

## Executive Summary

### Background

The Comptroller and Auditor General (C&AG) of India in the Performance Audit (PA) Report No. 7 of 2012-13 highlighted lack of transparency and objectivity in the allocation of coal blocks by the Central Government. The Hon'ble Supreme Court of India in its judgment on a writ petition, held that the allotments of coal blocks were arbitrary and illegal and vide its order of 24 September 2014 cancelled the allocation of 204 coal blocks - 42 coal blocks under 'producing' and 'ready to produce' category were cancelled from 31 March 2015 and the remaining 162 coal blocks were cancelled from 24 September 2014. The allottees of the 42 coal blocks were required to pay an amount of ₹295 per metric tonne (PMT) of coal extracted till 31 March 2015, as an additional levy.

As Government of India (GoI) wanted to re-allocate the 204 coal blocks cancelled by the Hon'ble Supreme Court of India, a legal framework through the Coal Mines (Special Provisions) Act, 2015 (preceded by the two Ordinances of October 2014 and December 2014) and the Coal Mines (Special Provisions) Rules, 2014 (the Rules) was laid down.

The Act provided for allocation of the cancelled coal blocks through public auction for specified end uses (SEUs) or allotment to Government companies. The SEUs were grouped under 'power' and 'non-regulated' (Iron and Steel, Cement and Captive Power Plant) sector categories. The Rules laid down enabling provisions for carrying out the auction and allotment processes and prescribed e-auction comprising of technical and financial parameters as the process for conducting auctions, among others. Rules were followed by issue of standard tender documents (STD) prescribing the conditions and the process for e-auction of the coal mines.

Prior to allocation of the cancelled coal blocks, the Cabinet Committee on Economic Affairs (CCEA) approved the "Methodology for fixing floor price and reserve price for coal mines/blocks proposed to be auctioned/allotted" which was notified by the Ministry of Coal (MOC) in December 2014. The methodology also provided for fixation of a ceiling price for power sector coal mines/blocks, which was to be Coal India Limited (CIL) notified price for the equivalent grade of coal. On the basis of the said methodology, the Central Mine Planning and Design Institute Limited (CMPDIL) calculated the intrinsic value based on the net present value (NPV) and the corresponding floor and additional reserve price of the coal mines/blocks.

The STD for power sector and non-regulated sector coal mines prescribed a two stage bidding methodology viz. Stage I and Stage II. The Stage I bidding comprised of submitting technical bid providing details regarding compliance with the eligibility conditions; and financial bid specifying the initial price offer (IPO). In the case of non-regulated sector coal mines, the IPO was to be higher than the floor price and in case of power sector coal mines the IPO was to be lower than the ceiling price. The bidders who qualified on the basis of Stage I bidding submitted their final price offer (FPO) at Stage II bidding (e-auction), which was carried out online on the platform for e-auction provided by MSTC Limited on its website.

### **Audit objectives and scope of audit**

Audit was conducted to ascertain the robustness and efficacy of the design adopted for allocation of coal mines through e-auction and proper implementation of the planned e-auction process/procedures and that the e-auction was conducted in a fair and transparent manner.

While the Audit examination was limited to the coal mines e-auctioned in the first two tranches, for the purpose of a comprehensive analysis of the e-auction and the mines allocated thereof, Audit has covered the allocations from the stage of design of the e-auction mechanism to the stage of production of coal and monitoring thereof.

### **Major Audit Findings**

It was observed in audit that the new mechanism for e-auction of coal mines was an improvement over the earlier system and attempted to incorporate the principles of objectivity, transparency and fairness in allocation of natural resources to private sector participants. However, Audit observed that there were some systemic and procedural issues, which needed to be addressed for further improvement in the e-auction mechanism, as mentioned below:

- Computation of intrinsic value of coal mines based on NPV required projections of cash flows, which in turn was dependent upon projections of revenue and costs (capital and revenue) associated with functioning of the concerned coal mine. Audit examined the records relating to computation of intrinsic value of 29 coal mines by CMPDIL. It was noticed that inconsistencies and inaccuracies in following some of the assumptions and various errors in computation of intrinsic values cumulatively resulted in under determination of upfront amounts in 15 coal mines, under

determination of floor prices in six non-regulated sector coal mines and revised fixed rates in all nine power sector coal mines.

**(Para 4.1)**

- Moitra coal mine contained 97 *per cent* coking coal out of its total coal reserves. It was washery grade coking coal, which was to be supplied to steel plant/s mainly for steel production and was to be washed for utilisation in the steel plant. There was provision for installation of washery in the MOC approved mine plan also. Though CIL did not notify the prices of washed coking coal, CIL's subsidiaries were selling washed coking coal at a much higher price than the notified price of raw coking coal. However, price of washed coking coal along with the capital cost of washery and related expenditure were not considered for calculation of intrinsic value of this mine. CMPDIL should have flagged the issue while carrying out the valuation and the matter should have been referred to the CCEA for reconsideration. Otherwise, keeping in mind the spirit of CCEA's approval, the price at which CIL's subsidiaries were selling washed coking coal, should have been considered for calculation of intrinsic value, the absence of which resulted in under determination of upfront amount and floor price of the mine.

**(Para 4.2)**

- Clause 3.3.2 of the STD provided that the technically qualified bidders (TQBs), which held first 50 *per cent* of the ranks or five TQBs, whichever was higher, would be considered as qualified for participating in the e-auction as qualified bidders (QBs). Simultaneously, Clause 4.1.1 of the STD provided that a joint venture (JV) company formed by two or more companies having a common SEU and which were independently eligible to bid in accordance with the Act, would be eligible to participate in the e-auction. Audit noted that in 11 out of the 29 coal mines successfully auctioned during the 1<sup>st</sup> and 2<sup>nd</sup> tranche, QBs ranging between two and three were from the same company/parent-subsidiary company coalition/JV coalition. Audit could not draw an assurance that the potential level of competition was achieved during the Stage II bidding of these 11 coal mines auctioned in the first two tranches. MOC subsequently amended Clause 4.1.1 in June 2015 with the objective of increasing the overall competition, for the coal mines auctioned in the 3<sup>rd</sup> tranche.

**(Para 5.1)**

- In terms of the STD, in the event that a bidder was a prior allottee, then it must have paid the additional levy within the time period prescribed for participating in the e-auction of coal mines. The Second Ordinance issued on 26 December 2014, amended the definition of the ‘prior allottee’ explaining that in case a mining lease has been executed in favour of a third party, then, the third party shall be deemed to be the prior allottee. However, in the auction of Sarisatolli and Trans Damodar coal mines, which were put up for auction on 27 December 2014, West Bengal Power Development Corporation Limited (WBPDCCL) was disqualified (February 2015) for non-payment of additional levy. This was done despite the fact that for the coal mines for which WBPDCCL was held as defaulter, the prior allottee, as per the amended definition, was a JV company i.e. Bengal Emta Coal Mines. Therefore, this disqualification was not as per the existing provisions.

**(Para 5.2)**

- The Nominated Authority (NA) recommended preferred bidder to the Central Government for declaration of successful bidders, as per the provisions of the Coal Mines (Special Provisions) Rules 2014. These Rules empowered the Central Government to direct NA to issue vesting order for the coal mine in favour of the successful bidder or provide such other binding directions to NA as deemed appropriate. After NA made recommendations for preferred bidder for 32 coal mines, MOC returned the cases of eight coal mines for re-examination. After submission of results of re-examination carried out on various parameters by NA, MOC examined these eight cases and rejected recommendation of NA for declaration of the ‘Preferred Bidder’ as ‘Successful Bidder’ in respect of three coal mines. While not commenting on any individual case, Audit is of the view that broad guidelines incorporating the parameters to be applied by NA and by MOC for evaluation of final bid prices would enhance transparency of the bidding process and may eliminate avoidable litigation.

**(Para 5.3)**

- Objectives of auction of coal mines for power sector were to augment power production for benefit of the economy and to provide cheaper coal to the power sector for benefit of consumers of power. Audit is of the view that in the light of vulnerabilities like stipulations regarding non-recovery of various charges from power consumers, weaknesses in the monitoring system and bank guarantee not being valid

for the life of the mine, the risk of non-compliance with contractual obligations was high. These may affect the sustainability of the model adversely in the long run.

**(Para 5.4.1)**

- The CCEA approved methodology allowed sale of 15 *per cent* of the generation capacity linked to the allotted coal mine on merchant basis, where the electricity tariff was not regulated. It also provided that coal utilised for generation of merchant power was to cost more than the coal used for generation of electricity to be sold at regulated rates. After the introduction of reverse then forward bidding, concept of payment of additional premium was introduced. However, the payment of additional premium was specifically excluded for the quantum of coal utilised for generation of power sold on merchant basis. This resulted in a scenario where the power producers would be paying lesser amount to the Government on utilisation of coal for producing power to be sold on merchant basis as compared to the coal utilised for production of power to be sold under the power purchase agreements (PPAs), which appeared to be not in consonance with the CCEA approval.

**(Para 5.4.2)**

- The e-auction process was carried out on the online e-auction platform provided by MSTC. Audit noticed that the audit trail was inadequate in the system and the system did not provide for linking specified end use plant (SEUP) with the registration ids.

**(Para 6.4.1 and 6.4.2)**

- Early auctioning of the coal mines in the first two tranches was taken up so that these could be brought under production speedily, as they were already producing/likely to produce/at an advanced stage of their statutory clearances at the time of their de-allocation. Though efforts were being made by the Government to start production from the successfully auctioned coal mines, only in 11 out of 26 coal mines, for which vesting orders were issued, production could be started/mine opening permission was issued. In the remaining coal mines, production could not commence as various statutory clearances/approvals were pending at the Central Government level, State Governments level and also at the level of allottees themselves. Delay in operationalisation of these coal mines had the potential to adversely affect an important objective of early auctioning of these coal mines, which was to ensure continuity in coal production thereby minimising adverse impact on core sectors such as steel, cement and power utilities.

**(Para 7.1 to 7.4)**

- The provisions of Coal Mine Development and Production Agreement laid down various terms and conditions for extraction and utilisation of coal and therefore, there was a need for strong and effective monitoring system. However, it was noticed in Audit that the monitoring mechanism at NA was under process of evolution. There was lack of clarity on the roles and responsibilities for various aspects of monitoring of the e-auctioned mines at the Coal Controller's Organisation (CCO), which was further accentuated by the weaknesses in the system, processes and resources at their disposal.

**(Para 8.2, 8.3.1 and 8.5)**

- There was a mismatch in eight cases between the production quantity submitted by prior allottees of the coal mines to State Governments vis-à-vis production quantity submitted to CCO. There was no mechanism to cross check the production figures given by the prior allottees indicating absence of regular monitoring and inspection of coal mines, which was one of the important activities of CCO. Further, additional levy of ₹3536.56 crore was pending from the prior allottees.

**(Para 8.3.2 and 8.4)**

- The Act provided that the allottee may use the coal from an allocated coal mine for any plant of the company or its subsidiary company, engaged in common specified end uses after providing written intimation (diversion notice) to the Central Government. Further, power sector coal mines were auctioned with the objective of providing cheaper power to the consumers. In such a scenario it was important to ensure that the benefit of the low cost of diverted coal was passed on to the consumers of the power produced by the 'other power plants'. However, Audit could not draw an assurance that a system existed/had been put in place to ensure that the diversion details are sent timely to the concerned authorities to ensure passing of benefit of cheaper coal to the consumers.

**(Para 8.6.1)**