Executive Summary

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Introduction

Rashtriya Ispat Nigam Limited (RINL), the first shore based Integrated Steel Plant in the country was incorporated on 18 February 1982 with an installed capacity of 3 million tonne per annum (MTPA) with the main objective of production and sale of iron and steel products. It commenced full-fledged operations from 1992-93. RINL has been making profit over the last 12 years and earned profit after tax of ₹ 366.45 crore on an income of ₹13,431 crore in 2013-14 while operating four captive mines at Madharam, Jaggayyapet, Garbham and Nellimarla, all situated in Andhra Pradesh and Telangana to meet its requirement of raw materials i.e. dolomite, limestone, manganese and sand. It has a Long Term Contract Agreement (LTA) with National Mineral Development Corporation (NMDC) Limited for supply of iron ore. RINL planned (2004) capacity expansion of installed capacity from 3 MTPA to 6.3 MTPA in two stages i.e. Stage-I and Stage-II.

Audit Scope and Audit Sample

We conducted performance audit of company's activities relating to capacity expansion covering the period, 2004-05 to 2013-14. We reviewed the activities of all the major projects of Stage-I i.e. Raw Material Handling Plant (RMHP), Blast Furnace (BF), Sinter Plant (SP), Steel Melt Shop (SMS) and two mills of Wire Rod Mill (WRM) and Seamless Tube Mill (SLTM) and Stage-II units namely Special Bar Mill (SBM) and Structural Mill (SM). A sample of 68 contracts of value ₹ 13275.79 crore representing 90 *per cent* of total 252 contracts valuing ₹ 14731 crore was examined in performance audit to assess the economy, efficiency and effectiveness of planning of capacity expansion including the system of award of contracts.

(Para 1.7 and Para 2.2.2)

Significant audit findings are as under :-

(i) Overshooting of target dates of capacity expansion

RINL took up capacity expansion from 3 MTPA to 6.3 MTPA at a cost of ₹ 8,692 crore from zero date i.e. 28 October 2005 with envisaged dates of completion of Stage-I in October 2008 and Stage-II in October 2009. Subsequently, RINL was conferred with Navaratna status in November 2010 by GoI. Accordingly, the Board of Directors (BOD) of RINL in July 2011 approved Revised Cost Estimates (RCE) of capacity expansion at an amount of ₹ 12,291 crore. In RCE, the completion dates of Stage-I and Stage-II were revised to October 2011 and October 2012 respectively. However, RINL has not achieved (August 2014) the dates of completion of capacity expansion and kept revising the same. Construction work in Stage-II units which was in progress was likely to be completed by February 2015 (as of August 2014) with a delay of

28 months against the revised time schedule of October 2012. Despite prolonged time and cost overrun, the capacity expansion has not materialised. The destruction caused by recent cyclone Hudhud (October 2014) would only compound the delays.

(Para 1.3 and Para 2.1.2)

(ii) Insufficient capacity of rolling mills

RINL was operating on insufficient rolling mills and earning lower margins on sale of semi steel instead of finished steel. RINL has not planned for establishment of sufficient matching capacity of rolling mills in the present capacity expansion from 3 MTPA to 6.3 MTPA. Further, RINL has dropped the work of SLTM (February 2008) on the ground of increase in cost estimates, technological, unfavourable market conditions etc. By that time RINL incurred an avoidable expenditure of ₹ 18.27 crore towards civil works of SLTM and missed out on conversion of semi steel into finished product that would have yielded higher margins.

(Para 2.5 and Para 2.5.1)

(iii) Risk to ensuring availability of raw material

With a view to having an uninterrupted supply of raw material, RINL acquired (January 2011) 51 *per cent* shares valuing ₹ 361 crore in Eastern Investments Limited (EIL) which had six licenses for iron ore and manganese mines in Odisha. However, RINL did not derive any benefit from this investment and all six licenses expired and were not renewed by Government of Odisha (March 2014). In respect of iron ore, RINL has Long Term Agreement (LTA) with NMDC Limited for supply of iron ore of 10.5 million tonne to feed up to the 6.3 MTPA capacity. As RINL has no captive mine of its own for acquiring iron ore and coking coal, it would be exposed to the risk of paying higher cost of raw material.

(Para 2.6)

(iv) Ineffectiveness in utilisation of services of consultant

Instead of preparing a Detailed Project Report (DPR), the consultant had prepared only a Project Report, which was submitted by RINL to MoS, which without insisting on DPR, communicated (October 2005) approval to capacity expansion proposed by RINL. There were variations from (-) 47 *per cent* to (-) 122 *per cent* in the updated cost estimates prepared by the consultant. RINL had not given any timeframe to the consultant for furnishing its recommendations on eligibility criteria, techno-commercial bids, finalizing the various stages of tenders, which eventually contributed to delays in execution of the project. The appointment of consultant had not served the intended purpose in expediting and ensuring quality of project management right from its conceptualisation to execution.

(Para 3.2.2.1)

(v) Inefficient contract management

In six civil contracts out of 18 civil works reviewed, the estimated cost varied by ₹ 158.64 crore and the percentage variation worked out between 31.76 *per cent* and 47.96 *per cent* of estimated costs which clearly indicated the failure of the consultant while estimating the BOQ.

(Para 3.2.2.2)

RINL paid mobilisation advance contrary to CVC guidelines, which resulted in extending undue favour to contractors of ₹ 156.02 crore including loss of interest of ₹ 38.68 crore on other than supply contracts like design and engineering, civil works, training, supply of maintenance spares etc.

(Para 3.2.2.4)

(vi) Inaccurate consideration of quantity of saleable steel and resultant deficient working of cash flow, PAT and IRR

The standard conversion rate for every tonne of liquid steel as per the production flow chart of RINL was 88.53 *per cent* of saleable steel for the existing plant. As per Project Report the conversion rate was envisaged at 92.23 *per cent* for the expansion plant. At the liquid steel production of 3.5 MTPA, the saleable steel could be 3.10 MTPA whereas RINL had considered production of saleable steel at base case only as 2.84 MTPA by considering production of liquid steel at 3.25 MTPA. Thus the production build-up of saleable steel in the base case was understated by 0.26 MTPA. At the level of 100 *per cent* capacity utilisation from the year 2014-15, RINL had estimated the production of saleable steel at 5.82 MTPA from liquid steel of 6.3 MTPA. At the standard conversion rate of 88.53 *per cent* from liquid steel to saleable steel for the existing plant and at the conversion rate of 92.23 *per cent* for the expansion plant against the production of liquid steel at 3.5 MTPA and 2.8 MTPA respectively, the production of saleable steel worked out only to 5.68 MTPA. Thus, the production build-up of saleable steel after capacity expansion was considered on higher side, by 0.14 MTPA. This error in considering quantity of saleable steel in base case and post expansion would have an adverse impact on cash flow, PAT and IRR. MoS, based on audit observations, has agreed that the IRR would come down to 12.96 *per cent* against the originally projected 14.02 *per cent*. This indicates that the IRR, cash flow and PAT calculated, while preparing the project report, were not realistic and not achievable.

(Para 3.1.3.2)

(vii) Monitoring Mechanism for Capacity expansion

In violation of MoS's directives (October 2005), RINL had not established an exclusive projects division headed by Director (Projects), who was appointed only in June 2009. Day to day monitoring of the project for capacity expansion was thus adversely affected for more than three and half years, at a crucial stage.

(Para 4.3 B)

Despite the directions of Board of Directors (BOD) (February 2006) for reporting the progress (both physical and financial) made in respect of capacity expansion at every Board meeting for its information, neither RINL ensured compliance with BOD's direction nor BOD insisted for compliance of its own directives. Documentation of project monitoring by RINL/BOD was deficient.

(Para 4.5)

(viii) Performance of RINL against MOU targets for capacity expansion

RINL made commitments in the Memorandum of Understandings (MOUs) entered with MoS for the year 2008-09 to commission the capacity expansion by 2010-11. Though RINL could not achieve the MOU target, it continued to make similar commitment in MOU for 2009-10, 2011-12 and 2012-13 with revised commissioning dates.

(Para 4.8)

Audit Recommendations:

Based on the audit findings, the following recommendations are made :-

1. RINL may take up the matter of non renewal of mining licenses in Odisha with the MoS/GoI, which, in turn, may take up the issue with appropriate agencies.
2. RINL may put in place a time bound programme to complete the work of capacity expansion by dovetailing the same with the revised scheduled dates of completion.
3. RINL may critically review the role of and value addition achieved with the engagement of the consultant in expediting the project of capacity expansion.
4. RINL may strengthen the monitoring mechanism to minimize controllable delays in project execution and delivery by fixing periodicity and levels of monitoring up to the Board of Directors.
5. MoS/RINL may ensure that there is a verifiable link between MOU targets and actual execution of work relating to capacity expansion.