CHAPTER VII

GOVERNMENT COMMERCIAL AND TRADING ACTIVITIES

GOVERNMENT COMMERCIAL AND TRADING ACTIVITIES

7.1 Introduction

This chapter deals with Government companies. Paragraphs 7.2 to 7.12 give an overview of the Government companies and the Government's investment in the Public Sector Undertakings. Paragraph 7.13 contains a review on the Operational performance of Pondicherry Textile Corporation Limited.

7.2 Overview of Government companies

As on 31 March 2006, there were 12 Government companies including one subsidiary company (all working) under the control of the Government of the Union Territory of Puducherry as against 11 (all working) Government companies as on 31 March 2005. During the year, Pondicherry Tourism and Transport Development Corporation Limited was bifurcated into two separate Government companies, *viz*., Pondicherry Road Transport Corporation Limited and Pondicherry Tourism Development Corporation Limited. The accounts of the Government companies (as defined in Section 617 of the Companies Act, 1956) are audited by the Statutory Auditors, who are appointed by the Comptroller and Auditor General of India (CAG) as per provisions of Section 619 (2) of the Companies Act, 1956. These accounts are also subject to supplementary audit conducted by the CAG as per provisions of Section 619 (4) of the Companies Act, 1956.

7.3 Working Public Sector Undertakings (PSUs)

Investment in working PSUs

Total investment in Government companies in the form of equity and loans as on 31 March 2005 and 31 March 2006 was as under:

(Rupees in crore)

Year	Number of companies	Investment			Total
		Equity	Share application money	Long term loans[1]	
2004-05	11	449.72	2.00	3.79	455.51
2005-06	12	471.55	2.10	6.81	480.46[2]

1 Long term loans are excluding interest accrued and due on such loans

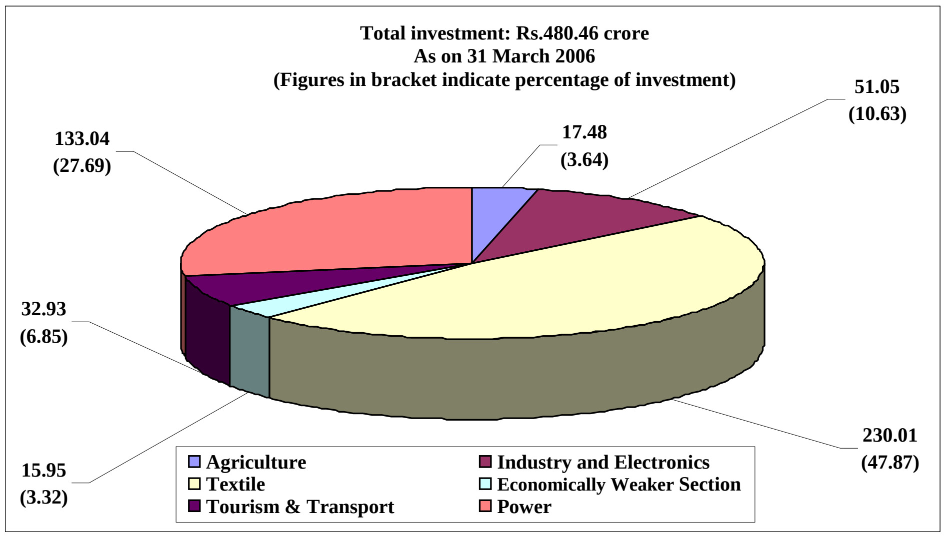
2 UT Government's investment in working PSUs was Rs 463.28 crore (others: Rs 17.18 crore). The figure as per Finance Accounts is Rs 475.30 crore and the difference is under reconciliation

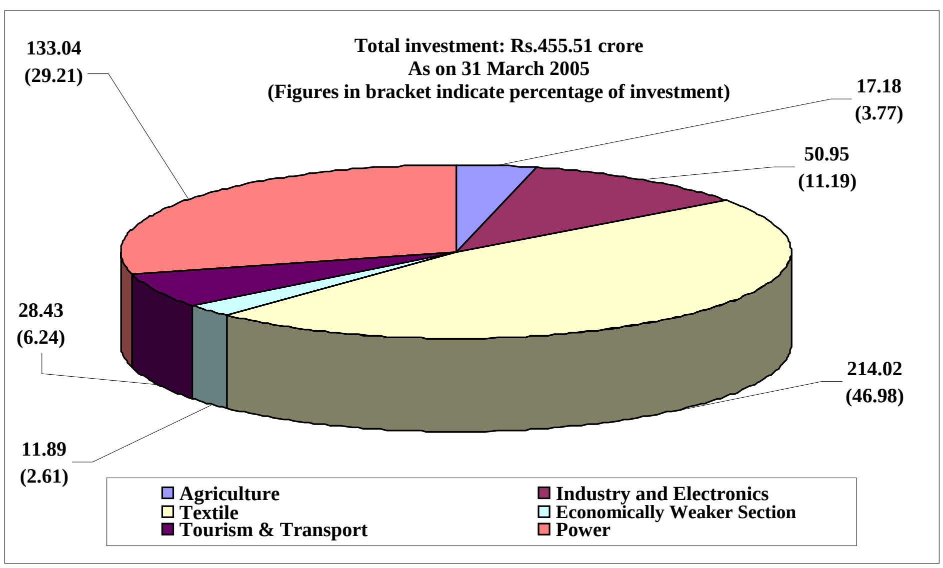
As on 31 March 2006, the total investment in the working Government companies comprised of 98.58 *per cent* equity capital and 1.42 *per cent* loans as compared to 99.17 *per cent* and 0.83 *per cent*, respectively as on 31 March 2005.

The summarised statement of Government investment in the working Government companies in the form of equity and loans is given in **Appendix XXIV.**

The investments (equity and long-term loans) in various sectors at the end of 31 March 2006 and 31 March 2005 are indicated below in the pie charts:

SECTOR-WISE INVESTMENT IN WORKING GOVERNMENT COMPANIES





7.4 Budgetary outgo, grants/subsidies, guarantees, waiver of dues and conversion of loans into equity

The details of budgetary outgo, grants/subsidies, guarantees issued, waiver of dues and conversion of loans into equity by the Government to the working Government companies are given in **Appendices XXIV and XXVI.**

The budgetary outgo (in the form of equity capital and loans) and grants/subsidies from the Union Territory Government to the working Government companies for the three years up to 2005-06 are given below:

(Rupees in crore)

Particulars	2003-04		2004-05		2005-06	
	Number	Amount	Number	Amount	Number	Amount
Equity capital outgo from budget	8	22.92	8	22.04	8	21.93
Grants	6	7.61	6	6.64	5	21.20
Subsidy towards Projects/ Programmes/Schemes	1	0.20	1	0.40	2	1.13
Total outgo	8[3]	30.73	8[3]	29.08	8[3]	44.26

At the end of 2005-06, guarantees of Rs 2.70 crore against one working Government company were outstanding.

7.5 Finalisation of accounts by working PSUs

The accounts of the Government Companies for every financial year are required to be finalised within six months from the end of the financial year under Sections 166, 210, 230, 619 and 619-B of the Companies Act, 1956 read with Section 19 of the Comptroller and Auditor General's (Duties, Power and Conditions of Service) Act, 1971. The accounts are to be laid before the Legislature within nine months from the end of the financial year.

Out of 12 working Government companies, only three companies finalised their accounts for the year 2005-06 within the stipulated period as can be seen from **Appendix XXV**. During the period from October 2005 to September 2006, four working Government companies finalised four accounts for previous years.

The accounts of nine working Government companies were in arrears for periods ranging from one to two years as on 30 September 2006 as detailed below:

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[3] These are the actual number of companies which received budgetary support in the form of equity, grants and subsidy from the Government during the respective years

Serial number	Number of working companies	Period for which accounts are in arrears	Number of years for which accounts are in arrears	Reference to Sl. No. of Appendix XXV
1.	4	2004-05 & 2005-06	2	2, 7, 8 and 11
2.	5	2005-06	1	1, 4, 5, 6 and 10

The administrative departments have to monitor and ensure that the accounts are finalised and adopted by the PSUs within the prescribed period. Though the concerned administrative departments were informed every quarter by Audit of the arrears in finalisation of accounts, no remedial measures had been taken, as a result of which the net worth of these PSUs could not be assessed in audit.

7.6 Financial position and working results of working PSUs

The summarised financial results of working Government PSUs as per the latest finalised accounts are given in **Appendix XXV.**

According to the latest finalised accounts of 12 working Government companies, three companies incurred an aggregate loss of Rs 19.79 crore and six companies earned an aggregate profit of Rs 14.23 crore. Details of profit and loss, as per their latest finalised accounts, are given below:

Year of latest accounts finalised	Profit earning companies		Loss making companies	
	Number of companies	Amount of profit (Rupees in crore)	No. of companies	Amount of loss (Rupees in crore)
2003-04	1	0.40	2	1.84
2004-05	3	2.55	1	17.95
2005-06	2	11.28	--	--
Total	**6**	**14.23**	**3**	**19.79**

In respect of two companies (serial numbers 8 and 9 of **Appendix XXV**), the entire loss was met by the Government of the Union Territory of Puducherry and one company (Pondicherry Tourism Development Corporation Limited) has not finalised its first accounts.

7.7 Profit earning companies and dividend

Out of the three Government companies which finalised their accounts for 2005-06, two companies (serial numbers 3 and 12 of **Appendix XXV**) earned an aggregate profit of Rs 11.28 crore and declared an aggregate dividend of Rs 1.16 crore for 2005-06. The dividend as a percentage of share capital in these companies worked out to 0.82. The total return to the Government by way of dividend of Rs 1.16 crore worked out to 0.25 *per cent* on the total equity investment of Rs 463.28 crore by the Union Territory Government in all the 12 Government companies as against the dividend of Rs 1.67 crore (0.38 *per cent*) in the previous year. The Government has not framed any policy for payment of minimum dividend.

7.8 Loss incurring Government companies

Out of the three loss incurring Government companies, two companies (serial numbers 6 and 7 of **Appendix XXV**) had accumulated losses of Rs 225.41 crore which exceeded their paid up capital of Rs 216.50 crore. Despite poor performance and complete erosion of paid-up capital, the Government continued to provide financial support to these companies in the form of equity, grant and subsidy, etc. As per available information, the total financial support provided by the UT Government to these companies during 2005-06 amounted to Rs 33 crore (equity:Rs 16.42 crore; grant and subsidy:Rs 16.58 crore).

7.9 Return on capital employed

As per the latest finalised annual accounts of PSUs, the capital employed[4] worked out to Rs 392.93 crore in 11 companies and total return[5] thereon amounted to (-) Rs 1.85 crore, as compared to capital employed of Rs 381.76 crore and total return of (-)Rs 2.96 crore in the previous year. The details of capital employed and the total return on capital employed of working Government companies are given in **Appendix XXV.**

4 Capital employed represents net fixed assets (including capital works-in-progress) PLUS working capital except in finance companies and corporations where it represents a mean of aggregate of opening and closing balances of paid-up capital, free reserves, bonds, deposits and borrowings (including refinance).

5 For calculating total return on capital employed, interest on borrowed funds is added to net profit/subtracted from the loss as disclosed in the profit and loss account.

7.10 Disinvestment, privatisation and restructuring of Public Sector Undertakings

During the year, Pondicherry Tourism and Transport Development Corporation Limited (PTTDC) was bifurcated into two separate companies. While the tourism activities of the PTTDC were taken over by Pondicherry Tourism Development Corporation (incorporated on 1 April 2005), the PTTDC was renamed (12 April 2005) as Pondicherry Road Transport Corporation Limited.

7.11 Internal audit/internal control

The Statutory Auditors (Chartered Accountants) are required to furnish a detailed report upon various aspects including the internal control/internal audit systems in the companies audited in accordance with the directions issued by the Comptroller and Auditor General of India to them under Section 619 (3) (a) of the Companies Act, 1956 and to identify areas, which needed improvement. Directions under the Act, *ibid*, were issued to the Statutory Auditors in respect of seven Government companies between October 2005 and September 2006 and reports in respect of three Government companies were received (September 2006).

Statutory Auditors of Pondicherry Textile Corporation Limited have pointed out the need for improvement in the internal audit system.

7.12 Response to inspection reports, draft paragraphs and reviews

Audit observations noticed during audit and not settled on the spot are communicated to the heads of PSUs and concerned departments of the Government through inspection reports. The heads of PSUs are required to furnish replies to the inspection reports through respective heads of departments within a period of six weeks. Inspection reports issued up to March 2006 pertaining to 10 PSUs disclosed that 89 paragraphs relating to 24 inspection reports remained outstanding at the end of September 2006. Department-wise break-up of inspection reports and audit observations outstanding as on 30 September 2006 is given in **Appendix XXVII.**

It is recommended that (a) the Government should ensure that procedure exists for action against the officials who failed to send replies to inspection reports/reviews as per the prescribed time schedule, (b) action to recover loss/outstanding advances/overpayment is taken within the prescribed time, and (c) the system of responding to audit observations is revamped.

INDUSTRIES DEPARTMENT

7.13 Operational Performance of Pondicherry Textile Corporation Limited

Highlights

- The Government of Union Territory of Puducherry took over the Mill as sick unit in December 1985. The Company, which was earning marginal profits up to 1992-93, started incurring losses from 1993-94. The accumulated losses of the Company rose from Rs 159.64 crore in 2001-02 to Rs 250.44 crore as at the end of 2005-06 which wiped out its entire paid-up capital of Rs 230.04 crore.

(Paragraphs 7.13.1 to 7.13.6)

- Failure to achieve the installed capacity and norms for efficiency resulted in production loss of yarn and led to extra expenditure of Rs 10.06 crore on the procurement of yarn from outside sources at higher rates during the five years ended 31 March 2006.

(Paragraph 7.13.8)

- Additional time taken for production of yarn as compared to the norms had resulted in excess consumption of power valued at Rs 5.24 crore. The Company did not have any system to measure production / consumption of steam. Excess consumption of heat *vis-à-vis* the norms resulted in excess consumption of heat valued at Rs 2.05 crore.

(Paragraphs 7.13.9, 7.13.13 and 7.13.14)

- Low capacity utilisation and failure to achieve norms for efficiency in cloth output resulted in production loss of 858.86 lakh metres of cloth during the five years ended 31 March 2006.

(Paragraph 7.13.10)

- Improper production planning resulted in extra expenditure of Rs 17.84 crore.

(Paragraph 7.13.11)

- Out of Rs 28.11 crore received for the modernisation programme, the Company spent Rs 10.99 crore only on modernisation and utilised the remaining amount of Rs 17.12 crore to meet its working capital requirements. As the modernisation programme has not been completed, the amount of Rs 10.99 crore spent has not yielded the desired results and the objectives of modernisation remain unfulfilled.

(Paragraph 7.13.15)

- Failure to contain labour cost within the prescribed norms resulted in extra expenditure of Rs 128.60 crore.

(Paragraph 7.13.16)

- Sale of cloth below variable cost of production resulted in cash loss of Rs 6.90 crore.

(Paragraph 7.13.20)

7.13.1 Introduction

A private textile mill in Puducherry in the name of Rodier Mill was started as a joint stock Company in 1898. It was renamed and registered as Anglo French Textiles Limited in 1951. The Company became sick in early 1980s and remained closed from July 1983. The Government of the Union Territory of Puducherry took over the mill in December 1985 by an Act (Acquisition and Transfer of Textile Undertaking Act, 1986) and assets were transferred to a new Company called Pondicherry Textile Corporation Limited and this Company was registered in December 1985 under the Companies Act, 1956. The Company earned marginal profits up to 1992-93 and thereafter it started incurring losses. The accumulated losses upto the end of 2005-06 were Rs 250.44 crore, which wiped out its entire paid-up capital of Rs 230.04 crore.

The textile mill of the Company is a composite one having spinning, weaving and processing units. There are three production units *viz*., A, B and C. In units 'A' and 'C', both spinning and weaving operations are carried out while in unit 'B' only weaving is carried out. Unit 'A' has a processing house which besides processing in-house cloth also processes cloth from other mills. Besides, the Company has a garment manufacturing unit to convert part of the cloth produced into value added items such as bed sheets, pillow covers, school uniforms etc.

The activities of the Company were last reviewed and reported upon in Paragraph No.7.5 of the Report of the Comptroller and Auditor General of India, Government of Union Territory of Puducherry for the year ended 31 March 1999. The Public Accounts Committee (PAC) discussed the Report (November 2002) and its recommendations are contained in its 23rd Report tabled in the Legislature of the Union Territory Assembly in March 2004. No action has been taken by the Government/Company on some of the recommendations of the PAC as pointed out in paragraphs 7.13.8 and 7.13.16.

7.13.2 Scope of Audit

The present performance audit conducted during January to May 2006 by reviewing the records of all the units and the Head Office of the Company, covers the operational performance of the Company during the five year period from 2001-02 to 2005-06.

7.13.3 Audit objectives

The review was conducted with a view to ascertain whether:

- the Company achieved the norms prescribed for capacity utilisation in spinning, weaving and other operations;
- the labour cost was kept within the industry norms;
- the Company improved its domestic and export sales performance; and
- the Company implemented the modernisation programme as per schedule.

7.13.4 Audit criteria

The criteria considered for assessing the performance of the Company were as follows:

- Norms prescribed by Ahmedabad Textile Industry Research Association (ATIRA) and South India Textile Research Association (SITRA).
- Norms fixed by the Company for capacity utilisation, consumption of raw material and cloth output.
- Policy of the Company on product-mix, sales and marketing and
- Objectives of the modernisation programme.

7.13.5 Audit methodology

The audit methodology adopted for attaining the audit objectives with reference to audit criteria were examination of:

- agenda and minutes of meetings of the Board of Directors;
- records relating to fixation of installed capacity and utilisation thereagainst;
- records relating to actual production, wastage, usage of raw material with reference to the prescribed norms;
- records relating to consumption of steam and power with reference to the prescribed norms;
- costing records and cost audit reports, records relating to modernisation and records relating to sale of clothes; and

- interaction with the management.

Audit findings

Audit findings, emerging as a result of test check were reported to the Government/Company in August 2006 and were also discussed in the meeting of the Audit Review Committee on Public Sector Enterprises held on 10 November 2006. The Managing Director of the Company along with a team of officials attended the meeting. The views expressed by the Management and reply given by the Government in October 2006 have been taken into consideration while finalising the report.

Audit findings are discussed in the succeeding paragraphs.

7.13.6 Financial position and working results

The Company has incurred losses in all the five years from 2001-02 to 2005-06. The main reasons for the losses were increase in cost of raw material and higher expenditure on labour and power and old machineries.

The accumulated losses of the Company rose by Rs 90.80 crore from Rs 159.64 crore in 2001-02 to Rs 250.44 crore as at the end of 2005-06. The Union Territory Government inducted additional capital of Rs 88.41 crore during the period from 2001-02 to 2005-06, which were mainly utilised for meeting the working capital requirements of the Company.

7.13.7 Production performance

The major activities involved in the production of cloth are spinning, weaving and processing. The performance of the Company in these activities is discussed below:

7.13.8 Spinning

Failure to achieve spinning capacity in full resulted in purchase of yarn from outside at an extra expenditure of Rs 13.19 crore.

The Company has spinning facilities in its ‘A’ and ‘C’ units. The Company had fixed a norm of 95 *per cent* for capacity utilisation and a norm of 88.8 grams of yarn production per spindle per shift of eight hours The details of installed capacity, capacity utilisation and actual production of yarn during the five years ended 31 March 2006 are given in **Appendix XXVIII.** It would be observed that the capacity utilisation in spinning was low and ranged between 52 to 60 *per cent* during the period. The performance of yarn production (efficiency) was worse as it was below 50 *per cent* in all the five years (except in unit ‘C’ in 2005-06). It is pertinent to mention that the PAC had recommended (March 2004) that efforts should be made to achieve the norms fixed for capacity utilisation. Audit analysis, however, revealed that the Company had not taken effective steps to achieve maximum capacity utilisation and yarn production in both the spinning units.

Due to low utilisation, the Company had to purchase yarn from outside to meet the cloth production requirement. As the procurement cost of yarn from outside was higher compared to the in-house cost of production, the Company could have avoided cash outflow of Rs 13.19 crore during the period by utilising its own capacity.

The Government stated (October 2006) that the capacity utilisation and efficiency could not be achieved due to roof collapse in Unit 'A', decline in labour strength year after year and reduction in spindle capacity in unit 'A'. The Government further stated that the management had taken steps to improve capacity utilisation by employing gate badlies[6].

The reply is not acceptable as the achievable capacity has been worked out with reference to the number of available spindles only while working out the low capacity utilisation. Further, the spindles under the collapsed roof had been disposed off prior to 2001-02 and the labour strength in unit 'C' remained constant and whereas in unit 'A', the reduction in labour strength was commensurate with the reduction in the number of spindles over the years.

On purchase of yarn from outside sources, the Government stated (October 2006) that the procurement cost of yarn from outside source is always less than in-house yarn production cost. The Government further stated that the mismatch between in-house yarn production and weaving requirement was met through outside purchase and that the absence of Autokoner (automatic winding and knotting machine), which is capable of producing high quality yarn, also contributed to outside purchase of yarn.

The reply is not tenable as (i) the comparison of cost should be between the variable cost of in-house production of yarn and the total procurement cost of outside yarn instead of comparing only variable costs. On this basis, the procurement of outside yarn was costlier by Rs 10.06 crore. (ii) The mismatch between the yarn requirement and in-house yarn production was only due to failure of the Company to achieve the yarn production capacity in full. (iii) The procurement of Autokoner was included in the Comprehensive Modernisation Programme (CMP) but the Company failed to purchase the same in time (discussed in Paragraph 7.13.15).

7.13.9 Excess consumption of power

Consumption of excess operative hours in yarn production led to excess consumption of power valued at Rs 5.24 crore.

The Company had fixed norms for operative hours for production of 100 kgs of yarn (adjusted to 40s count) at 30 hours. Audit analysis revealed that the actual operative hours for production of 100 kgs of yarn (adjusted to 40s count) during the five years 2001-02 to 2005-06 were higher than the norm and ranged from 52.83 to 72.26 hours in unit 'A' and from 45.91 to 50.12 hours in unit 'C', which indicated that the Company operated the spindles for additional hours without additional productivity. The additional time

[6] 'Gate badlies' are the daily wage workers being employed by the Company

taken for production of yarn compared to the norm resulted in excess consumption of power to the extent of Rs 3.56 crore in unit 'A' and Rs 1.68 crore in unit 'C' during this period (details in **Appendix XXIX**). The Government stated (October 2006) that the Company could not achieve the optimum level of production of yarn due to (i) roof collapse in unit 'A' (ii) shortage of labour and absenteeism and (iii) shortage of raw materials in 2001-02 and 2002-03. The Government further stated that the management is taking steps to increase the utilisation. The reply is not acceptable as the Company introduced VRS only to reduce the excess labour force. Labour absenteeism is a controllable factor and the shortage of raw material cannot be cited as a reason for non-achievement of per hour yarn production. The excess operative hours were primarily due to old machineries.

7.13.10 Weaving

The details of installed capacity of cloth production computed with reference to the norms fixed by Ahmedabad Textile Industry's Research Association (ATIRA) in 1997 and the actual production during the five years ended 31 March 2006 are given below:

Year	**Achievable cloth production as per norms**	**Actual cloth production**	**Production loss**	**Percentage of achievement**
	(In lakh metre)			
2001-02	335.71	139.61	196.10	41.59
2002-03	326.86	149.52	177.34	45.74
2003-04	320.69	145.80	174.89	45.46
2004-05	308.52	159.03	149.49	51.55
2005-06	295.86	134.82	161.04	45.57
TOTAL			**858.86**	

From the above table, it may be observed that the percentage of achievement was less than 50 during the three years ended 31 March 2004 and in 2005-06. It improved marginally to 51.55 *per cent* in 2004-05. The production loss during the last five years aggregated to 858.86 lakh metre.

The Government stated (October 2006) that production loss in weaving was due to high labour shortage and absenteeism. The Government further stated that higher work load and efficiency could be thought off only after a tripartite wage settlement. The reply is not acceptable as the Company has sufficient labour force in units 'A' and 'C' (as discussed in Paragraph 7.13.8 *supra*). In respect of unit 'B' also, there was no reduction in the staff strength over the years. Further, considering the huge cash losses that the Company suffered year after year, it should have aimed at higher workload and efficiency.

7.13.11 Improper production planning

Continued production of cloth in units 'A' and 'B' resulted in avoidable extra expenditure of Rs 17.84 crore

Audit analysis of the cost of production of 17 sorts (varieties of cloth) produced in units 'A', 'B' and 'C', revealed that the cost was lowest in unit 'C' and highest in unit 'A'. In such a situation, the Company should have taken effective steps to ensure that the available capacity in units 'B' and 'C' was utilised in full so as to keep the cost of production at the minimum possible level. This, however, was not ensured by the Company as it continued to produce major portion of some varieties of cloth in units 'A' and 'B' where the cost of production was higher as compared to that in unit 'C'. Failure to utilise the achievable capacity of unit 'C' as per standard loom efficiency norms as fixed by ATIRA, the Company incurred extra expenditure of Rs 17.84 crore during the period of review **(Appendix XXX)**.

While confirming that the working of unit 'A' looms was uneconomical, the Government stated (March 2006) that due to non co-operation of workers to work in other units, the production in unit 'A' had to be continued. The reply lacked justification as the Company should have motivated, educated and trained the employees to ensure their co-operation in bringing down the cost of production and attaining maximum efficiency.

7.13.12 Processing unit

The Company has processing facilities in its unit 'A' to process grey cloth produced in all the three weaving units. The grey cloth is processed, *viz*., bleached, mercerised, dyed and printed, before it is given final finishing in the stentering and calendaring machines. The Company also offers processing facilities to outside grey cloth producers on job work basis. The details of cloth processed, available machine hours and machine hours actually utilised are given below:

Year	Available machine hours	Machine hours utilised	Percentage of utilisation	Cloth processed		Revenue earned on processing of outside cloth
				In-house	Outside cloth	
	(lakh hours)			(lakh metres)		(Rupees in crore)
2001-02	4.43	1.79	40.35	104.67	20.49	4.67
2002-03	4.35	1.87	42.86	104.00	25.10	5.95
2003-04	4.47	1.94	43.26	116.64	23.45	5.45
2004-05	4.19	1.87	44.64	128.65	17.30	3.81
2005-06	3.81	1.57	41.21	140.61	2.60	0.44

It would be evident from the above details that the capacity utilisation in the processing unit ranged between 40.35 to 44.64 *per cent* during the last five years. Audit scrutiny revealed that the machines remained idle for want of work. In spite of this gross under utilisation, the Company installed one new stenter machine in August 2005 at a cost of Rs 1.16 crore and one calendaring machine in June 2005 at a cost of Rs 53.34 lakh. These new machines had not yet (October 2006) been put to effective use. Thus, the installation of one stenter machine and a calendaring machine at a total cost of Rs 1.69 crore lacked justification.

The Government stated (October 2006) that in the Comprehensive Modernisation Programme (CMP), wider width shuttle looms were included for processing wider width cloth. The reply is not tenable as the CMP was yet to be completed and these machines remained grossly under utilised.

7.13.13 Improper accounting of steam consumption

The Company has five boilers, each one with a capacity to produce five MT of steam per hour. Four boilers use coal as the fuel and the fifth one uses furnace oil as fuel for generation of steam which is used in the sizing and processing departments.

For the generation of steam, coal and other fuels like furnace oil, fire wood, coconut shells, *etc*., are used. A part of the heat generated from coal is utilised in steam production and the balance heat is used in the processing unit. The Company did not have any system to measure production/consumption of steam. As the Company is spending around Rs 3 crore every year on the purchase of coal and other fuels for generation of steam, a suitable system needs to be developed to monitor the production/consumption of steam.

While accepting that the Company did not have proper instruments to assess the quantum of steam produced/consumed, the Government stated (October 2006) that the Company was in the process of installing instruments, namely, steam flow meter at the boiler point and other utility points for measuring the steam flow from boilers to various utility points and also had taken steps to properly account for the generation and consumption of steam.

7.13.14 Excess consumption of heat

During the processing of cloth, activities such as finishing, printing and polymerising require heat. The Company uses two coal fired and one furnace oil fired thermic fluid heaters to generate heat required for the above activities.

A review of the heat consumed in the above mentioned activities during the five years ended 31 March 2006 revealed that there was excess consumption of heat *vis-a-vis* the norms in all the five years and the value of this excess consumption aggregated to Rs 2.05 crore (details in **Appendix XXXI**).

The Government stated (October 2006) that the Company was taking steps to reduce the excess heat consumption.

7.13.15 Comprehensive Modernisation Programme

The Company prepared and submitted (March 2000) to the Government a proposal for limited modernisation in the spinning and processing departments at a cost of Rs 6 crore in order to compete and survive in he market. The Government did not approve this and directed (June 2000) the Company to take up a time bound CMP and started releasing funds from September 2000. The Company prepared (March 2001) a CMP consisting of upgradation of the infrastructure for manufacturing quality and higher value added products at a total cost of Rs 104 crore in consultation with the Director of National Textile Corporation Limited (a Central PSU). The Board of Directors approved the programme in March 2001 and the Government accorded approval for the modernisation programme in November 2001. The modernisation programme was to be completed in three and half years from November 2001 and was proposed to be implemented in four phases as indicated below:

Phase	Details	Cost (Rupees in crore)	Additional revenue envisaged per annum (Rupees in crore)
I Phase	Spinning + Processing machines (Stage – I)	5.05	1.76
	Spinning machines (Stage – II)	6.65	2.54
II Phase	Building, spinning and weaving preparatory machines	32.91	12.38
III Phase	Weaving preparatory, weaving processing, engineering and quality assurance lab	31.60	33.01
IV Phase	Spinning, weaving, processing and engineering	27.79	40.79
TOTAL		**104.00**	**90.48**

A review of the implementation of the CMP revealed the following deficiencies:

- The Company implemented the CMP on piecemeal basis. The scheduled date of completion was over by May 2005, but none of the phases envisaged in the modernisation programme had been completed till date (March 2006). At present, the Company does not have any plan to continue with the implementation of CMP or to foreclose it.

- Since surplus spinning capacity was available in South India, a Textile Expert suggested (March 2001) that the Company should first go in for modernisation of weaving process before taking up modernisation of spinning operations. Further, without modernising weaving operations, quality improvement in cloth output cannot be ensured. The Company, however, did not take up modernisation of weaving first. The modernisation of spinning also remained incomplete.

- The Company could not redeploy the existing work force as envisaged in the modernisation programme due to labour resistance. This resulted in surplus labour, where there was less work and shortage of labour, where there was more work.

- The Government released a sum of Rs 22.20 crore between September 2000 and November 2001 and a further sum of Rs 15 lakh in March 2003 as share capital assistance to the Company for implementation of the modernisation programme. Further, the Company realised (December 1999 and January 2001) Rs 5.76 crore on sale of idle asset (land). The consortium of bankers to whom the Company had mortgaged the land permitted it to sell the land on the condition that the sale proceeds should be utilised for creation of assets. The Company received Rs 28.11 crore for the modernisation programme during the five years ended 31 March 2006. Against this, the Company had spent Rs 10.99 crore only on modernisation till March 2006, which included Rs 7.57 crore on machinery and Rs 2.08 crore as compensation for land. The Company had utilised the balance amount of Rs 17.12 crore for meeting its working capital requirements.

As such the modernisation programme has not been completed and the amount of Rs 10.99 crore spent has not yielded the desired results and the objectives of modernisation remained unfulfilled.

The Government stated (October 2006) that (i) the delay in implementing the CMP was due to non-release of adequate funds from 2003-04 onwards; resistance from workers for running the new machines in full capacity; delay in getting approval from the Government/Board, etc., (ii) the utilisation of modernisation fund for working capital was a short term arrangement and (iii) the Company took up the modernisation of both spinning and weaving simultaneously. The reply is self-contradictory as on the one hand, the Company had not spent the entire amount released on CMP and on the other, cites non-release of funds as one of the reasons for the delay. Further, the Company had not taken effective steps to install an Autokoner in unit ‘C’, which would complete the modernisation of that unit.

7.13.16 Abnormal labour cost

Failure to contain labour cost within the industry norm resulted in extra expenditure of Rs 128.60 crore.

The Company which was earning profits up to 1992-93, started incurring losses from 1993-94 onwards. The Company considered the excessive labour as the main reason for the loss. In order to reduce the work force and thereby reduce the cost of production, the Company introduced a Voluntary Retirement Scheme (VRS) in December 1996. Since then, 1,373 employees (1,296 workers and 77 staff/officers) had quit the Company on VRS and compensation of Rs 34.68 crore was paid to them. The Government funded the entire compensation amount as grant. In spite of the implementation of VRS, there was no significant reduction in the employee cost. The Company had not undertaken any scientific study of its labour force requirement clearly distinguishing between productive and non-productive labour. In the absence of such a study, the norm for expenditure on labour as fixed by the South India Textile Research Association (SITRA), which is 22 *per cent* of the total cost of production has been taken as the basis. Audit analysis revealed that the labour cost accounted for 45.5, 45.35, 40.37, 39.35 and 44.75 *per cent* of the cost of production respectively during the five years ended 31 March 2006. The excess labour cost over the SITRA norms of 22 *per cent* aggregated to Rs 128.60 crore during these five years.

In this connection, the Public Accounts Committee had also recommended (April 2004) that the Company should bring the labour cost within the norms. The Company, however, had not taken effective steps to keep the labour cost within the norms.

The Government stated (October 2006) that the Company had introduced VRS as a labour cost saving measure and that 1,371 employees had taken VRS from 1998-99 to 2005-06, which resulted in a saving of Rs 7.25 crore *per annum*. The fact, however, remains that the labour cost continues to be more than 40 *per cent* of the total expenditure as compared to the norm of 22 *per cent* for a composite mill.

7.13.17 Sales performance

The Company does not prepare a sales budget. The sales performance of the Company during the five years ended 31 March 2006 is given below:

(Quantity – in lakh metre) (Value – Rupees in crore)

Year	Export		Domestic		Total	
	Quantity	Value	Quantity	Value	Quantity	Value
2001-02	48.37	19.14	116.08	52.81	164.44	71.95
2002-03	46.22	17.51	118.25	49.27	164.47	66.78
2003-04	52.89	21.97	90.65	48.14	143.54	70.11
2004-05	49.09	21.71	102.65	54.22	151.74	75.93
2005-06	38.96	16.16	108.27	54.32	147.23	70.48

From the above details, it would be observed that export sale had declined from 52.89 lakh metres in 2003-04 to 38.96 lakh metres in 2005-06. The domestic sales had declined from 116.08 lakh metres in 2001-02 to 102.65 lakh metres in 2004-05 which marginally increased to 108.27 lakh metres in 2005-06. The main reason for decline in domestic sales, as analysed in audit, was the absence of a well knit dealer network and the Company's heavy dependence on agent dominated market for selling its cloth. It is pertinent to point out that an Expert Committee appointed by the Union Territory Government recommended (December 1994) that the Company should explore strengthening of its dealer network in metro cities and direct sales to institutions like hotels, hospitals and airlines. No action has been taken on this recommendation of the Committee so far.

The Government stated (October 2006) that in order to reduce the dependence on the indenting agents and to sell directly to institutions, the Company had started selling the products through direct marketing.

7.13.18 Closing stock of finished goods

The inability of the Company to improve its sales performance had led to huge accumulation of unsold stock. Audit scrutiny revealed that the Company had a closing stock of 38.38 lakh metres of cloth valued at Rs 23.87 crore as on 31 March 2006. Out of this, 15.89 lakh metres of cloth valued at Rs 7.02 crore had remained unsold for more than three years, 0.38 lakh metres of cloth valued at Rs 20.96 lakh had remained unsold for two to three years and 2.68 lakh metres of cloth valued at Rs 1.07 crore had remained unsold for one to two years. As the Company depends on borrowed funds for its working capital requirements, the inability of the Company to sell its entire production within one year resulted in its incurring inventory carrying cost of Rs 4.33 crore. Further, the quality of the cloth would also deteriorate due to efflux of time and the price realisable from sale of the old cloth would further come down.

7.13.19 Sales realisation

The details of sales realisation per metre *vis-à-vis* cost of sales per metre achieved by the Company during the five years ended 31 March 2006 are given in **Appendix XXXII.** From the Appendix, it would be evident that the sales realisation was less than the cost of sales in all these five years. The loss per metre in respect of grey cloth was more than the loss per metre in the sale of processed cloth.

Further, audit analysis revealed that the main reason for the low sales realisation was the over dependence of the Company on sale through agents as given below:

	2001-02		**2002-03**		**2003-04**		**2004-05**		**2005-06**	
	Q	**R**	**Q**	**R**	**Q**	**R**	**Q**	**R**	**Q**	**R**
(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**	**(9)**	**(10)**	**(11)**
Export sales	48.37	39.57	46.22	37.88	52.89	41.54	49.09	44.23	38.96	41.48
Agent sales	89.45	35.82	84.95	35.84	74.66	39.59	84.83	41.87	76.20	44.02
Government sales	18.98	57.45	24.14	47.26	8.48	128.74	12.46	89.96	35.01	50.02

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Retail and counter sales	3.02	66.85	4.75	38.43	2.64	84.05	2.07	138.62	5.31	72.16
FRC sales	4.63	8.98	4.41	11.32	4.88	12.51	3.30	23.85	4.18	16.14

Q=Quantity in lakh Linear metre; R=Realisation rupees per metre)

From these details, it is clear that the realisation from retail sales and sale of cloth to the Government departments was higher than the realisation from agent sales. The main reason for this, as analysed in Audit was that in respect of sale to the Government departments and sale through retail outlets, the Company fixed the selling price at cost of production plus margin. As regards sale to wholesale agents, the agents quote the price and the Company fixed the selling price by considering the previous years' selling price as a reference or base rate. The Company has not conducted any independent market survey to ascertain the prevailing rate in the market for the same variety. Consequently, the Company is following the method of fixing the selling price based on the Last Selling Price (LSP). However, the Company sells its cloth in its own showrooms at Puducherry fixing the rate at 20 to 30 *per cent* above the cost of production. As the selling price realised from the sale to wholesale agents was always lower than the cost of production, the Company's practice of comparing the offered price with the LSP instead of cost of production and market rates lacked justification. It is pertinent to point out that though the Company records the cost of production while preparing sale proposals, the same was not considered for the fixation of selling price. The Company did not compile data as to maximum or listed selling price for each sort/variety of cloth produced either periodically or at the year end.

The Government stated (October 2006) that the price realised in the wholesale market was driven by market forces and not by the cost of production of the Company and that the comparable products were available from the decentralised sectors at very low prices. The reply is not acceptable as the Company cannot carry on selling at below the cost of production and that the Company's basis for fixation of selling price is the previous realised price and not the current cost of production.

7.13.20 Loss due to sale at below the variable cost

Sale of cloth at prices below variable cost led to loss of Rs 6.90 crore.

The Company produces grey cloth in 48 to 67 varieties. A portion of this grey cloth is sold as such (based on demand) and the balance grey cloth is further processed into 50 to 75 varieties and sold as processed cloth based on customer/consumer requirement.

Audit analysis revealed that while fixing the selling price, the Company has been taking into account the material cost only and the other variable costs *viz*., direct labour cost, power and fuel, stores and spares, are not being taken into account. This has resulted in cash loss of Rs 6.90 crore during the period of review.

The Government stated (October 2006) that the Company could not fix the selling price based on cost of production and this was the reason for non-recovery of variable cost. The reply is not acceptable as failure to realise even the variable cost results in cash loss and the Company should identify the varieties in which it was incurring cash loss and dispense with the production of the same.

7.13.21 Discrepancy in the sale quantity

Audit scrutiny of closing stock statements for the four years 2001-02 to 2004-05 revealed that the quantity indicated as closing stock was physically verified by the Company but the sales figure shown in the respective years were not absolute but derived ones. To the opening stock, production quantity was added and from this closing stock of finished goods was deducted to arrive at the sales quantity. The Company's sale falls into four categories *viz*., exports, sales through agents, sale to Government and retail sale through showrooms. The sales quantum in the first three categories of sales was accounted on actual basis. The retail sale effected through the Company's showrooms were not accounted on actual basis but were derived. The retail sale consists of sale of cloth and different types of made ups (ready made garments). Audit analysis of the sales quantum effected through Company's showrooms (computed with reference to the norms of cloth in linear metre required for made ups) revealed that there were differences between the sales quantity computed by audit and the sales quantity accounted by the Company during the last four years as detailed below:

	2001-02	**2002-03**	**2003-04**	**2004-05**
Sales quantity computed by adopting norms (in linear metre)	3,51,105	2,99,270	4,12,308	5,14,919
Sales quantity accounted by the Company (in linear metre)	3,14,341	4,72,656	3,21,605	2,06,523
Difference (in linear metre)	36,764	(-)1,73,386	90,703	3,08,396

Note: The figures for 2005-06 are yet to be worked out by the Company.

Thus, during the three years 2001-02, 2003-04 and 2004-05, there was short accounting of sales by 4,35,863 linear metre valued at Rs 2.32 crore. It was also observed during audit that the Company did not include the cloth obtained as elongation (8.34 lakh metres) during the four years as production quantity in the respective years. Hence, sales had been under estimated to the extent of 8.34 lakh metres by the Company during these four years. The accounting of sales effected through the showrooms needs thorough review and remedial action. Further, the Company should account for only actual sales and realisations instead of resorting to derived figures as this system is fraught with the risk of fraud/manipulation.

The Government stated (October 2006) that steps had already been initiated to adopt showroom 'made-ups' sales as per norms specified by creating a database so as to account for sales on actual basis.

7.13.22 Acknowledgement

Audit acknowledges the co-operation and assistance extended by the staff and the Management of the Company and the concerned officers of the Union Territory Government at various stages of conducting the performance review.

7.13.23 Conclusion

The Company has been incurring losses on its production activities mainly due to its inability to utilise its manpower and machinery to their capacity and its failure to increase sales realisation commensurate with the increase in the cost of production. Due to stiff resistance from labour, the Company has not been able to introduce new work norms to improve labour productivity and in turn, increase production. Low capacity utilisation resulted in low production of yarn and purchase of yarn from outside at a higher cost. The Company has not been able to achieve any substantial increase in its sales realisation due to its overdependence on wholesale agents to market its products. Selling of cloth below the variable cost of production and wrong fixation of the variable cost has resulted in loss to the Company. The Company has not been able to complete the modernisation programme, which was expected to result in an increase of Rs 90 crore *per annum* in sales revenue.

Recommendations

- The Company should take immediate steps to increase labour productivity by introducing new work norms and keep labour within the prescribed norms.

- The Company should take steps to increase utilisation of its capacity for the production of cloth and should also increase production of yarn to minimise procurement of yarn from outside at higher price.

- The Company needs to reduce its dependence on wholesale agents for sale of cloth and should take immediate steps to put in place a well knit network of dealers to market its products.

- The Company should take steps to complete the modernisation programme at the earliest to achieve the objectives envisaged.

- The Government should examine and take measures to turn around the Company within a fixed time frame or consider alternative methods.

(Shankar Narayan)

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Countersigned

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