

## Chapter 4 Construction, Operation and Maintenance of 'Project Railway'

### 4.1 Highlights

- Even after completion of the work in March 2003, the completion report has not been prepared so far. In the absence of this the Railway was not able to recover an amount of Rs.17.88 crore from PRCL on account of Rs.0.89 crore required for removal of deficiencies, Rs.0.96 crore for pending contractual liabilities, Rs.7.74 crore as cost of material and Rs.8.29 crore on account of Departmental and General charges.  
*(Paras 4.8.1 & 4.8.2.1 to 4.8.2.4)*
- Railway's action to enter into agreement allowing the procurement of track and S&T material by PRCL has resulted in extra expenditure of Rs.28.36 crore.  
*(Para 4.8.3)*
- Underestimation of cost of existing assets of Railways leased to PRCL has resulted in loss of lease rental of Rs.15.24 crore. There would be a recurring loss of Rs.3.81 crore per annum for the entire lease period if corrective action is not taken.  
*(Para 4.8.5)*
- The Railway was yet to receive Rs.22.79 crore on account of operation and maintenance charges for the year 2003-04 and 2004-05 due in the year 2005-06. Moreover, the amount on account of fixed cost of material for the year 2004-05 is yet to be assessed.  
*(Para 4.8.6.1)*
- Despite specific provision in the agreement for recovery of compensation for the shortfall in guaranteed traffic, no action was taken by the Railway for recovery of compensation of Rs.66.17 crore from PRCL.  
*(Para 4.8.6.2)*

### 4.2 Recommendations

- Western Railway carried out the construction of 'Project Railway' as deposit work, therefore, they should follow rules strictly and obtain requisite funds in advance to avoid spending from their own resources.
- The Railway should either recover the agreed compensation cost from PRCL or take action for breach of agreement against PRCL as the guaranteed traffic has not been offered by them even after four years of commissioning the project.
- The Railway should follow the codal provisions for contract management and assessment of the cost of existing assets so that their interests are not compromised.

#### **4.3 Introduction**

The work of Gauge conversion of Meter Gauge section from Surendranagar-Bhavnagar- Dhola-Dhasa- Mahua with extension up to Pipavav was initially included in the Works Programme for the year 1996-97 at an estimated cost of Rs.1.00 crore chargeable to Railway's Capital. Accordingly, sub estimate of Rs.66.51 crore for civil portion of the works was sanctioned in February 1999 and works commenced. Subsequently Gujarat Pipavav Port Limited (GPPL) approached Railway with a proposal to convert the MG section into BG through a joint venture. Accordingly Railway Board and GPPL signed (January 2000) a Memorandum of Understanding (MOU) for formation of a Special Purpose Vehicle (SPV) for the gauge conversion of Surendranagar - Pipavav line. The project was to be funded through Equity Share Holding to the extent of 66.67 per cent of the total cost of project. Railway and GPPL were to contribute 50 per cent each in a company namely Pipavav Railway Corporation Private Limited (PRCL). As provided in the MOU the Western Railway was to construct, operate and maintain the 'Project Railway' as provided in 'concession', construction, lease, operation and maintenance agreements entered between Western Railway and PRCL.

#### **4.4 Audit objectives**

Keeping in view that the Western Railway was responsible for construction, maintenance and operations of the 'Project Railways' the following audit objectives were set to carry out the review:

- Whether the construction activities were carried out in accordance with the 'construction agreement' and whether the expenditure incurred by Railway was recovered from PRCL.
- Whether the existing assets required to be leased to PRCL were evaluated as per codal provisions and lease charges recovered accordingly.
- Whether the safeguards provided in the 'transportation and traffic guarantee' agreement were followed.

#### **4.5 Scope of Audit**

To study and evaluate the performance of Western Railway who carried out the work on 'deposit terms' during the period 1999-2000 to 2006-07 in detail concentrating on areas of planning, contract management, execution of the project and operation and maintenance of the Broad Gauge line.

#### **4.6 Audit Criteria**

The rules and provisions contained in the various codes applicable over Indian Railways as also relevant agreements and the guidelines and instructions issued by the Railway Board from time to time were taken as criteria for assessing the performance of the Western Railway in achievement of goals of the project.

#### **4.7 Audit Methodology**

Files and records in the office of Chief Project Manager and his field offices and in the office of Divisional Railway Manager, Bhavnagar were examined and information was collected through comparison of data, analysis, interaction with personnel and through questionnaires. Various agreements executed with PRCL were also examined critically. Records relating to Civil engineering, signal and electrical branches were taken up for review. Records of traffic handled by the project railway were also examined.

#### **4.8 Audit Findings**

PRCL appointed Western Railway as the Engineering, Procurement and Construction agency for carrying out the construction works and commissioning of the 'Project Railway' as a special Deposit work. During Audit of the records the following deficiencies were noticed.

##### **4.8.1 Non-preparation of completion Report of Project**

Entire Meter Gauge section was divided into ten sections, out of which six sections from Surendranagar to Pipavav were to be executed under SPV and remaining four section were to be executed with Railway's own funds as Non-SPV project. The Railway Board, in September 2000 sanctioned detailed estimates at a cost of Rs.423.63 Crore of which Rs.294 Crore was to be borne by PRCL for SPV portion and the balance cost Rs.129.63 crore was to be borne by Railway being non-SPV portion. The Project work was completed in March 2003 and opened to goods traffic on 27 April 2003. Subsequently in September 2003, the Project estimate was revised to Rs.528.49 crore and the cost of SPV portion was assessed at Rs.339.43 crore. Audit observed that the completion report of the project has not been prepared by Western Railway Construction Organisation even after four and half years of commissioning. As a result of this it could not be ensured whether the Railway has recovered the entire expenditure incurred on the construction of the project.

##### **4.8.2 Non-recovery of expenditure incurred/required to be incurred**

In terms of para 11 of the 'construction agreement' Western Railway was to submit a statement specifying requirement of funds for the next month and PRCL was to deposit the same in advance. Similarly in terms of Para 4 of the said agreement WR was to procure all material required for construction work except the material to be supplied free by PRCL. The free material was to be handed over to WR at the site of work. In case of delay in supply of free material causing delay in construction, the resultant cost was to be borne by PRCL. Audit scrutiny of records revealed the following:

###### **4.8.2.1 Non-removal of deficiencies in the track**

A joint inspection carried out prior to handing over of the newly converted section to open line had revealed deficiencies in the work such as shortage of ballast, cess repair and earth work, toe wall etc. As per estimate funds of Rs.1.09 were required for rectification of these deficiencies. Open Line has already incurred expenditure of Rs.0.33 crore on removal of deficiencies of

which construction organisation adjusted expenditure of Rs.0.20 crore against SPV work and balance expenditure of Rs.0.13 crore still awaits adjustments for want of deposits from PRCL. Balance works valuing Rs.0.76 crore for removal of deficiencies are still pending to be carried out as PRCL has not deposited the requisite amount with Railways. Thus an amount of Rs.0.89 crore was still recoverable from PRCL.

#### **4.8.2.2 Non clearance of outstanding contractual Liabilities**

Contractual liabilities amounting to Rs.0.96 crore were pending for want of requisite funds from PRCL. During the meeting with PRCL officials by the Chief Project Manager, Western Railway, Ahmedabad in May 2007 the pending amount has been accepted by PRCL. The realisation of dues however will materialise only after finalisation of the pending contracts during the year 2007-08. The delay of more than four years in clearance of contractual liabilities indicates that funds requirement was not assessed properly. Non-payment to contractors for such a long period may create unnecessary financial obligations.

#### **4.8.2.3 Non-Recovery of cost of materials supplied by Railway**

Though all the Permanent Way material such as rails, sleepers, fittings and the cable etc were to be supplied free by the PRCL, Railway Administration has issued P. Way materials worth Rs.2.79 crore and S& T cable worth Rs.2.72 crore for completion of works. Railway has incurred an expenditure of Rs.1.45 crore on transportation charges of rail panels for laying and linking and Rs.0.78 crore for transportation of surplus P. Way materials. Though Railway has been requesting the PRCL to pay the cost of the material and transportation charges, the amount of Rs.7.74 crore is still not recovered.

#### **4.8.2.4 Loss due to short booking of expenditure under general Charges**

As per Para 10.2 of the 'construction agreement' Departmental and General charges were payable to Railway on the basis of actual cost incurred for the project subject to a maximum of six per cent of the cost as per detailed estimate. The construction organization of WR who is engaged in various construction activities simultaneously has not maintained separate records for actual expenditure incurred on the establishment and other related activities. Audit noticed that provision of Rs.17.47 crore at the rate of 6.43 per cent of the cost of SPV portion of the work was made in the revised estimate sanctioned in September 2000. As against this WR has booked an expenditure of Rs.12.08 crore only leaving a shortfall of Rs.5.39 crore. Even if the D&G charges were to be restricted to a maximum of 6 per cent, a sum of Rs.20.37 crore was recoverable from PRCL against which only 12.08 crore had been adjusted. Thus an amount of Rs.8.29 crore has been short recovered.

#### **4.8.3 Loss due to procurement of materials at higher rates**

As per para 4 of the 'construction agreement', WR was to procure all materials required for construction works of the project except the rails and fastenings, sleepers and fittings, ballast, turnouts, cables and point machine which were to be supplied by PRCL. A comparison of cost of material procured by PRCL

with that of similar items procured by WR conducted by Deputy FA & CAO(C) Ahmedabad revealed that the rates paid by PRCL in procurement of 53 items were more than the rates paid by Railways. PRCL had incurred a total excess expenditure of Rs.28.36 crore. Since Railway is 50 per partner in the project, it has to bear a loss of Rs.14.18 crore due to procurement of materials at higher rates. This shows lack of proper planning and analysis regarding procurement of materials while framing the agreement.

#### **4.8.4 Loss due to incorrect allocation of credit of released materials**

As per clause 10.5 of the 'construction agreement' all the materials released as a result of replacement by new assets would be the property of Railway and credit if any realized out of its disposal would be retained by Railway. It is noticed from the work registers maintained by Accounts that Railway realized credit of released materials to the tune of Rs.0.20 crore up to March, 2003 under capital head and Rs.0.17 crore (up to August 2006) under Deposit head which was passed on to the PRCL. Thus credit of released materials to the tune of Rs.0.37 crore to PRCL is in contravention of the provisions made in the agreement and resulted in loss to the railway. Moreover, a scrutiny of revised estimate for SPV portion of the project sanctioned in September 2003 revealed that WR has made a provision of Rs.32.62 crore on account of credit for released material. Railway is yet to afford the exact credit on this account. It has, therefore, to be ensured that the benefit of cost of released material is not passed to PRCL.

#### **4.8.5 Deficiencies in assessment of cost of assets leased to PRCL**

In terms of 'lease agreement' the existing assets of the section as well as land to be acquired afresh was to be leased to PRCL and lease rent equal to prime lending rate prevailing on the date of execution of the agreement applicable for the book value of the assets was to be recovered. Audit observed that as against the book value of Rs.44.18 crore prepared by the Chief Engineer, WR for the existing assets and estimated cost of Rs.4.04 crore for the new land acquired, Railway adopted a cost of Rs.14.06 as value of existing assets and Rs.2.4 crore for the new land for calculation and recovery of lease charges. Thus the underestimation of the cost of existing assets as well as non adoption of exact value of newly acquired land has already resulted in loss of Rs.15.24 crore due to less realisation of leased rent. The Railway would be incurring a loss of Rs.3.81 crore per annum for the lease period of 33 years if the discrepancy is not set right.

#### **4.8.6 Deficiencies in operation, Maintenance and traffic transportation**

In terms of Para 2 of the Operation and Maintenance (O&M) agreement, immediately on certification of the section for freight operations, the assets (existing as well as old) were to be deemed to have been taken over by Railway for operation of freight movement and maintenance. Audit scrutiny of the operations and maintenance records revealed as under:

#### 4.8.6.1 Non-recovery of Operation and Maintenance charges

In terms of Para 3 of the 'O&M agreement' PRCL was to pay O&M cost to the Railway for carrying out the operation and maintenance. O&M charges were to be in two parts viz. fixed cost of staff deployed for the operations and maintenance and variable costs. The work on SPV portion of the project was completed and operations were commenced from March 2003.

Railway Board, however, deferred (September 2004) the recovery of O&M charges due for the year 2003-04 and 2004-05 and decided to recover the same from third year onward. In January 2007, Railway Board accepted the proposal of PRCL for deferment of payment of O & M charges for the year 2005-06 to 2007-08 and decided that these charges along with interest at the rate of seven per cent would be recovered in three equal installments beginning from 2008-09. It implies that the O&M charges for the first two years of operation were to be recovered in 2005-06.

Audit scrutiny of records revealed that WR had raised bills for O & M charges of Rs.46.99 crore (up to September 2007). Audit observed that while the bill of Rs.13.36 crore raised for 2003-04 included fixed and variable costs, the bill of Rs.9.43 crore for year 2004-05 was raised only for fixed cost (staff costs excluding material cost) and variable cost. Even this amount of 22.79 crore which should have been recovered in 2005-06 was not paid by PRCL. The amount on account of fixed cost on account of material for the year 2004-05 could not be assessed in audit.

#### 4.8.6.2 Non recovery of compensation for non-achieving targets of traffic

As per para 3.1 of the 'transportation and traffic guarantee agreement' (January 2003), the GPPL guaranteed a minimum annual aggregated quantity of its freight cargo equal to one million tonnes in the first year, two million tonnes in the second year and three million tonnes from the third year onwards till the termination of the concession period. For the purpose of Minimum Guaranteed Quantity (MGQ), both inward and outward freight traffic of the port shall be counted. In terms of para 3.2, GPPL was to compensate the Railway for non-fulfillment of the MGQ. The compensation payable was to be computed by a formula viz. [rate per tonne kilometer x 264(length of the project railway) x shortfall quantity] - the variable costs pertaining to the shortfall quantity.

As can be seen from the table given below the quantity offered by GPPL fell short by 67.12 per cent to 82.62 per cent.

(in Tonnes)

Year	Target (MGQ)	Actual traffic handled			Total	Shortfall	
		Inward	Outward	Container		Quantity	percentage
2003-04	1000000	186636	14501	63210	264347	735653	73.56
2004-05	2000000	0	0	347580	347580	1652420	82.62
2005-06	3000000	0	100919	458700	559619	2440381	81.34
2006-07	3000000	0	518453	467760	986213	2013787	67.12
Total	9000000	186636	633873	1337250	2157759	6842241	76.02

Audit also observed that despite specific provision in the agreement for recovery of compensation for the shortfall, no action was taken by WR for recovery. The compensation due works out to Rs.66.17 crore.

#### **4.9 Conclusion**

Despite various management control systems provided in the Code books to monitor and evaluate the implementation, execution and functioning of the various schemes/projects and offices, the viability of the joint venture was not properly assessed by Railways as can be seen from the fact that PRCL failed to provide adequate funds required for completion of the project. They even failed to bear expenditure on account of maintenance of the project railway which is vital for successful operation of any project. It is therefore utmost necessary to critically evaluate the financial capabilities of the associated partner of the joint venture before entering into any commitment with them to avoid any financial crunch in execution and operation & maintenance of the Project Railway in future.