CHAPTER IV: MINISTRY OF COMMERCE AND INDUSTRY

MMTC Limited

4.1 Loss due to non-adherence to the directions of Functional Management Committee of Directors

MMTC imported 43390 MTs of Manganese Ore (May 2014) from M/s UMK, South Africa, without adhering to the directions of Functional Management Committee of Directors (FMCoD) of MMTC (September 2013), to enter into Memorandum of Understanding (MoU) with the buyers prior to placement of indent on the foreign supplier. Since MMTC did not get committed buyers it could not sell substantial portion of the ore for 14 months and subsequently, sold it at almost half of the purchase price of the material. Thus, MMTC sustained net loss of ₹6.60 crore.

Functional Management Committee of Directors (FMCoD) of MMTC in its 102nd meeting granted (16 September 2013) in-principle approval, for import of one shipload (about 40000 MTs) of Manganese Ore of African origin, from M/s UMK, South Africa. As per the approval, Regional Office of MMTC at Kolkata was required to enter into Memorandum of Understanding (MoU) with the buyers prior to placement of indent on the foreign supplier of Manganese Ore. Further, two separate contracts were to be entered into between MMTC and Category-I buyers (who were to purchase on high sea sale[1] basis) and Category-II buyers (who were to purchase from MMTC under stock and sale[2] basis). All the terms and conditions were to be on back-to-back basis. At the time of placement of indent, earnest money deposit (EMD) of 15 *per cent* and 20 *per cent* of cargo value in case of 'high-sea-sales' and 'stock and sales' basis, respectively, was to be obtained from the party.

Accordingly, based on negotiations MMTC conducted (February 2014) with the supplier (M/s UMK), M/s UMK submitted an offer (04 March 2014) to sell the ore against 100 *per cent* payment through irrevocable letter of credit[3] (LC) payable at sight. MMTC accepted (05 March 2014) the offer and opened the LC as required (17 March 2014). There were no committed buyers on the date of signing of the contract. Subsequent to signing of the contract with M/s UMK, MMTC arranged committed buyers for the entire quantity (approx. 19650 MT) of Manganese Ore to be shipped to Haldia Port. However, MMTC

---

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

[2] ***Stock and Sales is a sale where goods are stored in godowns after import and the buyers are required to lift as per schedule agreed with the importer***

[3] ***A letter of credit (LC) is a document; typically from a bank (Issuing Bank), assuring that a seller (Beneficiary) will receive payment up to the amount of the letter of credit, as long as certain documentary delivery conditions have been met. In the event that the buyer (Applicant) is unable to make payment on the purchase, the Beneficiary may make a demand for payment on the bank. The bank will examine the Beneficiary's demand and, if it complies with the terms of the letter of credit, will honour the demand***

could arrange committed buyers for only 3000 MT of Manganese Ore out of 23740 MTs to be shipped to Vizag Port. The company imported a total quantity of 43,390 MTs of Manganese Ore @ USD 4.59 per dry metric ton unit (PDMTU) on CIF[4] basis. The total value of the cargo was ₹43.00 crore approx. including the company's margin of ₹0.86 crore approx. at the rate of two *per cent* of the value of total procurement.

Out of the total quantity of 43,390 MTs of Manganese Ore actually imported in May 2014, 23,740 MTs cargo was released at Vizag Port and the balance quantity of 19650 MT was released at Haldia Port. The quantity at Haldia Port was sold by MMTC at a net profit of ₹1.17 crore. Out of the cargo of 23740 MTs released at Vizag Port, MMTC could not sold any quantity on HSS basis and the entire cargo of 23740 MTs was stored (10 May 2014) in customs bonded warehouse. Later on, a quantity of 3000 MTs and 940 MTs was sold from the customs bonded warehouse to M/s Saikruthi Minmet Private Limited (May 2014) and M/s QVC (June 2014), respectively. Subsequently, to avoid interest and penalty on delayed clearance of unsold stock of 19800 MTs from customs bonded warehouse, MMTC paid the customs duty and de-bonded the cargo in September 2014.

As MMTC did not succeed in liquidating, the cargo at Vizag gainfully, it hosted the price circular on its website for sale of cargo on as-is-where-is basis (July 2015) and sold 11,000 MTs @ ₹6500/MT and the remaining quantity @ ₹6550/MT to sundry buyers against the cost price of approx ₹12,400 per MT. The net trading loss to MMTC on import of Manganese Ore from M/s UMK was ₹6.60 crore, after adjusting the trading profits of ₹1.17 crore earned by MMTC at Haldia.

Audit observed that:

MMTC did not identify and enter into MoU with committed buyers for the entire quantity to be imported on back to back basis, before entering into an agreement on 05 March 2014 with the foreign supplier viz. M/s UMK, as was desired by FMCoD in its in-principle approval granted for the above import.

Any decision to hold inventory in the MMTC's own account was required to be taken after carrying out risk analysis, as stipulated by the Audit Committee of Directors in its 41st meeting held on 29 January 2008. Further, in case of disposal of cargo on 'stock and sale' basis, the Risk Management Policy of MMTC also required fixing of 'stop-loss' norms in case of any steep fall in prices. However, the Management did not fix any 'stop-loss' norms in the present case. Resultantly, MMTC waited for 14 months to effect distress sale of the cargo at Vizag Port.

The Management in its reply (December 2015 / October 2016 / October 2017) stated that:

The entire quantity destined for discharge at Haldia port was sold/ committed before arrival of vessel at the port. However, due to the fact that Steel Authority of India Limited (SAIL) did not award any quantity to MMTC despite MMTC emerging as lower bidder in the tender, the quantity, earmarked for servicing of SAIL's tender, remained unsold for a long period.

---

[4] ***Cost, insurance and freight (CIF) is a trade term requiring the seller to arrange by bearing the expenditure for the carriage of goods by sea to a port of destination for the buyer***

The holding of inventory at Vizag was not planned at the time of import. MMTC was compelled to store the goods due to failure on the part of SAIL to award the quantity to MMTC and due to falling market prices. As such no risk analysis could be done before storage of the cargo.

The Ministry endorsed (December 2017) the reply of MMTC submitted (October 2017) to Audit.

The reply of the Ministry / Management was not acceptable because as per the in-principle approval granted by FMCoD for the above import, the Management was required to enter into Memorandum of Understanding (MoU) with the buyers prior to placement of indent on the foreign supplier of Manganese Ore viz. M/s UMK. However, the Management did not adhere to the above directions of FMCoD. Resultantly, substantial portion of Manganese Ore, released at Vizag Port, remained un-sold for 14 months, as there were no committed buyers. Further, the Management's dependence on the tender floated by SAIL in February 2014 for a quantity of 20,000 MT of Manganese Ore, without having any firm commitment from SAIL, cannot be considered as prudent.

Thus, due to non-adherence to the directions of Functional Management Committee of Directors to enter into Memorandum of Understanding with the committed buyers, prior to placement of indent on the foreign supplier of Manganese Ore, MMTC sustained loss of ₹6.60 crore. Further, omission to fix any 'stop-loss' norms resulted in delay of 14 months in disposal of Manganese Ore.

PEC Limited

4.2 Ineffective monitoring of contract resulting in non-recovery of dues

PEC sustained blockade of funds of ₹11.21 crore apart from interest of ₹7.29 crore thereon till 10 November, 2017 due to inefficient monitoring of the material stored in warehouse, inefficient and ineffective decision making in attaching the pledged goods and delayed action for encashment of post-dated cheques, on the part of the Management.

M/s Oshiya Industries Private Limited, Mumbai (OIPL), formerly known as M/s Kuber Steel Industries Private Limited, requested (August 2010) PEC Limited (PEC) for financing the purchase of Hot Rolled Steel Coils of various sizes from market to fulfil their obligation under supply contracts with different buyers of the steel products. Accordingly, PEC financed a number of procurement proposals of OIPL over the period 2010-11 to 2012-13. During the period 01 January 2014 to 7 March 2014, PEC entered into eight Associateship agreements with OIPL for procurement of 2882.992 MTs of Hot Rolled Steel Coils/sheets from different domestic suppliers on behalf of OIPL. The total procurement price in the above eight agreements was ₹12.50 crore. As per identical terms and conditions contained in all of the agreements, OIPL was required to pay to PEC in advance, an amount equivalent to 15 *per cent* of the value of Letter of Credit (LC) as earnest money in cash which was to be adjusted upon the delivery of last consignment. In case of increase in price of the contracted cargo after opening of LC by PEC, OIPL was required to pay additional advance for the price difference. OIPL was also required to give post-dated cheques towards 90 *per cent* of the total value of the consignment. On receipt of indent and the advance as stated above from OIPL, PEC was required to establish a LC for a maximum usance period of 120 days, in favour of the supplier. Further, OIPL was required to pay 1.5 *per cent* of the total value of the LC as PEC’s net trading margin, after making statutory deductions, if any. The material was required to be stored at a private warehouse, under the control and custody of the Central Warehousing Corporation of India (CWC) for which a Storage Agreement dated 8 November 2013 was entered into amongst PEC, CWC, OIPL and M/s Jeet Steel Industries Private Limited (JSIPL), where from PEC was to sell the entire quantity to OIPL. PEC was required to raise invoice on OIPL by loading 1.5 *per cent* trading margin on purchase value immediately. OIPL was required to pledge the material in favour of PEC (by signing an Agreement of Pledge), with the first charge of PEC over the material. On the request of OIPL the specified quantity of the material was to be de-pledged on receipt of full payment by PEC against such requested quantity. In case OIPL failed to pay the entire cost of the consignment as per the predetermined schedule, PEC was at liberty to sell the material to any other party at the risk and cost of OIPL and any loss, if any, to PEC, after the adjustment of margin money, OIPL was required to make good such loss suffered by PEC. Further, as per Clause 13 of the eight agreements, in case PEC remained out of pocket or PEC's funds were Blocked, OIPL was required to pay interest at the rate of 14.50 *per cent* per annum up to 180 days on monthly rest basis and 15.50 *per cent* per annum from 181 days to 365 days on monthly rest basis and for above 365 days as decided by PEC.

In order to procure aggregate quantity of 2882.992 MT of the material from various suppliers as per the above mentioned eight agreements, PEC opened eight LCs between 2 January 2014 and 13 March 2014, on behalf of OIPL, for a total amount of ₹12.50 crore. The material delivered by the suppliers was stored in the plant premises of JSIPL and pledged in favour of PEC.

As per the terms of the above agreements, OIPL was liable to pay an amount aggregating to ₹11.21 crore (after adjusting ₹1.88 crore i.e. 15 *per cent* of LC value received by PEC as advance, amount of trade margin of ₹0.19 crore i.e. 1.5 *per cent* of total value of invoice and bank charges, legal expenses etc.) to PEC on or before the LC due dates falling between 3 May 2014 to 12 July 2014. OIPL did not lift the stock, therefore, PEC had to release, out of its own funds, payment of ₹12.50 crore on LC due dates to various suppliers.

PEC carried out physical verification of the pledged stock on 7 July 2014 and identified total 125 Hot Rolled Steel Coils of 2882.343 MT, as mentioned in the stock certificate dated 1 July 2014 issued by CWC. Subsequent physical verification carried out by PEC on 29 October 2014, revealed that out of 125 coils, only 65 coils were found identifiable. The physical verification team of PEC advised CWC to keep coils at one place, use permanent marker /paint on coils for proper demarking of pledged stock etc. CWC sent (29 October 2014) a notice for exit from the storage agreement and asked PEC to take over the entire stock from the warehouse on or before 30 November 2014. In the meantime, the post-dated cheques given by OIPL (of value ₹11.50 crore) bounced when presented (October and November 2014) by PEC to bank. PEC filed (28 November 2014) a complaint regarding missing goods, with the police based on which an inspection conducted (8 January 2015) by the police also revealed non-existence of the stock. PEC lodged (21 January 2015) an FIR in this regard against OIPL, CWC and warehouse owner viz.

JSIPL. In the meantime, CWC gave a final notice (3 January 2015) to PEC conveying inability to take any further responsibility of the stock. PEC also filed criminal cases against OIPL under section 138 of the Negotiable Instrument Act for dishonour of post-dated cheques. As intimated (January 2017) by the Mumbai Branch Office of PEC to its Corporate Office, the case has been transferred to Economic Offence Wing.

Thus, PEC had to recover from OIPL an amount of ₹11.21 crore towards principal and ₹7.29 crore towards interest thereon (till 10 November 2017).

Audit observed:

(i) Due to non-receipt of payment from OIPL, the PEC had to release payment to suppliers out of its own funds, against the LCs which became due between 3 May 2014 and 12 July 2014. However, post-dated cheques worth ₹11.50 crore, available as security, were deposited by PEC in the bank in October and November 2014, which bounced later on. Thus, there was undue delay, on the part of PEC, in encashment of the post-dated cheques.

(ii) The last consignment of material was received on 13 March 2014, however, PEC conducted physical verification only in July 2014. Mismanagement in the storage of the material in the premises of JSIPL had come to the notice of PEC on 7 July 2014 as the material was not found stacked at one place. Subsequent physical verification carried out by PEC on 29 October 2014 revealed that out of 125 no. of coils available as per the stock certificate issued by CWC, more than 60 coils did not bear the internal coding of CWC marked thereon and also appeared quite new in comparison to coils marked with coding. Despite being aware of the above situation PEC did not take possession of the material and initiate action for liquidation of the same at the risk and cost of OIPL. PEC took the decision to invoke the deed of pledge and attach the goods only on 13 November 2014. This indicated inefficient and ineffective managerial control by PEC over the storage conditions of the material and on the verification of the authenticity of the weekly stock reports furnished by CWC.

(iii) PEC did not insist on inclusion of a penal clause in the Storage Agreement to hold CWC responsible for CWC's failure, if any, in safeguarding the pledged stock.

(iv) As per terms of Storage Agreement (November 2013) OIPL was required to arrange insurance for the material covering all the risks like theft, floods, fire, strike, riot, pilferage, etc. for 110 *per cent* of the value of the material stored in the warehouse at their own cost, showing PEC as the beneficiary. Agreement further provided that OIPL would be responsible for lodging and realisation of claims, if any, arising out of these insurance policies in time and in case, due to any reason, payment of insurance claim is not made by insurance company to OIPL, OIPL would be liable to make the payment to PEC without taking the plea of pendency of claim with the insurance company.

PEC failed to ensure compliance of terms of the agreement by OIPL, as contrary to the above provisions of the agreement, OIPL took standard fire, special perils and Burglary insurance policy which was renewed up to 22 December, 2015. PEC also did not foresee the risk of misappropriation of stock by OIPL itself, resultantly; PEC was unable to lodge the insurance claim in the matter.

The Management in its reply (January 2018), stated that:

1. PEC has been dealing with the Associate for 3-4 years and the track record of the Associate was satisfactory. In July 2014, OIPL had assured PEC to make part payment within July 2014 and balance to be completed in August 2014. When OIPL failed to honour the commitment, fresh cheques were obtained in September 2014 and presented to the bank. PEC further stated that after bouncing of the cheques PEC had filed cases, under section 138 of the Negotiable Instrument Act, against the Associate.

2. On getting the weekly reports that the coils were stored in a scattered manner and getting the letter from CWC that "the stocks were lying in haphazard manner mixed with other party and uncountable", PEC wrote letters to CWC asking for their explanations. PEC also wrote letter to CWC regarding the discrepancies found in physical verification of the material carried out in September 2014. PEC further stated that CWC being the custodian of PEC's material and a Public Sector Undertaking of Government of India, it was felt necessary to get the version of CWC regarding the discrepancies found, before taking any action. But CWC did not respond to any correspondence of PEC.

3. The Storage Agreement was vetted by Finance Division and Legal Division of PEC.

4. The terms related to insurance of the material as per the agreement with OIPL were duly complied with.

The Ministry endorsed (January 2018) the reply of the Management of PEC.

The reply of the Management was not tenable as past satisfactory track record of the Associate cannot justify undue delay, on the part of PEC, in encashment of the post-dated cheques. Reply was silent on the issue raised by Audit that PEC did not take possession of the material and initiate prompt action for liquidation of the same at the risk and cost of OIPL, despite being aware of the poor storage conditions at CWC warehouse. Prompt action was needed to be taken by PEC to protect its financial interests. However, PEC decided to invoke the deed of pledge and attach the goods only on 13 November 2014**.** Further, while agreeing to a condition in the agreement that OIPL would be responsible for lodging and realisation of claims, if any, PEC did not foresee the risk of misappropriation of stock by OIPL itself. Resultantly, PEC was unable to lodge the insurance claim in the matter.

Thus, due to inefficient monitoring of the material stored in warehouse, inefficient and ineffective decision making on attaching the pledged goods and delayed action for encashment of post-dated cheques, on the part of the Management, funds to the extent of ₹11.21 crore apart from interest of ₹7.29 crore thereon (till 10 November 2017) remained blocked and chances of its realisation from OIPL were remote.