Chapter II

2. Performance reviews relating to Government Companies

Punjab State Industrial Development Corporation Limited

2.1 Investments and Disinvestments

Highlights

During 2001-07, the investments (Rs.1.40 crore) were negligible, mainly, because of non-generation of funds due to inadequate disinvestments (ranging between nil *per cent* to 26.45 *per cent* of disinvestments due) because of deficient provisions in the Financial Collaboration Agreements.

(Paragraphs 2.1.8, 2.1.9 and 2.1.11)

The Company allowed one time settlement (OTS) to the collaborators of profit earning units without taking up the matter with the State Government to exclude such units. This resulted in undue benefit of Rs.78.86 crore to the collaborators.

(Paragraph 2.1.21)

The Company failed to disinvest its investment of Rs.30.46 crore in an erstwhile subsidiary company, resulting, not only in non-realisation of its investments, but, also in non-generation of funds badly needed for repayment of loans/bonds.

(Paragraph 2.1.17)

Doubtful recoveries of Rs.14.85 crore, as, the securities available as per Financial Collaboration Agreements were not effective.

(Paragraphs 2.1.12, 2.1.13 and 2.1.14)

The Company failed to dispose of 1.50 lakh shares when there was a purchase offer and there was dire need of funds. This resulted in loss of Rs.7.65 crore as these shares were sold at a lower rate subsequently.

(Paragraph 2.1.16)

The Company suffered a loss of Rs.7.60 crore by covering ineligible collaborators under one time settlement scheme.

(Paragraph 2.1.27)

The Company was resorting to huge borrowings through loans/bonds from FIs to repay the loans and bonds. Principal amount of loans/bonds and interest outstanding for repayment/ payment amounted to Rs.581.92 crore and Rs.312.33 crore respectively as on 31 March 2007

(Paragraph 2.1.31)

Introduction

2.1.1 Punjab State Industrial Development Corporation Limited (Company) was incorporated (31 January 1966) with the objective to promote, aid, assist and finance industries by way of investment in shares of units in joint sector, assisted sector and other units through direct subscription to their share capital for balanced regional industrial development in the State.

As per investment policy, the Company participates in the share capital of joint sector and assisted sector units with equity participation of not less than 26 *per cent* and 10 *per cent,* respectively. The balance share capital of the assisted units is raised through contribution by the collaborators and in case of joint sector units it is also raised through public issue. Besides, the Company also makes direct subscription in the private sector units up to 15 *per cent* of equity envisaged subject to maximum of Rs.60 lakh if there is no public issue and rupees two crore if there is public issue.

Disinvestment in the units is done as per the terms of Financial Collaboration Agreement (FCA) entered into by the Company with the collaborators of the promoted units.

All the proposals relating to investments and disinvestments are submitted to the Board of Directors (BOD) of the Company and are finally got approved from the Project Approval Board (PAB) constituted by the State Government. PAB, *inter alia,* includes the Chief Minister, Industries Minister, Finance Minister, Minister of State for Industries, Chief Secretary, Secretary Planning and Secretary Industries and Commerce.

The organisational chart of the Company is as follows:

The total equity investment of the Company in various sectors as on 31 March 2007 was Rs.239.85 crore in 130 units including Rs.3.29 crore in one subsidiary (ESPL)* of the Company. The equity investment and disinvestment of the Company during 2001-07 was Rs.1.40 crore (4 units) and Rs.138.42 crore (36 units) respectively.

The investments and disinvestments by the Company in units was last reviewed in the Report of the Comptroller and Auditor General of India for the year ended 31 March 1998 (Commercial), Government of Punjab which is still to be discussed by the Committee on Public Undertakings (COPU) (September 2007).

Scope of Audit

2.1.2 The present performance review covers the equity investments and disinvestments made/due by the Company during 2001-07. Audit analysed all the cases of investments made and disinvestments covering 90 units out of 170 units where the disinvestments was either made or due during the period of review.

Audit objectives

2.1.3 The audit objectives of the review were to ascertain whether:

- the Company was able to invest and disinvest its funds economically and effectively as per its policies/ State Government's directions;
- disinvestments were made as per the terms and conditions of FCAs;
- the funds raised through disinvestments were judiciously utilised;
- one time settlement (OTS) scheme as floated by the State Government for equity disinvestment was implemented in true spirit and was in the best interest of the Company; and
- the management information system/ internal control system evolved by the Company was qualitative, adequate and effective enough to achieve the objectives in an efficient and effective manner.

Audit criteria

2.1.4 The following audit criteria were adopted:

- Policy relating to investments and disinvestments of the Company.
- Investments due for disinvestments as per FCA.
- Targets fixed for availability of funds from the State Government and FIs for investments, repayment of loans and bonds.
- Terms and conditions of FCAs entered into with the collaborators.

* Electronic Systems Punjab Limited.

- Norms and guidelines issued by the State Government for investment/ disinvestment**.**
- Decisions/instructions issued by PAB and BOD from time to time.
- OTS scheme under Industrial Policy, 2003

Audit methodology

2.1.5 Audit followed the following mix of methodologies:

- analysis of Company's policy of investments and disinvestments portfolio;
- analysis of OTS scheme for equity disinvestment;
- analysis of existing data in respect of investments/disinvestments made in joint /assisted/private sector;
- scrutiny of minutes/ agenda of meetings of BOD and PAB; and
- examination of Internal Audit Reports and action taken thereon.

Audit findings

2.1.6 The audit findings were reported (March 2007) to the Government/ Management and discussed (26 July 2007) in the Audit Review Committee for State Public Sector Enterprises (ARCPSE). The meeting was attended by the Executive Director (Projects) of the Company and Superintendent, Department of Industries, Government of Punjab. Views of the Government/ Management have been considered while finalising the performance review. The audit findings are discussed in the succeeding paragraphs:

Financial performance

2.1.7 The financial performance of the Company during 2001-05[#] was as follows:

(Rupees in crore)

Year	Profit(+)/loss(-) during the year	Accumulated loss at the end of the year
2000-01	(-)111.69	144.73
2001-02	(-)92.15	236.88
2002-03	(-)79.80	316.68
sS2003-04	(+)52.00	264.68
2004-05 (Provisional)	(-)46.01	310.69

The Company has been continuously incurring losses over the years, except for the year 2003-04. The accumulated loss of Rs.144.73 crore during 2000-01 increased to Rs.310.69 crore during 2004-05. The Company did not analyse the reasons for the losses. The main reasons analysed by Audit in this regard were as under:

- non-buy back of shares by the collaborator as per terms of FCA;

[#] Accounts from 2005-06 onwards have not been finalised.

- non/delayed disinvestment of the equity shareholding in erstwhile subsidiaries/ units where the Company was single largest shareholder, at an opportune occasion when the market price of the share was high; and
- the OTS of buy back consideration at the rate of interest of 8-10 *per cent*, was not only lower than from the cost of borrowing of funds (12 to 18.5 *per cent*) made by the Company, for investment in the units, but was also lower than the rates of interest provided in the FCAs (14 to 21 *per cent*).

Investments

During 2001-07, equity investment was Rs. 1.40 crore only due to financial crunch being faced by the Company.

2.1.8 As mentioned in paragraph 2.1.1 *supra*, one of the main objectives of the Company was to promote industries by way of investments in shares of the units for balanced industrial development in the State. Audit, however noticed, that, investments declined over the years due to resource constraints. Investments of Rs.215.33 crore made by the Company during 1991-96 decreased to Rs.69.67 crore during 1996-2001 and to Rs.1.40 crore during 2001-07. This indicated negative growth of the Company. The Company, instead of overcoming the financial crunch by implementing the recommendations* (October 2002) of the Disinvestment Commission, Government of Punjab, decided (2002-03) to act as a facilitator♣ only and not as an investor.

As regards meagre investments made by the Company during the period under performance review, Audit observed the following:

- Industrial Policy 2003 of the State Government envisaged recapitalisation of the Company to enable it to perform its future role as a promoter of mega projects, developer of agro and food processing industries, information and technology industries, etc. No action in this regard was, however, taken by the Company.
- The Company had not maintained any consolidated record showing proposals received by it for investment or facilitation of the projects/units followed by signing of Memoranda of Understanding (MOUs) and FCAs. Test check of records revealed, that, during 2001-07, the Company had signed 13 MOUs with the promoters of the units having project cost of Rs.19,532 crore. Audit scrutiny revealed, that, the Company had not framed any guidelines regarding requirement of feedback from the promoters, such as their financial resources, availability of raw material and demand of the product in the area so as to ensure successful fructification of the projects. Audit further noticed, that, due to paucity of funds, the Company could not invest in any of the units and all the 13 MOUs were converted into facilitation. The projects

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* Recovery through OTS for closed units, approaching the State Government for reduction in stamp duty, registration charges, rightsizing to the top management, etc.

♣ Means rendering various services for setting up new projects.

of only two[♦] MOUs could fructify, which indicated poor performance of the Company in promoting industries even through facilitation.

- The Company had not prescribed any effective mechanism to ensure physical availability of the share certificates. A test check of the records revealed, that, share certificates worth Rs.2.14 crore against investment (June 1983 to February 1997) in seven units were not available with the Company (July 2007). The Company had neither taken any action to obtain duplicate certificates nor conducted any enquiry (July 2007) to find out lacunae in the system to avoid recurrence of such lapses.
- During 2001-07, the Company made investments of Rs.1.40 crore in four units only. Instead of augmenting the same from Rs.138.42 crore received on account of disinvestment, the Company utilized the same for repayment of loans/bonds.

Disinvestments

Performance in disinvestment

2.1.9 The total disinvestment made by the Company in one erstwhile subsidiary and 35 units during five years ending March 2007 was Rs.138.42 crore. In addition, investment of Rs.41.88 crore in five erstwhile subsidiaries was written off, as, the Company had no hope for the recovery from these dormant/defunct/ under liquidation units. The year wise position of disinvestments due in the subsidiaries, erstwhile subsidiaries and units, actual disinvestments made by the Company thereagainst and outstanding during 2001-07 was as detailed in ***Annexure 8.***

Actual disinvestments during 2001-07 ranged between nil and 26.45 *per cent* of disinvestments due.

A perusal of ***Annexure 8*** would reveal, that, the percentage of actual disinvestment made during 2001-07 to total disinvestments due in units ranged between nil (2001-02) and 26.45 *per cent* (2003-04). The maximum disinvestments of 26.45 *per cent* during 2003-04 were due to disinvestment in Punjab Tractors Limited. The broad reasons for poor state of disinvestments are discussed in the succeeding paragraphs:

Provision of Financial Collaboration Agreement (FCA)

2.1.10 Disinvestment in the units was to be done as per the terms of FCA entered into by the Company with the collaborators of the promoted units regarding buy back of shares by the promoters. After November 2004, this buyback clause was, however, excluded from the FCA and disinvestment was to be done by sale of shares in the open market at any time after the unit goes into commercial production or when its shares were listed in the Stock Exchange. Provisions of standard FCA (prior to November 2004) regarding buy back of shares in

[♦] Abbot Cold Storage (P) Limited (promoter) and M.K. Overseas (P) Limited promoted units by the collaborator, *inter alia*, provided that:

- the collaborator shall buy back the shares of the Company in promoted unit after a specified (five or seven years) period from the date of FCA at the price higher out of the following:
    - acquisition price plus interest charged by the Company on term loans;
    - if shares are listed, highest price at which shares were traded during the three months prior to date of buy back.
- the collaborator shall deposit 10 *per cent* of the offered amount and completes the buy back within one month;
- in case collaborator fails to buy back the shares:
    - interest at the rate of 24 *per cent* would be charged and nominee of the Company will be appointed as Managing Director of the unit;
    - the Company could sell its shares at the risk and cost of the collaborator; and
    - the Company could recover the amount payable by the collaborator as arrears of land revenue.
- the collaborator buys back the shares at acquisition price plus 24 *per cent* interest or the Company could sell the shares at his risk and cost in case the project did not fructify within the specified period.

Thus, the exclusion of the above buy back provision from the FCAs after November 2004 not only set the collaborators free from the liability towards the Company's investment in the units, it affected the financial health of the Company.

Doubtful recovery of investment in joint sector

Ineffective provisions of FCA

2.1.11 Low percentage of disinvestments was due to deficient provisions of the FCAs, which were loaded in favour of the collaborators, rather than safeguarding the interest of the Company. In case of default by the collaborators in buy back of shares, the FCAs provided either for sale of shares at the risk and cost of the collaborators, or, recovery of debts as arrears of land revenue. The FCA provisions are, however, not effective, as in case of units which had not fructified or are running in huge losses, sale of shares is either not possible or beneficial, considering the negligible market value of the shares of the units. Further, the process of recovery of arrears as land revenue involved very long procedures and resulted in low recovery. It would, therefore, be imperative if the FCA provided for collateral security, i.e., pledging of equity investment or mortgage of land/ machinery purchased by the units, so that the Company was not forced to accept proposals of the collaborators in hope of some recovery.

Some of the interesting cases of doubtful recovery noticed in Audit due to ineffective security are discussed below:

Undue extension for financial closures

2.1.12 The Company invested (December 1995 to May 1999) Rs.5.83 crore (equity: Rs.1.92 crore, secured loan against equity: Rs.2.50 crore and short-term loan: Rs.1.41 crore) in Brahma Steyr Tractor Limited (BSTL). As per terms of FCA, the private collaborator was to buy back shareholding of the Company at face value, plus interest at 24 *per cent,* in case the project did not fructify within seven years of signing of the FCA, i.e., up to December 2002. The project could not fructify within the stipulated period and the Company without taking into consideration financial position of the collaborator and inadequate collateral security, recommended (October 2002) to the PAB for conversion of loans of Rs.3.91 crore and outstanding interest of Rs.8.86 crore (as on 31 March 2003) into equity. PAB waived (November 2002) the penal interest of Rs.54.05 lakh with the condition, that, the collaborator would induct equity of Rs.3.98 crore for financial closure[♠] of the project by 31 March 2003. The collaborator, however, failed to honour the condition and kept on requesting (March 2003 to January 2006) for piece-meal extensions of financial closure, which was given by the PAB up to March 2007. Thus, investment of Rs.5.83 crore (besides interest of Rs.33.26 crore as on 31 March 2007) in a project, which had not gone into production even after a lapse of over 10 years, was at stake.

Despite failure of the collaborator to honour his commitments even after three years, piecemeal extensions given by the PAB resulted in doubtful recovery of Rs. 5.83 crore from him.

The Management stated (July 2007) that its loan of Rs.3.91 crore was secured against mortgage of properties at Chandigarh and Morinda, and for recovery of equity investment arbitration proceedings had been initiated. The reply is not tenable, because, despite due dates of payment of long term and short term loans already expiring (October 1997 to November 1999) the Company failed to invoke the securities which resulted in unnecessary blocking of funds. As regards arbitration proceeding, the same was initiated (December 2005) by the Company after a delay of three years from the due date of disinvestment.

Default in payment by newly inducted collaborator

2.1.13 The Company entered (June 1993) into a FCA with the collaborator for setting up of a unit (Diamond Agro Industries Limited) and released (August 1993 to May 1994) equity of Rs.3.08 crore to the unit. The unit started commercial production on 1 October 1994 and as such the buy back of the shareholding became due on 1 October 1999 as per FCA. Before the due date of buy back of shares, new promoters M/s Sunil Mittal & Associates(SMA), however, took over (November 1996) the unit from the collaborator. The Company in principle agreed (May 1997) to the take over and decided (August 1999) that SMA should buy back 25 *per cent* shares before approval of the take over. The Company allowed (April 2000) SMA option to buy back its equity shareholding by 31 October 2004 with interest at 24 *per cent* on the consideration amount of Rs.6.75 crore (13 September 1999) payable in twelve half yearly instalments, starting

[♠] Firming up of funds for implementation of the project.

from 30 April 2005. The Company, however, did not implement its previous decision (August 1999) on the plea, that, SMA was taking requisite initiative to revive the unit. Thus, the Company itself delayed the buy back of its equity by more than five years.

Failure to effect buy back of 25 *per cent* shares by the new collaborator before his induction and to effect recovery as per FCA resulted in doubtful recovery of Rs. 6.75 crore.

Audit noticed that SMA failed to honour its commitment to pay half yearly instalments starting from April 2005. Despite this, the Company did not invoke arbitration clause for recovery of Rs. 6.75 crore due from October 1999 and interest of Rs.16.53 crore (up to March 2007) thereon. Thus, the chances of recovery of investment of the Company in the unit were remote.

The Management stated (July 2007) that apart from signing (July 2000) of the arbitration clause with SMA, the Company had taken (August 2000) their personal guarantee that had been invoked (June 2007) for recovery of the amount. The reply is not tenable as the Company failed to invoke arbitration clause and also delayed action for invoking personal guarantee. Moreover, it extended undue benefit to SMA by delaying the buy back for more than five years. Thus, failure of the company to invoke arbitration clause and delayed invoking of personal gurantee resulted in doubtful recovery of its dues.

Delayed action despite default in down payment

2.1.14 The Company entered (January 1993) into a FCA with a collaborator for setting up a unit (Herman Milkfoods Limited) and released (February 1993 to May 1994) an equity of Rs.2.27 crore (26 *per cent* of the total share capital). The buy back of the shareholding became due on 1 October 1999. Instead of buying back the shares in terms of FCA, the collaborator requested (September 1999) for extension of two years and approval for induction of new promoters. The Company decided (November 1999) to advertise for sale of the assets of the unit, to identify a new collaborator. The Company, however, subsequently allowed (January 2000) the collaborator to go in for a change in management and approved (April 2000) extension of 24 months for the buy back, i.e., up to October 2001 provided the collaborator made a down payment of Rs.1.14 crore. The collaborator did not respond, but, applied (January 2001) to the Board for Industrial and Financial Reconstruction (BIFR) for declaring the unit as sick. The Company delayed invoking (March 2002) of arbitration clause by two years, meanwhile the BIFR declared (July 2001) the unit as a sick unit.

Failure to implement its own decision and to effect the recovery of dues timely facilitated the unit to be declared as sick and resulted in doubtful recovery of Rs. 2.27 crore.

Audit scrutiny revealed that although the unit failed to make down payment of Rs.1.14 crore, yet the Company did not take action under FCA immediately to recover its dues. Inaction on the part of the Company thus resulted in recovery of Rs. 2.27 crore excluding interest (Rs.15.96 crore) up to March 2007 becoming doubtful. The Management admitted the facts (July 2007).

Status of disinvestment in the subsidiaries/erstwhile subsidiaries

Delay in disinvestment caused writing off of the investment

2.1.15 The investments* of the Company in eight units (four subsidiaries and four erstwhile subsidiaries) as detailed in ***Annexure 9*** was to be disinvested after their successful establishment. Although, all these units were successfully established long back and the Company was required to disinvest its shareholding, the State Government/Company failed to take timely action for their disinvestment. Resultantly, the disinvestments were abnormally delayed causing writing off (February 2004) of the investments of Rs.41.88 crore in five (Sl. No. A-2 to 4 and B-1 and 2 of ***Annexure 9***) units as the Company had no hope for the recovery from these dormant/defunct/under liquidation units. Audit scrutiny of two units out of remaining three units revealed the following:

Failure to off load shares at opportune time

2.1.16 The Company had 52.08 lakh equity shares in Punjab Tractors Limited (PTL) when the PAB of the State Government approved (August 1997) disinvestment of six lakh shares keeping in view the fund constraints faced by the Company. The Company sold (December 1998 and March 1999) 1.50 lakh shares at Rs.760 per share and three lakh shares at Rs.950 per share to Unit Trust of India (UTI) on single bid basis against highest market price of Rs.825 and Rs.1,043 per share, respectively. For selling of remaining 1.50 lakh shares, the Company invited offers (September 1999). Out of two offers received (September 1999) one party withdrew the offer and only one offer of UTI for Rs.1,000 per share was left. The Company decided (October 1999) not to sell the shares on the plea that there was only single bid and the price offered was lower than the average market price of Rs.1,242.21 per share. Thereafter, the Company made no efforts to disinvest its shares, even when the market price of the shares had started declining (January 2000). The Company finally decided (May 2002) to disinvest its entire shareholding of 142.74 lakh shares (including 95.16 lakh bonus shares received during 2000-01) through Directorate of Disinvestments (DoD) and ultimately sold (July 2003) the shares at Rs.153 per share to CDC Financial Services Limited on single bid basis.

Failure to dispose of shares when there was an offer and the Company was in dire need of funds resulted in loss of Rs.7.65 crore on subsequent disposal thereof at lower rates.

Thus, by not selling the shares at appropriate time, the Company not only had to raise (March 2000) loan (Rs.50 crore) from the market by issue of bonds at the interest rate of 12.25 *per cent* per annum involving interest payment of Rs.3.68♣ crore, but, had also to suffer a loss of Rs.7.65 crore (after adjusting the benefit on account of three lakh bonus shares and dividend received by the Company during intervening years 1999-2003). Had the Company sold the balance shares (141.24 lakh including bonus shares) at the minimum average rate of Rs.627 per share

* As on 31 March 2003.
♣ Loan amount restricted to Rs.15 crore that would have been realised by sale of shares.

prevailing during November 1997 to June 2000, it would have avoided further loss of Rs.48.11[#] crore.

The Management stated (June 2007) that the matter of disinvestment in PTL was deliberated upon from time to time by the Disinvestment Committee under the chairmanship of the Chief Secretary, Punjab, BODs of the Company and the PAB but disinvestment could not take place. It further stated that complete disinvestment in PTL was to be carried out by following the elaborate procedure. The reply is not tenable as financial discipline demanded disinvestment at the opportune time so as to ensure that the Company/State Government does not suffer financial loss.

Unjustified deferment of disinvestment decision

Failure to take action to disinvest in an erstwhile subsidiary resulted in non- realisation of its investments of Rs. 30.46 crore.

2.1.17 The Company held (1981 to 1997) 90.90 lakh equity shares of Rs.30.46 crore (44.26 *per cent*) in Punjab Alkalies and Chemicals Limited (PACL) on 31 March 1998, but, it had not taken any concrete steps for its disinvestment despite decisions taken from time to time (October 1996 to February 2004) by PAB/State Government in this regard. The Company did not avail the opportunity even though one[@] private company was interested (August 2005) to purchase the shareholding of the Company. During that period, the market price of shares was Rs.126 per share. Reasons therefor were, however, not found on records. Since the Company did not disinvest its shareholding and the average market price of the share came down (March 2007) to Rs. 22.45 per share, the indecision caused, not only loss of revenue of Rs.94.13 crore, but, it also could not generate funds, which were badly needed for repayment of loans/ bonds and for industrial development in the State.

The Management stated (July 2007) that the DoD had done some exercise to disinvest the shareholding of the Company in PACL. The process had reached an advance stage when price of the share was also reasonable, (Rs.120-125) but, the Cabinet Committee on Disinvestment deferred (August 2005) the disinvestment. In ARCPSE meeting the Management stated (July 2007) that disinvestment involved elaborate procedure and the Company was always on a look out for an opportunity to disinvest its shareholding. The Management, however, failed to advance any cogent reasons for deferring the decision for disinvestments.

Disinvestment through one time settlement scheme (OTS)

2.1.18 OTS under Industrial Policy, 2003 introduced (March 2003) by the State Government, for facilitating buy back of shares by the collaborators, was adopted (27 March 2003) by the Company and was to remain operative from 1 April 2003 to 31 May 2003. The OTS was also applicable to cases where arbitration

[#] Worked out on 46.08 lakh shares which the Company held up to June 2000 and excluding 95.16 lakh bonus shares received thereafter and dividend of Rs.24.72 crore.

[@] DCM Shri Ram Industries, New Delhi.

proceedings had been initiated, provided the collaborator/promoter withdraw the arbitration case. The State Government *ex post facto* extended (June 2004) OTS and made it operative till 31 July 2003.

Audit analysis revealed, that the provisions of OTS were basically defective in view of the following:

- OTS provided, deposit of 10 *per cent* upfront payment by the promoters. It, however, did not ensure regular inflow of money to the Company, as, the periodicity against the balance 90 *per cent* payable by the collaborators under OTS, was not prescribed;
- OTS allowed settlement of dues of those units where buy back was not overdue;
- it allowed settlement of dues of units irrespective of their status (i.e., whether the units are profit earning or loss making); and
- it also allowed recovery of lower OTS rate of interest (10 *per cent*) where partial consideration amount against the shares already due for buy back had already been received by the Company but corresponding number of shares were pending for transfer to the collaborators.

A few cases of deficiencies in the formulation and implementation of OTS as noticed in Audit are discussed below:

Periodicity of OTS instalments not specified

Deprivation of regular flow of funds due to non-specification of the periodicity against balance payment of OTS.

2.1.19 OTS allowed the collaborators to pay balance 90 *per cent* consideration amount within three-four years, (as the case may be) without specifying periodical instalments thereof or obtaining any security in the shape of post dated cheques (PDCs) or bank guarantee thereagainst to discourage further default by the collaborators. Out of Rs.115.92 crore, being the balance 90 *per cent* consideration under OTS, only Rs.5.35 crore had been realised (March 2007) leaving unrealised balance of Rs.110.57 crore. The Company was, thus, deprived of regular flow of funds for recycling of repayment of loans and redemption of bonds carrying high rate of interest.

The Management admitted (July 2007) that in view of the BoDs decision (September 2004) it had asked the collaborators to deposit PDCs for the balance dues, (90 *per cent*) but, in the absence of any such provision in OTS scheme, the collaborator refused to do so. The Management further stated, that, the collaborators were even persuaded, (March/ April 2005) for commitment towards the payment, by offering discounted interest rate of 11.5 *per cent* in place of 12.5 *per cent*, but, no response was received.

Settlement under OTS where buy back was not due

OTS also covered those collaborators where buy back was not due.

2.1.20 The OTS was made applicable to all the collaborators, irrespective of the fact whether buy back of shares was due or not. Consequently, those units were also covered under OTS, where buy back was not due and collaborators could have bought back the shares at higher interest as per terms of FCAs. During the operation period of OTS (2003-05), the Company covered 11 collaborators (investment: Rs.9.59 crore) under OTS, where buy back was not even due. Audit noticed, that, against the consideration amount of Rs.20.74 crore under FCA, the OTS amount was only Rs.13.57 crore. This resulted in undue favour of Rs.7.17 crore (including foregone amount of Rs.7.05 crore relating to profit earning units). The Management admitted (July 2007) the facts.

OTS made applicable even to profit earning units

Covering profit earning units under OTS resulted in benefit of Rs.78.86 crore to the collaborators of these units.

2.1.21 A mention was made in paragraph 3.3 of the Report of the Comptroller and Auditor General of India (Commercial) Government of Punjab, for the year ended 31 March 2004, regarding allowing undue benefit of OTS to profit earning units. Audit noticed, that, despite this, the Company did not take up the matter with the State Government even when it modified (June 2004) the OTS, to disallowing it to profit earning units. Consequently, the Company did not make its claims under FCAs and allowed (2003-05) not only the financial benefit of Rs.78.86 crore to 35 (out of total 45) collaborators, who had applied for OTS and were running their units in profits. This also sent an unhealthy message to other profit earning collaborators to deliberately resort to willful default in making payments towards buy back and to avail the benefit under the OTS.

A few such cases noticed in audit are discussed below:

Piecemeal buy back was allowed to a collaborator

Preponement of buy back of shares by a collaborator of the profit earning unit was allowed in piecemeal due to which he was allowed undue benefit of Rs.3.58 crore.

2.1.22 The equity (Rs.7.86 crore) of the Company in Winsome Yarns Limited was due for buy back (March 1999). Since the unit was earning profit since 1997-98 (profit after tax transferred to reserves up to 2003-04 was Rs.34.86 crore) and was paying dividend since 2002-03, it pre-poned the buy back of 27 lakh shares during January 1998-February 1999. Thereafter, the unit further bought back (March 1999 to February 2001) 38 lakh shares. When OTS was introduced (March 2003), the Company covered the unit under OTS for the left over 13.60 lakh shares by settling the claim for Rs. 2.65 crore against the consideration of Rs. 6.23 crore as per the terms of FCA thereby foregoing Rs. 3.58 crore.

Thus, by not insisting the unit for buy back of shares in one go, as, it was earning profits, or, taking action under terms and conditions of the FCA before introduction of OTS, the Company extended undue benefit of Rs. 3.58 crore to a profit earning unit.

Release of collateral security after partial buy back

2.1.23 The Company invested (March 1995 to March 1996) Rs 3.45 crore and additional Rs. 30 lakh (December 1998) in the equity of Indian Yarns Limited representing 39.60 *per cent* of its total equity. The additional equity of Rs. 30 lakh was invested against mortgage of residential land of 2,151 square yards as collateral security, along with personal guarantee. The commercial production of the unit started in March 1996. The buy back of the equity became due in March 2001. As per FCA entered (February/May 1995 and August 1998) into with the collaborator, the additional equity was due for buy back in three instalments (March 1999, March 2000 and March 2001). The unit failed to adhere to the prescribed schedule and paid (December 2000-March 2003) Rs.25 lakh as partial payment against buy back of the additional equity. No payment was made against the original equity. The Company also did not take any action to appoint its nominee director as MD of the unit as per FCA. The Company accepted (July 2004) the offer of the unit for OTS at Rs.7.25 crore by foregoing its claim of Rs.4.74 crore towards interest. The collateral security of the land was released (January 2005) by the Company after the collaborator paid (June 2004) upfront payment of Rs.0.71 crore and Rs.0.18 crore against original equity and additional equity, respectively. Audit observed, that, the Company did not insist that the collaborator first clears his balance dues of Rs.6.36 crore under OTS before releasing the collateral security. No further payment towards balance amount of Rs.6.36 crore was received (July 2007) from the collaborator even though the unit was earning profits since 2002-03 and free reserves of the unit up to March 2006 were Rs.2.93 crore. Thus, release of collateral security without insisting the collaborator to first clear its dues against the original equity resulted in doubtful recovery of Rs.6.36 crore.

The Company did not insist upon the collaborator to first clear his balance dues of Rs. 6.36 crore under OTS before releasing the collateral security.

Unit with positive net worth allowed undue BIFR benefits

2.1.24 The Company invested (April 1988 to January 1989) Rs.78.50 lakh in the equity of Mohan Fibre Products Limited which was due for buy back in April 1995 as per FCA. The unit became sick and was registered (September 1995) with BIFR. The collaborator applied (April 2003) for OTS which was accepted (May 2003) by the Company at Rs.1.96 crore against the consideration amount of Rs.3.61 crore as per FCA. No reasons were recorded for settlement at reduced rate of interest. The unit paid (May to August 2003) Rs.97 lakh under OTS. In the meantime, the net worth of the Company improved and became (June 2003) positive. The OTS scheme was modified (June 2004), allowing certain additional concessions to the units registered with BIFR. The Company on the advice of the State Government again covered (December 2004) this unit under the modified OTS and settled its dues at par, i.e., at Rs.78.50 lakh and thus increasing the amount forgone by the Company from Rs.1.65 crore to Rs.2.64[♦] crore. Audit observed that the Company did not approach the State Government to exclude such units which were registered with BIFR but had become capable of buy back of shares, from the scope of OTS, as their net worth had become positive or had committed themselves by making payment under original OTS. Thus, non-taking up of the matter with the State Government for excluding units with positive net worth from the scope of modified OTS resulted in undue benefit of Rs.2.64 crore to the unit.

The unit was covered under modified OTS, even though its net worth had become positive and its collaborator had committed himself under original OTS.

♦ Treating the settlement at earlier received amount of Rs.97 lakh instead of at Rs.78.50 lakh.

Allowing OTS after its expiry date

The Company suffered loss of Rs. 1.18 crore by covering an ineligible profit earning unit under OTS.

2.1.25 The Company entered (August 1995) into a FCA with a collaborator (Shyam Indospin Limited) and released (September 1995 to March 1996) equity of Rs.1.04 crore due for buy back during October 2001. Against due amount of Rs.2.26 crore (including interest), the collaborator paid (May to December 2002) Rs.20 lakh only towards buy back in spite of the fact that the unit was earning profits and transferred (March 2002) Rs.1.32 crore to reserve and surplus. The collaborator also invested (June 2001 to December 2002) Rs.4.88 crore in the expansion of the project without the approval of the Company. The collaborator also did not invite the nominee director of the Company to participate in the BoDs meetings. The Company also failed to take requisite action under FCA to appoint its nominee director as MD of the unit or to dispose of its shareholding, instead, it accepted (July 2004) the offer of the collaborator under OTS after the expiry (July 2003) of OTS scheme and settled (July 2004) its dues of Rs.2.78 crore at Rs.1.60 crore. The collaborator paid the same without any delay (August 2004).

The Management stated (July 2007) that it had only implemented the policy which was introduced by the State Government. The same was made applicable to all the units, irrespective of their status due to the reason that the enforcement of buy back of equity was not effective. The reply is not tenable as the Company should have emphasized the need of amending the OTS scheme to the State Government. Fact is that implementation of the scheme was not in its interest, as it was preventing the Company from recovering even the borrowed cost of investment. Thus faulty implementation of OTS resulted in foregoing an amount of Rs.1.18 crore by the Company.

Loss due to non-transfer of shares

2.1.26 The Company had been receiving consideration amount in parts against the shares, which had already become due for buy back by the collaborators. The Company had, however, not prescribed any procedure/system to effect the transfer of proportionate shares equivalent to the consideration amount as and when it was received. Consequently, when OTS was introduced (March 2003) it had to be made applicable for such shares also, in respect of which, the consideration amount had already been received, but, the shares for the proportionate value were not transferred to the collaborators. This resulted in undue benefit of concessional interest (10 *per cent* instead of 14 to 21 *per cent*) of Rs.2.88 crore to 21 collaborators (Rs.2.69 crore relating to 19 collaborators of profit earning units pointed out in paragraph 2.1.21 *supra*) who had paid (up to 31 March 2003) Rs.9.80 crore against partial buy back of shares.

The Management stated (July 2007) that, as a normal practice, the shares were transferred to the collaborator only after the receipt of the entire amount due against buy back of shares, so as to maintain pressure on the collaborators to ensure the complete buy back of equity held by the Company. The reply is not tenable, as the Company had already compromised its position and had transferred the shares against partial buy back, in two cases[♣] (2001 to 2007). This was due to absence of any procedure or system for transfer of shares to the collaborators in proportion to the consideration amount received from them.

OTS to ineligible collaborators

The Company suffered a loss of Rs.7.60 crore by covering ineligible collaborators under one time settlement scheme.

2.1.27 The State Government *ex post facto* modified (June 2004) the validity of original OTS (March 2003) and made it operative for further two months upto 31 July 2003 allowing those collaborators who had deposited (April-July 2003) upfront payment less than 10 *per cent* to deposit the balance amount by 30 June 2004. The Company further made (June 2004) the OTS operative to all the collaborators and extended the OTS benefits to 12 new entrants (after 31 July 2003) by foregoing interest of Rs.37.88 crore. Out of Rs.37.88 crore foregone, an amount of Rs.30.28 crore *(*79.94 *per cent)* related to seven profit earning units as pointed out in paragraph 2.1.21 sup*ra*. This is indicative of the fact, that, move of the Company to extend OTS even beyond 31 July 2003 was deliberate, with the intention to extend benefit to the profit earning units. Only Rs.7.60 crore related to five loss making units which were not eligible for OTS.

The Management stated (July 2007) that the last date for making payment of 10 *per cent* of the OTS amount by the collaborators to be eligible for exercising option was 30 June 2004. The reply is not tenable as the ex-post facto extension of last date up to 30 June 2004 was for depositing the balance upfront payment so as to make it up to 10 *per cent* and not for new entrants to OTS. Even the extension upto 30 June 2004 allowing the collaborators to deposit the balance amount was not in the best commercial interest of the Company.

Loss due to delay in settlement

2.1.28 The Company sanctioned (January 1996) equity investment of Rs. 9.76 crore in a unit (Satia Synthetic Limited) in which equity contribution by the collaborator was to be Rs.6.64 crore. Further equity of Rs.11.84 crore was to be raised through public issue only after the contribution of equity by the Company and the collaborator. Had the Company contributed its entire sanctioned equity, its contribution would have become 51 *per cent* or more of the total paid up equity thereby making the unit a Government company. To overcome this, the Company invested (March 1996 to August 1997) Rs.6.64 crore in equity and balance Rs.3.12 crore as loan, subject to the condition that the unit would make public issue within two years. The unit, however, failed to make public issue within two years. The Company introduced (October 2002), the OTS scheme for loans, against which, the collaborator applied (October 2002) and also made payment of Rs. one crore as upfront payment. The BODs of the Company, however, deferred (February 2003) the decision to allow the settlement with the collaborator without any specific reasons. Subsequently, when the State Government announced (March 2003) the OTS for equity, the collaborator

[♣] Abhishek Industries Limited and Geeta Threads Limited.

requested (June 2003) the Company to cover its loan under OTS for equity which was allowed (June 2004) in contravention of provisions of OTS, to the collaborator thereby sustaining loss of Rs.1.82[#] crore.

Loss of Rs. 1.82 crore by covering a collaborator under OTS for equity who had committed himself under OTS for loan.

Thus, despite the consent of the collaborator to cover it under OTS for loan, failure of the Company to timely settle the case and covering the same under OTS for equity resulted in loss of Rs.1.82 crore.

The Management stated (July 2007) that it had implemented only the policy of the State Government. The reply is not tenable as the Company failed to take timely decision when the collaborator was willing to settle his loan under OTS for loan policy.

Public Interest Litigation on OTS

2.1.29 Mention was made in the paragraph 3.1 of Audit Report of the Comptroller and Auditor General of India-(Commercial), Government of Punjab, for the year ended 31 March 2005, regarding allowing undue benefit (Rs.26.58 crore) of OTS to profit earning units. Taking cognizance of this report, the Principal Investigator of Punjab Human Rights Organisation filed (May 2006), a Public Interest Litigation in the Punjab & Haryana High Court, for a direction to these profit earning units, to pay back to the state exchequer the undue benefit along with penal interest taken by them under the OTS. The Company keeping in view the instructions (February 2007) of the State Government on the issue approached (April 2007) the Court to make all the beneficiaries[$] a party to the case. Audit noticed that the Company had received cheques worth Rs.51.78 crore from such collaborators up to July 2007 in this regard, but the same were not presented for encashment. Subsequently, the Advocate General, advised (June 2007) the Company to encash the cheques after obtaining undertaking from the collaborators to the effect that encashment would not bind the Company to implement OTS. The Company was, however, able to encash cheques worth Rs.1.81 crore only (July 2007), as the Company failed to obtain undertakings from the remaining collaborators. Thus, non-obtaining the requisite undertakings from the remaining collaborators resulted in non-encashment of cheques worth Rs.49.97 crore.

Loss due to non claiming of interest

2.1.30 Mention was made in paragraph 2A.4.1 (ii) of the Report of the Comptroller and Auditor General of India (Commercial) Government of Punjab for the year ended 31 March 1998 regarding investment (April 1989 to June 1993) of Rs.3.77 crore in a project (Harpartap Steel Limited). This unit had not gone into production even after lapse of over 13 years at that time (March 1998). As per FCA, the collaborator was bound to buy back the equity investment of Rs.3.77

[#] Due under OTS for loan: Rs.5.54 crore (-) Rs.3.72 crore settled under OTS for equity = Rs.1.82 crore.

[$] 45 beneficiaries of OTS.

crore along with interest after five years of the start of commercial production. The unit even failed to complete the project till December 2005. Due to the absence of any clause in the FCA for buy back of shares by the collaborators in case the project did not fructify, the Company could not recover its dues amounting to Rs.13.12 crore (including interest).

In the meantime, the Empowered Committee of Punjab Government (ECP), decided (November 2005) to allow a third party* to set up a mega information and technology park by purchasing 15-acre plot of the unit with an investment of Rs.146.46 crore. The Director, Industries Department, Punjab conveyed (December 2005) that the outstandings of the collaborator in Harpartap Steel Limited towards the Company's equity contribution may be settled to the satisfaction of the Company before permission to sell the land was allowed to it. The Company, however, decided (January 2006) to settle the outstanding at a lump sum payment of Rs.3.77 crore (without insisting for recovery of interest of Rs.9.35 crore) and without due consideration of the high market value (Rs.108.97 crore$) of the plot. Finally, no dues certificate was issued by the Company to the collaborator on receipt of Rs.3.77 crore (February 2006).

The Company suffered loss of Rs. 5.19 crore due to non claiming of interest while settling the accounts.

Audit observed, that, when ECP had allowed (December 2005) the Company to settle the accounts with the collaborator to its satisfaction, before the sale of land by the collaborator to the third party for mega project, the Company was in a position to recover its reasonable interest of 10 *per cent* (applicable in the case of OTS) from the collaborator by negotiations. Failure of the Company to recover at least 10 *per cent* interest from the collaborator resulted in loss of Rs.5.19ϒ crore**.**

The Management stated (July 2007) that the observation of Audit for the loss/ sacrifice was misconceived as the amount could not have been recovered under the FCA. The reply is not tenable, as, the Company had made this investment by obtaining loans from the FIs at 16 and 18.5 *per cent* per annum and hence on account of the interest liability, the Company should have protected its interest and ensured recovery before agreeing to the above proposal.

Borrowings

2.1.31 Due to heavy defaults by the loanee units and non generation of sufficient funds from disinvestments, the Company had to face financial crunch and resort to borrowings through loans/bonds in order to repay the loans. The Company not only had to pay principal of Rs. 581.92 crore but was also liable to pay interest of Rs.312.33 crore on these borrowings as on 31 March 2007.

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* Globus Projects Private Limited.

$ As per Survey Reports of the allotment agency of Punjab Small Industries and Export Corporation Limited.

ϒ Worked out at 10 *per cent* interest from the date of investment (April 1989 to June 1993) to December 2005, i.e., up to date of decision of the Company.

The following table shows the details of loans/bonds raised during 2001-07 to repay the loans of the FIs:

(Rupees in crore)

	Opening balance		**Raised**		**Paid /Redeemed during the year**		**Balance**		**Interest**	
Year	**Loans**	**Bonds**	**Loans**	**Bonds**	**Loans**	**Bonds**	**Loans**	**Bonds**	**Paid on loans**	**Accrued on bonds**
2001-02	238.56	415.55	25.95	83.63	28.66	81.56	235.85	417.62	24.53	56.17
2002-03	235.85	417.62	-	174.59	97.07	81.04	138.78	511.17	19.28	58.62
2003-04	138.78	511.17	-	143.38	112.96	220.29	25.82	434.26	2.97	51.02
2004-05	25.82	434.26	-	237.11	25.82	144.79	-	526.58	-	50.18
2005-06	-	526.58	-	184.28	-	151.37	-	559.49	-	51.11
2006-07	-	559.49	-	130.00	-	107.57	-	581.92	-	45.23♣
Total	--	--	--	--	--	--	--	--	**46.78**	**312.33**

Audit scrutiny revealed the following:

- The Company paid (2003-04) interest of Rs.14.54 crore to the bond holders on overdue payment of bonds.
- Instead of ensuring funds by way of disinvesting the shares in wholly owned subsidiaries as well as in profit earning units, the Company resorted to (March 2001) raise a short term loan of Rs.50 crore from IDBI against the pledge of 54 lakh shares of Punjab Tractors Limited to repay dues to bond holders/ loanees and consequently paid (2002-03) Rs.5.65 crore (interest: Rs.4.96 crore and liquidated damages: Rs.0.69 crore).

The Management stated (July 2007) that it had succeeded in saving interest payments to bond holders during 2003-04 by paying interest at normal rate and not at coupon rate plus penal interest. It further stated that loan of Rs.50 crore was raised mainly because of failure of the loanees/collaborators to pay back their dues to the Company. The reply is not tenable as it was for the Company to evolve mechanism for ensuring timely payments against its loans and investments.

Arbitration cases

2.1.32 As per the terms of FCAs with the collaborators, all disputes were to be referred to the Arbitrator. Despite the opinion (June 1996/July 2000) of Advocate General, Punjab and a sub-committee of BOD of the Company, that the process of arbitral adjudication were cumbersome, lengthy and against the financial interest of the FIs, the Company continued to include this clause and that too without fixing any time limit for deciding the case.

The table below shows the number of units under arbitration in the beginning of the year, added and decided during the year and pending at the end of each year

♣ Interest paid on bonds.

during 2001-07.

(Rupees in crore)

Year	Opening Balance		Added during the year		Decided/withdrawn during the year		Balance	
	No. of units	Amount of investment	No. of units	Amount of investment	No. of units	Amount of investment	No. of units	Amount of investment
2001-02	18	33.25	10	23.05	-	-	28	56.30
2002-03	28	56.30	7	15.84	3	1.31	32	70.83
2003-04	32	70.83	4	10.89	4	5.07	32	76.65
2004-05	32	76.65	8	24.57	5	31.75	35	69.47
2005-06	35	69.47	2	1.00	4	3.35	33	67.12
2006-07	33	67.12	1	6.15	1	1.51	33	71.76
Total			**32**	**81.50**	**17**	**42.99**#		

During 2001-07, 28 *per cent* of total pending arbitration cases were decided.

Audit noticed that out of 50 units under arbitration (18 initiated before 2001-02 and 32 during 2001-07), the cases in respect of 14 units (28 *per cent)* were decided by the Arbitrators and the case in respect of three$ units were withdrawn to facilitate OTS during 2001-07.

Audit scrutiny of the pending cases of 33 units revealed the following:

- One unit involving investment of Rs.16 lakh was pending (before Tribunal of Arbitration) for the last 13 years since May 1994 and seven units (including five units with court for appointment of Arbitrators) involving investment of Rs.10.40 crore were pending for periods ranging between seven and 10 years.

Chances of recovery of Rs.79.52 crore in respect of cases decided in favour of the Company were remote due to non availability of record of attachable property.

- Out of the decided cases of 14 units, the cases of 13 units involving Rs.79.52 crore (Rs.17.11 crore investment plus Rs.62.41 crore interest and costs) were decided in favour of the Company. Since the details of attachable properties in these cases were not ascertained during pendency of the cases with Arbitrators, or before making investments, the Company could not recover its dues (July 2007) amounting to Rs.79.52 crore.

Entering into Financial Collaboration Agreement without the approval of PAB caused the Arbitrator to decide compensation of Rs.11.20 crore to be paid by the Company.

- One case (Indian Acrylic Limited) involving investment of Rs.18.34 crore was decided (December 2004) against the Company. In this case, the Company ignoring the default of Rs.1.75 crore made by the collaborator in another unit (Steel Strips Wheels Limited) entered into a supplementary agreement (February 1997) with the collaborator without requisite approval from PAB and contributed Rs. one lakh to the unit. When the Company sought approval from PAB, it declined (May 1997) and the Company did not release the balance amount (Rs. 4.99 crore). Due to breach of agreement, the Tribunal of Arbitration directed (December 2004) the Company to compensate the collaborator with Rs.11.20 crore, as the funds (Rs.15.71 crore) inducted by the collaborator for making the project viable had been blocked and also to allow the collaborator to buy back the shares at the face value only. The Company approached (March 2005) the District Court Chandigarh against the award of the Tribunal of

Includes the amount of investment of two units (2003-04) and one unit (2006-07) where arbitration awards were decided in favour of the Company in case of additional equity only but pending in case of original equity.

$ Suraj Solvent and Vanaspati Industries Limited, Mohan Fibres Limited and Aster Drugs & Pharmaceuticals Limited.

Arbitration and the court ordered (January 2007) for the execution of arbitration award. This order was, however, stayed (April 2007) by the High Court pending final decision.

Thus, the Company had put itself in unnecessary litigation by acting in haste to enter into the agreement without approval of PAB.

Internal control

2.1.33 Internal control is an essential pre-requisite for efficient and effective management of the Company. Following deficiencies were noticed in the internal control system in the Company:

- The Company did not maintain any record relating to financial health of projects financed, regular inspection/ project appraisals, details of attachable properties in cases of arbitration, attending the AGMs/BOD's meeting by the nominee directors in the units; maintenance of data bank of shares frequently traded in the market, etc.
  - The Company did not evolve any system to ascertain regular feedback about projects under implementation/ or failed to fructify, rehabilitation package under consideration/implementation, for facilitating timely action for disinvestment and of the financial health of the units by obtaining financial results of the units periodically to impress upon units earning profit to declare the dividend and to buy back its shares.
  - The Company did not maintain the consolidated record showing the investments/partial disinvestments made from time to time.

Conclusion

The investments made by the Company were negligible mainly because of non-generation of funds due to inadequate and delayed disinvestments. Even the funds realised through disinvestments were utilised for repayment of loans/bonds instead of utilizing the same for investments for promotion of new industries in the State, which was the main objective of the Company. In defiance of financial discipline, the Company created further liabilities by resorting to huge borrowings through issue of bonds in order to repay the loans to the Financial Institutions. The major reasons for fall in disinvestments of equity by the Company were that the existing FCAs were having inherent weak legal mechanism for enforcement. The provisions of OTS scheme for equity disinvestment were defective and not in the financial interest of the Company. The Company had to forego substantial amount by covering ineligible units under OTS.

Recommendations

- **The Company should redefine and overhaul its system of investment and recovery if it has to have an impact on promotion of new industries in the State.**

- **The terms and conditions of FCAs ought to be reviewed by the Company to include provision of effective security such as bank guarantee or collateral security in order to have effective disinvestment.**

- **The Company should approach the State Government to exclude those provisions from the OTS which are not in the financial interests of the Company such as allowing concessions to profit making units, etc.**

- **The Company should impress upon the State Government to compensate for the losses suffered by it due to implementation of OTS scheme which led the Company to debt trap.**

- **The Company needs to disinvest in the erstwhile subsidiaries.**

The above matter was referred to the Government in March 2007; their reply had not been received (September 2007)

Punjab State Civil Supplies Corporation Limited

2.2 Disposal of damaged wheat under Open Market Sale Scheme

Highlights

During lifting of damaged wheat in eight district offices, shortages of 0.38 lakh MT of damaged wheat valuing Rs.44.29 crore was noticed. The Company had not taken final action against delinquent officials so far.

(Paragraph 2.2.20)

Recovery from Food Corporation of India (FCI) of Rs.44 crore being difference between Open Market Sale Scheme (OMSS) rates and actual sale price realised for the sale of damaged wheat was doubtful as damage to wheat stocks was above the norms suggested by the Committee formed by FCI in this regard.

(Paragraph 2.2.15)

The Company failed to dispose of entire quantity of damaged wheat by the stipulated period for reimbursement of carry over charges which resulted in doubtful reimbursement of carry over charges of Rs.11.35 crore, incurred beyond the stipulated period, from FCI in respect of eight district offices.

(Paragraph 2.2.19)

The fixation of reserve price for the disposal of Group I of damaged wheat was not based on commercial prudence and there was loss of Rs.2.92 crore to the Company in eight district offices due to lower fixation of reserve price.

(Paragraphs 2.2.11 and 2.2.12)

Delayed/short raising of differential claims on FCI resulted in loss of interest of Rs.1.01 crore in eight district offices.

(Paragraph 2.2.16)

Introduction

2.2.1 Punjab State Civil Supplies Corporation Limited (Company) was incorporated in February 1974 as a wholly owned Government Company to procure, store, supply and distribute foodgrains and essential commodities of common consumption in the State.

The Company is engaged in the procurement of wheat and paddy for the central pool. It procures wheat conforming to fair average quality (FAQ) specifications from *mandis* at the minimum support price (MSP) fixed by the Government of India (GOI) and stores in godowns/plinths and delivers the same to Food Corporation of India (FCI) for the central pool as per movement plan drawn by FCI on first in first out (FIFO) basis. FCI reimburses the cost of wheat and incidental charges to the Company at the rates fixed by the GOI from time to time. As per Accounting Manual of the Company, the Company is responsible for the proper upkeep of health of wheat stocks and storage in safe and sound condition till its delivery to FCI.

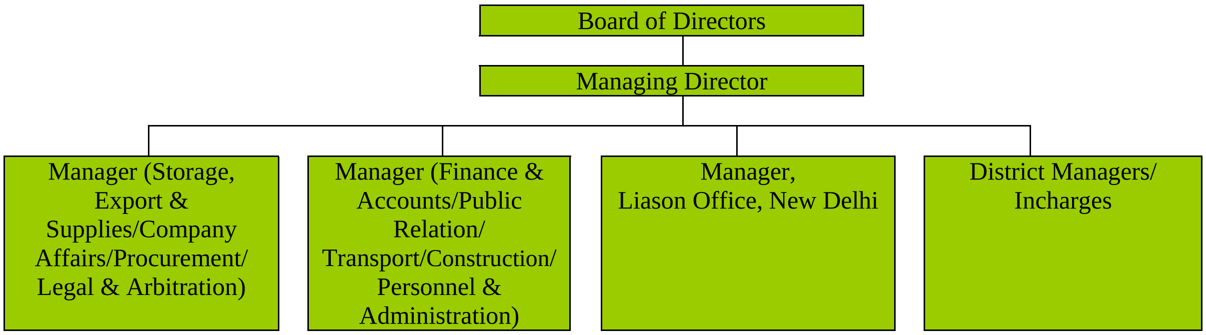
As per instructions of the GOI, the FCI was resorting to sale of foodgrains, i.e., wheat and rice at predetermined rates in the open market under Open Market Sale Scheme (OMSS) from time to time to achieve the following main objectives:

- to enhance the supply of foodgrains especially during the lean season so as to have a healthy and moderating influence on the open market prices; and

- to offload the excess stocks in the central pool so as to reduce the carrying cost of foodgrains to the extent possible and to save the foodgrains from deterioration.

The stock of foodgrains which exceeds the specifications, i.e., extent of damaged grains (six *per cent*), foreign element (three *per cent*), weevilled grains (10 *per cent*), etc., prescribed for foodgrains fit for human consumption is to be termed as damaged foodgrains. Such stocks are required to be disposed of for purposes other than human consumption by offering the same to the State owned departments or agencies thereunder, without entering into trade channel. If such stocks still remain unsold then the same are to be sold through open tenders to the parties registered with FCI after obtaining undertaking that the stocks would not be diverted to the purposes other than for which these were purchased. The GOI authorised (July 2003) the State Government/procuring agencies to liquidate over three year old stocks relating to crop years 1998-99 to 2000-01 under OMSS and later on it authorised (February 2005) the State Government/procuring agencies to dispose of damaged wheat for the crop year upto 2003-04.The Company disposed of 2.09 lakh MT of such stocks of wheat during February 2004 to March 2007 under OMSS/through open tender. As on 31 March 2007, 6,905 MT of damaged wheat was under process of lifting.

The organisational chart of the Company relating to this activity is as follows:



As on 31 March 2007, the Company had 17 district offices (covering 20 districts in the State) each headed by a District Manager/Incharge carrying out this activity.

Scope of Audit

2.2.2 The present performance audit conducted during October 2006–March 2007 evaluates the performance of the Company relating to disposal of damaged wheat under OMSS carried out during 2003–07. The audit findings are based on audit procedures applied to a sample of eight[*] out of 15[#] district offices selected on random sampling basis in addition to the Head Office of the Company. The sample covers 93 *per cent* of the transactions relating to the disposal of damaged wheat during 2003-07.

Audit objectives

2.2.3 The audit objectives were to ascertain whether:

- the Company was able to execute functions relating to categorisation[$] and sale of damaged wheat as per instructions of GOI;
- the categorisation of stocks of wheat and its disposal was appropriate, reliable and transparent;
- the disposal of stocks was made efficiently, effectively and in time;
- all-out endeavours were made to dispose of the foodgrains to State owned departments/agencies before resorting to sale through open tender;
- the bills for differential claims and carry over charges were raised on FCI and payments received thereagainst in time; and

[*] Ferozepur, Faridkot, Hoshiarpur, Jalandhar, Moga, Muktsar, Patiala and Sangrur.
[#] The district offices in which wheat was damaged.
[$] Represents classification of damaged wheat stocks into Feed I to Manure category depending upon extent of damage in it.

- the internal control and monitoring system was commensurate with the size and activities of the Company.

Audit criteria

2.2.4 The following audit criteria were adopted:

- instructions/guidelines issued by the GOI/State Government/FCI regarding categorisation and disposal of damaged wheat;
- instructions of GOI for reimbursement of differential claims and carry over charges;
- recommendations of the Technical Committees set up for categorisation of wheat stocks;
- terms and conditions of tenders and sale orders regarding disposal of damaged wheat;
- norms and time schedule (if any) fixed by FCI for making payments for the bills received from the State procuring agencies; and
- provisions in the Accounting Manual of the Company.

Audit methodology

2.2.5 The following mix of methodologies were adopted to achieve the audit objectives with reference to audit criteria:

- scrutiny of minutes/agenda of meetings of the Board of Directors;
- scrutiny of instructions issued by the GOI/State Government/FCI regarding categorisation and sale of the damaged wheat;
- scrutiny of the analysis reports of damaged wheat;
- scrutiny of tenders for sale of wheat under OMSS and terms and conditions thereof; and
- scrutiny of the Company's records relating to finalisation of sale rates, delivery of damaged wheat to the buyers, raising of claims of differential amounts with FCI and receipt of payment thereagainst.

Audit findings

2.2.6 The Audit findings were reported to the State Government/Management in April 2007 and discussed in the Audit Review Committee for State Public Sector Enterprises (ARCPSE) held on 10 August 2007. The meeting was attended by the Manager (Finance & Accounts) of the Company and

Controller, Food Accounts, Department of Food, Civil Supplies and Consumer Affairs, Government of Punjab. The views expressed in the meeting by the representatives of the Government/ Management have been considered while finalising the performance review.

The shortcomings noticed in Audit during categorisation and disposal of damaged wheat are discussed in the succeeding paragraphs:

Categorisation of damaged wheat stocks

2.2.7 As on June 2003, old wheat stocks (4.36 lakh MT) pertaining to the crop years 1997-98 to 2000-01 were lying with the Company. The FCI in a meeting (June 2003) with heads of procuring agencies stressed upon the agencies to liquidate three years or more old wheat stocks within three months. In another meeting (June 2003) under the chairmanship of the Principal Secretary (Food & Civil Supplies), Government of Punjab, the modalities of identification of non-issuable stocks[♦] of wheat were finalised. All procuring agencies in the State in association with FCI staff identified (January 2004) 4.21 lakh MT as non-issuable stock against total available wheat stock of 12.11 lakh MT available with all the procuring agencies in the State. Out of this, non-issuable stock pertaining to the Company was 1.40 lakh MT. After reviewing the position of disposal of wheat stocks under OMSS in the State, the GOI decided (12 February 2004) that the State Government would set up technical committees for appropriate categorisation of damaged wheat and dispose of the entire stocks by 31 March 2004 through open tenders. It further clarified that no carry over charges[Ω] beyond 31 March 2004 would be admissible to procuring agencies in the State.

During categorisation of wheat stock held by the Company, the quantity of damaged wheat increased to 1.80 lakh MT (crop years 1997-98 to 2000-01) up to August 2004 as per details given in ***Annexure 10***. Data given in the Annexure reveals that in six[♣] district offices, the actual quantity of non-issuable wheat categorised as damaged increased by 42,296 MT between January 2004 to August 2004. Evidently the Company could not save FAQ of its stock from deterioration by proper upkeep. Further, the wheat stocks (28,752 MT) for the crop years 2001-04 were also damaged and categorised up to July 2005. No quantity of stock of foodgrains after the crop year 2003-04 had been declared as damaged by the Company (August 2007).

The Management stated (August 2007) that the accumulation of old stocks and resultant deterioration thereof was due to prolonged storage because of slow pace of movement of wheat stock as adequate movement plan was not being given by FCI. It further added that the Company was regularly taking up the issue with FCI for early lifting of the stock. The reply is not tenable as the Company also failed to get the old stocks lifted as per FIFO principle. Audit contention is further supplemented by the fact that Senior Regional Manager, FCI in a meeting (28 March 2005) pointed out that it was the responsibility of

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[♦] Represents stock of wheat containing damaged grains above six *per cent*.

[Ω] It represents storage charges and interest costs.

[♣] Bathinda , Faridkot, Ferozepur, Muktsar, Patiala and Sangrur.

the State Government to off load the old stocks first, but, this was not done by the procuring agencies.

The details of total stock of wheat of the Company lying before its identification as non-issuable, issuable stock, wheat identified as non-issuable, quantity offered through tenders, quantity cleared and quantity yet to be cleared as on 31 March 2007 was as under:

(Quantity in metric tonnes)

Sl. No.	Crop year	Stock of wheat before its identification as non issuable	Issuable / Upgradable stock	Non issuable stock	Percentage of non issuable to total stock	Quantity offered through tenders	Quantity cleared as good (including shortages)	Quantity cleared against tendered quantity (including shortages)	Quantity yet to be lifted by the parties	Percentage of quantity yet to be lifted to total damaged stock
1.	1997-98	710	--	710	100	710	--	710	--	--
2.	1998-99	32,601	3,373	29,228	90	29,078	150	29,078	--	--
3.	1999-2000	1,70,188	99,210	70,978	42	62,264	8,714	60,010	2,254	3.18
4.	2000-01	2,32,467	1,53,496	78,971	34	78,971	--	75,974	2,997	3.80
5.	2001-02	43,921	23,351	20,570	47	20,570	--	18,916	1,654	8.04
6.	2002-03	6,16,727	6,08,918	7,809	1	7,809	--	7,809	--	--
7.	2003-04	16,23,352	16,22,979	373	--	373	--	373	--	--
	Total	**27,19,966**	**25,11,327**	**2,08,639**	**--**	**1,99,775**	**8,864**	**1,92,870**	**6,905**	**--**

The above table shows that quantity of damaged stock to total stock available as per the categorisation of stock carried out up to August 2004 for the crop years 1997-2001 was very high, ranging between 34 and 100 *per cent*. As per GOI's instructions, the Company was to dispose of the entire damaged stock for the crop years 1997-2001 by 31 March 2004. The Company, however, failed to clear these stocks in time and even after three years of the deadline (March 2004) 5,251 MT of damaged wheat pertaining to crop years 1999-2001 was pending for lifting as on 31 March 2007.

Doubtful categorisation

2.2.8 The stock categorised as damaged denotes that the damaged grains in the stock exceed the limits prescribed for human consumption under the Prevention of Food Adulteration Act (PFA), 1954 and these are not fit for human consumption by any process of reconditioning, cleaning or salvaging.

On being identified as damaged foodgrains jointly by the Company and FCI, the same are to be categorised by the technical committee consisting of officers of procuring agencies and FCI into Feed-I (85 to 94 *per cent* sound grains), Feed-II (70 to less than 85 *per cent* sound grains), Feed-III (55 to less than 70 *per cent* sound grains), Industrial use (30 to less than 55 *per cent* sound grains), Manure use (10 to less than 30 *per cent* sound grains) and Dumping (less than 10 *per cent* sound grains).

Doubtful categorisation as 7,610 MT wheat delivered to FCI was earlier categorised as damaged.

The technical committees of the three[♠] district offices (test checked in audit) categorised 13,030 MT of wheat stock for the crop year 1999-2000 as Feed I-3,486 MT; Feed II- 4,047 MT and Feed III-5,497 MT during February- March 2004. Out of this, 7,610 MT of stock was accepted (March to April 2004) by FCI for the central pool, considering the same to be fit for human

[♠] Faridkot, Sangrur and Muktsar.

consumption. This indicates that the system adopted by the technical committee for categorisation was not foolproof.

The Management during ARCPSE meeting stated (August 2007) that the technical committee headed by FCI declared these stocks as damaged and the same authority had later on accepted these stocks as FAQ as such the Company was saved from the financial loss as it was able to despatch these stocks after segregation/ upgradation as FAQ. The reply is not based on facts because as per guidelines of FCI, the wheat once declared as damaged cannot be made fit for human consumption by any process of reconditioning, cleaning or salvaging.

Sale of damaged wheat

2.2.9 As per guidelines issued (February 2004) by the GOI to the State Government regarding process to be followed for disposal of damaged wheat (which was also being followed by FCI), running rate contracts are to be entered into with the State Government departments (e.g. Animal Husbandry etc.) and other agencies[λ] for disposal of stocks declared fit for cattle feed and poultry feed. If no willingness to accept the stocks is received from the State Government departments/agencies within the prescribed time, the stocks were to be disposed of through All India Open Tenders or by auction amongst the bonafide users registered with FCI.

Audit scrutiny, however, revealed the following shortcomings in disposal of stocks of damaged wheat by the Company:

2.2.10 ***Deficiencies/ irregularities in execution of sale order***

- The damaged wheat stocks were not offered to the State Government departments/agencies, specifically before tendering to private parties, on the plea that the stocks proposed to be disposed of were held by all State procuring agencies and wide publicity had been given to attract maximum buyers including the State Government agencies. The decision making Committee accepted (March 2004) this plea and did not insist on offering these stocks specifically to the State Government departments/ agencies. Since these stocks were to be used by the State Government departments, i.e., Animal Husbandry, Municipal Corporation etc. and not by State procuring agencies, the decision making Committee should have insisted for specifically offering the stocks to these departments before allowing its sale through open tenders. This would have avoided the chances of diversion of damaged stocks by private parties for human consumption.

Accepting lesser amount than required against each release order for sale of damaged wheat to a party resulted in extension of undue favour to him.

- The terms of the sale order issued to a private party[$] provided that an amount (Rs.5.92 crore) equal to the cost of the minimum quantity of 15 *per cent* of total stocks against each release order (value Rs.39.46 crore) be deposited by the firm before issue of release order. The

[λ] Agricultural colleges, Military dairy farms, Municipal or Co-operative dairy farms etc.
[$] Lakshmi Overseas Industries Limited, Chandigarh.

release orders were, however, issued to the party after accepting lesser amount ranging between Rs.2.33 crore and Rs.5.50 crore in five out of seven lots during June–August 2004, resulting in loss of interest of Rs.16.29[#] lakh to the Company and undue favour to the party.

The Management, while admitting the facts, stated (August 2007) that it earned interest on earnest money deposit (EMD) till its refund to the party after clearance of entire stocks. The reply is not tenable as the Company was required to retain EMD till full compliance of sale order in normal course.

In the absence of obtaining disposal plan of damaged wheat from the parties, its use for human consumption could not be vouchsafed by audit.

- The Director, Food, Civil Supplies and Consumer Affairs, Punjab directed (June 2004) the Company to obtain a disposal plan for lifting of the damaged wheat stock from the party lifting the stock. The party was also required to give an undertaking that these stocks would not be diverted/ sold for human consumption. The party[^] lifted (June 2004 to September 2005) total quantity of 83,547 MT of damaged wheat stock. While lifting the stock, the party, however, did not submit the disposal plan for 44,947 MT, which was mandatory. For the remaining quantity of 38,600 MT, it stated (August 2004) that these stocks were exported, but, it did not furnish the copy of agreement or legal undertaking of the exporter for not utilising these stocks for human consumption. Audit further noticed that no disposal plans were obtained from 17 parties which lifted 36,728 MT of damaged stocks during the year 2006-07. Hence, audit could not vouch safe the final utilization of this damaged wheat stock.

The Management stated (August 2007) that the violations on the part of the party after lifting the damaged wheat were to be explained by the purchaser and not by the seller. The reply is not tenable because as per guidelines of the State Government, the Company was required to obtain disposal plans/actual use of damaged wheat from the parties to ensure its use before handing over each lot to the party.

In violation of instructions of GOI, damaged wheat was disposed of without obtaining requisite undertakings.

- The GOI's instructions (February 2004) to FCI and the State Governments for disposal of damaged wheat, *inter alia*, provided, that, release of stock to the bonafide registered parties was subject to their giving an undertaking that the damaged stock would not be used for human consumption. The Company categorised (February- March 2004) 20,074 MT (Patiala 7,441 MT and Muktsar 12,633 MT) as damaged wheat (category ranging from Feed I to Manure). Out of these 1,121.30 MT of damaged stocks sold for Rs.73.16 lakh was lifted by 11 parties. Audit noticed that damaged wheat was given to these parties, without obtaining undertaking regarding non-utilisation of these stock for human consumption in violation of the guidelines of GOI. In the absence of requisite undertaking its utilisation for human consumption could not be vouch safed. The Management during ARCPSE meeting stated (August 2007) that the undertakings obtained

[#] Worked out at the rates of interest on prevailing cash credit limit.

[^] Lakshmi Overseas Industries Limited, Chandigarh.

from the parties would be made available to Audit. No such undertakings were, however, furnished (September 2007).

Loss due to lower fixation of reserve price

2.2.11 A High Level Committee under the Chairmanship of Food & Civil Supplies Minister, Punjab decided (12 February 2004) to initially dispose of 25 *per cent* of the identified stock of non-issuable wheat (1.40 lakh MT) procured during procurement season[$] of crop years 1997-98 to 2000-01 after its proper categorisation through FCI. Accordingly, tenders were invited (February 2004) for disposal of 45,288 MT of damaged wheat on 'as is where is' basis, but, without getting these categorised into various categories of damaged wheat and without indicating any reserve price. The tenders were opened on 9 March 2004. After getting the said stock categorised (February-March 2004) the Company presented (March 2004) lot/centre wise rates received for these stocks to the Decision Making Committee (DMC) as if these were received as category wise. The DMC[#] after scrutinising the offers decided (March 2004) that stocks should not be sold at rates less than Rs.3,500 per MT for Feed I (Group I) and Rs.3,400 per MT for all remaining categories (Group II). This decision was arrived at after considering the following:

- reserve price fixed as per GOI's formula;
- average weighted rates received by all the procuring agencies of the State Government;
- rates obtained by FCI in the last tender; and
- receipt of a formal offer of an exporter by FCI to lift entire damaged stocks in the State at a rate of Rs.350 per quintal.

Loss of Rs. 1.10 crore due to lower fixation of reserve price of damaged wheat.

Audit, however, observed that the fixation of reserve price of Rs 3,500 per MT of Feed I stock (having 89.5 *per cent* average sound grain contents) was on lower side as compared to reserve price of Rs.3,400 of Group II (having average sound grains of 67.65 *per cent*). Even on the basis of reserve price fixation formula of GOI, the reserve price of Feed I was to be 66 *per cent* higher than the reserve price of Group II whereas the actual reserve price of Group I fixed was just three *per cent* higher than that of Group II. Based on sound grain contents of Group II and reserve price thereof, the reserve price of Group I category worked out to Rs 4,498[τ] per MT. The contention of the audit is further supported by the fact, that, 8,747 MT of Group II (against 10,787 MT offered) was disposed of at the rates ranging between Rs. 3,400 and Rs.4,205 per MT. Lower fixation of reserve price of Group I stocks resulted in loss of Rs. 1.10 crore on actual lifting (June-December 2004) of 12,633.17

[$] Procurement season is from April to June.

[#] Comprising Principal Secretary, Food and Supply Department, Sr. Regional Manager, FCI and Managing Directors of all the procuring agencies in the State.

[τ] Rs 3,400/67.65 x 89.5 = Rs.4,498.

MT of damaged wheat stock out of 13,948 MT (56.39 *per cent*) of Group I stock[$] offered for lifting.

The Management stated (August 2007) that the rates accepted were above the FCI reserve price and were based on the recommendations of the decision making Committee. The reply is not tenable as the Company did not secure its financial interest and could not get the reserve price fixed from the DMC based on sound contents of wheat contained in Group I category.

2.2.12 Similarly, Punjab State Warehousing Corporation (PSWC) floated (27 May 2004) a tender for disposal of damaged wheat stocks (crop years 1997-2001) of all the procuring agencies of the State by fixing reserve price of Rs 3,500 and Rs 3,400 per MT for Group I and II stocks, respectively. The intending buyers were to offer the rates for the stocks of at least one procuring agency. Two parties offered their rates for the stocks of the Company and the Inter–Departmental Monitoring and Implementation Committee decided (1 June 2004) to sell these stocks to a party[ψ] (the highest bidder) at Rs.3,830 and Rs.3,512.50 per MT for Group I and Group II stocks, respectively. Accordingly, the sale order was issued (7 June 2004) and party lifted 28,543 MT (Group I) and 55,004 MT (Group II) of damaged wheat.

Keeping in view the average element of sound grains of 68.10 *per cent* in Group II stocks and reserve price of Rs.3,400 per MT thereagainst, the average rates offered for Group I stock (containing average sound grains of 89.5 *per cent*) worked out to Rs.4,468[*] per MT.

Loss of Rs. 1.82 crore due to lower fixation of reserve price of damaged wheat.

Audit noticed that the same firm had offered (May 2004) the rate of Rs.4, 050 per MT for Group I stocks of Punjab Agro Foodgrains Corporation Limited (PAFC) in the same tender. Thus, lower fixation of reserve price (Rs.3, 500 per MT instead of Rs.4,468 per MT) resulted in loss of Rs.1.82 crore to the Company on actual lifting (May 2004 to September 2005) of 28,543 MT of damaged wheat stocks. Even if the Company had stressed upon the party to bring its rates of Group I to Rs.4, 050 (as offered by it to PAFC) the Company would have earned additional sale proceeds of Rs 62.79[#] lakh.

The Management stated (August 2007) that the rates secured were approved by the DMC as being competitive rates above the reserve price of FCI. The Management's contention is not acceptable as financial interests of the Company were not protected while fixing the prices based on the sound contents in the wheat.

Non inclusion of damaged wheat in tender enquiry

2.2.13 GOI directed (February 2004) the State Government to categorise and dispose of the entire damaged wheat stock of crop years 1997-2001 up to 31 March 2004. In pursuance of tender floated (27 May 2004) by PSWC, the

[$] Out of 45,288 MT of total stock 10,787 MT pertained to Group II category and balance 20,533 MT was not qualified for lifting being receipt of rates below reserve price.

[ψ] Lakshmi Overseas Industries Limited, Chandigarh.

[*] Rs.3,400/68.10x89.5= Rs.4,468.

[#] Rs.220 (Rs.4,050-Rs.3,830) x 28,543= Rs.62.79 lakh.

Company issued (7 June 2004) sale order for disposal of 1.09 lakh MT of damaged wheat (pertaining to all the categories except dumping). The terms of sale order provided that the quantity could be increased or decreased at any time during pendency (up to 6 September 2004) of the sale order.

Failure to include damaged quantity in the tender resulted in loss of Rs. 1.30 crore.

Audit scrutiny revealed that the Company failed to include 12,361 MT of wheat (Patiala: 3,829 MT, Muktsar: 2,636 MT and Ferozepur: 5,896 MT) categorised (February 2004) as damaged in the above tender enquiry and also failed to increase the quantity of the sale orders by 16,688[$] MT which was got categorised (up to August 2004) as damaged by the Company. This quantity of 29,049 MT of damaged wheat (12,361 MT and 16,688 MT) was subsequently included in the sale orders (March 2006 to January 2007), out of which, 16,330 MT was lifted (March 2006 to March 2007) and 12,719[#] MT was under lifting process (March 2007). Non inclusion of 29,049 MT in the sale orders (June 2004) resulted in loss of Rs.1.30[*] crore on actual lifted quantity of 16,330 MT of damaged wheat.

The Management in its reply and during ARCPSE meeting stated (August 2007) that quantity included in the tender pertaining to the Company was 1.09 lakh MT for particular stations/lots/plinths and rates were invited for particular stocks kept at those stations only. As such, it was not possible to offer the stocks rejected by FCI during the process of tender/lifting. The reply is not tenable as the Company failed to include (12,361 MT) already categorised as damaged stocks in the tender and also failed to subsequently offer this stock and wheat stock (16,688 MT) categorised during pendency of tender to the party as per terms and conditions of sale order placed on the firm which did not prohibit the Company to get the damaged stocks lifted pertaining to other centres.

Loss due to delayed disposal of damaged stocks

2.2.14 The Company's wheat stock of 0.37 lakh MT pertaining to the crop years 1998-2001 already categorised as damaged (Feed I, Feed II and Feed III) was not disposed of (December 2004). In addition, wheat stocks (0.29 lakh MT) for the crop years 2001-04 got damaged (Feed I to Manure) subsequently and were also got categorised as damaged stocks. The GOI accorded approval (February 2005) for the disposal of these stocks, which was communicated late to the Company by the State Government (July 2005). The State Government, however, directed (October 2005) all the procuring agencies to defer the disposal of damaged wheat immediately.

It was noticed in Audit, that, the State Government had deferred the disposal of damaged wheat because some private parties had filed (September 2005) writ petition in Punjab and Haryana High Court against the procuring agencies excluding the Company for sale of damaged wheat. FCI asked (November 2005) the State Government to comply with the directions of GOI clearly

[$] Pertaining to district offices Patiala, Moga, Muktsar and Faridkot.

[#] The shortages would be identified when whole quantity of damaged wheat of these centres is lifted.

[*] Carry over charges: Rs.1.95 crore less Rs.0.65 crore realised excess due to its subsequent sale.

stating that the State procuring agencies would have to bear the storage loss on account of damage to central pool stocks. After this the State Government decided (January 2006) to allow those procuring agencies to dispose of their stocks, which were not involved in the litigation. Though, the Company initiated action for disposal (February 2006) of its stocks, yet, it could dispose of only 51,996* MT of stock till March 2007 leaving a balance of 6,905 MT. The delayed communication of GOI's instructions coupled with blanket ban imposed (October 2005) on disposal of damaged wheat by the State Government on procuring agencies (including procuring agencies which were not involved in litigation) caused postponement of sale realisation from the parties and FCI. Failure of the Company to take up the matter with the State Government effectively bringing full facts of the case led to loss of Rs.1.18 crore (loss of interest: Rs.1.13 crore on the blocked sale proceeds and storage charges: Rs.0.05 crore from March$^{\Sigma}$ 2005 to January 2006).

Unjustified delay in disposal of damaged wheat resulted in loss of Rs.1.18 crore.

The Management stated (August 2007) that it took up the matter with the State Government (November 2004 to June 2005) for allowing it to dispose of the stock but the State Government deferred the disposal of such stocks (October 2005). The reply is not tenable as the Company took no action to dispose of the damaged wheat during July to September 2005. Further, as, regards State Government's deferment order (October 2005) since the Company was not a party to the litigation it should have obtained State Government's permission for disposal of damaged stock.

Doubtful reimbursement of loss

2.2.15 Under the OMSS, the GOI had fixed (June 2003 to June 2005) the rates per quintal ranging between Rs.660 and Rs.790 (up to September 2005) and Rs.670 and Rs.800 per quintal (from October 2005 onwards) for the crop years 1997-2004 for disposal of wheat. FCI was to reimburse the difference in economic price@ of wheat and OMSS price to the Company. As regards reimbursement of difference of OMSS price and actual sale price of downgraded stocks, decision was to be taken by the GOI after examining the justification based on the requisite details submitted by the State procuring agencies/State Government.

Recovery of Rs.44 crore, being difference of OMSS price and actual sale of damaged wheat at lower rates was doubtful as Company's damaged wheat stock exceeded the norms suggested by a Committee of FCI.

While disposing the damaged wheat stocks through open tenders, the Company got less rates than the OMSS rates, but, could not get reimbursement from FCI of the difference between OMSS rates and actual rates received by it as the circumstances that led to damage in each case were not furnished with the claim. Audit scrutiny of records of eight districts offices revealed that the Company disposed (May 2004 to March 2007) damaged wheat at the rates ranging between Rs.151 and Rs.571.87 per quintal. But, the Company had not got the reimbursement of Rs.44 crore from the FCI in actual lifting of 1.32 lakh MT of damaged wheat (Feed I to Manure category) procured during April 1997 to May 2004, so far. The matter for reimbursement of loss suffered by

* Pertaining to eight district offices.

$^{\Sigma}$ The loss has been worked out from March 2005 since GOI's instructions in this regard were issued in February 2005.

@ Means rates at which good wheat is delivered to FCI.

the Company for the quantity of damaged wheat disposed of up to December 2004[*] was taken up (January 2005) with the State Government/GOI. The GOI directed (March 2005) the State Government to submit the details of the circumstances in each case under which stock got damaged, clearly indicating the nature of investigation/enquiry conducted.

Audit noticed that the process of 48[@] enquiries (involving recoverable amount of Rs.44 crore) instituted by the Company at the instance of GOI during April 2004 to March 2007 was still in progress (August 2007). In these cases, the Management failed to finalise the departmental action (except in one case) against the defaulting employees (September 2007).

Further, for deciding the matter, in a meeting held (June 2007) under the chairmanship of Joint Secretary (Policy & FCI) the GOI directed that General Manager (Quality Control), FCI along with officers of the State Government would work out within one month, lot wise quantity of damaged stocks and determine the quantity which were within the norms (ranging between 0.2 and 2.40 *per cent* on the basis of period of storage) suggested by the Committee formed by FCI. Further developments were awaited (July 2007). Audit noticed that negligible quantity (0.80 *per cent*) of damaged wheat of the Company was within these norms.

The Management stated (August 2007) that the case concerning differential loss between OMSS rate and sale rate has been taken up (April 2005) by the State Government with the GOI. The matter is under their consideration and is being pursued vigorously by the State Government on behalf of all the procuring agencies. However, reimbursement of loss on this account appears remote, in view of the fact that damage to wheat was more than the norms suggested (February 2006) by a Committee set up by FCI.

Differential claims

Delayed/ short raising of differential claims

Delayed raising of differential claims on FCI resulted in interest loss of Rs. 1.01 crore.

2.2.16 After the sale of damaged wheat under OMSS, the Company was to claim differential amount (economic cost less OMSS price) from the FCI, but the Company had not fixed the time limit for raising the differential claims on FCI after lifting of stock. It was noticed that there were 164 (out of 188 cases test checked) cases of delayed raising of claims ranging between two and 249 days (computed after allowing a margin of seven days from the lifting of stock of a particular lot) causing loss of interest of Rs 1.01 crore[Φ] to the Company. The Company did not analyse the reasons for delayed raising of claims.

The Management stated (August 2007) that the matter was being enquired into

[*] The matter for reimbursement of loss on this account for disposal of damaged wheat during 2005-07 was not taken up with GOI as lifting of damaged wheat was still in progress (March 2007).

[@] Out of 48 enquiries, 45 pertained to shortages of wheat stocks also as referred to in paragraph 2.2.20 *infra*.

[Φ] Worked out at the prevailing rates of interest on cash credit limit.

about particular delay caused by the district offices and responsibility was being fixed.

Audit analysis (October 2006 to March 2007) of the differential claims in Ferozepur district office revealed that the claim of Rs.22.54 lakh was short raised with FCI due to incorrect application of OMSS rates. Thereafter, the Company submitted (February 2007) revised claim on FCI. The payment thereof had not been received so far (July 2007).

Interest claims for delay in payment by FCI

2.2.17 FCI instructions (December 1970) provide for payment of sale bills of wheat to the procuring agencies within 24 hours of presentation. The Director, Food, Civil Supplies & Consumer Affairs, Punjab also conveyed (December 2001) to the procuring agencies, the GOI decision taken in a meeting that FCI was liable to pay interest at the bank rate in case of delay in release of payments beyond the prescribed period.

Failure to raise claims of interest on FCI resulted in non-recovery of interest of Rs. 46.46 lakh.

Audit scrutiny revealed that although payments of differential claims were abnormally delayed by FCI ranging between 30 and 484 days (after excluding the prescribed period) in 53 cases yet interest bills for delayed payments were not raised by the Company (Accounts Wing) resulting in non recovery of interest of Rs.46.46 lakh. It was further noticed that only three district offices[@] of the Company had partially raised (April 2005-Februatry 2007) the interest claims for Rs.6.24 lakh and payments thereof had not been received (March 2007).

The Management stated (August 2007) that the concerned district managers (Jalandhar, Hoshiarpur and Patiala) were pursuing the matter with FCI for payment of interest on delayed payments. However, the Management did not furnish reasons for partial raising of claims by these district offices and non raising of requisite claims by other district offices.

Deductions on account of gunny bags

2.2.18 At the time of procurement and storage, wheat is filled in the gunny bags on the basis of their filling capacity. Owing to deterioration in the quality of wheat due to long storage, substantial quantity of stock becomes short due to weeviling[*], atta formation, etc. Thus, the quantity of the damaged wheat stock filled therein gets reduced. FCI was, however, making deductions on account of excessive gunnies used by the Company on the basis of actual damaged quantity lifted. Such deductions made by FCI from the sale bills (March 2004 to April 2007) in respect of eight district offices amounted to Rs.93.57 lakh. In the case of Patiala district office, deductions from differential bills (September 2004 to February 2005) were not yet made by FCI. The loss on this account would further increase as deduction can be made by FCI at any time pertaining to these bills. The Company had included loss on this account in the chargesheets of the concerned officials.

[@] Patiala, Jalandhar and Hoshiarpur.
[*] It means grains that are partially or wholly bored.

The Management stated (August 2007) that the matter was taken up with Senior Regional Manager, FCI for unjustified deductions made by FCI. No document in support of it was, however, furnished to Audit.

Doubtful reimbursement of carry over charges

Doubtful reimbursement of carry over charges of Rs. 11.35 crore due to excessive damage to wheat stocks.

2.2.19 The State Government while apprising (February 2004) the procurement agencies of the instructions of GOI directed them to ensure disposal of entire damaged stocks pertaining to crop years 1997-2001 after categorisation by 31 March 2004, as, otherwise it would not be entitled to reimbursement of carry over charges beyond this date from FCI. The Company, however, failed to dispose of any quantity of categorised/ damaged wheat stock by that date. Further for the disposal of damaged wheat for the crop years 2001-04, GOI also restricted (February 2005) the payment of carryover charges upto 31 March 2004. Audit scrutiny of records of eight district offices of the Company, revealed that out of 1.85 lakh MT of categorised/ damaged wheat (Feed I to Manure category) for the crop years 1997-2004 offered to the parties through open tenders, the parties lifted only 1.32[#] lakh MT of stocks (June 2004 to March 2007). Non-disposal of stocks within the stipulated period deprived the Company of reimbursement of carry over charges[@] of Rs.11.35 crore incurred during April 2004 to the month of actual lifting of stocks by the parties.

The Management stated (August 2007) that the matter has already been taken up by the State Government with GOI for reimbursement of carry over charges beyond 31 March 2004. The reply is not tenable as the chances of recovery of carry over charges are remote because as per GOI's instructions, these were to be reimbursed only upto 31 March 2004 even if the stock was cleared beyond this cut off date.

Shortage of wheat stocks

There were shortages of wheat stocks valuing Rs. 44.29 crore but the Company failed to take final action against the delinquent officials.

2.2.20 Due to improper upkeep of wheat stock over long period, it is obvious that not only quality will deteriorate, but, shortage may also occur due to weight loss, pilferage and exposure to pests. Scrutiny of records of eight district offices of the Company, revealed that against the sale orders (issued during May 2004 to January 2007) for damaged wheat of 1.94 lakh MT (all categories except dumping), 1.43[$] lakh MT was lifted by the parties (March 2007) and 0.13[#] lakh MT was under the process of lifting. Balance quantity of 0.38 lakh MT of wheat valuing Rs. 44.29 crore was found short.

Out of 32 centres, such shortages in 28 centres ranged between 2.16 and 58.06 *per cent* of the damaged wheat as per details given in ***Annexure 11***. It was

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[#] The balance of 0.53 lakh MT represents shortage: 0.37 lakh MT, quantity lifted but unbilled: 0.03 lakh MT and lifting under progress/unlifted: 0.13 lakh MT

[@] Represents storage charges and interest.

[$] Represents quantity lifted as damaged against tenders: 1.32 lakh MT and lifted as good/under OMSS, etc, 0.11 lakh MT.

[#] In certain cases shortages were not identifiable as balance quantity at plinths were not yet lifted (March 2007).

further noticed, that the main cause for such huge shortages were inadequate measures taken to maintain good health of stock during storage and accumulation of old wheat stock due to non-following of FIFO method of delivery of wheat stocks to FCI. This caused deterioration in quality of wheat stocks resulting in shortages due to weight loss. The Company issued chargesheets to the 66 erring officers/officials and enquiries thereagainst were initiated from April 2004 onwards. Scrutiny of these chargesheets revealed as under:

- The process of finalisation of action against chargesheeted employees was very slow as out of 45 cases initiated during April 2004 to April 2007, enquiries have been completed (January 2005 to January 2007) in 15 cases. But in none of the case, final action has been taken (September 2007);

- In 16 cases, amount involved in the chargesheets against employees exceeded rupees one crore each;

- Seventeen[*] officials against whom chargesheets involving Rs.24.26 crore were issued, were no more in the service of the Company; and.

- In 15 cases, results of enquiries were submitted (January 2005 to January 2007) within period ranging between six and 22 months from the initiation of enquiries against the norm of four months. In 20 cases, results of enquiries were awaited (March 2007). In remaining cases, chargesheets were under issue (seven cases), enquiry officers were yet to be appointed (two cases) and the official had expired before issue of chargesheet in one case.

The Management stated (August 2007) that enquiries were being finalised. It was, however, noticed in Audit that process of finalisation of enquiries was very slow. Further, in respect of officials who were no longer in the service, the amount of gratuity and other retirement dues payable to them had not been worked out by the Company.

Internal control

2.2.21 Internal control is an essential pre-requisite for efficient and effective management of the organisation. Internal control in the Company was deficient on account of following:

Deficient internal control

- It did not have effective control over periodical progress of categorisation of damaged wheat and its timely disposal.

- It did not fix norms for raising of claims with FCI to protect its financial interests.

[*] Thirteen retired: Rs.15.48 crore, two expired: Rs.4.79 crore and two dismissed: Rs.3.99 crore.

- It did not ensure obtaining of requisite undertakings/disposal plans from parties.
- It failed to monitor the violation of delivery of wheat on principle of FIFO and take action against erring officials.
- It failed to conduct physical verification of wheat stocks as per weighment norms prescribed in the Accounting Manual of the Company.

Conclusion

The Company failed to strictly observe FIFO method in despatch of wheat stocks which led to accumulation of old wheat stocks and its further deterioration. The Company also failed in getting the damaged wheat stocks categorised and disposed of timely with the result, it had to bear carrying cost. There was no system to ensure timely raising of differential claims and interest claims on FCI. It also failed to finalise departmental enquiries against its officers/officials involved in damage/shortage of wheat stocks.

Recommendations

- **The Company should redefine and restructure its system for speedy and efficient delivery of wheat stock on principle of FIFO to avoid damage to foodgrain stocks.**
- **A system of timely disposal of damaged wheat stocks on priority needs to be devised to avoid loss on account of carry over charges.**
- **Obtaining of undertakings/disposal plans in respect of damaged stock lifted by parties to avoid its misutilisation should be made mandatory by the Company.**
- **The Company should fix strict time frame for raising differential claims on FCI. Similarly, interest on delayed payments should be pursued with FCI on priority.**
- **Departmental enquiries against defaulting officers /officials are required to be finalised expeditiously by framing time bound programme.**

The above matter was referred to the Government in April 2007; their reply had not been received (September 2007).