**	**Establish ment Exp.**	**Town Admn. Exp.**
	Exec	**Non-Exec**	**Capital**	**Revenue**			
2009-10	743.89	2129.19	-	423.74	11378.27	1157.80	30.00
2010-11	675.52	2406.15	-	486.75	11979.54	356.83	30.42
2011-12	729.62	3214.68	-	496.22	15151.97	392.69	47.18
2012-13	810.13	3543.30	-	724.51	12822.94	534.93	73.09
2013-14	810.85	4007.69	19.01	764.99	14735.79	600.35	95.85

From the above it transpires that despite sustaining substantial amount of loss, DCC could not adopt any conscious cost saving measures with a view to reducing annual financial deficit. While revenue expenditure on salaries and maintenance was on the rise, there was no capital expenditure on plants.

SECL contended (February 2015) that DCC always incurred bare minimum expenditure which was essential to run the plant with safety measures.

However, it was noticed that establishment expenses and town administration expenses were on an increasing trend which implied that no effective cost cutting measures were implemented by the management.

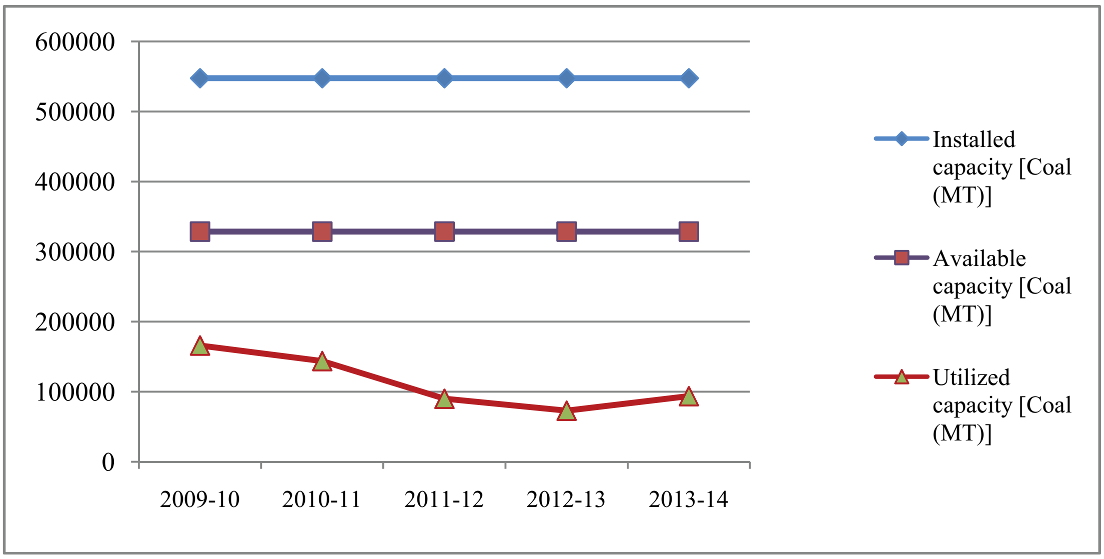
The accumulated loss of DCC stood at ₹ 650.97 crore as on 31 March 2014. The reasons for the loss can be traced to the issues as follows:

3.3.2.3 Under utilisation of plant capacity

Considering installed capacity of 1,500 tpd (ton per day) throughput of coal for 365 days in a year, i.e. 547500 MT coal in a year, the percentage utilised out of available throughput capacity (328500 MT) of DCC was in the range of 22 *per cent* to 51 *per cent* and, on the other hand, percentage utilized out of installed capacity was in the range of 13 *per cent* to 30 *per cent* in the last five years ended on 31 March 2014 **(Annexure-II).**

Chart 1

Capacity utilization at DCC during 2009-10 to 2013-14



The target for production of coal gas and coke were fixed below the level of available capacity. Moreover, gas, coke and coke fines, the major products of DCC, were produced below the target fixed during the last five years ended on 31 March 2014, as projected in **Chart 2, 3** and **4**.

Chart 2
Production of coal gas during 2009-10 to 2013-14 (in Nm^3)

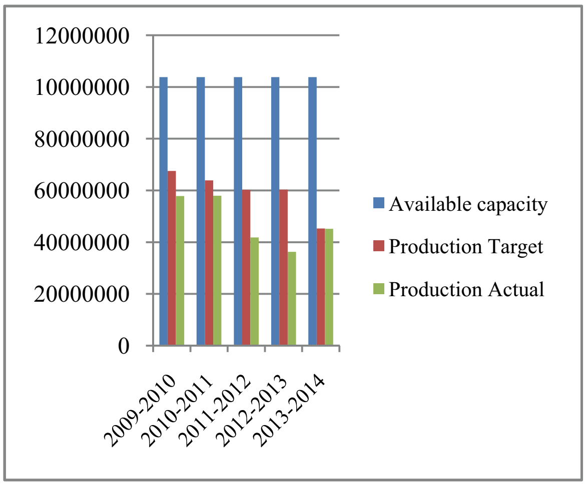


Chart 3
Production of coke during 2009-10 to 2013-14 (in MT)

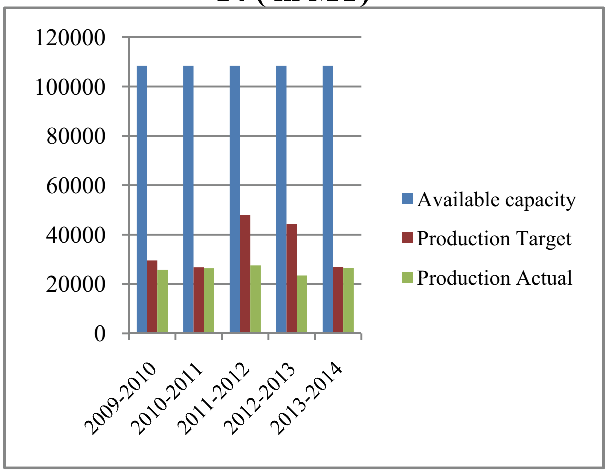
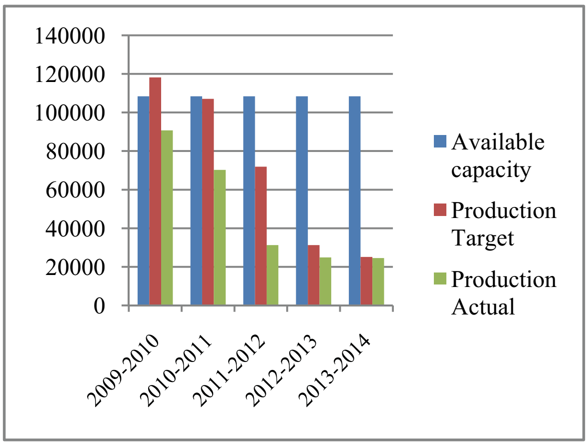


Chart 4
Production of coke fines during 2009-10 to 2013-14 (in MT)



It is seen in Audit that only a portion of the available capacity for coal gas and coke was planned as production target (in the range of 35-56 *per cent* and 56-75 *per cent* respectively)**.** Moreover, under performance against target was as high as 40 *per cent* for coal gas, 47 *per cent* for coke and 57 *per cent* for coke fines**.** This has resulted in loss of potential production to the extent of 5,81,35,249 normal cubic meter♠ (Nm^3) coal gas, 45,771 MT coke and 1,11,862 MT coke fines with an opportunity of earning potential revenue of ₹ 24.69 crore, ₹ 43.10 crore and ₹ 39.75 crore respectively during 2009-10 to 2013-14. Details are indicated in **Annexure-III**.

♠ ***Normal cubic meter is the metric expression of gas volume at standard conditions and it is usually defined as being measured at 0 °C and 1 atmosphere of pressure.***

Audit observed that the reason for underperformance in all areas of production was endemic to DCC since inception of the plant. Though established in 1990, CIL had decided (1995) to hand over the unit to SECL on rent as the plant had not been able to achieve financial viability and was beset with problems such as low capacity utilisation, low off-take of coke and gas and sourcing of raw materials. By 2000, the plant had already completed the normal life of a chemical plant of its kind and needed renovation. However, SECL could not accomplish the attempted capital rehabilitation for DCC till date. High landed cost of coal and consequential high cost of production of gas coupled with non-remunerative price of gas and failure of marketing of by-products resulted in continuing accumulated losses, as detailed in the subsequent paragraphs.

3.3.2.4 Delay in capital rehabilitation of the Plant

DCC was commissioned in May 1990. The normal life of a chemical plant like DCC is envisaged to be ten years only. CIL had expressed its desire to lease out or sell DCC and the Ministry of Coal accorded the approval (December 2000) for the same.

After a delay of almost seven years, a meeting was held on 26 June 2007 under the Chairmanship of Hon'ble Minister of Commerce & Industry, Govt. of West Bengal with the representatives of CIL, Hindustan Petroleum Corporation Limited (HPCL) and Ministry of Petroleum & Natural Gas, GoI for finding a way out for revival of DCC. Accordingly, CIL Board in its 235th meeting (25 September 2007) accorded the approval for entering into a Joint Venture (JV) by CIL (23 *per cent* share) with HPCL (51 *per cent* share) and Govt. of West Bengal (26 *per cent* share) for DCC.

However, in due course Govt. of West Bengal expressed their unwillingness to take part in the JV due to its financial crunch. Thereafter, HPCL appointed M/s SBI Capital Markets Limited (SBI CAPS) to carry out a detailed study of financial, legal, accounting and tax due diligence as well as valuation of DCC. SBI CAPS recommended that (November 2008) ₹ 69.03 crore was required for land purchase or ₹ 63.68 crore for land lease option by HPCL for acquiring 51 *per cent* stake in DCC. DCC would enter into a formal agreement with Greater Calcutta Gas Supply Corporation Limited (GCGSC), a Government of West Bengal undertaking and the sole distributer of coal gas in and around Kolkata for adequate supply of coal gas, on an 'arms-length' basis. CIL/SECL would execute the deed of transfer for transferring the land presently under the possession of DCC to the proposed JV with proper title and free of any encumbrances. CIL/SECL would obtain the revalidation/ renewal of all the relevant certificates/ consents/ approvals required from various statutory authorities in order to ensure smooth operations of the plant.

CIL Board considered (December 2008) the revised JV proposal with equity participation of HPCL (51 *per cent*) and CIL (49 *per cent*) along with due diligence report prepared by SBI CAPS. After more deliberations and setting up of a subcommittee, CIL held a meeting (April 2009) with HPCL and SBI CAPS, where HPCL expressed eagerness to complete the formation of JV and also establish Gas Distribution Pipelines network before emergence of any new player/competitor to capture the virgin gas market in West Bengal. HPCL also requested CIL for immediate decision and execution of draft Memorandum of Understanding (MoU) at the earliest for formation of the proposed JV. Agenda papers for Board meetings of CIL that were made available to Audit for the period 2009-10 to 2013-14 revealed no progress in the matter and nothing affirmative could be ascertained from the reply (November 2013) furnished by SECL.

Meanwhile, in January 2005, DCC submitted a capital rebuilding scheme to SECL which envisaged augmentation of production capacity of gas to the extent of 4,50,000 Nm^3 per day planned to be achieved under three phases with proposed total capital investment of ₹ 58.83 crore. Later, DCC twice re-submitted modified revival plans, in 2005 and 2012 which were not supported by cost benefit analysis.

Revival plan for rebuilding of Retort Benches and enhancement of gas production to the extent of 2,75,000 Nm^3 in phased manner, involving capital investment of ₹ 54.17 crore in DCC, was submitted (June 2012) in SECL Board. It was seen in Audit that during 2009-10 to 2013-14, SECL and CIL held 43 and 58 Board Meetings respectively. No concrete decision regarding rehabilitation of the plant was taken as seen from test check of records.

SECL management stated (November 2013/January 2014) that the revival plan worth ₹54.17 crore had been under consideration and further action would be taken only after revision of price of co-products like coke, coke-fines, de-hydrated tar, etc and disposal of piled-up stock of these products. Further, in February 2015, it was stated that SECL was contemplating comprehensive capital rehabilitation and drawing out a roadmap for it in the form of upgradation of technology/adoption of new technologies.

The fact, however, remains that SECL as controlling authority of DCC failed to take any action so far to implement the revival plan which was necessary to bring DCC into economic health.

3.3.2.5 Procurement of poor quality coal at higher landed cost

As per the Feasibility Report (September 1977) of the unit, coal was proposed to be purchased from the collieries[1] of Eastern Coalfields Limited (ECL) as coal from these collieries was considered to be conducive to the Plant in terms of ash content, volatile matter and moisture. DCC, therefore, used to procure raw coal from ECL since inception.

In April 1995, DCC was handed over to SECL by CIL on operating lease basis since it had not achieved financial viability. CIL specified a need to identify adequate quantity of appropriate coal from alternative sources and endorsed sourcing coal from collieries[2] of SECL while handing the unit over.

However, contrary to the purpose envisaged, on test check of records it was noticed that coal received from different collieries of SECL included coal fines and stones, which could not be fed into the Retort Plant. Further, procured coal, especially from Bhatgaon and Amlai area of SECL contained higher moisture and ash leading to lower calorific value[3] of the products.

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[1] ***JK Nagar, New Kenda and Sripur colliery***

[2] ***West Chirimiri, Korba, Baikanthpur, Amlai, Bishrampur, Jamuna & Kotma, Bhatgaon and Hasdeo.***

[3] ***Calorific Value is the amount of heat produced by the complete combustion of a material or a fuel.***

Audit observed that DCC had to incur average railway freight for G4 & G5 (ROM) coal as high as ₹ 1440 per MT during 2009-10 to 2013-14, resulting in high landed cost of coal at DCC (as high as ₹ 5283 per MT during 2009-10 to 2013-14), as collieries of SECL are situated more than 800 kms from DCC. Thus, Audit had pointed out (August 2013) that during the period, 20-37 *per cent* of the landed cost of coal was towards railway freight as indicated in the table under:

Year **(1)**	**Landed cost of coal per mt including freight (₹)** **(2)**	**Freight charges per mt (₹)** **(3)**	***per cent* of Freight charges over Total landed cost of coal** **(4)=(3/2)*100**
2009-10	2930.65	1102.18	37.60
2010-11	3319.59	1097.58	33.06
2011-12	5282.73	1091.60	20.67
2012-13	4334.71	1292.39	29.81
2013-14	4581.04	1441.56	31.47

While accepting the contention of Audit, SECL stated (November 2013) that DCC had already started procuring coal from ECL (Raniganj) since September 2013 to bring down the landed cost of coal. SECL worked out the difference in cost between coal procured from ECL and SECL to be in the range of ₹ 1000 per MT approximately.

Thus, it was only after the issue was flagged in Audit (August 2013), that DCC started procuring coal from ECL since September 2013 while continuing to procure coal from SECL too. DCC, therefore, lost the opportunity of potential savings in railway freight of ₹ 138.45 crore during 2009-10 to 2013-14 (**Annexure-IV**) by not procuring coal entirely from ECL. It was further seen that upto March 2014, DCC had been able to prevent loss of revenue to the tune of ₹ 10.50 crore on account of freight charges only by procuring coal from ECL since September 2013.

3.3.2.6 Absence of a formal agreement between DCC and GCGSC leading to non-remunerative pricing of coal gas

DCC commenced its commercial production in May 1990. MoU was signed (May 1990) between DCC and GCGSC for supply of gas indicating therein the price offered by GCGSC. Accordingly, price of coal gas was fixed at ₹ 8.50 per therm[1] excluding sales tax and the same was applicable for a promotional period of one year only. It was also decided that the price would be reviewed jointly amongst GCGSC, DCC, representatives of Govt. of West Bengal and GoI after six months of commencement of supply of gas. However, with a view to fetching remunerative price for coal gas, the then CMD, CIL, suggested (April 1979) a price escalation formula[2] which was duly accepted (May 1979) by the Govt. of West Bengal. The MoU was valid for a promotional period of only one year, i.e. upto April 1991. No further MoU was entered into between the parties

[1] unit of heat energy approximately the energy equivalent of burning 100 cubic heat of natural gas

[2] $P_f = P_i\{0.35 + 0.4*C_f / C_i + 0.1*E_f / E_i + 0.05*L_f / L_i + 0.1*Ch_f / Ch_i\}$; where C stands for Coal, E stands for Power, L stands for Wages and Ch stands for Chemical prices.

thereafter. Though GCGSC is the only distributor of DCC produced coal gas, there is no legal agreement in existence between the two parties. Hence, business between the parties was carried out without any valid agreement. Though GCGSC proposed (December 2003) to enter into a legally enforceable agreement, DCC abstained from taking any initiative (December 2003) in this direction, and rather emphasised on immediate revision of coal gas price. There was no concrete decision on the part of DCC towards reframing of MoU or entering into a legal agreement with GCGSC (till December 2014).

However, it would appear that DCC could have been in a better position had it accepted the proposal (December 2003) offered by GCGSC for drafting a legally enforceable agreement covering every aspect mutually beneficial to both the parties.

As far as CIL is concerned, it only participated in a meeting (18.03.2004) where representatives of DCC, SECL and Govt. of West Bengal were also present. CIL showed its concern for non-remunerative price of coal gas for DCC but at the same time declared that it (CIL) was not in a position to substantially invest in DCC's revival. Further, no effective role of CIL in regard to DCC was found on record.

Audit observed that the price of coal gas has been revised and fixed solely by the Government of West Bengal from time to time unilaterally only after series of requests from DCC that the same was not remunerative enough as depicted under:

Year & Month	**Prices of coal gas per therm (in ₹)**	**Cost of production of coal gas per therm (in ₹)**
Upto: 1996 July	8.50	-
w.e.f: 1996 August	9.50	-
1997 November	11.50	-
1999 November	13.00	-
2000 September	14.00	-
2002 February	15.40	-
2004 January	17.00	-
2004 October	19.19	-
2006 February	22.00	-
2008 January	25.00	47
2010 April	30.00	47
2010 November	33.00	62
2011 September	38.00	91/93
2014 January	45 to 85 (progressive)	81

It would be observed that in 18 years, price of coal gas had increased only around 500 per cent. In the meanwhile, within a span of six (6) years, the per therm cost of production of coal gas at DCC went up by almost 200 *per cent*, being ₹ 47 in 2009-10, ₹ 62 in 2010-11, ₹ 93 in 2011-12, ₹ 91 in 2012-13 and ₹ 81 in 2013-14, which was not matched by the prices allowed. Thus, DCC had to bear loss during 2009-10 to 2013-14 arising out of dispatch of gas to GCGSC to the tune of ₹ 112.83 crore **(Annexure-V*)*.** There was, as such, insufficient incentive for DCC to enhance its production as more production would have meant more loss.

However, after the issue was flagged in Audit (August 2013), the price of coal gas has been increased (December 2013) to ₹ 45 per therm with progressive increase in rate with increase in demand, upto a maximum of ₹ 85 per therm w.e.f. January 2014. It was further noticed that even after the price was revised in 2014, the per therm cost of production of coal gas was ₹81 in 2013-14. Therefore, in spite of the continuing accumulated loss, the company was able to earn additional revenue of ₹3.33 crore from January 2014 to December 2014 as a result of the latest price revision giving it partial relief. But this price revision was also not sufficient to cover the gap between the cost and the sales price.

It is pertinent to mention that GCGSC charged prices as high as ₹51/ therm, ₹ 110/ therm and ₹ 100/ therm, retaining margins of ₹ 25/ therm, ₹ 55/ therm and ₹ 54/ therm from Domestic, Commercial and Industrial consumers, respectively, during 2009-10 to 2013-14 (**Annexure-VI**).

DCC while accepting the facts, stated (August 2013) that though price of gas was reviewed by GCGSC from time to time, the specific formula-based review of the price was never done jointly by DCC, GCGSC, Government of West Bengal and Government of India.

Though the matter of fetching remunerative price of coal gas was regularly taken up in the meetings and discussions with GCGSC and SECL, it was not taken up with CIL and GOI. However, on being pointed out (August 2013) by Audit, the issue was taken up with the Government of West Bengal only in December 2013.

Thus, scrutiny of records made available in Audit revealed that DCC/SECL did not make any serious effort to escalate the issue to the level of CIL and Government of India earlier than August 2013 so as to fetch remunerative price for coal gas though the same was incumbent on the part of DCC for its survival.

3.3.2.7 Low offtake of gas against committed demand by a single customer and consequent flaring of gas leading to loss

Feasibility Report (September 1977) of DCC indicated that Government of West Bengal would arrange for uniform offtake of coal gas. Later, GCGSC, a Government of West Bengal undertaking became the sole customer of DCC coal gas with the finalization of MoU (1990) which was to be valid for a promotional period of one year. GCGSC was only to distribute the same to the ultimate consumers in industrial, commercial and domestic sector in and around Kolkata. GCGSC set up a PRS[♣] inside the Plant area of DCC for drawing coal gas for distribution.

The position of production, supply vis-à-vis loss of coal gas for last five years ended on 31 March 2014 was as follows:

♣ ***Pressure Reducing Station (PRS) is set up alongside gas pipelines to filter out ingresses of solids and liquids and to control the gas pressure to bring up the same to the contractual specifications for delivery.***

(In Lakh Nm^3)

Year	Production	Supply	Gas loss due to flaring and venting
2009-10	578.42	549.47	28.94
2010-11	579.80	557.87	21.93
2011-12	418.34	413.80	4.56
2012-13	363.01	358.27	4.71
2013-14	451.61	440.28	11.35
TOTAL	**2391.18**	**2319.69**	**71.49**

In this regard, Audit observed that GCGSC did not draw gas against committed demand in several occasions (December 2008, March 2009, January and February 2014) which led to the flaring and venting of coal gas to the extent of 71.49 Lakh Nm^3 during the period 2009-10 to 2013-14. This also created environmental problems leading to complaints by local people. DCC stated (September 2013) that gas production is based on demand of GCGSC being the sole distributor of gas. Thus, when GCGSC's demand fluctuated, especially during the weekends and holidays and GCGSC did not alert DCC about the low demand well in advance, DCC could not control the production which, in turn, resulted in flaring of gas.

The fact, however, remains that DCC /SECL management had never done a detailed techno-economic feasibility study including a strategy for direct marketing of gas based on proposed demand of coal gas by prospective customers**.** Also, a scientific marketing strategy for the products of DCC needed to be adopted at the earliest to prevent wasteful flaring of gas and enhance its customer base to ensure its commercial viability.

3.3.2.8 Unsuccessful modernisation efforts

DCC uses the 'Continuous Vertical Retort' supplied by M/s Woodall-Duckham Limited, United Kingdom (UK) since inception.

It was noticed in Audit that formation of a Joint Venture (JV) between Gas Authority of India Limited (GAIL) and CIL was proposed (September 2011) by GAIL for setting up a coal based synthetic natural gas (SNG) production facility by utilizing the existing facilities at DCC for enhancing production of coal gas with advanced technology. Even, on recommendation of the Government of West Bengal, Ministry of Coal, Government of India directed CIL to examine the proposal of aforementioned JV floated by GAIL. However, no action was initiated by GAIL in this regard in view of the following uncertainties:

- The plant, being a very old one, was to be replaced with a new one, but land for the new unit was not available.
- The existing system was not considered suitable for SNG.

Further, it was also noticed that CIL advised (August 2012) SECL to invite an open Expression of Interest (EOI) for upgradation of the plant and to select one from the interested parties. But, no further step was taken by SECL in this regard.

SECL, in their reply, (November 2013 and January 2014) did not offer any comment on the above observation of Audit.

However, at the behest of SECL (October 2013) DCC took up the matter with Central Institute of Mining and Fuel Research, Dhanbad (CIMFR) with a view to exploring new initiatives for modernization. In this regard CIMFR suggested (July 2014) that before taking up the work of technological upgradation and modification, it would be prudent to opt for detailed technical assessments and marketing analysis. No further development in this regard was observed by Audit (February 2015) from DCC/SECL management and modernization efforts remained unfruitful.

3.3.2.9 Low yield of by-products coupled with poor dispatch

During the process of operation, DCC produces various by-products like coke, coke fines, coal fines, coal tar, ammonium sulphate and light oil which are obtained as by-products while producing coal gas so as to effectively utilize the raw coal. The yield of the by-products from one tonne of coal as per the pre-operational (1976) norms as well as the latest available (July 2011) norms fixed by SECL vis-à-vis actual production is indicated below:

Year	Coal consumption (in Thous-and MT)	Coke			Coal Tar			Light Oil		
		Norms 1976 (660 kg) (in Thous-and MT)	Norms 2011 (670 kg) (in Thous-and MT)	Actual (in Thousand MT)	Norms 1976 (40 kg) (in Thous-and MT)	Norms 2011 (55 kg) (in Thous-and MT)	Actual (in Thous-and MT)	Norms 1976 (----)	Norms 2011 (3.6 Litre) (in Thous-and Ltr.)	Actual (Ltr.) (in Thous-and Ltr.)
2009-10	346.82	228.90	232.37	25.78	13.87	19.08	8.75	-	1.25	0.34
2010-11	319.70	211.00	214.20	26.36	12.79	17.58	7.87	-	1.15	0.33
2011-12	263.50	173.91	176.55	27.57	10.54	14.49	5.29	-	0.95	0.31
2012-13	260.23	171.75	174.36	23.47	10.41	14.31	4.44	-	0.94	0.22
2013-14	297.28	196.21	199.18	26.47	11.89	16.35	3.66	-	1.07	0.28
Total		**981.77**	**996.66**	**129.65**	**59.5**	**81.81**	**30.01**	**-**	**5.36**	**1.48**

From the above, it is evident that production of by-products was far below both pre-operational and latest available norms.

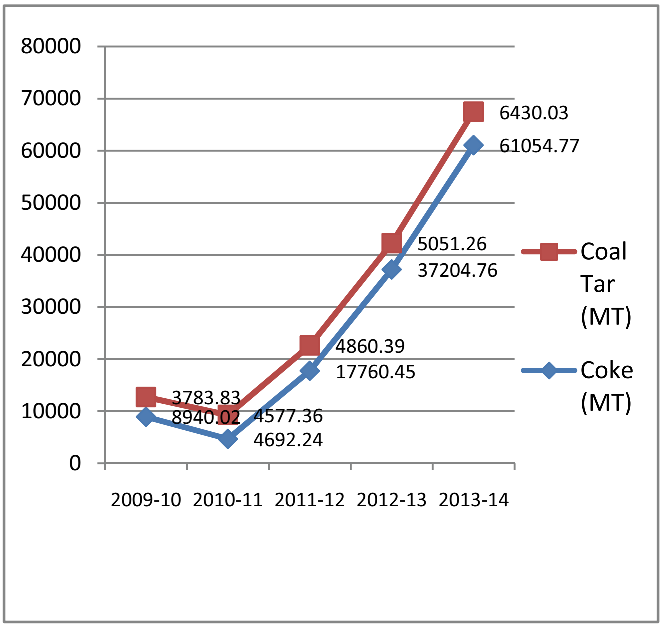
Records revealed that even though production was below the norms, revenue generated through sale of by-products constituted a substantial amount of revenue realised out of total sale of all products. This was as high as 74 *per cent* (2009-10) of the total sale proceeds of DCC in the last five years ended on 31 March 2014 **(Annexure-VII)**.

In the light of the above, Audit observed that during the concerned period, as yield of by-products, particularly coke, coal tar and light oil was far below the norms, DCC suffered loss of opportunity to earn revenue valuing ₹ 663.26 crore (867005 mt), ₹ 188.10 crore (51813 mt) and ₹ 9.48 crore (3879 kl) respectively **(Annexure-VIII).**

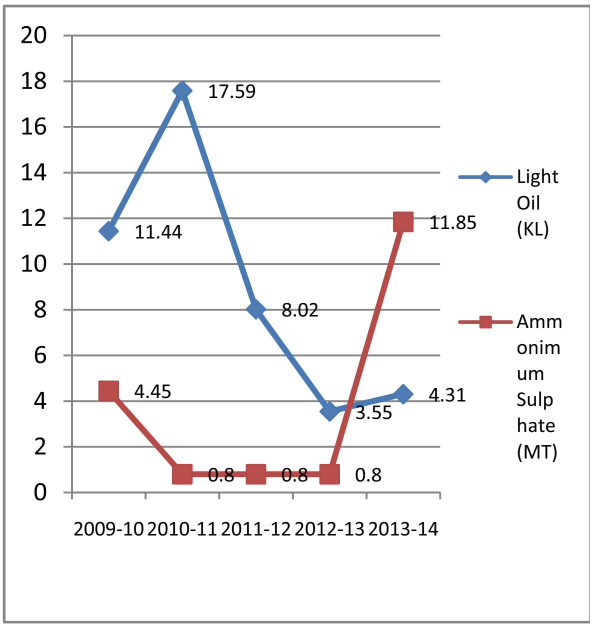
It is also pertinent to note that effective marketing by DCC would have helped it to recover a portion of its loss. However, in the absence of competitive rates, DCC could not insist on the customers for regular lifting even by lowering the prices of products and offering rebate.

Therefore, though there was potentiality of earning revenue on sale of by-products, DCC could not tap that as it did not augment coal gas production. Even the produced by-products were accumulating as stock on year to year basis **(Annexure-IX)** which can be seen from the graphs given below:

Year-wise position of closing stock of coke and coal tar



Year-wise position of closing stock of ammonium sulphate and light oil.



Audit observed that DCC neither explored the possibility of getting new buyers nor insisted on the existing customers to lift products regularly resulting in huge accumulation of stocks. DCC attributed (September 2013) the reason for low off take of by-products to poor demand on account of low fixed carbon content of products coupled with higher price.

Thus, in the absence of quality control as mentioned above as well as a professional and innovative marketing strategy, DCC was deprived of benefits from liquidation of accumulated stock of by-products.

3.3.2.10 Faulty effluent discharging system resulting environmental pollution

While issuing environmental clearance, the Ministry of Environment and Forests (MoEF), Government of India stipulated (April 1989) that the regulations made by the West Bengal Pollution Control Board (WBPCB) must be adhered to rigorously. Hence, as a measure to control environmental pollution, DCC commissioned (1990) an Effluent Treatment Plant (ETP) of 1000 cubic meter (m^3)/ day capacity. During the operation at

DCC, toxic chemical wastes are generated, which needed prior treatment through ETP, before disposing of the same to Dankuni Canal and thereafter to the Ganges.

However, ETP set up by DCC was inadequate to treat its effluents as per pollution control norms of WBPCB. Inspite of denial of consent to operate by WBPCB several times (in 2003, 2004 and 2005) and notice from the Hon'ble Kolkata High Court (October 2004), early steps on urgent basis were not taken by DCC in this direction. This ultimately resulted in non-issuance of consent to operate and a notice for closure (July 2010) by WBPCB.

Audit observed (February 2015) that though the requisite statutory charges (₹ 6.50 lakh towards consent to operate for the period 2013-15, ₹ 35,328 quarterly towards water cess and ₹ 7,800 towards collection and analysis of effluents) are being regularly collected by the State (WB) environment body, the closure notice had not yet been revoked.

It was also noticed that National Environmental Engineering Research Institute (NEERI), Nagpur suggested (January 2010) construction of a new ETP of 1300 M^3/day capacity for upgradation at an estimated cost of ₹ 3.92 crore (approx.), later revised at ₹ 7.09 crore. SECL Board also accorded approval to the same (June 2011). While tender prepared by CMPDI was floated in December 2011, it could not be finalized (February 2015). Thus, there was lack of action and commitment on the part of DCC/SECL in improving the situation towards adhering to statutory requirements.

In reply, SECL stated (November 2013) that the updated cost-estimate of new ETP was under preparation in consultation with CMPDIL and NEERI. It was further admitted (February 2015) by SECL that exceptionally long time is taken for scrutinizing the technical and commercial aspects of tender papers as offered by the parties for this "*never-done-before-item*" and therefore could not be further taken up with the Government of West Bengal, GCGSC, WBPCB and the like.

The Ministry stated (February 2015) that initiatives were being taken to address the issues raised by Audit.

Conclusion

DCC was established to produce coal gas, coke, coal tar and other chemicals from low temperature carbonization of non-coking coal with a view to producing environment friendly coal gas and coke for domestic and industrial use. Audit, however, observed that since inception DCC did not operate efficiently to achieve financial viability. The Unit has been sustaining substantial loss as it operated far below its installed capacity in the absence of capital infusion towards revival/capital rehabilitation of the plant coupled with outdated technology, poor offtake of gas by customer, non-remunerative price fixed by customer, poor sale of by-products and absence of marketing strategy. Moreover, DCC did not take effective measures to control environmental pollution. Thus, neither DCC, nor SECL or CIL took any coordinated and productive steps to address the core issues pointed out above which would have helped DCC to get its financial health restored.

Recommendations

In view of the above, Audit recommends that:

- ***SECL/CIL may guide DCC for putting in place well defined cost cutting measures which may also be monitored periodically.***
- ***SECL/CIL may take up the issue of pricing of coal gas with Government of West Bengal and Ministry of Coal to ensure reasonable fixation of price which would help DCC/SECL in gainful recovery of cost.***
- ***DCC may enter into a formal agreement with GCGSC, West Bengal with a view to fetching remunerative price of coal gas and also explore adding alternative consumers.***
- ***SECL/ CIL may assist and guide DCC in putting in place professional/ innovative marketing strategy for liquidating accumulated stock of by-products.***
- ***DCC/ SECL may expedite the process of commissioning new ETP, with the aim of making operations environment-friendly.***

Coal India Limited and its Subsidiaries

3.4 Irregular payment towards encashment of Half Pay Leave/Earned Leave/Sick Leave

Encashment of half pay leave/sick leave/earned leave in deviation from DPE guidelines, resulted in irregular payment of ₹ 75.29 crore.

In line with the Department of Personnel & Training, GOI guidelines (October 1997) enhancing the ceiling for accumulation of Earned Leave (EL) to 300 days for Central Government employees, DPE allowed (August 2005) enhanced accumulation of EL up to 300 days for the employees of CPSEs. On a reference made by the Ministry of Shipping, DPE clarified to all the CPSEs on 26 October 2010 that employees of CPSEs were not permitted to accumulate EL for more than 300 days and CPSEs are not permitted to encash leave beyond 300 days at the time of retirement of its employees.

In September 2008, GOI allowed consideration of both EL and Half Pay Leave (HPL) for encashment for Central Government employees with effect from January 2006, subject to a limit of 300 days for both kind of leave taken together. In a further clarification of 17 July 2012, DPE referred to its instructions of April 1987 and reiterated that on retirement for CPSEs employees, EL and HPL could be considered for encashment subject to an overall limit of 300 days and that cash equivalent payable for HPL would be equal to leave salary as admissible for half pay plus dearness allowance and commutation of HPL would not be permissible to make up the shortfall in case EL to the credit of a CPSE employee was less than 300 days. Further, GOI guidelines do not permit encashment of sick leave, which has been reiterated by GOI in December 2012 and February 2014 also.

Audit observed that the following CPSEs deviated from the DPE guidelines and made irregular payment of ₹ 75.29 crore to their employees towards HPL/EL encashment on superannuation/separation over and above the ceiling of 300 days.

Sl. No.	**Name of CPSE**	**Period**	**₹ in crore**
1.	Coal India Limited including North Eastern Coalfields Limited	2009-10 to 2013-14	5.57
	Mahanadi Coalfields Limited		4.92
	Eastern Coalfields Limited		11.86
	Northern Coalfields Limited		6.07
	Western Coalfields Limited		10.15
	South Eastern Coalfields Limited including Dankuni Coal Complex		10.44
	Bharat Coking Coal Limited		5.46
	Central Coalfields Limited		15.26
	Central Mine Planning & Design Institute Limited		5.56
Total			**75.29**

CIL in reply stated (October 2014) that the guidelines issued by DPE were advisory in nature as clarified in the DPE's office memorandum dated 08 April 1991. Government of India conferred Maharatna status on CIL with the delegation of power to structure and implement schemes related to personnel and human resource management and training. Therefore, there was no violation of the overall policy of Government of India in the matter of leave provisions for the executives of CIL.

Reply is not acceptable as leave encashment beyond the overall policy of GOI was not permitted as per DPE instructions of April 1987. Further, DPE's circular of 26 October 2010 clarified that CPSEs were not permitted to encash leave beyond the overall ceiling of 300 days. In another clarification issued in July 2012, referring to instructions of April 1987, DPE reiterated that EL and HPL could be considered for encashment on superannuation subject to overall limit of 300 days. Moreover, clarification issued by DPE in July 2012 specifically disallowed encashment of sick leave. Further, the contention that even in GoI service, commuted leave is encashable as a good health reward is not factually correct as in GoI Service, only leave on half pay (HPL) is permitted to be encashed to the extent the encashment of Earned Leave at superannuation falls short of prescribed ceiling of 300 days and HPL is not allowed to be commuted for the purpose of encashment.

Therefore, encashment of HPL to employees on retirement/separation beyond the overall ceiling of 300 days was in violation of DPE guidelines and was, thus, irregular.

The matter was reported (November 2014) to the Ministry of Coal in respect of irregular payment in CIL, their reply was awaited (March 2015).

CHAPTER IV: MINISTRY OF COMMERCE AND INDUSTRY

MMTC Limited, PEC Limited and the State Trading Corporation of India Limited

4.1 Trading Activities of Agro Commodities

4.1.1 Introduction

MMTC Limited (MMTC), The State Trading Corporation of India Limited (STC) and PEC Limited (PEC) are trading companies under Ministry of Commerce & Industry (MoCI). All the three companies undertake import, export and domestic trade by extending financial assistance to their business associates for a fixed trading margin.

Audit reviewed the trading activities of agro commodities where dues were recoverable/written off as on March 2013 in MMTC, STC and PEC to identify the causes of specific failures in their operations leading to loss.

4.1.2 Audit Findings

4.1.2.1 Unauthorized lifting of agro commodities by the private associates

As per the business model followed, the trading companies extend pre-shipment credit♣ to the associates against export orders received by them or in the case of import of commodities on behalf of associates, arrange buyers credit to discharge the import liability and subsequently recover the amount. In both the scenarios the goods remained pledged to the trading company till payment is received. The associate is responsible for arranging for foreign buyer/seller and also for ensuring payment. In the following cases it was seen that the PSUs continued trade with associates in spite of outstanding dues. It was also noted that the PSUs failed to safeguard their assets pledged to them. This resulted in the PSUs incurring heavy losses.

♣ ***Pre-shipment financing {either on Letter of Credit (LC) or Documents against Payment (DP) terms of payments} is made available before goods are shipped (usually against a confirmed order) to help an Associate to fulfil an export order. In LC basis, buyers establish LC in favour of trading PSU. In case of DP terms of payment, buyer remits stipulated percent (10-20per cent) as advance payment to trading PSU. Associate starts the process of domestic procurement and approaches trading PSU for release of pre-shipment finance. The Associate submits Surveyor's report of pre-shipment inspection for quantity and quality of the commodity proposed to be exported. Based on Surveyor report and only after the procured cargo reaches the port of shipment in the custody of Cargo Handling Agent (CHA), who issues a "Trust Deed" in favour of trading PSU for the 100 per cent cargo, trading PSU releases finance to the associate. Associate ships the procured cargo and submits the documents to trading PSU for negotiation through Bank, in case of LC and in case of DP terms of payment the documents are sent to overseas buyers for collection through the Bank of trading PSU. On receipt of payment from foreign buyers in the account of trading PSU, the trading PSU, after adjusting its trading margin, advance made to associate, Bank charges and applicable interest etc. releases the balance amount to associate.***

4.1.2.2 Export of maize, sugar and other agricultural commodities

STC extended pre-shipment credit for export of agricultural commodities by M/s. Mehak Feeds Industry [now Mehak Overseas Private Limited (MOPL)] during the period 2006-07 to 2009-10. However, due to backing out by foreign buyers, non-acceptance of cargo on account of fall in international prices, demurrage charges at the destination port, etc. STC/MOPL could not recover the dues. Resultantly, an amount of ₹ 44.59 crore was outstanding as on October 2010 against MOPL. Subsequently (October 2010) STC again extended financial support to MOPL for export of maize. But in this trade also, STC could not recover the dues of ₹ 22.03 crore from MOPL. Physical verification of Indian Yellow Maize stocks procured by MOPL for export and kept in godowns at Kakinada, Kolkata, Nasik and Navi Mumbai, conducted by STC in March/April 2013, revealed that no stock was available in the godowns.

Audit observed that though MOPL was a persistent defaulter, STC extended pre-shipment credit beyond October 2010. Resultantly, ₹ 22.03 crore was added to recoverable from MOPL. Though STC was entitled to encash the Post Dated Cheques (PDCs) in the event of default by MOPL, STC failed to encash the available PDCs on the date of default. Subsequently the PDCs were dishonoured on presentation in February 2013. As a result, STC could not recover outstanding dues of ₹ 91.51 crore (including interest of ₹ 15.65 crore and overdue commission charged by SBI ₹ 9.24 crore) from MOPL (March 2014). The associate was absconding (since July 2012).

Management in its reply (November 2013) accepted the facts and stated that legal action for recovery of dues was initiated by the branch and provisions in the accounts for doubtful debts had been made during 2013-14 for ₹ 91.51 crore.

4.1.2.3 Import of Canadian Yellow Peas (CYP)

STC entered into an agreement (June 2010) and imported 27500 MT of CYP on behalf of M/s Prime Impex Limited (PIL) which was stored at different sheds of Kolkata Port Trust. STC arranged buyers credit and payment of ₹ 36.72 crore was made to foreign supplier. As PIL did not make the payment, STC decided to invoke risk and cost clause and conducted physical verification of stock on 17 January 2011 in the presence of PIL's representatives, CHA and Surveyor and full stock was found available in different sheds. STC invited tenders and allotted 2500 MTs to bidders but Cargo Handling Agent (CHA) was not effecting the delivery. STC on 03 March 2011 learnt that the stocks were lifted by the associate in connivance with the CHA and the surveyor.

Audit observed that as per the agreement the goods were to remain hypothecated and pledged to STC, till final payment by PIL. Further, clause 5 of the agreement provided that CHA was to be appointed by STC. However, in contravention of the agreement, CHA was appointed by PIL; resultantly PIL in connivance with CHA lifted the stock unauthorizedly. Further, STC neither obtained any security against the amount financed nor took steps to secure the pledged stock safely. Against the outstanding dues of ₹ 36.01 crore (March 2011), STC could recover only ₹ 2.34 crore by encashing security deposit/ available credit balance and balance recoverable from the associate was ₹ 33.67 crore, which was written off by STC (May 2012).

Management accepted (March 2014) the audit observation and stated that FIR has been lodged against associate, CHA, surveyor and others for unauthorized lifting of stock. It has also initiated arbitration and legal action and in order to avoid such situations in the future, steps are being taken to revise the modus operandi.

4.1.2.4 Export of rice bran

STC entered into three agreements on 25-9-2007, 27-11-2007 and 5-12-2007 with M/s. Saraf Impex Private Limited (SIPL) for financing export of aggregate quantity of 12000 MTs of deoiled rice bran from October 2007 to February 2008. Against the total quantity procured, SIPL exported 5970 MTs and defaulted in exporting balance quantity of 6430 MT (March 2010). The balance quantity valuing ₹ 3.05 crore was stored by STC in a private warehouse. STC assigned the work of assessing the stock and its quality to a Surveyor, whose survey report (December 2010) revealed that stock was available only to the extent of 985.8 MT against 6430 MT reported previously, the differential stock of 5444.20 MT having been lifted by SIPL without the knowledge of STC. Further, post dated cheques (PDCs) furnished by SIPL were dishonoured for which a legal case was filed by STC. Audit observed that STC neither obtained any security against the amount financed nor was it able to secure the pledged stock. STC made a provision (June 2013) of ₹ 3.49 crore in the accounts against the amount recoverable from SIPL.

Management replied (March 2014) that it filed a legal case against SIPL and on the basis of court order an amount of ₹ 78 lakh was recovered (February 2014) but thereafter the party stopped making payment. It was further stated that the company was in the process of filing arbitration case against SIPL to recover the balance dues of ₹ 2.71 crore.

The reply is not tenable as the management failed to protect its financial interest and could not recover the balance dues of ₹ 2.71 crore even after lapse of more than four years and the recovery of which has become doubtful.

4.1.2.5 Import of CYP in PEC Limited

PEC entered into five agreements between 8 September 2008 and 3 September 2010 with M/s Prime Impex Limited (PIL) for import of 102500 MT of CYP and opened Letters of Credit (LCs) during September 2008 to September 2010. As per the agreements, the goods, at the risk and cost of Associate were to be pledged to PEC and were to be released only on authorization/written instructions of PEC. An independent surveyor was also to be appointed by PEC who was to be present at the time of each release. Against the total imported quantity of 102100 MTs, as per surveyor report dated 21 February 2011, PIL lifted only 34395 MTs. As PEC observed shortages in the last week of February 2011 a physical verification was conducted on 4 March 2011 which revealed that almost the entire stock leaving a balance of 7975.314 MT had been unauthorisedly removed by PIL. CHA admitted that they released the balance quantity merely on the verbal assurance/ confirmation by PIL that they had obtained the de-pledge order from PEC.

Audit observed that associate was required to lift the material before the expiry of usance[1] period, failing which PEC was at liberty to sell the goods at the risk and cost of the associate. However, though there was delay in lifting the stock by PIL, PEC failed to invoke the said clause. PEC also failed to ensure day to day supervision and monitoring of the pledged stock and PIL in connivance with the CHA and Surveyor lifted the stock of 59729.686 MT of CYP. Resultantly recovery of ₹ 121.33[2] crore (including overdue interest) (November 2013) became doubtful. Moreover, the claim lodged had also been denied by the insurance company on the ground that the cargo was removed unauthorizedly by the party.

Management replied (March 2014) that all the relevant files had been seized and after investigation the CBI-EOW Kolkata filed charge sheet in CBI court at Kolkata. PEC had also written off the losses of ₹ 81.73 crore.

4.1.3 Acceptance of security in variance with accepted trade practices

4.1.3.1 Allowing lifting of material on the basis of PDCs

PEC sold 118519 MT of imported wheat to M/s. Sree Laxmi Trading Corporation (SLTC) on High Sea Sales[3] basis (agreement entered between September 2006 and January 2007) which was pledged in favour of PEC. Release of the pledged stocks to associate was to be done against 100 *per cent* payment of cost of goods, PEC's service charges and other expenses as per clause 16 of the Associateship Agreement. However, the lifting of wheat was very slow and 67343.801 MT of stock was lying with PEC (21 January 2010). Audit observed that contrary to the aforesaid clause, PEC within one day of request by SLTC (30 March 2010), permitted (31 March 2010) to lift the balance stock valuing ₹ 61.63 crore against PDCs of ₹ 51.00 crore. PEC issued delivery orders on 31 March 2010 against which SLTC took the delivery of entire material. Though four other cheques issued by the associate of ₹ 2 crore each dated 30 March 2010 were available but PEC could not present these cheques before issuing delivery orders on 31 March 2010 and subsequently on presentation between 20 April 2010 and 28 September 2010 all the four cheques were dishonoured. The PDCs of ₹ 51 crore were also dishonored by the bank on presentation in June 2011 as the bank account of the party was closed on 1 November 2010. Thus, failure to ensure the recovery of cost before issuing delivery order led to a situation where recovery of ₹ 58.35 crore became doubtful (March 2014).

Management replied (March 2014) that it had initiated legal proceedings against SLTC and also invoked arbitration clause with Indian Arbitration Council.

4.1.3.2 Non-recovery of interest and service charges

PEC entered (17 November 2009) into an agreement with M/s PBR Impex for procurement of paddy with a financial assistance limit of ₹ 50 crore. The associate had to

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[1] Period for which buyers credit is arranged, usually 120 days.

[2] Booked in accounts only ₹ 81.73 crore.

[3] High Seas Sales (HSS) is a sale carried out by the carrier document consignee to another buyer while the goods are yet on high seas or after their dispatch from the port of origin and before their arrival at the port of destination. HSS agreement should be signed after dispatch of goods from origin and prior to their arrival at destination port.

pay interest @ 10.5 *per cent* on the amount financed and the applicable service charges. The financial limit was enhanced (December 2009) to ₹ 70 crore. PEC provided financial assistance to the tune of ₹ 72.70 crore (November 2009 to February 2010) to M/s PBR towards procurement of 32761.65 MT of paddy. Though the entire stock was to be lifted by December 2010 but even after lapse of more than three years the party lifted 32523.40 MT up to March 2014. Instead of recovering interest and service charges on the amount financed to the party in terms of the agreement, PEC decided to raise the claim on these accounts only after realization of principal amount. Resultantly, an amount of ₹ 13.13 crore was recoverable from M/s PBR, as on 31 March 2014, against which stock of only ₹ 0.64 crore was available with PEC.

Management replied (March 2014) that Company was holding un-lifted stock valuing ₹ 0.64 crore and PDCs for more than the outstanding amount towards interest cost.

The reply is not tenable as the PDCs available against the security of balance recoverable amount were later on dishonoured in August/September 2014, for which PEC has initiated legal action. As no security is available with the Company, chances of realisation of dues of ₹ 12.49 crore (March 2014) have become doubtful.

4.1.3.3 Export of sugar in STC

STC entered (March 2007) into back-to-back contract with M/s PKS Limited, Kolkata for export of sugar to various countries. As per agreement, STC made 100 *per cent* payments towards cost of sugar (rake-wise) to Sugar Mills after getting 15 *per cent* payment from M/s PKS Limited and its request for release of payment to specific sugar mill. After exporting the consignment and receipt of export proceeds, STC was to release balance payment to PKS after recovering its trade margin, interest and other bank charges. PKS deposited post dated cheques (PDCs) of 110 *per cent* value of export order plus interest against amount financed by STC which could be encashed by STC, in case of any failure on the part of M/s PKS. Due to drop in international prices, buyers did not lift the goods at the port of discharge in time and resultantly PKS sold the consignment at discounted rates. STC had financed ₹ 182.04 crore till 2009-10 to M/s PKS against which STC could recover ₹ 164.33 crore leaving balance outstanding of ₹ 20.89 crore (including interest up to 31 March 2011). Further, cheques presented by STC for payment were dishonoured by banks.

Besides initiating legal action under Negotiable Instruments Act, STC invoked Personal and Corporate Guarantees furnished by PKS. As a result of legal action, Kolkata High Court appointed a Receiver who took possession of about 1.07 lakh MT Iron Ore stock lying at Gua, Jharkhand belonging to PKS Limited, which was hypothecated by M/s PKS to STC, in lieu of outstandings of STC, and covered the outstanding amount.

Audit observed that as per agreement payment of consignment was to be made by foreign buyer on sight LC basis and funds disbursed by STC were to be liquidated by PKS within 30 days from released date. However in the instant case, though outstanding dues were of 2008-09 and default on the part of foreign buyer was clear, but STC failed to take timely action. The available PDCs were deposited only on 22 February 2011 and were dishonoured by the bank. As a result, the recovery of ₹ 20.89 crore became doubtful.

Management in its reply (April 2014) stated that it had initiated legal action under Section 138 of the Negotiable Instruments Act and also under Section 9 of Arbitration and Conciliation Act for recovery of outstanding dues. It had also invoked personal and corporate guarantee. Further, as per the directions of Kolkata High Court a receiver was appointed for possession of 1.07 lakh MT of iron ore stock of PKS and the matter was referred to Indian Council of Arbitration (ICA), Delhi, which was pending. STC had also written off in 2012-13 total dues of ₹ 20.89 crore outstanding against M/s PKS.

The reply is not tenable as the management while writing off of outstanding dues admitted the fact that it would be difficult to sell the iron ore stock due to numerous restrictions on export/movement of iron ore from mines. Thus, failure to take timely action as per the provisions of the agreement, resulted in loss of ₹ 20.89 crore to STC.

4.1.4 Non-lifting of stock

4.1.4.1 Import of crude palm oil

PEC imported (July 2012) 2999.766 MT of Crude Palm Oil (CPO) for M/s Mihijam Vanaspati Limited (MVL). MVL had to lift the CPO within usance period of 180 days. Though usance period was extended twice for 90 days each and lifting period was extended for 60 days but still MVL could not lift the entire material and a balance of 2385.766 MTs remained in stock (July 2013). The surveyor's report (21 October 2013) revealed that stock of only 2333.341 MT was available. PEC also noticed (July 2013) that due to prolonged storage the stock might not be fit for human consumption. The PDCs of ₹ 5.47 crore were dishonoured (September 2013). Audit observed that PEC failed to secure its financial interest for ₹ 15.45 crore and was also at risk of losing the pledged stock due to constant deterioration of the quality. Further, PEC failed to reconcile the difference of 52.425 MTs in the stock of CPO.

Management replied (June 2014) that PEC is taking all necessary steps to safeguard its interests and was also exploring opportunity to auction the cargo at the right time. PEC has also filed a court case against MVL for dishonour of cheque.

4.1.4.2 Blocking of funds due to non-lifting of pulses

M/s. R. Piyarelall Import & Export Limited (RPIEL) associated regularly with PEC for import of agro products and on 31 March 2010 there were outstanding dues of ₹ 114.53 crore against the associate. Despite this, PEC again entered into agreements with RPIEL for import of pulses between August 2010 and February 2011. Audit observed that neither did the associate lift the entire stock nor did he pay the entire cost prior to payment of foreign LCs. PEC, however, failed to sell the stock at the risk and cost of the associate to recover the dues.

Management replied (June 2014) that the party was in financial crunch and had requested time for settling the dues and was liquidating the stock in lots on daily basis. RPIEL had also provided documents for mortgaging a property valuing ₹ 35 crore towards collateral security for outstanding dues.

However, the fact remains that PEC failed to take action as per the agreement even after more than three years of default which led to blocking of funds of ₹ 80.74 crore (February 2013).

4.1.4.3 Supply of pulses to Govt. of West Bengal

On the request (July 2009 and August 2009) of Department of Food and Supplies (DoFS), Government of West Bengal, MMTC offered (12 August 2009) to supply 5000 MTs of red lentils and 1000 MT of moong beans at a value of ₹ 25.72 crore and ₹ 5.03 crore respectively. DoFS confirmed the offer (13 August 2009) and assured to submit bank guarantee within 1-2 days. MMTC informed (16 September 2009) DoFS that the entire consignment of moong beans had sailed and the consignment of red lentils was also expected to be shipped shortly and requested to release bank guarantees. However, DoFS did not provide the BG and vide letter dated 24 September 2009 informed MMTC of their decision to cancel the import of pulses.

Audit observed that, though execution of contract by MMTC was subject to 100 *per cent* financial bank guarantee from DoFS, but it executed the contract without ensuring the receipt of bank guarantees. Subsequently, the material was sold in open market at a loss of ₹ 11.37 crore.

Management confirmed (March 2014) the facts and figures contained in the audit observation.

4.1.4.4 Delay in disposal of cotton waste

MMTC entered into an MOU (November 2009) with M/s Suchetan Export Private Limited (SEPL) for procurement of cotton waste from local suppliers for 100 *per cent* back-to-back sale. Accordingly, MMTC procured 1042.101 MT of cotton waste in November 2009 and 102.059 MT in the year 2010-11. As per terms of the MOU, the cotton waste was to be lifted within 120 days by making payment to MMTC. As SEPL failed to liquidate the entire stock within the stipulated period, the balance stock of 607.20 MT (July 2012), was sold at risk and cost of SEPL in August and November 2012, i.e., after a delay of more than two years. The amount recoverable from SEPL on account of price differential and interest cost after adjusting available EMD was ₹ 1.33 crore.

Audit observed that delay in decision to invoke the 'risk and cost' sale clause and failure to ensure adequate financial security resulted in non-recovery of ₹ 1.33 crore.

Management in its reply (July 2014) stated that MMTC had PDCs of ₹ 1.50 crore but the same were dishonoured on presentation for which a criminal case was filed against the party.

4.1.4.5 Loss due to sale on risk and cost basis

MMTC entered into contracts (2010-11) for sale of pulses (Lemon Toor and Toor Malawi) on ex-godown basis with three associates. Though all three associates did not lift the quantity within the prescribed time limit, MMTC did not obtain additional EMD to cover mark-to-market losses as per the agreements and sold the un-lifted quantity on risk and cost basis, resulting in loss of ₹ 3.40[1] crore (July 2014).

Management accepted (July 2014) the facts and stated that EMD of all the three parties were forfeited and arbitration proceeding initiated for recovery of dues of ₹ 3.40 crore.

4.1.4.6 Non-lifting of imported Yellow Peas in STC

STC imported pulses (2008-09 and 2009-10) on behalf of M/s R. Piyarelall Import & Export Limited (RPIEL). The stock was pledged to STC and the same was to be lifted on cash and carry basis within a period of 120 days. RPIEL was slow in lifting of the imported stock since beginning and also not co-operating in physical verification of stock. Ultimately, RPIEL failed to lift 21927.59 MT Yellow Peas (September 2013). In spite of this, STC did not take action to dispose of the material at the risk and cost of the party. The cheques given by RPIEL were also dishonoured on presentation (December 2012). Resultantly, an amount of ₹ 131.61 crore was outstanding against RPIEL (February 2014), out of which STC had already written off ₹ 75.26 crore.

Management replied (March 2014) that legal action had been initiated against RPEIL under Section 138 of Negotiable Instrument Act to recover the outstanding dues.

4.1.5 Unfruitful results of decree passed by Arbitration/Courts

A review of records relating to arbitration and court cases in MMTC revealed that in three[2] cases even though the arbitration awards/High Court orders were in favour of MMTC but as the parties were either declared sick or filed an appeal against arbitration award, MMTC could not realize its dues of ₹ 12.63 crore[3].

Management in its reply (July 2014) stated that the claims in two cases (M/s Varuna Agro Proteins and M/s Surya Agro) were pending before the official liquidator, while in one case (M/s Priyanka Overseas Limited) the matter was pending before the Delhi High Court.

Reply of the management is factual and as the matter is pending before liquidator/court, the chance of recovery of dues of ₹ 12.63 crore is remote. Failure to recover dues inspite of court orders only buttresses the audit point of highly risky nature of activity.

Conclusion

Trade in agro commodities by the three CPSEs highlights mismanagement, possible fraud, negligence and absence of financial prudence. As the entire activity of identifying supplier, buyer, storage, arranging for shipment, etc. was performed by the associates which are private parties, it is a moot point whether these would qualify to be termed as 'trading activity'. In fact, the three CPSEs failed to assess the credit worthiness of associates and have been involved in providing finance to

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[1] ***M/s Badri - ₹1.12 crore, M/s R. Piyarelall - ₹0.93 crore and M/s Balaji - ₹1.35 crore***

[2] ***M/s Varuna Agro Proteins, M/s Surya Agro Oil and M/s Priyanka Overseas Limited.***

[3] ***M/s Varuna Agro Proteins ₹7.36 crore, M/s Surya Agro Oil ₹3.37 crore and M/s Priyanka Overseas Limited ₹1.90 crore***

highly risky ventures without adequate safeguards. Resultantly, they suffered losses because of inadequate security against the amount financed and they were also not able to secure the pledged stock safely. Inordinate delays in disposal of un-lifted material and in taking decision to invoke the 'risk sale' clause as also release of stock on the basis of PDCs indicated culpability on the part of the Management. Though each CPSE has Government nominees on the Board of Directors, nothing came to notice to show that they had effectively protected the interests of the Government by insisting on adequate safeguards.

Ministry of Commerce & Industry in its reply (September 2014) stated that as the issues related to commercial activities of CPSEs, they had no further comments in the matter.

Neelachal Ispat Nigam Limited

4.2 Irregular payment of bonus

An irregular payment of bonus amounting to ₹ 7.03 crore was made to the employees in deviation from the approved Annual Performance Linked Reward Scheme of the Company

Neelachal Ispat Nigam Limited (Company) introduced (September 2006) an Annual Performance Linked Reward Scheme (APLRS) for its employees for a period of three years beginning 2005-06 which was extended thereafter. The scheme replaced the then existing system of payment of ex-gratia in lieu of annual bonus and was based on fulfilment of targets with respect to the budgeted pig iron production, oven pushing and techno-economic factors for coke rate having weightages of 35 *per cent*, 35 *per cent* and 30 *per cent* respectively. The first two parameters were to have an earning potential only on achievement of at least 80 *per cent* performance. The amount payable per employee in a year depended on the sum total of earnings from the above three parameters multiplied by a profitability factor to be decided by the management based on net profit for the year. The total potential for payment under the scheme (including all the three parameters) on 100 *per cent* fulfilment was stipulated at ₹ 8000 per employee. The scheme also had an additional earning potential of one *per cent* for every five *per cent* increase in performance over 100 *per cent* performance level for all three parameters.

Audit examination revealed that in spite of incurring loss for 2010-11 and 2012-13 when related profitability factor became ‘zero’, the Company disbursed bonus amounting to ₹ 4.52 crore. Further, computation of bonus for 2008-09 to 2011-12 included earnings from the first two parameters though the minimum required performance level of 80 *per cent* was not achieved. The computation for 2006-07 also included earnings of more than 100 *per cent* from its third parameter, though the scheme did not contemplate any such earning potential for individual parameters. This resulted in an excess payment of bonus amounting to ₹ 2.51 crore for 2006-07 to 2011-12 (except 2010-11).

It was also observed that payment of bonus relating to 2006-07 to 2012-13 exceeded the stipulated amount of ₹ 8000 per employee, though 100 *per cent* performance level was never achieved for all the three parameters. Further, the scheme lacked clarity in determining the profitability factor with respect to the net profit earned each year which was completely unrelated to the level of net profit earned.

The Company stated (October 2014) that the profitability factor was decided in consideration of profit earned in the previous year, expectation of employees and practices followed in neighbouring industries. It was also stated that under the prevailing scheme, in the year the Company incurred losses, the profitability factor was 'one' and hence employees were entitled to bonus payment for the components under production and productivity only. Also, considering general expectations of the employees, prevailing payment to employees during Puja time in neighbouring industries as well as in SAIL and in other units of public sector, relaxation and deviations were considered.

The above contention is not acceptable in view of the fact that in the years the company incurred losses, the profitability factor was 'zero', and not 'one', as claimed by the management. As such, there should not have been any earnings under the scheme in the years when losses were incurred. Further, other factors like expectation of the employees were beyond the scope of the approved scheme. Moreover, Department of Public Enterprises had stopped (November 1997) payment of reward to employees of CPSEs which was beyond the scope of any approved scheme.

Thus, the Company made an irregular payment of bonus amounting to ₹ 7.03 crore[•] in deviation from its approved Annual Performance Linked Reward Scheme.

The matter was reported to the Ministry (November 2014); their reply was awaited (March 2015).

PEC Limited, MMTC Limited and the State Trading Corporation of India Limited

4.3 Non-compliance to the directions of Government of India for export of rice to African Countries

PEC Limited, MMTC Limited and The State Trading Corporation of India Limited, while exporting rice to African Countries, failed to get the directions of Government of India complied with by their 'Associates'; resultantly, associates directly negotiated with foreign countries and earned huge profits, which otherwise could have been earned by these CPSEs.

Ministry of Commerce & Industry (MoCI), Department of Commerce allowed export of non-basmati rice to the African countries, namely Comoros and Mauritius in January 2008 through MMTC Limited, Republic of Sierra Leone in March 2008 through PEC Limited, and Madagascar and Ghana in January 2008 and October 2008, respectively, through The State Trading Corporation of India Limited (STC). Export of rice was subject to conditions stipulated by Director General of Foreign Trade (DGFT) notifications dated 24-01-2008 that the CPSEs would (i) undertake the exports in consultation with Department of Food and Public Distribution (DFPD); (ii) buy rice from the market from those rice mills who had already delivered levy rice to STC/State Agencies, and (iii) ensure that the price paid for procurement of rice was as close to the MSP/levy price as possible so as not to disturb the procurement operations within the country.

[•] *₹4.52 crore + ₹2.51 crore*

Audit observed that the CPSEs did not adhere to the aforesaid conditions. The 'Associates' were also selected in a non transparent manner without inviting bids[1] and in most of the cases governments of African countries nominated Indian suppliers to carry out the export of rice. The 'Associates' (suppliers) made direct negotiations with the State agencies/buyers in these countries and fixed export price of the rice ranging between USD 430 PMT to USD 684 PMT against the Minimum Support Price (MSP)[2] of rice USD 329.52 PMT as may be seen from the details given below:

Name of PSU	Country exported to	Quantity awarded (in MTs)	Name of Associate	Quantity exported (in MT)	Export Rate/MT (in USD)	PSU's Margin/MT (in USD)	Margin retained by Associate in excess of MSP of rice USD 329.52/MT (in USD)
PEC	Republic of Sierra Leone	40000	Shivnath Rai Harnarain Ltd. (SRHL)	22047.5	430	5	95.48
				17952.5	470	5	135.48
MMTC	Mauritius	9000	LMJ International Limited.	9000	455	87	38.48
	Comoros	25000	SRHL	25000	495	14	Contract cancelled.
			SRHL	3100	640	10	300.48
			Emmsons International Limited.	2700	640	10	300.48
			Amira Foods India Ltd. (AFIL)	2700	640	10	300.48
STC	Ghana	15000	AFIL	15000	684	10.26	344.22
	Madagascar	50000	Jayamjay Export	50000	410-420	1.5 *per cent*	Contract cancelled.
			SRHL	45000	450	6.75	113.73
			SRHL	5000	458	6.87	121.61

Thus, while the associates enjoyed profit margins in the range of USD 38.48 PMT to USD 344.22 PMT, the CPSEs earned a meagre margin ranging from USD 5-10 PMT (except in case of export made by MMTC to Mauritius where it was USD 87/MT). Further, though the rice was to be procured from those rice mills which had already delivered levy rice to STC/State Agencies, the CPSEs neither ensured that procurement was made from such mills nor obtained any certificate from the associates, except in the case of export to Ghana.

[1] ***Except in case of export made by MMTC to Mauritius***

[2] ***Rate of rice procured by 'Associates' in 2008-09 was not available. As such the rate of rice has been derived on the basis of rates of MSP of paddy and other charges for Custom Milled Rice delivered to the Food Corporation of India for Central Pool during the Kharif Marketing Season 2008-09 in respect of Government of Uttar Pradesh and its agencies vide Government of India, Department of Food and Public Distribution circular No. 192(23)/2008-FC.A/Cs dated 4 November 2008, as under:***
Rate of Raw Rice (Grade-A) = ₹ 1512.84/qtl. or ₹ 15128.40/MT or USD 329.52/MT (considering 1 USD=₹ 45.91)

CPSEs also did not obtain approval of the respective Boards of Directors before execution of rice export though the ceiling of contract in all cases had exceeded the limit prescribed in their Delegation of Powers (DoP).

CPSEs replied (MMTC: January 2014, STC: May 2014 and PEC: June 2014) as under:

- Associates were nominated by the concerned foreign governments which also settled the price and commercial terms with them directly. The associates procured the rice from those mills that had already discharged their levy obligations and exports were made on 'back to back' basis. Also, no funds of the CPSEs were involved and there was no loss in these transactions.
- The export price was summation of pre-shipment activities, ocean freight, etc. and was considered appropriate due to risky nature of trade with African countries.
- The trade transactions were approved as per the Delegation of Powers by the Committee of Management/Directors (COM/COD) comprising CMD and all functional Directors. Moreover, the minutes of SPCOD/FMCOD ♦ were submitted to Board on quarterly basis.

Ministry of Commerce & Industry (MoCI) while endorsing replies of the three CPSEs stated (September 2014) that after examining the records of export of rice to African countries, three private sector firms involved in these transactions were blacklisted and debarred from all further transactions with CPSEs of the Department of Commerce for a period of four years. An advisory was also issued to other Ministries/Departments to abstain from doing business with these firms. Further, on the advice of Central Vigilance Commission, departmental enquiries were held by three separate Additional Secretary level officers of the MoCI. On the basis of the enquiry reports, the Disciplinary Authority awarded punishment to nine officials of the CPSEs. MoCI further stated that to prevent recurrence of such a situation in future, remedial action has been taken by the Ministry through issue of detailed guidelines.

Reply given by CPSEs is not acceptable as they had not adhered to the conditions for export of rice stipulated by DGFT. Impact of guidelines of the Ministry, to prevent recurrence of such incidents will be assessed in future audits.

The State Trading Corporation of India Limited

4.4 Non recovery of dues due to operational lapses in Post Shipment Finance

Lapses in implementation of post shipment finance scheme led to non-recovery of dues of ₹ 446.29 crore. Discounting of export documents of dubious legality conceded by EXIM Bank, were also noticed besides infructuous expenditure on insurance premium of ₹ 17.07 crore.

♦ *SPCOD – Sale Purchase Committee of Directors; FMCOD – Functional Management Committee of Directors*

4.4.1 Credit Linked Insurance Scheme

4.4.1.1 The Committee of Management (COM)[1] of the State Trading Corporation of India Limited (STC) approved (September 2005), post shipment finance (PSF)[2] under Credit Linked Insurance Scheme (CLIS) for export and import operations. As per the approved scheme, the Associate was to export the goods on STC's account and submit export documents, which were to be routed through the Lender Bank i.e. HSBC for discounting[3]. HSBC was not to have any recourse against STC up to a loss of ₹ 50 crore per annum. The Associate would be paid on 'Document against Acceptance' (DA)[4] basis and payment from foreign buyer was expected to be realised within 90 to 180 days. The terms and conditions of the trade were to be as per 'Business Credit Shield' Policy of M/s New India Assurance Company (NIA) (May 2005).

4.4.1.2 While Mumbai branch of STC had initially proposed to source post shipment finance (PSF) from HSBC, STC also considered subsequent proposals from Export-Import Bank of India (EXIM Bank) and ABN AMRO and selected EXIM Bank as its Lender Bank through an agreement in January 2006, for PSF for agricultural commodities and other products, with a credit limit of USD 50 million. EXIM Bank was to discount export bills at 90 *per cent* of invoice value. Repayment was to be made within 180 days from the date of disbursement or out of export proceeds, whichever was earlier.

In a significant departure from the arrangement offered by HSBC as indicated in para 1.1 above, STC was responsible for all operational risks under insurance policy and EXIM Bank had full recourse to STC. Thus loss due to defaults by foreign buyers in repayment of dues not covered by insurance was to be borne by STC. Funding was restricted to transactions covered under insurance policy and buyer's limit as specified therein.

4.4.1.3 STC took credit insurance policy (November 2005) from NIA up to November 2006 under which NIA was to decide revolving credit limit of foreign buyers. Fresh receivables would remain uninsured in case of debts older than 60 days from the foreign buyer. STC was to promptly inform NIA when a debt was partially or wholly unpaid beyond 30 days and furnish details of buyers making late payments by more than 30 days. Maximum liability of NIA was 30 times the premium paid and maximum term of payment was 180 days from the invoice date. Subsequently, STC took (June 2006) another credit insurance policy from ICICI Lombard up to June 2007, with terms and conditions similar to NIA policy, except that the maximum liability was enhanced to 50 times premium paid.

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[1] Committee of Management comprised of Chairman & Managing Director, all functional Directors and Executive Director (Vigilance).

[2] Post shipment finance is a kind of loan provided by a financial institution to an exporter or seller against a shipment that has already been made. PSF is granted from the date of extending the credit after shipment of the goods to the stipulated date of realisation of the export proceeds.

[3] Cashing or trading a bill of exchange at less than its par value and before its maturity date. The Bank then presents the Bill to the borrower's customer on the due date of the Bill and collects the total amount.

[4] An arrangement in which an exporter instructs a bank to hand over shipping and title documents to an importer, only if the importer accepts the accompanying bill of exchange or draft by signing it.

4.4.1.4 As per contractual agreements executed by STC (February 2006 to July 2009) with its 'Associates', out of 90 *per cent* discounted bill value received from EXIM Bank, STC would retain 1.5 *per cent* as trading margin and 5 *per cent* towards incidentals. While 83.5 *per cent* of invoice value was to be released against post dated cheques (PDCs) obtained from the 'Associates', the remaining 10 *per cent* was to be released after receipt of final payment from foreign buyers by Lender Bank and its release to STC.

Exports made under CLIS by STC during 2005-06 to 2009-10 amounted to ₹ 1565.13 crore. STC did not realize its dues fully from the foreign buyers. Resultantly, EXIM Bank converted (December 2010) outstanding dues of ₹ 397.17 crore (including interest) into Working Capital Term Loan (WCTL).

4.4.2 Audit findings

Audit reviewed PSF transactions during 2005-06 to 2009-10, relating to eight[♣] Associates with outstanding dues amounting to ₹ 347.70 crore (excluding interest on overdue receivable). The information/data on the basis of which the audit findings have been arrived at was compiled by audit and was referred to STC for confirmation in October 2013. Though STC confirmed (December 2013) the financial data, it expressed its inability to confirm the outstanding/recoverable amounts against exports under CLIS. However, as on 31 March 2014, STC had made a provision of ₹ 446.29 crore against net receivables under CLIS.

Lapses noticed in Audit are discussed in the succeeding paragraphs.

4.4.2.1 Failure to safeguard interest of STC

Agreements entered into with the Associates did not include any provision to obtain Bank Guarantees etc., for safeguarding the financial interests of STC. Even in agreements where a few safeguards were provided, the same were not enforced. Illustratively, a clause for recovery of PSF disbursed to Associates in case of buyers' default in making remittances included in agreements with M/s Masumi and M/s Ushma was not enforced and a similar clause was missing in agreements with other Associates.

Further, as per agreements with Associates, payment from foreign buyers was required to be remitted to STC within 180 days and 90/120 days respectively from the bill of lading/airway bill date. While the default in payment by foreign buyers was seen in 71.43 *per cent* transactions in 2005-06, it was more than 99 *per cent* in transactions entered into during 2006-07 to 2009-10. Though default in making payments by foreign buyers was a major risk, STC did not enter into any agreement with the foreign buyers to safeguard its financial interests.

STC stated (September 2014) that it had safeguarded its interests by way of legal provisions in the agreements which enabled it to take legal action against defaulter

[♣] ***M/s: (i) Masumi ₹ 45.70 crore, (ii) Bonito Impex ₹ 85.02 crore, (iii) Ushma ₹ 157.74 crore, (iv) Vidyut ₹ 3.97 crore, (v) Ganesh ₹ 5.00 crore, (vi) Indo Bonito ₹ 1.80 crore, (vii) Shalimar ₹ 22.00 crore and (viii) Space ₹ 26.47 crore (in case of M/s. Space, PSF was obtained from EXIM Bank as well as Standard Chartered Bank).***

Associates including M/s Masumi and M/s Ushma. STC also justified not entering into agreement with foreign buyers on the ground that export orders were received from the buyers, which were backed by agreements with STC's Associates.

The reply does not consider the fact that legal action is resorted to as the last recourse and is a long and cumbersome process with uncertain outcome. The point remains that safeguards, such as Bank Guarantees etc, which would have precluded legal action were not part of the agreements.

4.4.2.2 Acceptance of full risk by STC by deviating from approved Scheme

As per CLIS, Lender Bank (HSBC) would not have recourse against STC in case of default by foreign buyers. However, deviating from the approved scheme, STC selected EXIM Bank as the Lender Bank primarily to avail credit facility of USD 300 million and assumed liability of full recourse but did not devise a mechanism to safeguard its financial interests against default by the foreign buyers.

STC stated (September 2014) that EXIM Bank was preferred as it was under the same administrative Ministry. It further stated that business was carried out through EXIM Bank and not with HSBC since as per agreement, entire responsibility for repatriation of export proceeds was of the Associates.

The reply ignores the fact that in case of default by foreign buyer/Associate, STC was liable to settle the liability of Lender Bank.

4.4.2.3 Failure to comply with the requirements of insurance policies

(a) In respect of two foreign buyers (M/s Mohammed Hamza and M/s Naif Kingdom) of M/s Masumi, though no credit limit was sanctioned by insurance companies, STC went ahead and traded with them.

STC replied (September 2014) that PSF was availed from Standard Chartered Bank (SCB) in the case of M/s Masumi’s foreign buyers whose limits were sanctioned by insurance companies.

The reply is not acceptable as the list of buyers in the agreement with SCB (June 2008) indicating credit limits approved by SCB, did not include the said two parties.

(b) In order to safeguard financial interests of STC, outstanding dues of foreign buyers should not have been allowed to exceed the credit limits sanctioned by insurance companies. Audit scrutiny revealed that out of total 42 foreign buyers to whom exports were made, in respect of 25 buyers, the outstanding dues exceeded the sanctioned limit. This indicated ineffective monitoring of CLIS by STC.

STC stated (September 2014) that they had stopped further transactions with overseas buyers on noticing the same. The reply does not deny that there was weakness in monitoring in STC.

(c) STC failed to comply with the conditions in the insurance policies designed to control default in payment by foreign buyers as shown in Tables 1 & 2:

Table 1: Non-compliance with terms of insurance policy with NIA

Details of Transactions	Policy-1	Policy-2	Policy-3
Total Transactions	**33**	**71**	**49**
Less: Records relating to transactions not available/provided by STC	7	Nil	Nil
Less: Cases where date on which payment was to be received from foreign supplier is not available with STC	Nil	17	07
Transactions for which records were available	**26**	**54**	**42**
Transactions with delayed payments by buyers	25	52	42
Transactions which were not covered by insurance as debt due for more than 60 days were not reported to NIA	11	24	31
Transactions where STC failed to comply with condition of notifying NIA of non-payment by buyer beyond 30 days	15	37	39
Transactions with default exceeding six months 'Protracted Default'	Nil	Nil	15
Transactions where STC failed to comply with condition of notifying consistent non-payment beyond 30 days by the buyer in the last 12 months	13	43	39

Table 2: Non-compliance with terms of insurance policy with ICICI Lombard

Details of Transactions	Policy-1	Policy-2	Policy-3 & 4
Total Transactions	394	413	23
Less: Cases where date on which payment was to be received from foreign supplier is not available with STC	100	350	23
Transactions for which records are available	**294**	**63**	**0**
Transactions with delayed payments by buyers	292	63	0
Transactions with default exceeding four months 'Protracted Default'	128	21	0
Transactions where STC failed to comply with condition of notifying consistent non-payment by buyer with least possible delay	349	163	23

STC stated (September 2014) that departmental proceedings and CBI inquiries were going on against the delinquent officials.

4.4.2.4 Mismanagement of credit insurance policies

(a) STC had taken credit insurance policies from NIA and ICICI Lombard paying a total premium of ₹ 17.07 crore for the period November 2005 to February 2010. As per the terms and conditions of the policy, STC was required to file various declarations periodically, viz. insurable turnover and overdue payments, etc. However, due to failure in complying with these conditions, STC could not lodge the claims with the insurance companies. Further, insurance policy taken in February 2009 from NIA with Maximum Loss Liability (MLL) of ₹ 250 crore required quarterly payment of premium of ₹ 1.04 crore. STC did not pay the 4th instalment due in November 2009. Resultantly, the policy was rendered inoperative. Thus, the amount of insurance premium paid to NIA in the previous three instalments totalling to ₹ 3.13 crore♥ was rendered wasteful.

Here also, STC stated (September 2014) that the departmental proceedings and CBI inquiries were ongoing against the delinquent officials.

(b) Insurance policies taken by STC restricted the loss recoverable by it to the Maximum Loss Level (MLL) i.e. 30-60 and 50 times of premium paid in case of NIA and ICICI Lombard, respectively. Though MLL had remained lower than the dues in default, no remedial measures were taken by STC to revise the insurance premium to increase MLL. This was in spite of the fact that as per agreement, the insurance premium was recoverable from the Associates.

STC stated (September 2014) that as MLL remained less than the loss recoverable from the insurance companies, it had initiated action against STC's officials responsible for the same. CBI enquiries were also on going.

4.4.2.5 Renewal of credit limit without assessment of its benefits

Recovery of dues from buyers was not satisfactory from the very first year of operation of CLIS, as there were delays/defaults in 102 out of 103 transactions as on 31 January 2007. Operational/ financial prudence required an analysis of transactions of the previous year before renewal of the credit, STC renewed the credit of USD 50 million from EXIM Bank in February 2007 without such analysis. In the above stated 102 cases where receipt of payment from buyers was delayed, no correspondence with EXIM Bank or with the insurance companies was available.

STC stated (September 2014) that buyers were making payments through EXIM Bank which was aware of the situation.

Reply does not explain how renewal of credit limits without assessment of performance of foreign buyers could be considered a prudent financial decision.

4.4.2.6 Discounting of export documents of dubious legality with EXIM Bank

Due to continued default in payment by foreign buyers, by 31 March 2009 the credit advanced by EXIM Bank, had to be graded as a ‘Non Performing Asset’ (NPA). In order to avoid NPA situation, STC submitted to EXIM Bank, photocopies of 28 invoices purportedly evidencing export of 'cut and polished' diamonds undertaken by M/s Ushma valuing USD 14.48 million. EXIM Bank discounted these bills and adjusted the amount against their dues. However, STC actually received only 18 shipping documents worth ₹ 73.64 crore after a long gap in May 2009. Again on 30 June 2009, to avoid NPA situation, STC submitted another batch of export documents evidencing export of 'cut and polished' diamonds by M/s Ushma, M/s Indo Bonito and M/s Masumi, which were discounted and adjusted by EXIM Bank against the dues towards credit under CLIS.

♥ ***This is included in the total premium of ₹ 17.07 crore paid to insurance companies as mentioned in para 2.4(a).***

However, despite repeated demands by EXIM Bank, STC did not provide the Bills of Exchange duly accepted by respective foreign buyers.

Adjustment of CLIS overdues as mentioned above was questionable as the diamond export documents purportedly evidencing exports of ₹ 385.73 crore were of dubious legality as no buyers' acceptance of the Bills of Exchange was ever received in respect of the said export documents.

STC accepted (September 2014) that diamond shipping documents were submitted to EXIM Bank against which STC did not avail any credit from the latter. It further stated that departmental proceedings and CBI inquiries were on against their officials who had handled the jewellery, 'cut and polished' diamonds documents to EXIM Bank, without buyers' acceptance when transactions were on Documents against Acceptance (DA) payment terms.

4.4.2.7 Non formulation of guidelines

CLIS being a new business model required guidelines for its effective formulation and implementation which was not done. STC replied (September 2014) that business was carried out as per the drill/terms contained in the COM note and also agreement signed between STC and Associates.

Reply is not tenable as the COM note/agreements did not include any safeguards to protect financial interests of STC. The reply also contradicts the fact mentioned in the report given in June 2009 by a committee formed by STC to review CLIS, which stated that no drill/line of action was formulated for operations under the scheme.

4.4.2.8 Reply of Ministry of Commerce & Industry

Ministry endorsed (June 2014) the reply given by STC and also intimated that a criminal complaint was lodged with CBI, Mumbai and the matter was under investigation. CBI had registered cases against business Associates and their executives, insurance consultants and three officials of STC. Disciplinary action had also been initiated by STC against its seven officials.

Conclusion

STC was negligent in safeguarding its interests while entering into a new business scheme leading to huge losses. STC's failure to comply with the conditions of credit insurance policies rendered it unable to recover trade losses from insurance companies. The corporate office of STC camouflaged the outstanding dues by allowing adjustment thereof by EXIM Bank against shipping documents for jewellery/diamond export, the legitimacy of which was doubtful.

Lapses in the PSF scheme, brought out above, could have been rectified during the course of its implementation by undertaking a critical review and putting in place adequate safeguards, which would have avoided non-recovery of dues of ₹ 446.29 crore apart from infructuous expenditure of ₹ 17.07 crore on insurance premium.

The Ministry is advised to review and correct deficiencies in monitoring and control of business activities of STC by its Corporate Office/Board of Directors, without necessarily awaiting results of disciplinary action and CBI investigation.

STCL Limited

4.5 Unfruitful expenditure at Spices Park, Chhindwara, Madhya Pradesh

Unfruitful expenditure of ₹ 7.13 crore on establishment of Steam Sterilization Unit and Grinding and Packing Unit at Spices Park, Chhindwara, Madhya Pradesh

STCL Limited (Company), a Government of India Undertaking and subsidiary of The STC of India Limited, headquartered at Bangalore intended (March 2008) to establish a Steam Sterilization Unit (SSU) and Grinding and Packing Unit (GPU) at Spices Park, Chhindwara, Madhya Pradesh. These two units were to carry out the functions of cleaning, fumigation, grading, grinding, processing and packing of spices. The main objectives of setting up these two units was to ensure high quality of processed spices, reduce use of pesticides and other contaminants and thus comply with international food safety standards and quality specifications, promote marketing of branded spices directly to consumers in the international market, ensure higher returns for spice farmers through value addition in processing, enhance production of spices and help exporters to earn valuable foreign exchange. The project cost for setting up the two units was estimated at ₹ 8.04 crore, including cost of land, building, plant and machinery, power, water, preliminary and pre operation expenses, working capital, furniture and contingency. It was proposed that the above project cost would be financed by the Company to the extent of ₹ 1 crore, while the remaining ₹ 7.04 crore would be allocated by Government of India (GoI) under the ASIDE (Assistance to States for Developing Export Infrastructure and Allied Activities) scheme.

Accordingly, the Company submitted a project proposal for establishment of the above two units and requested (March 2008) Ministry of Commerce and Industry (Ministry) for sanction of funds amounting to ₹ 7.04 crore, along with duly filled application, including detailed project report on technical feasibility and economic viability. In response, the Ministry sanctioned (August 2008) only ₹ 6.29 crore for the above project, with the instruction that GoI would not be releasing any more funds and remaining ₹ 1.75 crore of the total estimated project cost of ₹ 8.04 crore would have to be met by the Company. Cost escalation, if any, would also have to be borne by the latter. The sanction letter also specified that utilization certificate for the amount sanctioned would have to be furnished by March 2010 and that a penal clause be built into the contract with the implementing agency so that the project was not delayed.

While importing required plant and machinery for the two above units, the Company availed (November 2008) concessional customs duty of three *per cent* under the Export Promotion Capital Goods (EPCG) scheme and thereby saved ₹ 1.21 crore. As per the EPCG scheme, the Company would be liable to export products valued at eight times the duty saved within eight years, failing which it would have to forfeit EPCG bond of ₹ 3.77 crore deposited with Customs authorities.

The Company submitted (March 2010) a utilization certificate for ₹ 6.29 crore to the Ministry, along with an assurance that the project was virtually fully completed, that civil and mechanical works were completed and that final testing and commissioning of the two units were in progress. It was further mentioned that the total expenditure incurred to that date (March 2010) was ₹ 7.23 crore. In addition, the Company incurred ₹ 0.30 crore towards commissioning of the two units. The Company forfeited the bank guarantee (Euro 59000 equivalent to ₹ 0.40 crore) of equipment supplier (M/s Steam Lab, Germany) for non fulfilment of contractual obligations. Thereby, the total expenditure incurred stood at ₹ 7.13 crore.

Audit examination revealed that though the two units in the project were commissioned (October 2010), the Company did not operate them on its own, as it faced acute financial crises. Accordingly, the Company leased out (March 2012) the use of the two units to M/s RDM Care (India) Private Limited i.e. after 18 months of non operation of the commissioned units. However, just nine months later (January 2013), the lease agreement with the private firm was terminated at the request of the latter. Subsequently, eight months later (September 2013), the two units were leased out to M/s A-Tech Engineering and Management.

The Company stated (September 2014) that the two units were not operated as intended and there was no export either by the Company or through its lessees. No commercial production had been carried out. However, efforts were being made to operate the Steam Sterilisation Unit. Ministry endorsed (January 2015) the views of the company.

The reply of the Company/Ministry needs to be viewed against the fact that none of the objectives stated at the time of establishing the two units was achieved, defeating the purpose of bringing about improvement in the quality of spice processing. Thus, the Company's inability to operate its two units at Spices Park, even after lapse of 48 months since they were commissioned, either on its own or through lessees to achieve the intended objectives, resulted in unfruitful expenditure of ₹ 7.13 crore (including ₹ 6.29 crore from GoI) as in September 2014. In addition, there is the further possibility that the EPCG bond of ₹ 3.77 crore deposited with Customs authorities would be forfeited, if the Company failed to ensure adequate value of exports from the two units in compliance with the provisions of EPCG scheme.

CHAPTER V: MINISTRY OF CONSUMER AFFAIRS, FOOD AND PUBLIC DISTRIBUTION

Central Warehousing Corporation

5.1 Lack of transparency in awarding Strategic Alliance Management contracts

Central Warehousing Corporation (CWC) did not adhere to the CVC guidelines and mandated tendering procedure while entering into Strategic Alliance Management agreements for operation of two of its container freight stations in the West Zone. Deficiency in the contract resulted in undue benefit to one of the contractors to the tune of ₹ 6.79 crore.

CWC, in addition to operating its warehouses, also operates Container Freight Stations (CFSs) throughout the country, where composite services for containerized movement of import/export cargo are provided. Some of these CFSs are operated through Strategic Alliance Management and Operation/Operators (SAMOs) whereby private firms operate the CFSs at a fixed fee and additional variable fee, payable to CWC, depending on the storage quantity.

The Central Vigilance Commission (CVC) guidelines (May 2006) state that all works awarded on nomination basis should be brought to the notice of the Board of the respective PSU for scrutiny and vetting *post facto*. CWC's delegation of powers of July 2000 envisaged that in case of award of contract by negotiation, without calling for tenders in emergent cases, reasons are to be recorded in writing and the cases in excess of ₹20 lakh each are to be reported to the Board of Directors.

The CVC guidelines (July 2007), while referring to a Supreme Court of India judgment[♥], state that tendering process or public auction is a basic requirement for 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.

However, in rare and exceptional cases, for instance during 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 days but there were no bidder or the bid offered was too low, etc., this normal rule may be departed from and such contract may be awarded through 'private negotiations'.

Audit observed that in two cases, discussed below, CWC did not follow the mandated procedure of awarding SAMO contracts:

[♥] ***Nagar Nigam, Meerut Vs Al Faheem Meat Export Private Limited [arising out of SLP(civil) No. 10174 of 2006]***

(i) In case of a contract of CFS at Impex Park, Navi Mumbai, CWC awarded (September 2006) the contract to M/s ZIM Integrated Shipping Services Limited and M/s ZIM Integrated Shipping Services (India) Private Limited (jointly as ZIM), on nomination basis without going for open competitive bidding, at the rate of ₹ 4.50 crore per annum with escalation of 5 *per cent per annum* on compoundable basis. Though awarding of contract to ZIM was placed before the Executive Committee in their meeting (November 2006) for ratification, bringing this to the notice of the Board of Directors could not be discerned from the records made available to audit. As such, it could not be ascertained whether mandated provisions of CVC guidelines (May 2006) and CWC's delegation of power (July 2000) were adhered to. Further, it was seen that when the CWC decided to opt for price discovery through open tender (July 2012) after the contract with ZIM was over (February 2012), the contract awarded to M/s Total Transport Systems Private Limited (October 2012) was significantly higher at ₹ 11.03 crore, which was 88 *per cent* more than what was paid by ZIM to CWC (₹5.87 crore) in the immediately preceding year 2011-12.

Audit further noticed that though in other contracts for similar CFSs the standard provision was for a fixed fee and a minimum guarantee amount of variable fee for storage units, in case of ZIM the condition was different whereby variable fee was payable only in respect of storage units handled beyond 15,000 Twenty Equivalent Units[♠] (TEUs). This caused undue benefit to the firm to the tune of ₹ 5.14 crore over the period from 2006-07 to 2011-12 (upto February 2012). Moreover, reimbursement of cost recovery charges of Customs staff was also not included in this agreement with ZIM though it was a standard clause in other similar agreements. This resulted in further undue benefit to the firm to the tune of ₹ 1.65 crore for the period from 2006-07 to 2010-11.

Thus, CWC not only awarded contract to ZIM in a non-transparent manner but also gave undue benefit of ₹6.79 crore to the contractor by having non-standard conditions in the contract.

The Ministry stated (March 2015) that decision to give the facility to M/s ZIM was taken after repeated failure of tenders for entering into Strategic Alliance for this facility and the contract was not awarded by nomination as the agreement was for 100 *per cent* reservation whereby there was no need to either issue the tender or fix the reserve price. It further stated that the rates of M/s Total Transport Systems Private Limited of 2012 should not be compared with rates of earlier contract entered into six year ago in 2006 with M/s ZIM and that no undue benefit was given to M/s ZIM. It also stated that there was no violation of CVC guidelines.

The reply of the Ministry is not acceptable in view of the following facts:

The terms and conditions for the contract entered with M/s ZIM, stated to be on 100 *per cent* reservation basis, are similar to Strategic Alliance Management operations of CFSs whereby the Corporation receives fixed lease amount every year as well as predetermined amount (per TEU basis) to earn marginal profit. Thus, the contract was *de facto* awarded

[♠] ***One TEU being equivalent to 20 foot container. The container measuring more than 20 foot is to be treated as two TEUs.***

to M/s ZIM on a nomination basis, a fact which was not brought before the Board of Directors for approval as required. Moreover, undue benefit was given to M/s ZIM due to non-inclusion of standard provisions of minimum guaranteed amount of variable fee and reimbursement of cost recovery charges of Customs staff. Further, audit has compared the rates the Corporation had fetched in October 2012 with the rates the Corporation got from M/s ZIM in the immediate preceding year i.e., 2011-12 and not with those of six year ago as stated by the Corporation.

(ii) The Corporation entered into a SAMO agreement on 22 January 2008 with M/s Hind Terminal Private Limited (HTPL) for utilizing CFS, Mundra, Gujarat for a period of two years with an option to extend it by another one year.

The proposal for expression of interest was stated to have been sent by the Corporation's Regional Manager, Ahmedabad, through e-mail (7 November 2007) to six-seven parties whose selection criteria were not on record. A generic expression of interest without any financial figure was received on 13 November 2007 only from one party namely HTPL. The management entered into an agreement (January 2008) with HTPL at a fixed fee of ₹ 3 crore *per annum* and ₹ 210 per TEU for a minimum of 24000 TEUs. As no reserve price was fixed to evaluate the bids, the reasonability of the rates in the contract entered into by the Corporation with HTPL could not be vouchsafed in audit. Further, the Management did not report this proposal to the Board of Directors as was required. The contract with HTPL was extended in March 2010 for a further period of one year at a fixed amount of ₹ 3.60 crore *per annum* with additional warehousing charges of ₹ 250 per TEU for a minimum guarantee of 30000 TEUs, adding to ₹ 4.35 crore *per annum*.

Audit further observed that when the Corporation went in for price discovery for CFS, Mundra through open competitive bidding (July 2011) it fetched a rate of ₹ 6.12 crore *per annum*, which was 41 *per cent* higher than the minimum rate of ₹ 4.35 crore payable by HTPL in the previous year 2011-12.

The Management stated (August 2014) that the contract was awarded to HTPL keeping in view the circumstances prevailing in the trade and citing dearth of business due to fear of competition. However, reply of the Management is not acceptable as proposal for awarding contract to HTPL at CFS, Mundra was not brought to the notice of the Board of Directors as envisaged in CVC guidelines.

The Ministry stated (March 2015) that the selection criteria was on records as the communication was sent to top users of Mundra International Container Terminal and as the contract was finalized on 100 *per cent* reservation basis there was no need to either fix reserve price or float a tender for the same. It further stated that the market conditions were recorded by the Regional Office level committee on 30 November 2007 and Corporate Office level in January 2008.

The reply of the Ministry is not tenable as tendering process is a basic requirement of award of a contract by any Government agency (CVC guidelines of July 2007). Moreover, the market conditions were recorded for the first time on 30 November 2007 whereas the proposal for expression of interest was sent by Regional Office Ahmedabad through email on 7 November 2007. Thus, clearly the process for utilizing CFS Mundra had already started even before the market conditions were taken on records by the Corporation.

Thus, the process adopted by the Corporation to award the contracts was in violation of CVC guidelines and against the mandated tendering procedure in both the above cases.

Food Corporation of India

5.2 Loss due to non-availing of concessional railway freight

Food Corporation of India failed to avail the benefit of concessional railway freight in terms of the agreement entered into with a private developer-cum-operator which resulted in loss of ₹ 27.23 crore.

Food Corporation of India (FCI) entered (June 2005) into two service agreements with a private developer-cum-operator (DCO) viz. M/s Adani Agri Logistics Limited (AALL) on 'build, own and operate' basis for integrated storage and bulk handling and transportation of foodgrains between base depots[1] and field depots[2] of FCI in Circuit-1[3] and Circuit-2[4]. In consideration of the services provided by the DCO, FCI was required to pay storage-cum-handling charges to the DCO in accordance with the terms of the service agreements. The commissioning of the project and commencement of commercial operations of the facilities was to be accomplished by the DCO within 36 months from the date of execution of the agreements. The agreements were to be operative for a period of 20 years from the date of commencement of operations.

The terms and conditions of the service agreements, *inter alia,* provided that the DCO would develop, procure and own at its cost special bulk foodgrains wagons and lease them to the Indian Railways for the duration of the service period under the Railways' Own Your Wagon Scheme (OYWS). Further, the DCO and FCI would jointly negotiate with the Indian Railways the station to station railway freight rates or general rebate in freight charges for rail transportation between base depots and field depots. The DCO would enter into an appropriate OYWS agreement with the Indian Railways, the draft of which would be approved by FCI. The railway freight so negotiated and finalised would be paid by the DCO to the Railways and be reimbursed by FCI to the DCO.

The service agreements with DCO were entered into by FCI after getting a cost-benefit analysis carried out (June 2003) by RITES Limited[5] (Consultant). The cost-benefit analysis was done by the Consultant on the assumption that a freight concession of 22.5 *per cent* on the normal tariff would be granted by the Railways under OYWS as per the

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[1] ***Base depot refers to the depot located in the foodgrains producing area.***

[2] ***Field depot refers to the depot located in the distribution/consuming area.***

[3] ***Circuit refers to a set of facilities forming a chain, comprising base depot and field depots. Circuit-1 consisted of base depot at Moga (Punjab) and field depots at Chennai, Coimbatore and Bengaluru.***

[4] ***Circuit-2 consisted of base depot at Kaithal (Haryana) and field depots at Navi Mumbai (Maharashtra) and Hooghly (West Bengal).***

[5] ***RITES Limited is a multi disciplinaryconsultancy organisation in the fields of transport, infrastructure and related technologies.***

then existing practice. Based on this assumption, the Consultant concluded that the project of bulk handling, storage and transportation of foodgrains would be financially remunerative for FCI. Thus, the underlying premise for entering into the service agreements by FCI was the expected savings that would accrue to FCI on account of rebate in railway freight charges.

Audit observed that during the period of 36 months provided under the service agreements for operationalisation of the project, the FCI/DCO did not negotiate and finalise the rebate in freight to be granted by the Indian Railways under OYWS. Meanwhile, the Ministry of Railways introduced (April 2008) a new liberalised wagon investment scheme (LWIS) superseding OYWS. Under LWIS, concession of 15 *per cent* in the railway freight was admissible only to the end-users i.e. consumers or producers of goods. Thus, the DCO, being a logistic company, became ineligible for the rebate. However, despite the fact that the rebate in railway freight was no longer admissible to the DCO, FCI allowed the DCO to commence transportation of foodgrains between base depots and field depots in Circuit-1 and Circuit-2 from November 2008 and October 2008 respectively and made payment of freight charges at normal tariff rates. The Ministry of Railways did not agree (May 2009) to grant any rebate to FCI under LWIS even after pursuance of the matter since the rebate under LWIS was not available to a logistic company. Audit further observed that LWIS provided that the customers who had already invested in wagons or had obtained approval of the Ministry of Railways under any earlier wagon investment scheme including OYWS shall have the option to continue as per the terms and conditions of that particular scheme. Thus, had FCI/DCO ensured that the rebate in railway freight was negotiated and finalised with the Railways in time, the admissibility of rebate would have continued under LWIS at least to the extent of 15 *per cent* of the normal freight.

The DCO moved a quantity of 5,04,928 metric tons (MT) and 4,82,310 MT of foodgrains in Circuit-1 and Circuit-2 respectively since operationalisation of the project on which expenditure of ₹ 107.70 crore and ₹ 73.86 crore respectively were incurred by FCI till May 2014 on account of basic railway freight. The loss suffered by FCI due to non-admissibility of concessional freight at the rate of 15 *per cent* of basic freight, therefore, worked out to ₹ 27.23 crore.

Thus, failure of FCI and the DCO in obtaining approval of the Ministry of Railways for grant of rebate in freight under OYWS and allowing the DCO by FCI to commence transportation of foodgrains at normal freight rates resulted in loss of ₹ 27.23 crore. Further, as the service agreements with the DCO were operative for a period of 20 years from the date of commencement of operations, the non-admissibility of rebate in railway freight would result in recurring loss to FCI over this period thereby defeating the very purpose of venturing into bulk handling, storage and movement of foodgrains.

The Regional office, Haryana of FCI stated (January 2014) that the issue was taken up (May 2008) by the DCO as well as FCI Headquarters (May/June 2008) with the Railways to get rebate in freight under LWIS but the Railways denied (May 2009) to grant any rebate. Further, the Zonal office of FCI stated (March 2014) that the Railways was having complete monopoly over its operations and whatever they did was almost final. The pursuance by field offices of FCI with the Railways was a futile exercise and the matter was taken up with FCI Headquarters for appropriate action.

The Management reply is not tenable as there was a time lag of 36 months in operationalisation of the project from the date of agreements (June 2005) during which FCI/DCO failed to come to favourable terms with the Railways in respect of rebate in railway freight under OYWS despite the freight concession being the basis of financial viability of the scheme. Such rebate granted under OYWS would be admissible even after introduction of LWIS. The contention of the Management that the Railways denied any rebate is not acceptable since the matter was taken up by FCI with the Railways only in May/June 2008 i.e. after OYWS was superseded by LWIS under which the DCO became ineligible for the rebate.

FCI stated (January 2015) that it was incomprehensible to forecast closure of the rebate scheme (OYWS) and FCI had no mechanism available for anticipating or pre-empting this move on part of the Railways. Further, the DCO had started taking up the matter with the Railway Board in July 2007 itself and requested Railways to notify the concessional freight. Ministry of Railways did not respond to it till May 2008 and then only the matter was taken up by FCI with the Railways. However, the Railway Board informed (May 2009) that the request of FCI had not been agreed to. Further, the movement of foodgrains was started at the normal freight rates in order to fulfil the PDS requirements and on the assumption that the decision on rebate in freight, whenever decided, would be made applicable from retrospective date. The Ministry endorsed (January 2015) the reply of FCI Headquarters.

The reply of FCI/Ministry is not acceptable because of the fact that even though it was the joint responsibility of DCO and FCI to negotiate and finalise the rebate in railway freight, FCI took up the matter with the Railways only in May 2008, almost 3 years after the agreement between two parties when OYWS had already been superseded by LWIS under which the rebate was not available. Before May 2008, it was only the DCO which was taking up the matter with the Railways. Moreover, the assumption made by FCI that the decision on rebate in freight would be made applicable from retrospective date is not backed by any assurance from the Railways to that effect. Further, while taking into account the fact that FCI commenced the movement of foodgrains at normal freight rates in order to fulfil PDS requirements, it is observed that non-finalisation of rebate in railway freight would result in continuing loss to the exchequer over the 20-year period of the service agreements entered into by FCI with the DCO. FCI Management should have taken up the matter with the Railways before operationalisation of the long-term project which was not done leading to the recurring loss.

5.3 Excess payment of mandi labour charges

Food Corporation of India made excess payment of ₹ 16.96 crore to the Government of Uttar Pradesh and its agencies during the years 2010-11 and 2011-12 due to reimbursement of inadmissible elements as part of mandi labour charges on procurement of wheat.

The Ministry of Consumer Affairs, Food and Public Distribution (Ministry) conveyed (April 2010 and June 2011) the provisional rates of procurement incidentals to be paid by

Food Corporation of India (FCI) to the Government of Uttar Pradesh and its agencies for procurement of wheat for the Central Pool during the Rabi Marketing Seasons (RMS) 2010-11 and 2011-12 respectively. These provisional incidentals included a sum of ₹ 10.91 per quintal for each of the two RMS on account of mandi labour charges to be paid for handling of wheat in mandi.

As per the guidelines for submission of incidental claims by the State government/agencies as issued (September 2010) by the Ministry, mandi labour charges are the charges incurred in the mandis/markets for engaging the labour to perform various activities like cleaning grains, filling in the bags, weighing, stitching, labeling, stacking, loading in truck, etc. The guidelines further clarified that the expenditure incurred for making arrangement for lights, drinking water, temporary sheds are not included in the cost of mandi labour charges as these are part of the services provided by the marketing committees for which separate market fee is paid.

Audit, however, observed that the provisional rate (₹ 10.91 per quintal) of mandi labour charges fixed for RMS 2010-11 and 2011-12 included inadmissible elements viz. arrangements at purchase centre for tent (₹ 1.90 per quintal), drinking water (₹ 0.50 per quintal) and petromax (₹ 1.00 per quintal). As the expenditure on these elements was already included in 'mandi charges', these were to be excluded from the mandi labour charges. Thus, the expenditure on inadmissible elements aggregating ₹ 3.40 per quintal were reimbursed by FCI to the Government of Uttar Pradesh and its agencies as part of mandi labour charges. During RMS 2010-11 and 2011-12, FCI Uttar Pradesh region procured 498.81 lakh quintals of wheat on which the excess reimbursement of mandi labour charges at the rate of ₹ 3.40 per quintal worked out to ₹ 16.96 crore.

Thus, the Ministry violated its own guidelines by including such elements in the mandi labour charges which were already paid under other heads of expenditure in the provisional cost sheet. Further, as FCI was also aware of these guidelines as well as the fact that mandi labour charges were to be paid only in respect of handling of wheat in mandi, it was necessary on the part of FCI to take up the matter with the Ministry for removal of overlapping elements from the mandi labour charges before releasing the payment on this account to the State Government/State Government Agencies. The Ministry, in turn, should have excluded the inadmissible elements from mandi labour charges. Thus, failure to exercise due diligence by FCI resulted in excess payment of ₹ 16.96 crore.

The Management stated (August 2013) that since there was no bifurcation of mandi labour charges, FCI was not aware about the overlapping elements and the reimbursement had been made to the State Government Agencies under the cost sheet determined by the Ministry. The Ministry elaborated (December 2014) on the procedure for working out the mandi labour charges by indexing the final or provisional rates of the previous year with the Consumer Price Index. It further added that in case of Uttar Pradesh, mandi labour charges of ₹10.91 per quintal were allowed accordingly during 2010-11 and 2011-12 and further stated that FCI was being advised to ensure payment after thorough check of claim and ensuring no overlapping of claims.

The reply of the Management is not acceptable as being nodal agency for implementing food policy of the Government of India, FCI should have ensured compliance of the

Guidelines for State Governments/Agencies for Submission of Incidental Claims. As such, FCI was bound to verify the admissibility of the components of mandi labour charges before making reimbursement. Further, the Ministry did not furnish specific reply regarding admissibility of components of mandi labour charges and also remained silent on recovery of excess payment from the Government of Uttar Pradesh.

5.4 Excess payment of interest

Food Corporation of India made excess payment of interest of ₹ 5.22 crore due to ineffective monitoring and lack of internal checks on the cash credit

Food Corporation of India (FCI) entered (June 1989) into an agreement for cash credit facility from a consortium of banks led by State Bank of India (SBI) for financing its day-to-day operations. As per procedure under cash credit facility, the branches of banks maintaining cash credit accounts of FCI Regional/District Offices were required to transfer the net debit or credit balances to FCI Zonal cash credit accounts invariably before end of the day's transactions through auto sweep facility. Further, the branches of banks maintaining FCI Zonal cash credit account would have to transfer any credit balance or debit balance exceeding the overnight limit to the centralised cash credit account maintained in Industrial Finance Branch (IFB) of State Bank of India, New Delhi. The interest on the credits availed by FCI would be calculated on daily balance and would be charged to FCI on quarterly basis.

During test check of records relating to cash credit accounts of FCI Zonal Office (East), Regional Office Ranchi (Jharkhand) and nine District Offices[♥], Audit observed the following:

- The daily transfer of all credit balances in the cash credit account of Regional/District Offices to the Zonal cash credit account would ensure adjustment of all credit balances against debit balances and payment of interest on the net outstanding balance. However, there were instances of delayed transfer of credit balances by the bank branches in respect of FCI Regional Office, Ranchi (Jharkhand) and nine District Offices during the period 2008-09 to 2013-14. This resulted in excess payment of interest on cash credit account by FCI to the tune of ₹ 5.02 crore. This excess payment of interest, however, remained undetected until it was brought to the notice of FCI by Audit, which indicated ineffective monitoring and absence of necessary control by the former over the cash credit facility.

- There was no mechanism at the FCI Zonal Office (East), Kolkata to check the accuracy of interest charged by the bank on the daily balance in the cash credit account. Audit detected (June 2013) that the bank had charged excess interest on cash credit account of FCI Zonal Office (East), Kolkata to the tune of ₹ 19.45 lakh (August 2012: ₹ 18.73 lakh, February 2013: ₹ 0.28 lakh and March 2013: ₹ 0.44 lakh). After the excess payment of interest was pointed out by Audit, FCI claimed (July 2013) this amount from the bank.

[♥] ***24-Parganas, Durgapur, Port Depot, Ranchi, Gaya, Chhapra, Muzaffarpur, Patna and Bhubaneswar.***

Thus, due to ineffective monitoring and lack of internal checks over cash credit facility, FCI incurred excess payment of interest amounting to ₹ 5.22 crore.

The Management stated (December 2014) that after persuasion with SBI, the excess interest of ₹ 19.45 lakh was received back (October 2014). As regards the excess interest due to delayed transfer of credit balances of cash credit accounts by the bank branches at FCI Regional/District Offices to the FCI Zonal cash credit account, persuasion for its refund was being made.

The Ministry of Consumer Affairs, Food and Public Distribution, Department of Food and Public Distribution (Ministry) stated (December 2014) that it had asked FCI to send quarterly report for instances of delayed transfer of credit balances. The Ministry further stated (January 2015) that after due persuasion with the SBI for the refund of excess interest, the bank had principally agreed to the claim of FCI and issued instructions to its concerned branches to settle the same.

Audit observed that IFB of SBI, New Delhi had forwarded (October 2014) the FCI's claims for refund of interest due to delay in transferring the credit balances to respective bank branches with the request to verify and arrange to settle the same. However, refund of the excess interest was awaited (January 2015).

5.5 Avoidable payment of terminal charges

FCI paid to the Railways non-leviable destination terminal charges amounting to ₹ 5.01 crore in respect of its own sidings from July 2007 to March 2013

Food Corporation of India (FCI) moves foodgrains from procuring States to deficit States by rail. In addition to the normal freight charges, the Ministry of Railways introduced (May 2007) levy of terminal charge of ₹ 10 per tonne per terminal with effect from 1 July 2007 for movement of goods on Railways owned terminals and sidings. These terminal charges were leviable on loading/ unloading terminals, independently and separately, on the basis of chargeable weight at the time of issue of Railway Receipt (RR). The rate of terminal charge was enhanced (January 2008) by the Ministry of Railways to ₹ 20 per tonne per terminal with effect from 1 February 2008.

A total of 102 railway sidings[1] were owned by FCI all over the country out of which the records of 53 railway sidings[2] were test checked in Audit. It was observed that out of these 53 railway sidings, in case of 41[3] sidings, the RRs raised for the foodgrains consignments also included destination terminal charges amounting to ₹ 5.01 crore which were paid by FCI along with freight charges to the Railways during the period July 2007 to March 2013. As these sidings were owned by FCI and not by the Railways, the destination terminal charges were not leviable in these cases. Audit observed that the monthly movement plan prepared by FCI Headquarters clearly indicated whether there

[1] The 102 owned sidings of FCI consisted of 19 sidings in East zone, 6 sidings in North-East zone, 15 sidings in West zone, 25 sidings in North zone and 37 sidings in South zone.

[2] These 53 sidings consisted of 19 sidings of East zone, 8 sidings of North zone and 26 sidings of South zone.

[3] These 41 sidings consisted of 19 sidings of East zone, 6 sidings of North zone and 16 sidings of South zone.

was FCI owned siding at the destination terminal and thus there was no ambiguity about the ownership of railway sidings at the destination. Therefore, the destination terminal charges of ₹ 5.01 crore were not required to be paid at all in such cases. However, FCI did not verify the RRs with regard to the ownership of sidings at the destination end, before making payments to the Railways. This resulted in avoidable payment of railway freight by FCI to the extent of ₹ 5.01 crore during the period July 2007 to March 2013 (**Annexure-X**).

While accepting the audit observation, the Management stated (May 2013) that claims for refund of the wrongfully paid terminal charges were lodged with the Railways by the dispatching regions. Further, with effect from 1 April 2013, the Railways had stopped levying terminal charges even for its own railheads.

The Management further stated (December 2014) that a reply to the audit para would be sent upon receipt of necessary information from the concerned zonal/regional offices of FCI. The final reply of the Management was awaited (January 2015).

The matter was reported to the Ministry in September 2014; their reply was awaited (March 2015).

CHAPTER VI: MINISTRY OF DEVELOPMENT OF NORTH EASTERN REGION

North Eastern Regional Agricultural Marketing Corporation Limited

6.1 Misappropriation of cash

Poor internal controls and non-observance of the bank operation mandate resulted in fraudulent withdrawal of ₹ 1.41 lakh from the bank accounts of North Eastern Regional Agricultural Marketing Corporation Limited.

North Eastern Regional Agricultural Marketing Corporation Limited (Company) maintained current accounts with several banks such as State Bank of India, New Guwahati (SBI) and Union Bank of India, Guwahti (UBI) and withdrew cash from the current accounts through cheques drawn on self for making petty payments during the course of its day-to-day operations. Test check of records pertaining to the period from April 2010 to March 2013 revealed that four cash withdrawals aggregating ₹ 1.41 lakh were made during April 2010 to June 2010. These included one withdrawal of ₹ 41,000 (12 April 2010) from the Company's account with SBI and three withdrawals of ₹ 30,000 (06 May 2010), ₹ 50,000 (17 May 2010) and ₹ 20,000 (03 June 2010) from its account with UBI.

Audit observed (November 2013) that the entries for the above four cash withdrawals were not recorded in the cash book. The requisite entries in the cheque issue register were also not recorded in respect of all the withdrawals, except that for ₹ 41,000. Besides, there was no system of preparing monthly statements showing reconciliation between bank statements and cash book, due to which the cash withdrawals of ₹ 1.41 lakh remained undetected during the period from June 2010 to November 2013. The bank reconciliation statements for the years 2009-10 to 2011-12 were not available in the records of the Company; hence Audit could not verify as to how unaccounted withdrawal of ₹ 1.41 lakh was dealt with and reconciled by the Management. Audit further observed that the Statutory Auditor of the Company had reported (August 2012) that the latter had not prepared any comprehensive accounting manual laying down the rules for financial accounting and delegation of financial powers, etc.

Further, as per the bank operation mandate of the Company, the cheques issued in the name of the Company should be signed by two authorised signatories viz. the Managing Director (MD) and the General Manager (Finance and Accounts) (GM-F&A). Audit, however, observed that the self cheque for withdrawal of ₹ 41,000 was issued (31 March 2010) under the joint authorisation of the then GM (F&A) and the then MD while those for the other three withdrawals of ₹ 1 lakh were issued under the single authorisation of the then GM (F&A) only. It was further noticed that in respect of the three withdrawals amounting to ₹ 1 lakh made during May 2010 and June 2010, the then GM (F&A) had requested the bank to clear the cheques under his signature only on the ground that the other signatory i.e. the then MD was out of station for official work. The Management, however, confirmed (November 2013) that the then MD was available in the office on 17 May 2010 i.e. on the date of withdrawal of ₹ 50,000.

Thus, not recording entries of daily cash withdrawals in the cash book and poor internal controls such as issue of cheques without entering in cheque issue register, non-preparation of monthly bank reconciliation statements, non-observance of the bank operation mandate by the Management resulted in misappropriation of cash to the extent of ₹ 1.41 lakh. No disciplinary action was taken by the Company against the delinquent official.

On being pointed out (November 2013) by Audit, the Management stated (March 2014) that a notice for recovery was sent (February 2014) by the Company to the then GM (F&A) wherein he was asked to deposit a sum of ₹ one lakh along with interest at the rate of 28 *per cent* per annum from the date of withdrawal to the date of deposit. The then GM refunded (February 2014) the amount of ₹ one lakh to the Company and requested for waiver of interest. The Management further stated (April 2014) that a notice had been issued to the then GM to repay the balance amount of ₹ 41,000 together with interest on the total amount of ₹ 1.41 lakh at the rate of 14.5 *per cent* per annum from the date of withdrawal of money. However, the latter refused (May 2014) to repay the amount and stated that the same was drawn by the then cashier for specific purposes as mentioned in the cheque issue register.

Audit, however, observed that the Company did not take any further action for recovery of the balance amount of ₹ 41,000. Further, the rate of recoverable penal interest was reduced from 28 *per cent* per annum to 14.5 *per cent* per annum without recording any justification for the same. On being enquired, the Management stated (July 2014) that the decision was taken by the former MD and no reasons were available on record for that decision.

Thus, poor internal controls over cash and bank transactions resulted in fraudulent withdrawal and misappropriation of cash to the extent of ₹ 1.41 lakh. Although an amount of ₹ 1 lakh has been recovered at the instance of audit, the remaining amount of ₹ 41,000 along with penal interest on the total amount of ₹ 1.41 lakh was still pending for recovery (July 2014).

The Ministry, in its interim reply, stated (November 2014) that it did not accept the comments received from the Company in the matter and had sought pending action on inquiry outcomes and inquiry report from the Company. The Ministry would submit reply to Audit on receipt of a satisfactory report from the Company.

CHAPTER VII: MINISTRY OF FINANCE

India Infrastructure Finance Company Limited

7.1 Fund Management and Financing

7.1.1 Introduction

India Infrastructure Finance Company Limited (the Company) was incorporated in January 2006 as a wholly-owned company of the Government of India under the Companies Act, 1956 to provide long term finance to viable infrastructure projects under 'Scheme for Financing Viable Infrastructure Projects through a Special Purpose Vehicle called India Infrastructure Finance Company Limited (SIFTI)'. It extends financial assistance to the sectors included in the harmonized list of infrastructure sub-sectors approved by the Cabinet Committee on Infrastructure on 1st March 2012 viz. transport, energy, *etc* mainly for projects under Public Private Partnership.

7.1.2 Financial highlights

Details of fund mobilization and disbursement by the Company during the three years ended March 2014 are summarized below:

(₹ in crore)

Mobilisation	**2011-12**	**2012-13**	**2013-14**
Bonds	0	5041.32	7176.21
Bilateral/ Multilateral borrowings	1033.74	1079.57	907.45
Domestic Loan	0	1000	0
Total mobilisation	**1033.74**	**7120.89**	**8083.66**
Disbursements			
Direct Lending	4191.00	5138.00	3774.00
Refinance	668.00	250.00	1838.00
Takeout Finance Scheme	560.00	2018.00	893.00
Total disbursements	**5419.00**	**7406.00**	**6505.00**

7.1.3 Audit objectives

Audit was carried out to assess:

- Whether funds were raised after proper financial planning commensurate with the business requirement;
- Whether due diligence was ensured before borrowing;
- Whether controls relating to sanction and disbursement of loans were sound, effective and adequate to cover the risk of lending;
- Whether adequate monitoring mechanism existed to ensure timely recovery of dues; and

- Effectiveness and efficiency in utilization of funds.

7.1.4 Audit criteria

The performance of the Company was assessed against the following audit criteria:

- Scheme for Financing Viable Infrastructure Projects through a Special Purpose Vehicle called India Infrastructure Finance Company Limited (SIFTI);
- The internal guidelines/policies/procedures of the Company relating to mobilization of fund, sanction of projects, disbursement and recovery;
- Agenda & Minutes of the meetings of Board of Directors, Audit Committee and other Internal Committees of the Company;
- Best practices followed in the Industry; and
- Resource plan and Memorandum of Understanding (MOU)/Statement of Intent (SOI) targets of the Company.

7.1.5 Scope of Audit and sample

Audit examined the system of fund mobilization and disbursement followed by the Company during the period 2011-12 to 2013-14. The audit sample was selected based on Stratified Random Sampling Method using IDEA package from the total funds raised and disbursements made as indicated below:

Number of total borrowings during 2011-12 to 2013-14 and sample selected for audit					
Amount raised	₹1000 crore or more	₹500-1000 crore	₹100-500 crore	Less than ₹100 crore	Total
Bonds (Number of cases)	3	7	15	14	39
Bilateral/ Multilateral borrowings (Number of tranches)	0	0	7	127	134
Domestic loan (Number of cases)	1	-	-	-	1
Total (Number of cases)	4	7	22	141	174
Percentage selection	100	50	40	0	
No. of cases in sample	**4**	**4**	**9**	**0**	**17**
Overall selection percentage out of total population					10

Number of total projects sanctioned during 2011-12 to 2013-14 and sample selected for audit						
Particulars	₹1000 crore or more	₹500-1000 crore	₹200-500 crore	₹100-200 crore	Less than ₹100 crore	Total
Direct lending (Number of Projects)	0	1	19	26	58	104
Refinance Scheme (Number of Projects)	1	2	2	0	0	5
Takeout Finance Scheme (Number of Projects)	0	3	7	9	13	32

Total (Number of Projects)	**1**	**6**	**28**	**35**	**71**	**141**
*percent*age selection	100	50	35	25	15	
No. of cases in sample	**1**	**3**	**10**	**9**	**11**	**34**
Overall selection percentage of total population						24

7.1.6 Audit findings

7.1.6.1 Achievement of targets as per Statement of Intent (SOI) set by Ministry of Finance

Based on the inputs from the Company, annual targets for resource mobilization and disbursement by the Company are approved by the Ministry of Finance (Ministry) in the form of Statement of Intent (SOI). Actual performance of the Company as against the targets approved by the Ministry during 2011-14 was as under:

(₹ in crore)

Sl. No.	**Parameters**	**2011-12**		**2012-13**		**2013-14**	
		Targets	**Achievements**	**Targets**	**Achievements**	**Targets**	**Achievements**
1	Resources[1]	6500.00	3297.00	11635.00	8803.00	Not fixed	Not fixed
2	Share of resources raised without sovereign guarantee	Not fixed	Not fixed	Not fixed	Not fixed	62 *per cent*	77 *per cent*
3	Disbursements under:						
(a)	Refinance	0.00	668.00	2000.00	250.00	2500.00	1838.00
(b)	Takeout	5400.00	560.00	4000.00	2018.00	3500.00	893.00
(c)	Direct Lending	6100.00	4191.00	6800.00	5138.00	5500.00	3774.00
4	Net Profit[2]	462.00	547.00	725.00	787.00	1050.00	646.00
5	Return on Average Assets (ROA)	1.27	1.90 *per cent*	1.90 *per cent*	2.18 *per cent*	2.80 *per cent*	1.48 *per cent*

It was noticed that:

- targets for resource mobilisation remained under-achieved during 2011-12 and 2012-13.
- disbursements made under different schemes also fell short of the given targets ranging between 42.14 *per cent* to 52.88 *per cent*.
- both Net profit and Return on Average Assets exhibited significant decline during 2013-14 over the targets for the year.

[1] ***Targets for resources for 2011-12 & 2012-13 were defined in terms of amount excluding capital, whereas the same for 2013-14 were as a percentage of resources raised without government guarantee to total resources raised.***

[2] ***Net Profit and corresponding ROA target till 2012-13 was for Net Profit available for Distribution and subsequently for 2013-14 these were for Net Profit (after Taxes).***

Reasons for downfall in the performance of the Company have been elaborated in the following paragraphs.

7.1.6.2 Deficient Fund Planning

The Company formulated its Annual Resource Raising Plan (ARRP) to estimate the requirement of funds mainly based on the following:

(i) Cumulative amount of sanctions and disbursements as at the end of the respective previous years,

(ii) Expected amount of loan to be disbursed under different schemes of the Company,

(iii) Funds available at the beginning of the year,

(iv) Funds to be kept liquid,

(v) Funds to be borrowed / raised and

(vi) Loan repayment and servicing

However, an examination of the system of estimation of projected fund requirements by the Company disclosed the following inadequacies:

(i) Detailed workings of fund requirements on account of expected loans to be disbursed under different schemes of the Company and funds expected to be raised through borrowings were not found in records of the Company and the same were also not provided to Audit despite specific request (19 March 2015). Accordingly, Audit made an attempt to assess the effectiveness of the projections made by the Company with reference to actual results. It was observed that there were significant variations between the amount of actual and projected borrowings and disbursements as shown below:

(₹ in crore)

Particulars	**2011-12**	**2012-13**	**2013-14**
Projected borrowings	7053.00	11700.00	14600.00
Actual borrowings	1033.74	7120.89	8083.66
Projected disbursements	10000.00	10000.00	11900.00
Actual disbursements	4409.22	6229.00	5459.85

(ii) The Company considered net cumulative sanctions at the end of previous year for assessing the fund requirements for 2011-12 whereas gross amount of cumulative sanctions was considered for assessing fund requirements for 2012-13 and 2013-14. Net sanctions represented the amount of loans allocated to Company (in case of consortium finance the amount is finally allocated to each lender by the consortium) related to projects which had achieved financial closure and gross sanctions included amounts sanctioned by the Company even for the projects where financial closure was yet to be achieved. There were significant differences in the amount of net and gross sanctions for 2012-13 and 2013-14 as detailed below:

(₹ in crore)

Year	Amount of cumulative Gross sanctions at the end of previous year	Amount of cumulative net sanctions at the end of previous year
2012-13	40373	32278
2013-14	51887	38841

Due to consideration of gross sanctions instead of net sanctions, the fund requirements assessed by the Company turned out to be higher than the actual requirements and the Company was saddled with surplus funds at the end of the year as shown below:

(₹ in crore)

Particulars	March 2012	March 2013	March 2014
Projected liquidity as assessed by the Company	5000.00	3000.00	4200.00
Actual liquidity represented by Total Fixed Deposits-Total Overdrafts	5370.50	7945.49	11141.55
Difference being excess actual liquidity than planned	370.50	4945.49	6941.55

Thus, due to deficient assessment of fund requirements, the Company landed in a situation of surplus funds compared to actual requirements which progressively increased over the years.

The Company/Ministry stated (January/March 2015) that the Company prepares Annual Resource Raising Plan (ARRP) on the basis of the latest SOI available which was based on information regarding expected disbursement and fund raising for the same considering the liquidity requirements of the Company. Credit Department, Corporate Planning Department and Resource and Treasury Department(s) analyzed past achievements of sanctions, disbursements etc, focus on future business activities and market conditions for projecting disbursements and borrowing required by the Company. It was also mentioned that financial projections though might carry element of subjectivity, were not made arbitrarily. Further, the Company also tries to raise funds at appropriate cost through tax free bonds which requires Government approval and takes time.

The fact remains that the Company was not maintaining detailed workings of expected disbursements and borrowings with their tentative time schedule based on past experience and was not consistent in considering net sanctions instead of gross sanctions for assessing fund requirements resulting in a situation where it found itself with progressively increasing surplus resources.

7.1.6.3 Management of Fund

(a) Holding excess unutilised funds

As indicated in the paragraph 7.1.6.2 above, the Company was having progressively increasing funds over the years due to inadequacies in the assessment of fund requirements. The surplus available funds were parked in fixed deposits (FDs) which extended for a period upto one year. For meeting its temporary fund requirements, it was taking overdraft against such FDs as and when the need arose. Outstanding balance of FDs and overdraft against FDs as on 31 March 2012, 2013 and 2014 were as under:

(₹ in crore)

As on	Balance of total FDs	Balance of overdraft raised against FDs
31 March 2012	8114.18	2743.69
31 March 2013	9429.34	1483.86
31 March 2014	13225.47	2083.92

As seen from the above, the Company borrowed funds in excess of requirements and parked the same under fixed deposits against the spirit of the main objective of the Company to channelize funds in infrastructure projects. The Company availed overdraft against fixed deposits for all purposes including disbursements.

The Company/Ministry stated (August 2014/January 2015/March 2015) that actual timing and quantum of disbursement in infra sector is highly unpredictable due to long gestation period and unexpected delay which might happen during the course of the project. Sixty projects funded by the Company had suffered average delay of 15 months from COD proposed at the time of appraisal. Hence the resources raised by the Company till the time of disbursement were parked in FDs with PSU banks as bank provided a risk free investment with high security, at yield higher than other investment opportunities available to the Company like Government Securities (G Sec.) etc. Further, the Company would not want to get into compelling situation to raise funds at prohibitive costs. Therefore, it borrowed for longer tenures to meet requirement of funds, for long term infrastructure projects, while meeting short term requirement of funds from overdraft of bank deposits.

The replies are to be viewed against the fact that parking of funds in FDs was not the core business of the Company. The Company needs to put in place a well documented system and standard operating procedure after considering the requirements of stakeholders to assess the requirements of funds and to channelize them in the infrastructure as per its main objective.

7.1.6.4 Borrowings

Examination of the selected cases of borrowings revealed the following instances of borrowing at cost that was higher than the prevailing rates or other options available to the Company:

(a) Issue of Taxable Bonds

The Company decided (4 July 2012) to raise ₹ 2000 crore through long term bonds in tranches for tenors[♣] of 15, 20, 25 and 30 years during 2012-13. Since the available amount of credit rating was ₹ 1109.04 crore only, the Company invited (11 July 2012) bids for a bond issue of ₹ 1100 crore from top 15 arrangers for 20, 25 and 30 years' tenor

[♣] ***Implies tenure or period of loan or bond as used by the Company in its records.***

bonds. In response to the above, 12 arrangers submitted their bids (10 for 25 years' bonds and 11 for 30 years' bonds), which were opened on 17 July 2012. Audit observed that:

(i) Board of Directors (Board) had passed the resolution to raise the fund for tenor of 15, 20, 25 and 30 years; however, the Company did not call for the bids for 15 year tenor bonds without recording any reasons therefor. G-Sec rates (semi-annualized) prevailing as on coupon fixation date *(i.e.* 20 July 2012) for a tenor of 15 years was 0.2385 *per cent* lower (i.e., 8.5369 minus 8.2984) than that for the 25 years' tenor. In such a scenario, raising fund through bonds with 15 years' tenor was more advantageous. Thus, not raising bonds for 15 years as per the decision of Board, saddled the Company with an avoidable burden of extra interest cost to the tune of ₹ 37.56 crore in 15 years @ ₹ 2.5043 crore p.a.

(ii) The Company without recording any reasons, did not raise fund through 20 years' tenor bonds though it had called for and received bids for a total sum of ₹ 1100 crore. The semi-annualised G-Sec rates and the quoted spread, taken together for 20 years tenor bonds, was 0.0905 *per cent* lower than that for 25 years' tenor bonds. The Company could have raised fund for 20 years' tenor instead of 25 years and avoided the extra interest cost amounting to ₹ 19.01 crore (*i.e.,* 0.0905 *per cent* p.a. x ₹1,050 crore x 20 years).

The Company stated (January 2015) that they were in the business of financing long term infrastructure projects for which long term funds are required. Further, DFS[♠] had advised (March 2012) the Company to raise resources for a longer tenor of 15-20 years and above so that the development of bond market takes place. Since, there were many 15 year bonds already in the market; a benchmark (with actively traded bonds) for 15 year tenor already existed. By issuing these bonds, a benchmark for 25 and 30 years was created for future long tenor bond issuances by the Company and other Corporates and a benefit of this shall be reaped by the entire country in the future. This effort by the Company was also praised by the Ministry. Considering the Company's long term funds requirement and DFS' advice, preference was given to raise funds with a longer tenor i.e. 30 years, 25 years and 20 years. Accordingly, at the time of book-building, first the bids for longer tenor bonds were allotted and the entire issue size/ rating limit of ₹ 1,100 crore was exhausted by 25 year tenor bonds. Also, it is not possible to ascertain the coupon rates based just on the benchmark G-Sec yield as the final coupon depends upon the spread over the G-Sec yield which is arrived at after the book-building process.

The fact, however, remains that:

(i) The Company, did not adhere to the approval of the Board and directions of the Ministry, and did not invite bids for 15 years' tenor bonds to explore the expected coupon rates. Further, comparison of G-Sec rates for 15 years' tenor bonds and 25 years' tenor bonds reflected an extra burden towards interest cost of ₹ 37.56 crore over 15 years. Further, comparison of spread for 15 years bonds was not possible as the Company did not invite the bids for these bonds.

[♠] ***Department of Financial Services, Ministry of Finance***

(ii) Out of bids received for ₹ 690 crore for 30 years' tenor, the Company issued bonds for only ₹ 50 crore. Therefore, even the stated criteria of first priority to long tenor bonds was also not followed by the Company.

(b) Raising loan from LIC

The Company requested (24 February 2012) Life Insurance Corporation of India (LIC) to provide indicative term sheet for ₹ 1000 crore debt/bond for a tenor of 15 years fully backed by Government of India.

Though the Company had a balance of ₹ 8114.25 crore in FDs as of 21 March 2012, it requested (21 March 2012) LIC to provide long term debt of ₹ 1000 crore backed by GoI guarantee for 15 years' period taking the plea that the funds were required within the same financial year urgently for onward lending to infrastructure projects. LIC agreed (29 March 2012) to grant the Company a Rupee Term Loan of ₹1000 crore. The loan agreement was signed on 30 March 2012 and the loan was drawn on 28 May 2012.

Having entered into an agreement with LIC the Company had no other option but to draw the loan at an interest rate of 9.36 *per cent* p.a. plus guarantee fee to GOI @ 0.25 *per cent* p.a. i.e. making the effective cost of the borrowing as 9.61 *per cent* against the then prevailing AAA rates of 9.45 *per cent* for 15 years as per Reuters screen as on 28 May 2012. Even after considering the likely bond issue expenses of approximately 0.24 *per cent*•, the extra avoidable cost of the borrowing from LIC at higher rate of 0.16 *per cent* (*i.e.* 9.61 *per cent* less 9.45 *per cent*), worked out to ₹ 21.57 crore (i.e., ₹ 1000 crore x 15 years x 0.16/100 less bond issue expenses of ₹ 2.43 crore). Moreover, though the borrowing was planned to be made within 2011-12 on an urgent basis, the same was deferred till end of May 2012 without recording any reasons therefor.

The Company/Ministry stated (August 2014/January 2015/March 2015) that keeping in view the high volatile conditions of the bonds market, the Company deferred the drawl of loan till May 2012, but since turbulent market conditions were not observed to cease in near term, and GOI guarantee was approved for the same, the Company raised the fund from LIC at the appropriate time as per the then market conditions. The Company also indicated the instances of bond issues at similar rates by Power Finance Corporation Limited (in April 2011 for 10 years @ 9.18 *per cent*), Indian Railway Finance Corporation Limited (in May 2011 for 20 years @ 9.47 *per cent*) and Rural Electrification Corporation Limited (in June 2012 for 10 years @ 9.35 *per cent i.e.85 basis points over G-Sec rates*).

The replies substantiated the fact that the funds were borrowed without assessing actual requirements and at rates higher than prevailing rates. As regards bond issues by other CPSEs quoted by the Company, the same were not comparable as the bonds of Power Finance Corporation Limited and Indian Railway Finance Corporation Limited were of 10 year and 20 year tenors, and were issued more than one year ago, whereas, the replies of the Company/Ministry in respect of the bond issue of Rural Electrification Corporation

• ***Based on the bond issue expenses of ₹ 12.52 crore incurred by the Company on issue of secured and unsecured bonds aggregating ₹ 5142.28 crore during 2012-13 which works out to 0.24 per cent.***

Limited supports the audit observation as the same was raised at a rate of interest lower by 0.26 *per cent* than the rate at which the Company had borrowed the funds from LIC (i.e., 9.61 *per cent* effective rate).

7.1.6.5 Analysis of lending schemes of Company

The Company has been providing finance to different infrastructure projects under four different schemes viz. SIFTI, refinance, take out finance and credit enhancement scheme. The audit findings in respect of these lending schemes were as under:

(a) SIFTI

As already indicated in paragraph 7.1.1, the Company was incorporated to provide long term finance to viable projects under SIFTI. However, Ministry conveyed (24 October 2011) that the Company might be brought under the regulatory oversight of RBI by registering it as a Non-Banking Financial Company – Infrastructure Finance Company (NBFC-IFC). The Company was registered with RBI in September 2013. Accordingly, the Company after September 2013 was required to follow two set of guidelines *viz.* SIFTI and RBI guidelines.

Requirements of SIFTI restricted the Company from sanctioning the loans:

- To borrowers other than through a consortium,
- Beyond 20 *per cent* of total project cost,
- having average maturity lesser than 10 years, and
- to projects falling under sectors not covered in SIFTI.

Audit came across nine instances where projects involving proposed loan amount of ₹ 3098.36 crore were not approved by the Company on account of above restrictive clauses of SIFTI. The Company stated (January 2015) that they had taken up the matter regarding limitation of provisions of SIFTI with the Ministry.

The Ministry stated (March 2015) that they had approved (4 March 2015) modifications in SIFTI enabling the Company to lend:

- Under multiple banking arrangement instead of consortium;
- Upto 40 *per cent* of the total project cost; and
- To projects having average maturity of less than 10 years in case of flexible structuring.

Audit appreciates the action taken by the Ministry. However, the modifications only partially address the restrictive clauses because:

- The Company would still not be able to finance projects as a sole lender and beyond 40 *per cent* cap in otherwise eligible cases; and
- The scope of SIFTI was not reviewed to examine the possibility of inclusion of other sectors to make it broadbased and attractive.

(i) Non-compliance of SIFTI guidelines in respect of loan sanctioned for KMP Expressway

The project for construction of 135 km stretch of access controlled and elevated Kundli-Manesar-Palwal Expressway was awarded (31 January 2006) by Haryana State Industrial and Infrastructure Development Corporation Limited (HSIIDC), the Concessioning Authority, to KMP Expressways Limited (KMP) for a concession period of 23 years and 9 months. The scheduled commercial operation date of the project was 1 July 2009.

Due to change in the composition of KMP, writ petitions were filed (May 2006) by the initial constituents of KMP *viz*. Madhucon Projects Limited and Gammon India Limited for quashing the award of project. After dismissal (March/April 2008) of the petitions, an appeal and a special leave petition filed by Madhucon Projects Limited and Gammon India Limited with the Supreme Court of India, were also dismissed in May 2008 and June 2008 respectively.

Without waiting for the final outcome of the above disputes, a loan of ₹ 380 crore was approved (11 December 2006) by the Company, part financing the project having the total project cost of ₹ 1915 crore.

Audit observed that the loan was sanctioned despite the fact that the stipulated conditions of the then prevailing SIFTI guidelines of the Company were not fully complied with *viz.,* (i) the appraisal was not done by the lead bank (Para 6.1 of SIFTI) and (ii) no guarantee from lead bank was obtained for recovery of loan (Para 7.6 of SIFTI).

As the developer had failed to execute the project, the substitution clause of the agreement was invoked, the earlier developer was removed and the efforts were made by Consessioning authority for locating a new developer (April 2014).

Thus, the Company compromised on compliance of SIFTI guidelines and failed to protect its own financial interests. The loan of ₹ 135.25 crore (outstanding amount as on April 2014) extended to the borrower ultimately became a non-performing asset for the Company.

The Company stated (August 2014) that all the decisions had been taken in line with the Lead and other Lenders in the Consortium as per the SIFTI and added that the Information Memorandum was prepared and circulated by SBI Caps and all the participating Lenders had sanctioned loan on that basis. Further, in infrastructure loans, lead lender also take care of the recovery on behalf of all the participating Lenders in the Consortium.

The Ministry added (March 2015) that the project was being re-tendered without taking into consideration lenders' dues and in view of this lenders had filed intervener application in the Supreme Court for protecting their interests.

The reply is to be viewed against the fact that IDBI Bank was the lead lender in this consortium and appraisal was required to be done by them and not by SBI Caps as per SIFTI guidelines. Further IDBI Bank did not guarantee recovery of loan through them in this case.

(ii) Term loan assistance to Srinivasa Gayithri Resource Recovery Limited.

Srinivasa Gayithri Resource Recovery Limited, the concessionaire, was awarded a 'waste to energy project' by Bruhat Bengaluru Mahanagara Palike, the Concessioning Authority, on Public Private Partnership (PPP) basis. For part financing the project, the Company, sanctioned (May 2007) a term loan assistance of ₹ 14 crore to Srinivasa Gayithri Resource Recovery Limited, the borrower, in consortium with Indian Bank (Lead Bank) and Oriental Bank of Commerce (OBC) on the basis of the appraisal done by the lead bank. The scheduled Commercial Operation Date (COD) was March 2010 which was rescheduled multiple times, for the first time upto December 2010 and latest upto March 2013.

The lead bank informed (9 April 2014) the Company that it had assigned its share in the project to one M/s Edelweiss Asset Reconstruction Company Limited (EARCL). The Company requested (21 April 2014/ 25 August 2014) the Indian Bank (the erstwhile lead bank) to hold a Joint Lenders Meeting and to inform the terms and conditions of the transfer of their stake to EARCL. Meanwhile, the Concessioning Authority, informed (16 August 2014) the Company that since the concessionaire had not been able to operationalize the project and neither had taken any convincing steps to remedy the default as per the concession agreement, they were considering terminating the said agreement.

Finally, the consortium meeting was held on 10 September 2014, which was attended only by the Indian Bank and the Company wherein the latter learnt that the other member of the consortium i.e., OBC had also sold its stake to EARCL. A copy of the Assignment Agreement entered into with EARCL was circulated in the meeting which revealed that for a consideration of ₹ 18.50 crore, the share of Indian Bank against the overdue amount of ₹ 29.45 crore was transferred to EARCL resulting into sacrifice @ 37.18 *per cent*. The Indian Bank also informed that since the asset had been assigned to EARCL, no conclusive decision could be taken in that meeting and they had no role to play and further action if any, could be taken by EARCL and the Company only. Lately, the Company also requested (17 September 2014) EARCL for taking over of its share of loan (totalling to ₹ 21.80 crore as on August 2014) on similar lines as of the other consortium members.

Audit observed that:

- Common Loan Agreement did not contain any clause prohibiting the consortium members from quitting / assigning their stake to a third party. There was no standard operating procedure in the Company to ensure continued commitment of lead lender through insertion of such clause in the common loan agreement.
- The Company was left with the option of either continuing with the existing project which was not progressing or to transfer its share to EARCL bearing a loss of ₹ 8.11 crore (i.e. ₹ 21.80 x 37.18 *per cent*).

The Company/Ministry stated (January/March 2015) that they had already informed Department of Financial Services vide their letters 30 September 2014 and 23 December 2014 of the unilateral action taken by the Lead Bank under Consortium Arrangement and highlighted that to protect the spirit of consortium it was desirable that Lead

Bank/Syndicator maintained their share in the debt and did not exit the consortium. The Company added that the possibility of incorporating a 'tag-along' clause in future agreements to safeguard the interest of the Company was being explored. The Company is also parallely exploring other options to maximize recovery and exit from the account.

The replies substantiate absence of standard operating procedures in the Company to safeguard its interests against quitting of lead/other lenders of the consortium.

(iii) Non-funding of cost overrun

On examination of the records relating to selected cases of restructured loans, it was seen that the Company had been declining to fund cost overrun in the projects of direct lending taking different pleas viz., (i) the Company was not authorized to fund cost overrun under SIFTI, or (ii) the internal guidelines of the Company did not permit funding of cost overrun.

As per the credit policy of the Company, restructuring of loan account is done after establishing the financial viability and reasonable certainty of repayment from the borrower as per the terms of restructuring package. While the projects are assessed viable by the Company in terms of the restructuring packages approved by it, the Company did not find it appropriate to finance the cost overruns on such restructured packages without any recorded reasons. The system needs to be examined so that the business opportunities for financing do not get lost in case of restructured projects which are otherwise viable. Audit observed that while restructuring the loans, the Company did not agree to finance cost overruns without any documented reasons in 13 cases involving a business opportunity of ₹ 1064.94 crore.

The Company stated (January 2015) that they generally had not been financing cost overrun in the projects. SIFTI, however, has not barred the Company from funding cost overrun. The matter was discussed at the MIC meeting held on 22nd September 2014. It was observed that most of the infrastructure projects were currently facing cost overrun. It was also observed that such cost overruns were funded invariably by existing lenders on pro-rata basis. Non-participation by the Company in which it was a member of consortium might result in non-release of funds by other lenders, putting the project in jeopardy. This also went against the spirit of consortium lending and had already resulted in bitter complaints from other lenders. DFS (Department of Finance Services), Ministry of Finance vide letter dated 3rd November, 2014, had urged the Company to participate in cost overrun and sanction additional funding/ priority loan, which would resurrect the infrastructure projects facing difficulties. The Company should also participate in the CDR[♠] forum by becoming regular member and sanction re-structuring packages in line with members of banks, involving revision in interest rate, additional funding, re-structuring of existing liabilities and repayment period. In view of the foregoing, the Company had reviewed the matter at its MIC meeting held on December 16, 2014 and decided to participate in the cost-overruns, wherever necessary.

The Company/Ministry (January/March 2015) accepted the audit observation.

[♠] ***Corporate Debt Restructuring***

(b) Refinance Scheme

As per the lending terms of SIFTI, the Company could fund viable infrastructure projects through Refinance to banks and Financial Institutions towards loans granted by them with tenor exceeding 10 years. In February 2009 (*i.e.,* nearly three years after approval of SIFTI), Government of India (GOI) defined the *modus operandi* for refinance by approving the Refinance Scheme and permitted the Company to raise ₹ 10,000 crore through tax free bonds in tranches. The Company adopted the Refinance Scheme in February 2009. Salient features of the Refinance Scheme were as under:

- Refinance would be made available to new projects in road and port sectors only for which bids were submitted on or after 31.01.2009;
- The Company would provide refinance up to 60 *per cent* of the loans provided by the individual banks to infrastructure projects in roads and port sectors; and
- The banks would not charge more than 2.5 *per cent* over and above the rate charged by the Company.

The Company informed (26 October 2009) the Empowered Committee (EC) that the restrictions of the Refinance Scheme *viz.,* providing finance in the projects (a) which pertained to road and port sectors only, and (b) for which bids were submitted on or after 31 January 2009, had collectively constrained the disbursement under the scheme, and the Company could not utilize ₹10,000 crore raised in January/March 2009 *i.e.* for more than six months. Despite piecemeal relaxations by EC permitting the Company to extend refinance to Public Financial institutions in addition to banks (December 2009), relaxation in the restrictions relating to rate of interest and road and port sectors (March 2011) the Company could utilise only ₹ 6256 crore since inception of scheme in 2009 to March 2014 for the Refinance Scheme.

The Company/Ministry stated (January/March 2015) that though certain covenants have been modified suitably over a period of time to make the Refinance scheme more attractive, the important factor, which determines the attractiveness of the scheme, viz. the Rate of Interest (RoI) offered by the Company under Refinance scheme was not attractive enough to expand the scheme to the desired level. The Company had been raising the funds by issue of bonds or raising resources from multi-lateral/bilateral agencies. The total cost of funds after considering the hedging of foreign currency lines of credit works out to be on-par with the costs of funds of mobilizing resources by issue of bonds. As the other banks, Financial Institutions/NBFCs also had access to the bonds markets, the USP[♣] of Refinance scheme offered by the Company had been blunted.

The replies substantiate the audit observation that the Refinance scheme was largely unsuccessful.

(i) Irregular sanctions under Refinance Scheme

The Company under the Refinance Scheme sanctioned loans to Rural Electrification Corporation Limited (REC), Power Finance Corporation Limited (PFC) and

♣ ***Unique Selling Proposition***

Infrastructure Development Finance Company Limited (IDFC) in deviation with the terms of the scheme after obtaining approval from the EC (**Annexure-XI**). Audit observed that:

- The Company curtailed the tenor of the loans sanctioned to REC, PFC and IDFC under the refinance Scheme from the stipulated minimum tenor of 10 years to upto 1 year in 9 out of 10 cases against the spirit of the refinance scheme.
- The Company did not fulfill the main objective of Refinance Scheme by linking the date of maturity of such loans with that of the tax free bonds under which funds for the refinance scheme were raised by the Company.
- Due to inclusion of pre-payment clause in deviation of the scheme, the Company had to accept the pre-payment of the loan amounting to ₹ 1195 crore on 10 September 2014 (i.e., interest reset date) from REC.

The Company/Ministry stated (January/March 2015) that the USP of the scheme viz. the Rate of Interest (RoI) offered by the Company under Re-finance Scheme was not attractive enough to expand the scheme to the desired level. As the other banks, FIs/NBFCs also had access to cheaper sources of funds like deposits, the bonds markets, etc., the USP of re-finance scheme offered by the Company has been blunted. Further, the interest rate was to be reset every year. It was normal commercial practice to stipulate Annual Reset for longer tenor loans. REC had chosen to repay the loan on the reset date, as it could mobilize the funds at more competitive rates than that offered by the Company.

(c) Takeout Finance Scheme

With the objectives to boost the availability of longer tenor debt finance for infrastructure projects and to address the sectoral/ group / entity exposure issues and asset-liability mismatch concerns of lenders, the Company submitted the Takeout Finance Scheme before the EC for its approval, which was approved by EC in January 2010 (10th meeting). The scheme was implemented from 16 April 2010. The salient features of the Scheme were as follows:

- The eligible entities were the scheduled commercial banks or any other participating entities who had extended loans under the Common Loan Agreement to the Borrower.
- The projects should have achieved financial closure and have a residual debt tenor of at least 6 years.
- The extent of takeout finance on the outstanding amount of loan of a lender from whom the loan is to be taken over on the scheduled date of occurrence of takeout was 75 *per cent*. However, the total takeout amount could not exceed 50 *per cent* of the total residual loan of the infrastructure project.

Despite multiple modifications having been made in various clauses of the Scheme to make it more attractive business growth under the scheme was not good as seen from the following:

- Since introduction of Takeout Finance Scheme in 2010, the Company sanctioned 61 projects amounting to ₹ 11,348.21 crore till March 2014 out of which 28 projects (45.90 *per cent*) wherein total amount sanctioned of ₹ 4864.35 crore (42.86 *per cent*) was involved were cancelled subsequently.

- Out of remaining 33 projects, disbursement of ₹ 3870.76 crore was made in 23 projects against sanctioned amount of ₹ 4120.30 crore, and in 10 projects, wherein loan of ₹ 2363.56 crore was sanctioned upto March 2014, no disbursement was made (June 2014).

The Company stated (January 2015) that major reason for cancellation of sanctions made under Takeout Finance Scheme was refusals on the part of existing lenders to furnish NOC for takeout finance. Further, in certain cases, the existing lenders themselves had come forward to reduce the rate of interest in line with the interest rates offered under takeout finance by the Company, which discouraged the borrowers to avail takeout financing from the Company. Though the Company's rate of interest under Takeout Finance Scheme and Re-finance scheme are generally lower than the interest rates offered under direct finance scheme, the impediments to the Takeout Finance Scheme were being created by the existing lenders with a view to retain projects which have become operational thereby overcome major risk viz. the implementation risks. The Ministry further informed (March 2015) that ₹ 1851.98 crore had since been disbursed in six cases and in balance four cases, the Company was continuously pursuing with borrowers.

(d) Credit Enhancement Scheme

The Company approved (18 August 2011) the 'Outline – Credit Enhancement Scheme' for viable infrastructure projects. Under the scheme, the Company was required to extend the credit enhancement in the form of guarantee to commercially viable infrastructure projects up to ₹ 4000 crore, wherein the projects had minimum rating of BBB any credit rating agency, and had achieved the Commercial operation date.

Audit observed that though the first pilot project had been approved by the Ministry of Finance in September 2012, the Company had not funded any project up to September 2014 under this scheme.

The Company stated (January 2015) that while they had given in-principle approval to a few transactions under this pilot scheme, no bond issue availing the Company guarantee had taken place mainly due to the prevailing market conditions. The Ministry added (March 2015) that Regular Credit Enhancement Scheme had since been approved in March 2015.

The replies to paras 7.1.6.5 (b) (i), 7.1.6.5 (c) and 7.1.6.5 (d) need to be viewed against the fact that not a single bond issue had taken place under Credit Enhancement Scheme even after lapse of more than three years since the scheme was launched. The results of Regular Credit Enhancement Scheme of March 2015, in terms of its attractiveness, popularity and performance, can only be known after a reasonable period of time. Refinance and Takeout Finance Schemes also remained largely unsuccessful. Therefore, there is a need for the Company to critically revisit the two schemes mentioned above considering the market trends, prevailing rate of interest, publicity requirements and other financial terms to make them attractive to borrowers.

7.1.7 Monitoring

7.1.7.1 Non-adherence to the directions of BOD

Review of the agenda and minutes of the meetings of the Board of Directors revealed the following:

(i) The Company noticed (23 October 2012) that as per audited standalone financials for the quarter ended 30 June 2012, the Company had suffered diminution in the Net Present Value of restructured assets by ₹ 4.42 crore. The Board of Directors advised that valuable lessons should be learnt from experiences gained from problems/impediments/issues leading to restructuring of accounts and the same should be incorporated as checklist points for future reference and guidance.

In the same meeting, the Board also desired that cumulative cost overrun in respect of restructured accounts should also be placed before the Board. Audit did not find any such information having been placed before the Board till date (September 2014).

(ii) While approving its Standalone Financial Statements for the Quarter ended 30 June 2013, the issue of restructuring was again deliberated by the BOD (29 July 2013) when it was observed that in most of the restructured accounts, the Company had sanctioned loans without availability of land in road projects and without Fuel Supply Agreement (FSA) and/or Power Purchase Agreement (PPA) in power projects. Consequently, there was inordinate delay in implementation of projects entailing requirement to make huge provisions. The Board also advised the Company to ensure that these critical requirements were not compromised in future.

Audit observed that, even after the direction of the Board, the Company continued to sanction[♦] loans without ascertaining the availability of required land in full and availability of FSA/PPA in violation of the directions of the Board.

The Company stated (January 2015) that the aspects advised by the Board of Directors were meticulously followed during sanction as well as monitoring stages. The position on cumulative cost overrun in respect of restructured accounts would be placed in subsequent meeting of the Board of Directors. It was further submitted that the Company did not carry out original appraisal and adopted the appraisal memorandum prepared by the Lead Bank or FIs. However, stipulating the same as pre-commitment conditions might result in inordinate delay in financial closure and the Company might lose its edge in the market and potential business.

As the Board had taken a well considered decision to ensure availability of land and signed PPA/FSA before sanction of loan by the Company, it was desirable for the Company to present to the Board the problems being faced by it in implementation of their directions and to obtain the guidance of the Board on this issue.

[♦] ***Five loans were sanctioned under direct lending scheme without availability of entire land or signing of PPA/FSA in May 2014.***

The Ministry stated (March 2015) that as per Board directives, conditions pertaining to availability of adequate land, FSA and PPA are to be stipulated as pre-disbursement conditions and the Company was following the same.

The reply of the Ministry is not correct because the Board had directed (29 July 2013) the Company to ensure availability of land and critical requirements of FSA and PPA while sanctioning loans i.e. as pre-sanction conditions and not as pre-disbursement conditions. Moreover, no further directive of Board to modify their directive of 29 July 2013 was provided by the Company to Audit.

Conclusion

Inadequacies in assessment of requirement of funds led to the Company facing a situation of progressively increasing surplus liquidity remaining parked in fixed deposits with banks which was not the core business of the Company. The Company was also unable to achieve its lending targets partly due to unattractive lending schemes and partly due to restrictive clauses of its Special Purpose Vehicle. As regards raising of funds, there were instances where the Company did not explore possibilities of cheaper finance available to it. Audit also observed deficiencies in the processing of loan appraisals, sanctions and monitoring.

Recommendations

The Company may:

- ***Assess fund requirements on a realistic basis and maintain detailed workings with documented reasons in support of assessment of requirement of funds.***
- ***Critically review the lending schemes considering the market trends, prevailing rate of interest, publicity requirement and other financial terms to make them attractive to the borrowers and ensure accelerated flow of funds in infrastructure sector.***
- ***Consider inclusion of a 'tag-along' clause for lead lender in the common loan agreements in 'consortium lending' to ensure that the lead lender stays committed to the consortium and the financial interests of the Company are safeguarded.***

MCX Stock Exchange Limited

7.2 Failure of MCX-SX to safeguard its interests

Review of agreements signed by MCX Stock Exchange Limited and Liquidity Enhancement Scheme implemented by the Company.

The MCX Stock Exchange Limited (the Company) was incorporated on 14 August, 2008. Multi Commodity Exchange of India Limited (MCX) and Financial Technologies (India) Limited (FTIL) were its promoters. The Company, upon incorporation in August 2008 had three Directors on the Board. Two Directors were from MCX and one Director was from FTIL who was also Chairman of the Company i.e. MCX-SX (October 2008 to September 2009). Thereafter, representatives from FTIL on the Board increased to two with the induction of Shri Jignesh Shah as Vice Chairman. Shri Joseph Massey, who worked as MD of MCX, joined as Director of the Company in August 2008 and was appointed as MD & CEO of the Company from June 2009. Shri Jignesh Shah joined the Board of Directors of the Company in October 2008. Both continued until they resigned in October 2013 consequent to the show cause notice issued by Forward Market Commission (FMC) directing them to show cause why they should not be declared not to be 'fit and proper' to be Directors in MCX due to eruption of payment crisis in NSEL.

MCX-SX started its operations from October 2008. In order to operationalise its activities, the Company entered into a series of agreements with FTIL for procurement of software, maintenance services, rendering personnel support services, sharing of services, leasing of accommodation and so on during August 2008 to September 2013. The agreements with FTIL were signed during the tenure of Shri Joseph Massey as Director/MD & CEO. The Company entered into 161 Agreements with different entities, of which audit examined all the 30 Agreements entered into with FTIL, being related party agreements.

Audit scrutiny revealed the following:

7.2.1 Restrictive clauses in agreements in favour of FTIL:

The Company entered into long term agreements with FTIL for its Exchange operations which included purchase and maintenance of DOME and CnS software, ODIN Software licenses, Development and maintenance of Alert Management Software (AMS) and Service Provider Point of Presence (POP) i.e. network infrastructure service. These agreements had restrictive clauses that were against the interests of the Company which made exit from the agreements by way of termination and finding alternate vendor difficult for the Company. MCX-SX made a total payment of ₹ 303.75 crore to FTIL during 2008-09 to 2013-14 which amounted to 52 *per cent* of the total expenditure of the Company.

Some of the major restrictive clauses in the agreements were as under:

- The Company could not use any other software or introduce a new version of any hardware without the consent of FTIL and all hardware was to be of the kind that FTIL agreed to support.
- There was no clause of penalty or compensation in terms of delay in deliverable in any of the agreements entered with FTIL.
- The Company could not obtain similar services from any other service provider during the term of these agreements unless mutually agreed.
- The initial tenure of the purchase of DOME & CnS agreement was 33 years effective from August 2008 which would automatically stand renewed for further block of 33 years. With an addendum (November 2012), the tenure was changed to the effect that the agreement would be automatically renewed for a further block of 33 years and the total duration of agreement became 99 years which is beyond normal comprehension of standard agreements.

- Under the agreement for ODIN software license, FTIL would charge the Company for trading members' licenses for a minimum period of three months being the lock in period. Even if a member disassociated himself from the exchange during lock-in-period, MCX-SX was not entitled to reduce the number of software licenses.

- The agreement for ODIN software license provided for minimum monthly commitment, of ₹ 35 lakhs for first year, ₹ 50 lakhs and ₹ 60 lakhs per segment respectively for second and third year. The basis of the minimum monthly commitment or the extent of actual for providing ODIN licences was not on record.

- In case of premature rescission of the agreement for DOME and CnS, Alert Management Software (AMS) license, Service provider Point of Presence etc. MCX-SX had to make payments to FTIL for the remaining term of the agreement. The AMS agreement further contained a clause for payment of penalty @ 50 *per cent* of the AMC charges payable in the event of premature rescission.

The charges payable to FTIL in case of termination were as under:

Name of agreement	**Total amount payable (₹ in crore)**
DOME and CnS	324
AMS	90
Service Provider Point of Presence and co-location	16.58

From the above, it is clear that the agreements with FTIL were not on 'arm length' basis but on 'arm child' basis as the influence of the elder party was significant. The conditions in the agreements made the Company dependent on FTIL with no reasonable route of exit from the agreement.

The Company stated (December 2014) that the new management had initiated a review to establish the reasonableness of charges for similar line of business. Renegotiation of the commercial terms of the agreements with FTIL was in progress. Some agreements were suspended partially.

Reply establishes the fact that the terms of agreement with FTIL unduly favored FTIL and did not safeguard the interests of MCX-SX.

7.2.2 Defective assessment of requirements:

The Company entered into two agreements for Co-Location services (January 2013) to avail the space at FTIL's data center for hosting and offer co-location services to its trading members and service agreements for Web Services and Cost sharing arrangements for utilizing the services of personnel from FTIL for various activities and also for sharing the cost of infrastructure, computer peripheral, hardware, software etc. (effective from August 2008 / February 2009). Fees was payable in advance on yearly basis. The Company paid ₹ 6.40 crore for hiring 32 full racks for Co-location services for 2013. The requirement was reduced to 16 full racks in December 2013 and the Company paid ₹3.20 crore for 2014. The Company paid FTIL a total of ₹ 6.42 crore towards web services and cost sharing.

Audit observed that the Company projected its requirement at higher level without flexibility for downward reduction and could not fully utilize the capacity available in respect of Co-location services. The Company did not conduct an independent review of the terms and conditions of the agreements in terms of the requirement of facilities, deployment of manpower, the rates and the tenure of the agreement etc. Also, FTIL was not responsible for any delay in the delivery of the deliverables, under the agreement. Thus the terms of agreement were loaded in FTIL's favour. Further, audit could not satisfy itself of the details of actual availment of services by the Company from FTIL, in the absence of records.

The Company stated (January 2015) that the agreement for service provider POP & Co-location services were made by erstwhile management and the new management has suspended the Co-location services agreement from 1 July 2014. The activity has been shifted to the Data Centre in the new premises and is being managed by the Company and services are being availed on actual basis.

The suspension of agreement is in line with the audit contention and is only an interim measure which does not relieve the Company from its liabilities.

7.2.3 Non-review of Liquidity Enhancement Scheme despite fall in business volume and the accumulated losses

SEBI introduced 'Liquidity Enhancement Scheme (LES)' from 2 June 2011 to enhance liquidity of illiquid securities in equity derivative segment (EDS) and extended it to Equity Capital Market (ECM) in February 2013. MCX-SX having commenced trade in ECM and EDS in the same month, without waiting for the performance of the members enrolled, introduced the scheme immediately. The Company additionally introduced an 'Additional Incentive scheme' for a period from March 2013 to June 2013 with specific cash rewards in each category.

During the period of operation of the scheme only 51 new members were admitted to the exchange. Also the volume of trade in the exchange in ECM increased from ₹ 27.18 crore (March 2013) to ₹ 2972 crore (June 2013) and then declined continuously upto ₹ 416 crore (March 2014). The volume of trade in EDS increased from ₹ 7707.22 crore (March 2013) to ₹ 32685.58 crore (July 2013) and then declined continuously upto ₹ 1280.19 crore (March 2014). The scheme envisaged incentive payment for any performance of trade on the exchange, without incentivizing volume of trade above a certain level or any focus on illiquid stocks.

Audit observed that as the Company was faced with difficulty in volume growth coupled with heavy operating expenditure, it should have reviewed the performance of its members before introduction of such scheme as the scheme envisaged payment of incentive even for normal performance. The Company discontinued the scheme on 10 April 2014 during which period, it had already paid a total incentive of ₹ 43.30 crore.

The Company replied (August/December 2014) that the scheme was introduced with the approval of its Board of Directors and the operation of the scheme was reported to the Board periodically. Further, in view of reducing the operating costs and to initiate steps for revival of the exchange, LES was discontinued in April 2014.

The reply supports the audit observation that the introduction of the scheme entailed high operating cost and was not beneficial to the Company and had to be ultimately discontinued.

7.2.4 Infrastructure and Personnel issues:

(a) Imprudent decision to acquire office accommodation on lease at Bandra Kurla Complex (BKC) Mumbai resulting in avoidable expenditure of ₹ 13.79 crore

The Company entered into an agreement (May 2013) with M/s. BKC Properties Private Limited for taking the premises (15000 sq. ft) at Vibgyor Tower, BKC, Bandra (East), Mumbai on lease for a period of five years (60 months) effective from 15 March 2013. The Company paid (May 2013) a refundable interest free security deposit of ₹ 4 crore. The rent payable for the accommodation was ₹ 44.48 lakh per month in addition to maintenance charges. The property was on lease to FTIL before being taken up by MCX-SX and the assets left over by FTIL were purchased by the Company for ₹ 2.63 crore. Thus, the Company paid ₹ 13.796 crore (August 2014) towards Deposit (₹ 4 crore), license fee, maintenance charges and car parking charges (₹ 7.16 crore) and towards used assets from FTIL without assessing the necessity for additional space.

In this regard, audit observed the following:

- The Company committed itself for occupation for 5 years in March 2013 itself by signing the term sheet even before the Management Committee of the Board of Directors approved the proposal in May 2013.
- The space at BKC was not fully occupied till August 2014 and therefore was only partially utilized during March 2013 to July 2014.
- There was no valuation report/justification available on record for the leftover assets purchased from FTIL. The assets are being depreciated at the book rate obtained from FTIL.
- The agreement contained a lock-in period of 36 months. Therefore, license fee had to be paid for a minimum period of 36 months irrespective of actual utilization of the premises. Thus, the Company committed itself to payment of license fee alone, to the extent of ₹16.01 crore (₹ 44.48 lakh x 36 months).

The Company stated (December 2014) that the new premise was fully occupied from August 2014.

(b) Outsourcing the functions of Personnel, Administration and Procurement

The Company entered (26 December 2008) into Memorandum of Understanding with FTIL for availing Management and other support services effective from October 2008 at monthly service charges of ₹ 35 lakh. The scope of agreement was later revised to ₹ 15 lakh per month (effective April 2011).

Audit observed the following:

- The initial MoU gave FTIL the right to take decisions in respect of critical areas like business strategy, strategic recommendations to the business team, review of product performance, review of requirements for expansion and enhancement of capacity etc. This made the Company vulnerable and dependent on FTIL and compromised the confidentiality of its operations.

- The Company did not recruit its own personnel or attempt to outsource through tender mechanism.

- Additionally, Exchange specific services viz. Auditor, Business Analyst etc. were availed through exchange of correspondence with the approval of MD & CEO and were not backed by any formal agreement or approval of the Board. An amount of ₹ 14.36 crore on this account was paid during the three years period ending 31 March 2014.

- The reasonability of the rate of payments, confirmation of deliveries and requirement for continuation of these resources was not on record and could not be verified.

The Company stated (December 2014) that the services as per the MoU have been discontinued by the new management and all these functions are now been carried out by the Company itself.

(c) Payment of gratuity to MD &CEO on resignation

Shri Joseph Massey joined the Company as MD & CEO from 1st June 2009 and through agreements (June 2010 and March 2013) his tenure was extended for a further period of three years each. He resigned on 9 October 2013 as a fallout of the show cause notice issued by FMC declaring him as not 'fit and proper' person to hold any post in any Exchange.

Audit observed that the Company paid gratuity of ₹ 53.31 lakh to Sh. Massey for rendering total service of 11 years which included his earlier service in MCX. As Sh Massey was not transferred from MCX to MCX-SX and rather joined the Company upon resignation from the former, as per the Group Gratuity Policy, his service in MCX-SX alone was to be counted for payment of gratuity. Further, as he rendered less than 5 years of service in MCX-SX, he was not entitled to payment of gratuity at all. Thus, the payment of gratuity amount of ₹ 53.31 lakh was not in order.

The Company stated (August 2014) that it has sought legal opinion on the issue which is still awaited.

Conclusion

MCX-SX had entered into long term agreements with its related party FTIL that entailed various restrictive clauses as well as high costs. Further, the PSU Banks had 67 *per cent* shareholding as on 31 March 2010 and had their nominees on the Board of the Company during 30 April 2010 to 20 September 2012. These nominees of PSU banks on the Board of MCX-SX did not review these unfavourable agreements and failed to protect the interests of the banks they represented. Despite present action by new management, by way of suspension of various agreements with FTIL, the liability due to restrictive clauses in these agreements would continue as only interim action to suspend only a few agreements has been taken (January 2015).

The matter was reported (September 2014) to the Ministry; their reply was awaited (March 2015).

Security Printing and Minting Corporation of India Limited

7.3 Infructuous expenditure due to printing of fresh bank notes bearing the signature of former Governor of RBI

Security Printing and Minting Corporation Limited continued printing bank notes with the signature of former Governor of RBI even in 2014 though the then Governor had completed his tenure in September 2013 and thereby incurred an infructuous expenditure of ₹ 36.69 crore.

Bharatiya Reserve Bank Note Mudran Private Limited (BRBNMPL) is the nominated agency of Reserve Bank of India (RBI) for issuing the designs/printing plates with the approved signature of Governor of RBI to Security Printing and Minting Corporation of India Limited (the Company). Dr. D. Subbarao was the Governor of Reserve Bank of India (RBI) from 5 September 2008 to 4 September 2013 and Dr. Raghuram G. Rajan assumed office from 4 September 2013. BRBNMPL intimated Bank Note Press (BNP), Dewas (Madhya Pradesh), a unit of the Company, vide letter dated 14 September 2013 that approval of RBI to specimen note of ₹ 10 denomination with signature of new Governor was received and requested BNP to collect security material to start regular bank note printing. BRBNMPL also intimated (17 October 2013) BNP the approval of machine proof of ₹ 50, ₹ 100 and ₹ 500 denomination bank notes incorporating the signature of new Governor and asked BNP to furnish details for preparation of Nickel Altos.

Audit examination revealed that RBI had advised (September 2008) (at the time of change of charge of the then RBI Governor in that year) that all the bank note printing presses may start printing bank notes bearing the signature of new Governor in all denominations w.e.f. 1 January of 2009. Accordingly, at the time of change-over of RBI Governor in 2013, BNP, Dewas should have followed the same instruction and started printing bank notes with the signature of new Governor of RBI w.e.f. 1 January 2014. While Currency Note Press, Nashik, another unit of the Company, followed this procedure, BNP did not incorporate the signature of new RBI Governor w.e.f. 1 January 2014 but continued printing bank notes with the signature of former RBI Governor till 25 February 2014. BNP printed 372 million pieces (mpcs) bank notes during January to

February 2014 and remitted 146 mpcs to various regional offices of RBI which intimated (25 February 2014) that printing of notes with the signature of former Governor of RBI was not in order and directed the Company not to remit such notes forthwith. Audit examination revealed that 226.48[♥] mpcs of bank notes of ₹ 20, ₹ 100 and ₹ 500 denomination costing ₹ 36.69 crore were still lying at BNP store (March 2015) and the chances of lifting of these notes by RBI were very remote as these notes were printed in 2014 carrying the signature of former Governor, who had completed his tenure in September 2013.

The Company stated (February 2015) that:

(i) Bank notes, which were printed between 1 January and 25 February 2014 were not rejected by RBI;

(ii) BNP, Dewas had supplied 146 mpcs bank notes to RBI valued at ₹ 38 crore in 2013-14 and the payment for the same had already been released by RBI; and

(iii) According to press release issued by RBI on 4 March 2014, these bank notes were legal tender. Part of these bank notes had already been issued by RBI to the Public being valid legal tender. Further, the bank notes in stock would be despatched as soon as instruction was received from RBI.

The reply is to be viewed in the light of fact that RBI had categorically asked the Company in February 2014 itself to stop sending such bank notes which were not in order. Further, RBI did not issue any delivery schedule for lifting of these bank notes even after lapse of more than one year. Moreover, RBI did not respond to request of the Company made in June/December 2014 so far (February 2015). Accordingly, the chances of lifting of these notes by RBI were bleak.

Thus, the expenditure of ₹ 36.69 crore, being cost of production of 226.48 mpcs bank notes bearing the signature of former RBI Governor with 2014 as the year of printing had become infructuous.

The matter was reported to the Ministry in December 2014; their reply was awaited (March 2015).

The New India Assurance Company Limited

7.4 Co-insurance business with private general insurance companies

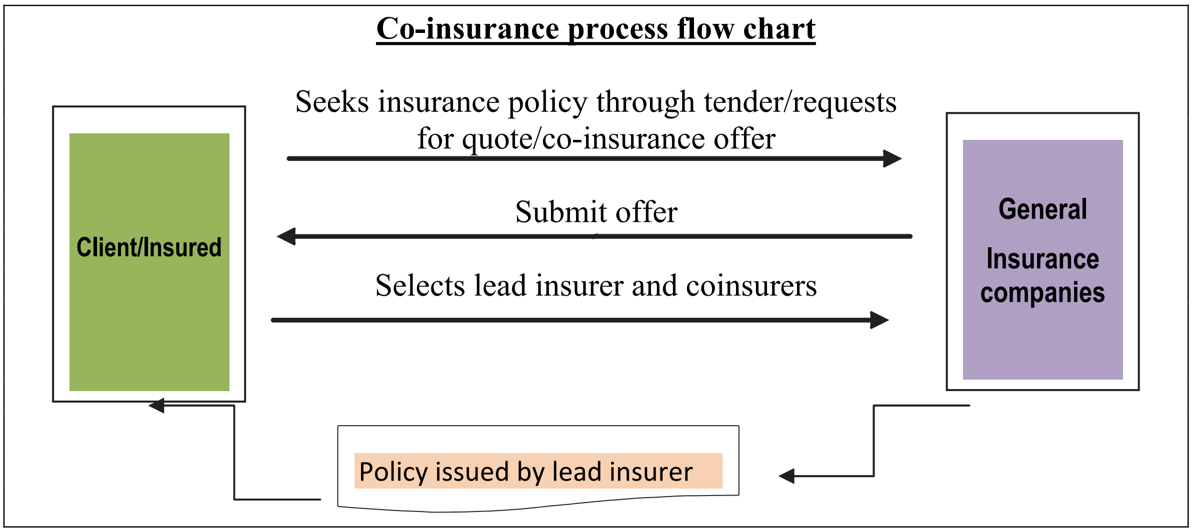
7.4.1 Introduction

The insurance market was opened by the IRDA (Insurance Regulatory and Development Authority) in August 2000 to private insurance companies, thus ending the monopoly of PSU general insurance companies. There are co-insurance arrangements between the PSU insurance companies and the private insurance companies. Under co-insurance, one

[♥] ***60.82 Mpcs intaglio printed, 21.17 Mpcs numbered printed, 41.49 Mpcs bundled and 103.00 Mpcs Packed.***

company (known as the "lead insurer") underwrites the insurance business and shares a part of that business with other public/private insurance business. The premium is shared by these companies and the claims, if any, are also made good by them. The following flow chart explains the co-insurance process. As can be seen, the insured plays a prominent role in selecting the lead insurer and the co-insurance share of each co-insurer as well. The insurance companies resort to co-insurance arrangements in order to spread risk emanating from underwriting mega risk/high risk policies.

Flow Chart



During the period April 2012 to March 2013, New India Assurance Company Ltd (the company) assumed 968 co-insurance incoming businesses, where private general insurers were the leaders, for a total premium income of ₹ 135.94 crore. Audit reviewed 38 cases pertaining to the Mumbai Regional offices of the company out of 968 cases for the year 2012-13. These 38 cases registered a premium income of ₹ 69.80 crore (51.35 *per cent* of the total premium) and incurred a claim of ₹ 23.46 crore (33 *per cent* on the premium of ₹ 69.80 crore). Of the 38 test checked cases, 20 cases belonged to Fire class of business, 5 cases pertained to Engineering, 8 cases to Marine, 4 cases to Health and 1 to Miscellaneous (Public liability) class of business.

Audit scrutiny focused on whether the company had underwriting norms for co-insurance in place and whether these norms were followed consistently. Audit also looked into the safeguarding of financial interests by the company while entering into the co-insurance arrangements with the private insurance companies. The audit findings are stated below:

7.4.2 Underwriting Policy/Guidelines

The company put in place the revised underwriting policy (November 2007) which prescribed the general underwriting principles (self-sustainability), underwriting limits of officials, the authorities to decide the limits etc. This did not cover co-insurance arrangements. The Company has not yet framed specific guidelines for its co-insurance business.

Ministry has stated in its reply (March 2015) that, the underwriting guidelines adopted by the company are applicable to the incoming coinsurance. However, in view of the nature of co-insurance business wherein role of the lead insurance Company and that of the client in determining the terms and conditions of the insurance contract, is significant, specific guidelines for this area of business are essential.

7.4.3 Inadequate Risk and Client Profile

Prudent and sound underwriting warranted that an underwriter maintained a risk profile and client profile which influenced the underwriter in deciding whether to accept or reject the risk. A prudent judgment was made by the underwriter by analyzing the existing loss record and future risk exposure. Hence in order to assess the prudency of underwriting co-insurance business, the Audit test checked whether the Company recorded the most vital information such as Incurred Claims Ratio of the risk in the previous three years, Average Combined Ratio on the risk in previous three years and details of risk such as the location of the risk, total exposure, break up of Sum Insured, the project report, annual reports, risk inspection reports, mode of conveyance in the case of marine cargo business etc., as relevant to the case before acceptance of the risk. It was observed that in only 3 out of the 38 cases basic details in respect of risk and client profile were maintained by the Company.

The Underwriting guidelines (Brokers policy-HO:FTD:9-12, dated 30th July 2012) directed that for proper evaluation of risks/proposals, finalizing prudent terms and rates and mitigating the probability of any bad underwriting, the mandatory submission of minimum 3 years premium and claims experience by the brokers was to be ensured. Audit noticed that in 19 out of 38 cases the Incurred Claims Ratio which is the most vital information in decision making was not available. In 7 out of these 19 cases, claims for an amount of ₹ 3.03 crore were settled. Thus the company assumed risk without assessing the gravity of risk.

Ministry stated in its reply (March 2015), that Company has instructed (August 2014) the operating offices to file all such details while accepting incoming co-insurance business.

The company issued a circular based on the audit observation. However, the company needs to make a policy, on the issue of Co-insurance.

7.4.4 Inadequacies in Risk Assessment and Approval

The company vide its Board note dated December 2007, laid down a broad framework for classification of risks, rating of risks, rating pattern of risk, merit rating or scoring of risks and acceptance limits of risks for the operating offices.

Risk Inspection is one of the tools of risk assessment followed in Insurance Industry. Further, the IRDA instructions (December 2007) also stated that individual rated risks, i.e., risks above a certain limit of Sum Insured (as per the product classification of the underwriting policy) were to be rated based on the Inspection report.

Audit observed that in none of the 25 fire and Engineering cases, risk inspection was carried out by the company itself or the Inspection report of the lead insurer obtained before acceptance of the risk. It was seen that of these 25 cases the Company settled 6 claims for an amount of ₹ 21.78 crore.

Audit observed that none of the 38 cases had justification notes for acceptance, duly approved by the Competent Authority. It was observed that though 12 out 38 risks were of Sum Insured (SI) exceeding ₹ 500 crore, the laid down procedure in respect of risk inspection was not followed.

Ministry stated in its reply (March 2015), that the Company has instructed the operating offices to adhere to the procedure for acceptance of incoming co-insurance specially with reference to collection of data along with incurred claims ratio for the last three years and fire fighting and inbuilt safety measures.

7.4.5 Acceptance of Risk at Lesser Rate under Co-insurance

Audit observed in 9 out of 38 cases coinsurance shares was accepted at a rate lower than that quoted by the Company at the time of participation in the tender for 100 *per cent* share in these nine cases. The lower premium amounted to ₹ 2.02 crore in these nine cases. Of these 9 cases Company settled 3 claims of ₹ 2.27 crore. The percentage of under quote exceeded 15 *per cent* in 5 cases resulting in total under quote of premium by ₹ 1.48 crore.

Ministry has stated in its reply (March 2015) that the co-insurance share is accepted only after proper assessment and evaluation of the risk. Due diligence is also observed while accepting coinsurance share. Further, the premium rates are based on certain assumptions as perceived by the underwriter.

However, as the Company did not provide any justification for accepting the same risk subsequently at a lesser rate and in the absence of guidelines, the acceptable range of variance could not be verified.

7.4.6 Inconsistencies in the policies of the company and the lender

The Public sector general insurance companies and private sector general insurance companies entered into Coinsurance agreement on 20 February 2009 which provided that as soon as the policy was issued by the leader a certified true policy copy was to be made available to the co-insurers.

Audit observed that in all the 38 cases, the company did not collect a copy of the original policy issued by the Lead insurers. At the instance of Audit, the company obtained the copy from the lead insurers and inconsistencies were noticed in 6 out of the 38 cases. A comparison of the significant inconsistencies is cited below:

Sl. No	Insured / Leader	Particulars
1	Deepak Fertilizers (12140144125100000003) (Leader Bajaj Allianz General)	The company policy copy showed sum insured (SI) at ₹ 3000 crore whereas leaders policy showed SI at ₹ 300 crore.

2	Deepak Fertilizers (12140144125100000002) (Leader Bajaj Allianz General Insurance)	The company policy copy showed SI at ₹ 5.72 crore whereas leaders policy showed SI at ₹ 10.35 crore.
3	Tinplate (12140244125800000001) (Leader: TATA AIG General Insurance)	SI in the leader's policy copy was ₹ 2,62,45,738 whereas it was ₹ 2,64,81,358 in the company's copy, i.e., it was higher by ₹ 2.36 lakh. The company policy copy showed 100 *per cent* premium at ₹ 37,735 whereas the leader's policy copy showed it at ₹ 37,400.
4	Gallant Metals Ltd (11280011120600000001) (Leader: ICICI Lombard)	Leader's policy showed SI of ₹ 396.75 crore whereas company policy showed SI of ₹ 356.75 crore. The company policy showed premium of ₹ 40,02,145 whereas Leader's policy showed a premium of ₹ 40,04,984.
5	AES Solar Ltd (12050011120600000004) (Leader: TATA AIG General)	Sum insured for MLOP and FLOP under Business Interruption insurance section was Nil in the company's policy copy whereas it was ₹ 31 crore in leader's policy copy.
6	Deepak Fertilizers (121401441111201000000025) (Leader: Bajaj Allianz)	The company's policy copy showed premium at ₹ 2.154 crore and SI at ₹ 2705.90 crore whereas the leader's policy showed premium at ₹ 2.146 crore and SI at ₹ 2410.32 crore.

Ministry has stated in its reply (March 2015) that, though the lead insurers are required to share policy copies, sometime the Company do not get the same. To book the premium the underwriting office indexes the coinsurance share by inputting the available information.

7.4.7 Inadequacies in the Underwriting Software (CWISS)

The company has developed a software called CWISS (Centralised Web based Insurance System Solution) to facilitate its insurance activities. Current year's policy issued by the company carries the previous year's policy number if the company has 100 *per cent* share in the policy (non co-insurance policy). However, if a policy under co-insurance is renewed, the previous year's policy number is not indicated. As this facility would enable the company in obtaining the previous history of the risk, CWISS needs to have this functionality.

Ministry has stated in its reply (March 2015) that the service provider is in the process of devising a workflow whereby this can be put to production.

Conclusion

The Company needs to address the issues of obtaining risk profile and client profile before acceptance of co-insurance contracts. Detailed justification for accepting co-insurance at lesser rate than higher rate quoted for 100 *per cent* share should be recorded. Copies of co-insurance contracts should necessarily be obtained from the lead insurer to rule out possible inconsistencies.

Audit holds the view that the system and procedures adopted by the company in accepting the co-insurance business need review and improvement.

Ministry replied that the Company had noted the discrepancies pointed out by audit and assured remedial measures to streamline the procedures.

CHAPTER VIII- IRREGULARITIES IN PAYMENT OF ENTITLEMENTS AND RECOVERIES BY CPSEs AT THE INSTANCE OF AUDIT

8. Following significant instances of irregularities in payment of various entitlements and allowances to the employees of CPSEs were noticed in audit:

Airports Authority of India, Coal India Limited and its Subsidiaries

8.1 Irregular payment of allowances and perks beyond admissible ceiling

Non-adherence to guidelines of Department of Public Enterprises (DPE) regarding grant of allowances and perks to executives to a maximum ceiling of 50 *per cent* resulted into irregular payment of ₹ 543.77 crore and ₹ 29.33 crore to the employees of AAI and CIL respectively.

The Department of Public Enterprises (DPE) issued (November 2008) guidelines on revision of scales of pay in Central Public Sector Enterprises (CPSE) effective from 01 January 2007. The guidelines further stated that in respect of other allowances/perks, 'The Board of Directors would decide on the allowances and perks admissible to the different categories of the executives subject to a maximum ceiling[1] of 50 *per cent* of the basic pay. Instead of having a fixed set of allowances, the CPSEs may follow 'Cafeteria Approach' allowing the executives to choose from a set of perks and allowances'.

A. Audit observed that beside the payment of perks and allowances under the cafeteria approach, Airports Authority of India (AAI) was also paying perks and allowances in the form of Rating Allowance, Proficiency Allowance and Medical Allowance[2] to its employees over and above the ceiling of 50 *per cent* and other exempted allowances in contravention of the directions[3] issued by DPE on the same. Further, though AAI discussed this matter in the meeting of Manpower Advisory Board held in May/July 2012 and decided to refer the matter to MoCA for seeking the Cabinet approval specifying the objectives and reasons, but till date (February 2014) the approval of Cabinet was not accorded.

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[1] *The following allowances would be outside the purview of ceiling of 50 per cent of the Basic Pay:*
- *(i) North-East Allowance limited to 12.5 per cent of Basic Pay.*
- *(ii) Allowance for Underground Mines limited to 15 per cent of Basic Pay.*
- *(iii) Special Allowance up to 10 per cent of Basic Pay for serving in the difficult and far flung areas as approved by concerned Ministries in consultation with Department of Public Enterprises from time to time.*
- *(iv) Non-Practicing Allowance limited to 25 per cent of Basic Pay for Medical Officers.*

[2] *Rating allowance to executives of Air Traffic Controllers, Proficiency Allowance to CNS executives and Medical Allowance to all employees*

[3] *DPE OM dated 26 November 2008, OM dated 2 April 2009, OM dated 1 June 2011, OM dated 29 June 2012 and OM dated 11 June 2013*

AAI stated (July 2013) that payment of allowances over and above the 50 *per cent* prescribed by DPE were a legacy issue in AAI. It was also stated that these allowances were being paid for specialized jobs which the ATC/CNS and other executives performed for which they had acquired special technical skills. Further, these allowances were being paid prior to the wage revision effected by DPE, i.e., 01 January 2007. The management also decided (January 2014) to submit the issue to Cabinet for approval.

The reply is not tenable as the DPE guidelines categorically states that no allowances/benefits/perks other than those mentioned in DPE OM dated 26 November 2008 was admissible outside the 50 *per cent* ceiling. Further, AAI has not obtained the approval of the Cabinet till date.

Resultantly, the payment of allowance and perks amounting to ₹ 543.77 crore made during the period from 2007-08 to 2013-14 in the form of Rating Allowance, Proficiency Allowance and Medical Allowance was in contravention of DPE guidelines.

B. Audit observed that the subsidiaries of Coal India Limited (CIL) unduly allowed either allowances for cooking gas or provided free LPG cylinder to its executives over and above the ceiling of 50 *per cent* of basic pay, deviating from the DPE guidelines and accordingly extra payment was made to the executives over the years except by MCL, CMPDIL and SECL where benefit of gas allowance was discontinued in 2012, 2014 and 2015 respectively.

Audit further observed that there was no uniformity in the practice of allowing the benefit of Gas Allowance /LPG cylinder to the executives across the coal subsidiaries under the same Holding Company (CIL). In some coal subsidiaries, viz BCCL, NCL, WCL, MCL, SECL and ECL, gas allowance/LPG facility was allowed to the executives working at Subsidiary Headquarters as well as in area offices, while in other coal subsidiaries (CCL and CMPDIL), the same was not allowed to the executives working at subsidiary headquarters. The Holding Company, CIL, however, did not allow gas allowance to the executives working at its Head Office. Even as regards the compliance of DPE guidelines, there was no common approach towards discontinuing the benefit of gas allowance/LPG facility in the coal subsidiaries under CIL as MCL, SECL and CMPDIL had already discontinued gas allowance/facility but other subsidiaries of CIL are still continuing the same.

Based on the records examined in Audit in respect of Coal India Limited and its subsidiaries, an irregular payment of ₹29.33 crore to their executives was observed during 2009-10 to 2013-14 as given below:

Sl. No.	Name of CPSEs	Irregular Payment on account of LPG allowance/facility (₹ in crore)
1.	North Eastern Coalfields Limited (NECL) under control of Coal India Limited	0.18
2.	Mahanadi Coalfields Limited	0.81
3.	Northern Coalfields Limited	4.76
4.	South Eastern Coalfields Limited	10.56

5.	Western Coalfields Limited	4.63
6.	Central Coalfields Limited	2.64
7.	Bharat Coking Coal Limited	2.90
8.	Eastern Coalfields Limited	2.73
9.	Central Mine Planning and Design Institute Limited	0.12
	Total	**29.33**

CIL stated (November 2014) that:

- The supply of free coal to all employees including executives for domestic use had been in vogue in collieries of CIL subsidiary companies since pre-nationalization era and the practice was continued after nationalization of coal companies.

- Since the practice of free supply of coal had been contributing to health hazards, environmental pollution etc. in the coalfield areas and also due to escalation of the price of coal, substitution of LPG cylinder with coal supply had become a necessity and was cost effective to the company. Hence, the supply of free coal was discontinued and one LPG cylinder per month per employee was provided in its place.

- The supply of free coal or LPG cylinder in its place to executives had never been a component of pay and perks of any of the executive pay revisions since 1973/1975 and thus it could not be considered as perks or allowance. Therefore, the supply of LPG cylinder in lieu of the domestic supply of coal did not violate the DPE guidelines on perks and allowance.

The subsidiaries of CIL viz., WCL, CCL, ECL and BCCL offered (September/October/November 2014/February 2015) the same views in line with the Holding Company (CIL). NCL stated (November 2014) that supply of one LPG cylinder free of cost was not included in the list of perks as provided in cafeteria approach. CMPDIL, MCL and SECL, however, stated (September 2014/ January 2015/ February 2015) that the present practice of reimbursement to executives for LPG had been discontinued.

The above contentions are not acceptable in view of the following:

- DPE guidelines dated 26 November 2008 categorically stated that no allowances and perks would be admissible to the executives over and above the maximum ceiling of 50 *per cent* of the Basic Pay. Further, Gas Allowance did not come within the purview of four allowances which were specifically kept by DPE outside the purview of the above 50 *per cent* ceiling.

- CIL had itself admitted that the supply of free coal or LPG cylinder in its place to executives had never been a component of pay and perks of any of the executive pay revisions. As such, extending benefit of LPG allowance or facility is not regular and is in violation of DPE guidelines. Further, free supply of LPG cylinder to the executives for domestic cooking should have been considered as one of the components of Perks as per definition of 'Perquisites' in terms of Section 17(2) of the Income Tax Act, 1961.

- The DPE Office Memorandum dated 1 June 2011, 29 June 2012 and 11 June 2013 directed all the ministries/departments for strict compliance of the relevant provision and decided that no other allowance or perks would be kept outside the 50 *per cent* ceiling except the four that have been provided in the DPE OM dated 26 November 2008.

- MCL, one of the subsidiaries of CIL, had already issued instructions (July 2012) to ensure that no other payment was made to any executive on account of any allowance/benefit/perks outside the prescribed 50 *per cent* ceiling in pursuance of the DPE directives and accordingly stopped payment of LPG allowance. CMPDIL and SECL have also accepted to discontinue the practice of reimbursement to executives for LPG. However, the other subsidiaries of CIL are still continuing the practice of allowing gas allowance/facility to their executives though they are under the same Holding Company (CIL).

The matter was reported to the Ministry of Civil Aviation (August 2014) and Ministry of Coal (November 2014); their response in respect of AAI and CIL and its subsidiaries was awaited (March 2015).

The New India Assurance Company Limited, General Insurance Corporation of India Limited, United India Insurance Company Limited, Export Credit Guarantee Corporation of India Limited, The State Trading Corporation of India Limited, Coal India Limited and Food Corporation of India

8.2 Recoveries at the instance of audit

In 22 cases pertaining to seven CPSEs, audit pointed out an amount of ₹ 58.59 crore that was due for recovery. The management of CPSEs had recovered an amount of ₹ 56.60 crore (97 *per cent*) during the period 2013-14 as detailed in **Appendix-I.**

CHAPTER IX

Follow-up on Audit Reports (Commercial)

Audit Reports of the CAG represent the culmination of the process of scrutiny of accounts and records maintained in various offices and departments of CPSEs. It is, therefore, necessary that appropriate and timely response is received from the executive on the audit findings included in the Audit Reports.

The Lok Sabha Secretariat requested (July 1985) all the Ministries to furnish notes (duly vetted by Audit) indicating remedial/corrective action taken by them on various paragraphs/appraisals contained in the Audit Reports (Commercial) of the CAG as laid on the table of both the Houses of Parliament. Such notes were required to be submitted even in respect of paragraphs/appraisals which were not selected by the Committee on Public Sector Undertakings (COPU) for detailed examination. The COPU in its Second Report (1998-99-Twelfth Lok Sabha), while reiterating the above instructions, recommended:

- setting up of a monitoring cell in each Ministry for monitoring the submission of Action Taken Notes (ATNs) in respect of Audit Reports (Commercial) on individual Public Sector Undertakings (PSUs);
- setting up of a monitoring cell in Department of Public Enterprises (DPE) for monitoring the submission of ATNs in respect of Reports containing paras relating to a number of PSUs under different Ministries; and
- submission to the Committee, within six months from the date of presentation of the relevant Audit Reports, the follow up ATNs duly vetted by Audit in respect of all Reports of the CAG presented to Parliament.

In the meeting of the Committee of Secretaries (June 2010) it was decided to make special efforts to clear the pending ATNs/ATRs on CAG Audit Paras and PAC recommendations within the following three months. While conveying this decision (July 2010), the Ministry of Finance recommended institutional mechanism to expedite action in the future.

While reviewing the follow up action taken by the Government on the above recommendations, the COPU in its First Report (1999-2000-Thirteenth Lok Sabha) reiterated its earlier recommendations that the DPE should set up a separate monitoring cell in the DPE itself to monitor the follow-up action taken by various Ministries/Departments on the observations contained in the Audit Reports (Commercial) on individual undertakings. DPE informed (March 2015) that a separate monitoring cell had been set up to monitor the follow up on submission of ATNs by the concerned administrative Ministries/Department. DPE also informed that they had also requested all the concerned departments having jurisdiction over CPSEs to set up Monitoring Cells in their department. Three monitoring meetings were also convened by DPE to review pending ATNs.

A review in Audit revealed that despite reminders, 36 ATNs are awaited from various Ministries, as detailed in **Appendix-II.**

(PRASENJIT MUKHERJEE)
Deputy Comptroller and Auditor General
and Chairman, Audit Board

New Delhi
Dated: 28 May 2015

Countersigned

(SHASHI KANT SHARMA)
Comptroller and Auditor General of India

New Delhi
Dated: 29 May 2015

APPENDICES
&
ANNEXURES

Appendix-I

(Referred to in para 8.2)

Recoveries at the instance of Audit during 2013-14

(Amount ₹ in lakh)

Name of Ministry/ Department	Name of the Central Public Sector Enterprise (CPSE)	Audit observations in brief	Amount of recovery pointed out by Audit	Amount recovered by the Management
Finance	The New India Assurance Company Limited	Non recovery of advance	8.79	3.12
	General Insurance Corporation of India	Incorrect claim settlement under FAC policy *(facultative policy)*	152.00	152.00
	General Insurance Corporation of India	Short charging/short collection of premium and improper grant of NCB. General Insurance Co. Treaty No.45359 and 47570	48.00	32.93
	United India Insurance Company Limited	Excess claim due to error in calculation of the value of iron scrap salvage	3.00	3.00
Commerce and Industry	Export Credit Guarantee Corporation of India Limited	Excess payment of claim	4.93	3.94
	The State Trading Corporation of India Limited	Failure to safeguard the interest of the company resulted in unwarranted transfer of gain	3194.00	2802.00
Coal	Coal India Limited, MM Division	Incorrect calculation of interest on loan provided to M/s BEML	4.44	4.00
	Food Corporation of India	Excess payment of storage cum handling charges	177.00	261.00

Ministry of Consumer Affairs, Food and Public Distribution	Divisional office, Moga	to private contractors in violation of contractual terms		
	Food Corporation of India Divisional office, Gurdaspur	Non recovery of storage cum stacking charges on replacement of BRL rice due to delay in replacement of substandard rice by State Agencies/Millers	1.03	5.60
	Food Corporation of India Regional office, Punjab	Acceptance and movement of substandard foodgrains and resultant quality complaint	9.81	13.28
	Food Corporation of India Divisional office, Faridkot	Overpayment of overtime allowance to ancillary labour	9.65	6.42
	Food Corporation of India Divisional office, Kapurthala	Excess payment of gunny depreciation	85.76	85.76
	Food Corporation of India Divisional office, Kurushetra	Excess payment to State Govt. and its agencies due to non-deduction of Storage gain on direct delivery of wheat during Rabi Marketing season 2004-05	723.24	720.88
	Food Corporation of India	Reimbursement of unauthorized Hill transport subsidy in respect of sugar on movement to Andaman & Nicobar Islands.	389.00	388.79
	Food Corporation of India	Inadmissible payment to State Govt. agencies on account of custody & maintenance charge for custom Milled Rice.	19.85	8.66
	Food Corporation of India Divisional office, Dimapur	Irregular payment of incentive	70.30	29.33
	Food Corporation of India	Avoidable loss due to excess issue of maize against allocation to the Poultry industry in Maharashtra	35.39	56.31
	Food Corporation of India Divisional office, Jaipur	Irregular payment towards Arhathia charges to State Agencies on procurement of wheat.	349.23	187.74

Ministry of Consumer Affairs, Food and Public Distribution	Food Corporation of India Regional office, Gonda	Irregularities and non-maintenance of records for purchases of wheat and rice excess payment of Mandishulk.	7.85	7. 85
	Food Corporation of India Regional office, Bareilly	Payment of gunny depreciation against instruction of GOI	32.10	377.00
	Food Corporation of India Regional office, Bareilly	Inadmissible society commission paid to state Government agency	379.00	356.00
	Food Corporation of India Regional office, Bareilly	Unadjusted claims standing in the name of state Govt. agencies.	155.00	154.00
Total			**5859.37**	**5659.61**

Appendix-II

(Referred to in Chapter IX)

Statement showing the details of Audit Reports prior to 2014 (Commercial) for which Action Taken Notes are pending

No. & year of Report	Name of Report	Para No.
Department of Atomic Energy		
13 of 2013	Compliance Audit	Para 1.1
13 of 2014	Compliance Audit	Para 1.1
Department of Chemicals		
13 of 2014	Compliance Audit	Para 2.1
Ministry of Civil Aviation		
13 of 2013	Compliance Audit	Paras 3.1, and 3.3
13 of 2014	Compliance Audit	Para 3.1
Ministry of Coal		
3 of 2011-12	Compliance Audit	Para 3.2
8 of 2012-13	Compliance Audit	Paras 3.1
13 of 2014	Compliance Audit	Paras 4.1
Ministry of Development of North Eastern Region		
13 of 2014	Compliance Audit	Para 8.1
Department of Fertilizers		
03 of 2011-12	Compliance audit	Para 8.1 and 8.2
13 of 2013	Compliance audit	Para 8.1
13 of 2014	Compliance audit	Para 2.2
10 of 2010-11	Performance Audit of activities of selected PSUs	Chapter-IV
Ministry of Finance , Department of Financial Services		
24 of 2009-10	Compliance Audit	Para 8.2.1
10 of 2010-11	Performance Audit of activities of selected PSUs	Chapter V **(03 Companies)**
3 of 2011-12	Compliance Audit	Para 9.2, 9.3, 9.4, 9.5 and 9.6

8 of 2012-13	Compliance Audit	Para 8.1
13 of 2013	Compliance Audit	Paras 9.1, 9.2 **(04 Companies),** 9.3 9.4, 9.6 and 9.7
Department of Food and Public Distribution		
13 of 2013	Compliance Audit	Para 6.3
13 of 2014	Compliance Audit	Para 6.1

Annexure-I
(Referred to in para 3.3.2.1)

Statement showing operating results of DCC during 2009-10 to 2013-14

(₹ in crore)

Particulars	**2009-10**	**2010-11**	**2011-12**	**2012-13**	**2013-14**
Income from Sales (A)	144.06	159.20	181.34	165.56	196.69
Variable Cost* (B)	110.93	116.23	148.39	124.12	143.35
Contribution (C)=(A)-(B)	33.13	42.98	32.95	41.44	53.34
Fixed Cost (D)	48.56	47.78	63.55	65.37	69.87
Total Cost (E)= (B)+(D)	159.49	164.01	211.94	189.49	213.22
Profit(+) /Loss(-)(F)= (A)-(E)	-15.43	-4.81	-30.60	-23.94	-16.53
Contribution on Sales *(Per cent)*	23	27	18	25	27
Contribution on Fixed Cost *(Per cent)*	68	90	52	63	76

Includes Prior Period Adjustments and cost of other job of non-recurring nature

Annexure-II
(Referred to in para 3.3.2.3)

Statement showing capacity utilization at DCC during 2009-10 to 2013-14

	2009-10	**2010-11**	**2011-12**	**2012-13**	**2013-14**
Installed capacity [Coal (MT)]	547500	547500	547500	547500	547500
Available capacity [Coal (MT)]	328500	328500	328500	328500	328500
Utilized capacity [Coal (MT)]	166016	143778	89946	72894	93614
Available capacity in relation to installed capacity (*Per cent*)	60	60	60	60	60
Capacity utilization in relation to installed capacity (*Per cent*)	30.32	26.26	16.43	13.31	17.10
Capacity utilization in relation to available capacity (*Per cent*)	50.53	43.77	27.38	22.19	28.49

Annexure-III

(Referred to in para 3.3.2.3)

Statement showing actual production against target fixed and deviations from target during 2009-10 to 2013-14

A) Coal gas: **(in Nm^3)**

Year (1)	Available capacity (2)	Production Target (3)	Production Actual (4)	Deviation of target from available capacity *(Per cent)* (5)=(2-3)	Deviation from available capacity (6)=(5/2)*100	Deviation of actual from target (7)=(3-4)	Deviation from target *(Per cent)* (8)=(7/3)*100	Deviation from target (in therm) (9)	Rate per therm (₹) (10)	Opportunity loss due to low production against target (₹) (11)=(9*10)
2009-10	103806000	67525000	57841462	36281000	35	9683538	14	1229809	25	30745225
2010-11	103806000	63875000	57979700	39931000	38	5895300	9	748703	30/33	22461090
2011-12	103806000	60225000	41834474	43581000	42	18390526	31	2335597	33/38	77074701
2012-13	103806000	60335000	36301373	43471000	42	24033627	40	3052271	38	115986298
2013-14	103806000	45293069	45160811	58512931	56	132258	1	16797	38/46	638286
Total				**221776931**		**58135249**		**7383177**		**246905600**

***1 Nm^3= 0.127 therm, approximately**

***** In case of more than one prevailing price, the lowest price has been considered as per conservative approach.***

B) CIL Coke: **(in MT)**

Year (1)	**Available capacity (2)**	**Production Target (3)**	**Production Actual (4)**	**Deviation of target from available capacity (5)=(2-3)**	**Deviation from available capacity** *(Per cent)* **(6)=(5/2)*100**	**Deviation of actual from target (7)=(3-4)**	**Deviation on target** *(Per cent)* **(8)=(7/3)*100**	**Rate per MT (₹) (9)**	**Opportunity loss due to low production against target (₹) (10)=(8*9)**
2009-10	108405	29542	25780	78863	73	3762	13	5000	18810000
2010-11	108405	26776	26359	81629	75	417	2	5000 / 5062 / 5362 / 9862	2085000
2011-12	108405	47932	27569	60473	56	20363	42	9862	200819906
2012-13	108405	44266	23465	64139	59	20801	47	9862	205139462
2013-14	108405	26898	26470	81507	75	428	2	9862	4220936
Total				**366611**		**45771**			**431075304**

**** In case of more than one prevailing price, the lowest price has been considered as per conservative approach.***

C) Coke Fines: **(in MT)**

Year (1)	**Available capacity (2)**	**Production Target (3)**	**Production Actual (4)**	**Deviation of target from available capacity (5)=(2-3)**	**Deviation from available capacity** *(Per cent)* **(6)=(5/2)*100**	**Deviation of actual from target (7)=(3-4)**	**Deviation on target** *(Per cent)* **(8)=(7/3)* 100**	**Rate per MT* (9)**	**Loss due to low production (₹) (10)=(7*9)**
2009-10	108405	118169	90758	-9764	-9	27411	23	2250 / 2560	61674750
2010-11	108405	107105	70221	1300	1	36884	34	2560 / 2576 / 2776 / 5076	94423040
2011-12	108405	71898	31263	36507	34	40635	57	5076	206263260
2012-13	108405	31263	24848	77142	71	6415	21	5076	32562540
2013-14	108405	25093	24576	83312	77	517	2	5076	2624292
Total				**188497**		**111862**			**397547882**

Note: * In case of more than one prevailing price, the lowest price has been considered as per conservative approach.
***** Considering price of Coke Fines (0-10mm) which is lower than that of Coke Fines (6-35mm).***

Annexure-IV
(Referred to in para 3.3.2.5)
Statement showing amount of extra freight paid by DCC on procurement of Coal from SECL instead of ECL (From 2009-10 to 2013-14)

Year	Coal purchased during the year (in MT)	Extra freight per MT (in ₹)	Total (₹)
2009-10	3,59,400	1,000	35,94,00,000
2010-11	3,18,844	1,000	31,88,44,000
2011-12	2,68,495	1,000	26,84,95,000
2012-13	2,48,137	1,000	24,81,37,000
2013-14	1,89,662*	1,000	18,96,62,000
Total	**-**	**-**	**138,45,38,000**

During 2013-14 DCC procured coal from both ECL (w.e.f. September 2013) as well as SECL. Hence the figure in 2013-14 represents coal procured from SECL only.

Annexure-V
(Referred to in para 3.3.2.6)
Statement showing cost of production of gas vis-à-vis price of gas paid by GCGSC and consequent loss due to poor pricing of coal gas:

Year (1)	Dispatch (in Nm^3) (2)	Dispatch (in Therm) (3) = (2)* 0.127	Cost of production at DCC per therm (₹) (4)	Price paid by GCGSC per therm (₹) (5)	Unrecovered Cost per therm (₹) *(6)=(4-5)	Loss due to non-recovery of Cost (₹) (7)=(3*6)
2009-10	54947000	6972774.3	46.97	25	21.97	153191851
2010-11	55787000	7079370.3	62.44	30 / 33	30.94	219035717
2011-12	41379567	5251067.05	92.76	33 / 38	57.26	300676099
2012-13	35827000	4546446.3	90.84	38	52.84	240234222
2013-14	44028000	5584104.37	80.54	38/46	38.54	215211382
					Total	**1128349271**

Note: * In case of more than one price (paid by GCGSC) prevailing in a year, the applicable rate has been considered on average basis.

*****1 Nm^3= 0.127 therm, approximately***

Annexure-VI

(Referred to in para 3.3.2.6)

Statement showing price offered by GCGSC against its tariff of gas per therm to domestic, commercial and industrial consumers during the last five years ended on 31 March 2014:

(in ₹/therm)

	2009-10	2010-11	2011-12	2012-13	2013-14
A) Price offered by GCGSC to DCC	25	30/33	33/38	38	38/46
Tariff of gas collected by GCGSC:					
B) Domestic consumers	50	51	51	51	51
C) Commercial consumers	70	85	85	85	85/110
D) Industrial consumers	60	70	70	70	70/100
Profit earned by GCGSC through sale of DCC gas:					
E) Domestic consumers **(B-A)**	25	21/18	18/13	13	13/5
F) Commercial consumers **(C-A)**	45	55/52	52/47	47	47/64
G) Industrial consumers **(D-A)**	35	40/37	37/32	32	32/54

Annexure-VII

(Referred to in para 3.3.2.9)

Statement showing sales of co-product vis-à-vis overall sales during 2009-10 to 2013-14 (in ₹ lakh)

Year (1)	Sales of Co-products						Total Sales of All products (8)	Co-products as a percentage of Total Sales (9) =(7) * 100/(8)
	Coke (2)	Coke Fines (3)	Coal tar (4)	Light Oil (5)	Ammonium sulphate (6)	Total (7)=(2)+(3)+(4)+(5)+(6)		
2009-10	852.60	3544.89	1570.27	88.42	29.32	6085.54	8204.07	74.18
2010-11	16.21	26.70	20.51	0.74	0.14	64.30	864.87	7.44
2011-12	1407.39	435.59	1976.72	85.04	0	3904.74	5759.82	67.78
2012-13	396.52	150.74	1813.88	61.30	0.50	2422.94	4149.85	58.39
2013-14	258.38	35.29	989.08	75.39	20.56	1378.7	3627.08	38.01

Annexure-VIII

(Referred to in para 3.3.2.9)

Statement showing loss due to shortfall in obtaining other products vis-à-vis norms during 2009-10 to 2013-14

COKE

Year (1)	Coal Consumption (in MT) (2)	Norms (in MT) (3)	Actual (in MT) (4)	Difference (in MT) (5)= (3-4)	Rate per MT (₹) (6)	Opportunity loss due to low production (₹) (7)= ((5*6)
2009-10	346824	232372	25780	206592	5000	1032960000
2010-11	319697	214197	26359	187838	5000 / 5062 / 5362 / 9862	939190000
2011-12	263503	176547	27572	148975	9862	1469191450
2012-13	260234	174357	23465	150892	9862	1488096904
2013-14	297280	199178	26470	172708	9862	1703246296
TOTAL				**867005**		**6632684650**

Note: * As per norms (July 2011) yield of coke from one mt of coal carbonisation is 670kg.

***** In case of more than one prevailing rate, the lowest rate has been considered as per conservative approach.***

****** Coal Consumption = Opening Stock + Purchase – Closing Stock***

COAL TAR

Year	Coal Consumption (in MT)	Norms (in MT)	Actual (in MT)	Diff (in MT)	Rate per MT (in ₹)	Loss due to low production (in ₹)
2009-10	346824	19075	8753	10322	24999	258039678
2010-11	319697	17583	7865	9718	29360	285320480
2011-12	263503	14493	5288	9205	39487	363477835
2012-13	260234	14313	4440	9873	43368	428172264
2013-14	297280	16350	3655	12695	43006	545961170
TOTAL				**51813**		**1880971427**

**** As per norms (July 2011) yield of coal tar from one mt of coal carbonisation is 55 kg.***

***** Coal Consumption = Opening Stock + Purchase – Closing Stock***

LIGHT OIL

Year (1)	Coal Consumption (in MT) (2)	Norms (in Ltr) (3)	Actual (in Ltr) (4)	Diff (in Ltr) (5)	Rate per KL (₹) (6)	Loss due to low production (₹)(7)= (5*6)
2009-10	346824	1248	340	908	19425	17637900
2010-11	319697	1151	326	825	19425/23425/ 26950	19361719
2011-12	263503	949	306	643	26950	17328850
2012-13	260234	937	223	714	26950	19242300
2013-14	297280	1070	281	789	26950	21263550
TOTAL				**3879**		**94834319**

Note:* * *As per norms (July 2011) yield of coke from one mt of coal carbonisation is 3.6 Ltr

***** In case of more than one prevailing rate, the lowest rate has been considered as per conservative approach.***

Annexure-IX

(Referred to in para 3.3.2.9)

Year	Coke (MT)	Coal Tar (MT)	Light Oil (KL)	Ammonium Sulphate (MT)
2009-10	8940.02	3783.83	11.44	4.45
2010-11	4692.24	4577.36	17.59	0.8
2011-12	17760.45	4860.39	8.02	0.8
2012-13	37204.76	5051.26	3.55	0.8
2013-14	61054.77	6430.03	4.31	11.85
Total	**129652.24**	**24702.87**	**44.91**	**18.7**

Statement showing position of Closing Stock of Co-Products

Annexure-X

(Referred to in para 5.5)

Sl. No.	**Name of FCI owned siding at the destination/ Food Storage Depot**	**District Office**	**Destination terminal charges paid by dispatching unit of FCI (₹)**
EAST ZONE			
1	Jamshedpur	Ranchi	5321263
2	Dhanbad	Dhanbad	841110
3	CSD New Jalpaiguri	Siliguri	3270515
4	GFD New Jalpaiguri	Siliguri	
5	FSD Cossipore Road	Kolkata North	1991542
6	Kalyani	Non-port depot	2455240
7	Budge Budge	Non-port depot	7607668
8	Durgapur	Durgapur	1016490
9	Dankuni	Hooghly	1776566
10	Adra	Bankura	411500
11	FSD, Mangalbari	Malda	656440
12	Phulwarisharif	Patna	1112751
13	NRPA	Muzaffarpur	3300720
14	Mokama	Patna	1110730
15	Buxar	Patna	1190740
16	Dighaghat	Patna	287130
17	Gaya	Gaya	1017820
18	Jharsuguda	Sambalpur	1320860
19	Khurda Road	Bhubaneshwar	4196525
NORTH ZONE			
20	Barabanki	Faizabad	354920
21	Dhamora	Moradabad	211818
22	Gorakhpur	Gorakhpur	602324
23	Hapur	Hapur	229180
24	Varanasi	Varanasi	1121060
25	Chandari	Kanpur	169390
SOUTH ZONE			
26	Chingavanam	Kottayam	496870
27	Kazhakuttam	Thiruvananthapuram	495480
28	Mavelikara	Allepey	53040
29	Karunagapally	Kollam	93760

30	Quilon	Kollam	473140
31	Hubli	Hubli	524200
32	Angamaly	Ernakulam	308380
33	FSD Malankunnathukavu	Thrissur	288120
34	FSD Sevur	Vellore	1414990
35	FSD Avadi	Chennai	327040
36	FSD West Hill	Kozhikode	993060
37	FSD Thikkodi	Kozhikode	307110
38	FSD Palakkad	Palakkad	489750
39	Krishnajanpuram	Bangalore	1202600
40	Whitefiled	Bangalore	692360
41	FSD Payannur	Kannur	333900
		TOTAL	**50068102**

Annexure-XI

(Referred to in para 7.1.6.5 (b) (i))

Comparison of the terms of the Company's Refinance Scheme and those as per sanction letters

Name of the borrower	Amount of loan/date of sanction letter	Terms as per Refinance Scheme		
		Tenor of Refinance	**Repayment of Refinance**	**Prepayment**
		Tenor of refinance shall be 10 years with a reset after 5 years. However, If the GoI considers necessary may allow an extension with reset for 5 more years after 10 years.	The repayment of refinance would be linked with the repayment schedule of the loan fixed by the consortium in a manner so as to ensure total repayment of Refinance amount within a period of 10 years.	Prepayment of refinance instalment is permitted only in cases where the borrowing units have prepaid the corresponding loan instalments.
Terms as per sanction letter(s) in respect of loans sanctioned to REC, PFC and IDFC				
REC	870 crore / 26.03.2010	Four years.	Bullet payment on 19.03.2014 i.e. the maturity of tax free bonds.	Not mentioned
	1000 crore / 30.12.2010	Three years.	Bullet repayment on 21.01.2014.	Not mentioned
	1195 crore / 06.09.2013	Ten years with annual resets.	Bullet repayment	Prepayment option on reset with 7 days' notice period.
PFC	630 crore/ 26.03.2010	Four years.	Bullet payment on 19.03.2014 i.e. the maturity of tax free bonds.	Not mentioned
	1000 crore / 30.12.2010	Three years.	Bullet repayment on 21.01.2014.	Not mentioned
	1083 crore / 13.06.2014	Five years with annual reset with put and call option on reset.	Bullet repayment	Prepayment of refinance installment is permitted in case of reset with a 7 day notice period, or where the borrowing units have prepaid the corresponding loan installments.
IDFC	668 crore/ 30.03.2012	One year 10 months with half-yearly reset.	Bullet repayment on 20.01.2014 co-terminus with the maturity of bonds raised for	Prepayment of refinance installment is permitted only in

			Refinance by the Company.	case where the borrowing units have prepaid the corresponding loan installments. Further, IDFC to have an option to prepay at the time of reset with a month's notice without any prepayment penalty.
	250 crore/ 05.03.2013	One year.	Bullet repayment on 19.03.2014 co-terminus with the maturity of bonds raised for Refinance by the Company.	Prepayment of refinance installment is permitted only in case where the borrowing units have prepaid the corresponding loan installments.
	393 crore/ 06.09.2013	Five years with annual reset.	Bullet repayment	Prepayment of refinance installment is permitted in case of reset with a 7 day notice period, or where the borrowing units have prepaid the corresponding loan installments.
	668 crore/ 21.03.2014	Five years with annual reset.	Bullet repayment	Prepayment of refinance installment is permitted in case of reset with a 7 day notice period, or where the borrowing units have prepaid the corresponding loan installments.