

Chapter-2

Performance Audit

Chapter - 2

Performance Audit of Government Companies

Punjab Agro Foodgrains Corporation Limited

2.1 Procurement, Storage and Custom Milling of paddy

Executive Summary

Punjab Agro Foodgrains Corporation Limited was incorporated in July 2002 as a wholly owned subsidiary of Punjab Agro Industries Corporation Limited mainly for handling the activities relating to the procurement of foodgrains. The important findings are as under:

Company did not consider the desirability to fix the transportation rate on per quintal per km basis to bring uniformity which resulted in extra burden of ₹ 4.03 crore on the Company during 2010-14.

(Paragraph 2.1.8.2)

Expenditure amounting to ₹ 20.71 crore on transportation of paddy to rice mills within 8 kms was not recovered from the millers though these were inbuilt in the milling charges.

(Paragraph 2.1.8.3)

Against the weighted average period of two months allowed by GoI for milling of paddy, the State Government without compensating the Company allowed excess milling period in the CMPs resulting in loss of interest of ₹ 188.87 crore during crop years 2010-14.

(Paragraph 2.1.9.1)

An amount of ₹ 143.11 crore was recoverable from the millers on account of short delivered/ misappropriated rice, cost of gunnies and other recoveries.

(Paragraphs 2.1.9.2)

The Company neither preferred reimbursement of ₹ 13.07 crore, the remaining cost of bags from FCI as per the guidelines, nor took up the matter with GoI for finalisation of rates for once used gunny bags.

(Paragraphs 2.1.10.3)

Introduction

2.1.1 Punjab Agro Foodgrains Corporation Limited (Company) was incorporated in July 2002 as a wholly owned subsidiary of Punjab Agro Industries Corporation Limited (holding company) mainly for handling the activities relating to the procurement of foodgrains. The Company is one of the five¹ State foodgrains procurement agencies entrusted with procurement of foodgrains in the State and its share was nine *per cent* of paddy procured in the State during the year 2014-15. It procures paddy from various mandis allotted to it by the Food, Civil Supplies & Consumers Affairs Department (FS&D) of the State at Minimum Support Price (MSP) fixed by the Government of India (GoI) for each crop year, which is then got milled from the authorised rice millers at specified rates under Custom Milling Policy (CMP) framed by the State Government for each year. The resultant rice is delivered to Food Corporation of India (FCI) for central pool at rates fixed by GoI for each crop year.

The Company procured 60.40 lakh metric tonne (MT) of paddy of ₹ 9141.38 crore during crop years 2010-15 and delivered 39.31 lakh MT resultant rice valued at ₹ 8941.76 crore to FCI during the same period.

Organisational set up

2.1.2 The management of the Company is vested in a Board of Directors (BOD). As on 31 March 2015, the Board comprised five directors including Chairman and Managing Director (CMD), who is the Chief Executive of the Company. All the Directors including the CMD are appointed by the State Government. There are 20 district offices² carrying out the procurement and milling operations.

Audit Objectives

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

- The Company utilised the sanctioned cash credit limits efficiently and received reimbursement of guarantee fees and other statutory levies imposed by the State Government;
- The Company executed functions relating to procurement, storage, transport, custom milling of paddy and delivery of resultant rice in an efficient, effective and economical manner and as per the prescribed norms;

¹ Punjab Agro Foodgrains Corporation Limited (PAFCL), Punjab State Civil Supplies Corporation Limited (PUNSUP), Punjab State Grains Procurement Corporation Limited (PUNGRAIN), Punjab State Warehousing Corporation (PSWC) and Punjab State Co-operative Supplies and Marketing Federation Limited (MARKFED).

² Ludhiana, Sangrur, Barnala, Patiala, Moga, Mansa, Kapurthala, Faridkot, Hoshiarpur, Ropar, Mohali, Jalandhar, Amritsar, Tarantaran, Ferozepur, Mukatsar, Gurdaspur, Fatehgarh Sahib, Nawanshahar and Bathinda.

- The Company delivered rice to FCI within the stipulated / extended period fixed by GoI and raised bills within the stipulated period;
- The Company had an effective internal control system.

Scope of Audit and Methodology

2.1.4 The issue regarding procurement and milling of paddy for central pool by Punjab Agro Foodgrains Corporation Limited was last reviewed in the Report of the Comptroller and Auditor General of India, Government of Punjab (Commercial) for the year 2005-2006. The Performance Audit was discussed (February 2015) by the Committee on Public Undertaking and was remitted to the Administrative Secretary for taking further action at their level. No further action has been initiated by the Administrative Department so far (September 2015). Audit observed that no concrete action was taken on issues such as use of cash credit facility and guarantee fee, delayed raising of claims/ non-recovery/ delayed recovery of receivables from millers/ FCI, losses in procurement and milling operations, etc. and are still continuing.

The present performance audit conducted between November 2014 and March 2015 covers the activities of procurement and milling of paddy for central pool during the years 2010-11 to 2014-15. The audit examination involved scrutiny of records at the head office and seven³ out of 20 district offices selected on the basis of Probability Proportional to Size sampling method, which covered 53.10 *per cent* of the total paddy procured by the Company during 2010-15. We explained the audit objectives to the Company and representative of the Administrative Department during an entry conference (January 2015). Audit findings were reported to the Company and the State Government (June 2015) and discussed in the exit conference (August 2015). The exit conference was attended by the representatives of the Company. The views expressed by the Company along with the replies received from Management have been considered while finalising this performance audit report.

We acknowledge the co-operation and assistance extended by the Company at various stages of conducting this performance audit.

Audit methodology consisted of:

- Scrutiny of agenda and minutes of meetings of Board of Directors, custom milling policies, instructions issued by the State Government and milling progress reports of district offices;
- Scrutiny of records relating to cash credit limits, payment of guarantee fee and other charges and their reimbursement from FCI;
- Examination of records relating to delivery of rice to FCI, raising of claims and receipt of payment there against;
- Examination of Internal Audit Reports and their follow up; and
- Issue of observations and queries with the officers and staff of the Company.

³ Fatehgarh Sahib, Jalandhar, Ludhiana, Moga, Mohali, Patiala and Sangrur

Audit Criteria

2.1.5 The audit findings were evaluated against audit criteria which is sourced from the following:

- Instructions/guidelines issued by the GoI/State Government/FCI with regard to activities of procurement and custom milling of paddy and CMPs issued by the State Government of respective crop years;
- Terms and conditions of the cash credit limits availed by the Company;
- Instructions of GoI for re-imbursement of cost, incidentals and differential claims;
- Terms and conditions of handling and transportation contracts;
- Norms/rates for timely raising of bills for rice and other related expenses fixed by the GoI and their reimbursement from FCI;
- Provisions in the accounting manual and internal control mechanism in the Company.

Audit Findings

2.1.6 The audit findings are discussed in the subsequent paragraphs.

Working Results and Financial Arrangement

2.1.7.1 The Company has not prepared its financial statements for the year 2014-15 by October 2015, which were required to be completed within six months of the close of the financial year i.e. by September 2015 in accordance with Section 96(1) of the Companies Act 2013. The Company finalised and submitted its financial statements for all the years from 2010-11 to 2013-14 with delay ranging between nine and 18 months; 2010-11 (15 March 2013), 2011-12 (6 January 2014), 2012-13 (11 August 2014) and 2013-14 (25 June 2015). The working results of the Company for the four years ending 31 March 2014 and impact of audit comments are given below.

(₹ in crore)					
Sl. No.	Particulars	2010-11	2011-12	2012-13	2013-14
1.	Sales and other income	5630.29	3315.15	3871.75	4988.78
2.	Expenditure	5630.07	3315.10	3871.89	4989.08
3.	Reported Profit (+)/Loss (-) after tax	0.22	0.05	(-)0.14	(-)0.30
4.	Impact of comments of Statutory Auditor and CAG	(-)390.97	(-)445.36	(-)734.87	(-)901.42
5.	Loss after impact of comments	390.75	445.31	735.01	(-)901.72

Statutory Auditors' have consistently remarked that the financial statements of the Company do not reflect a true and fair view of the state of affairs of the Company. The table above shows that after considering the qualifications of the Statutory Auditors and those of CAG, the reported profits of the Company

will convert into huge losses. There was an accumulated loss of ₹ 3763.88 crore as against the reported accumulated surplus of ₹ 4.90 crore at the close of the year 2013-14. The Company has been showing interest (₹ 983.32 crore), custody and maintenance charges (₹ 390.94 crore), transportation charges (₹ 380.20 crore), etc. as recoverable without their confirmation.

Management stated (August 2015) that claims are booked on the basis of past practice with the hope that these will mature on finalisation of rates by GoI pending since 2004. The reply is not acceptable as the Company has been booking receivable without any confirmation/rules of GOI/FCI etc. and contrary to the principles of accounting and applicable accounting standards on recognition of revenue.

2.1.7.2 Utilisation of cash credit facility

The Company was availing cash credit (CC) facility from State Bank of India (SBI) for procurement of foodgrains and related incidental expenses against hypothecation of stocks on guarantee given by the State Government. Agreement between SBI and the State Government on behalf of the procuring agencies provided that the value of hypothecated stocks should fully match with the CC outstanding. However, we observed that the Company was availing CC much above the value of closing stock i.e. the value of closing stock was not adequate to cover CC outstanding. The cumulative CC outstanding at the close of the year 2010-11 was ₹ 2090.32 crore against which the value of closing stock was ₹ 929.44 crore i.e. outstanding cumulative CC exceeded the value of stock by ₹ 1160.88 crore. This gap increased to ₹ 2799.36 crore by the financial year 2013-14. The year wise position is placed below:-

(₹ in crore)			
Position as on	Value of closing stock	Cumulative CC outstanding	Gap
31 March 2011	929.44	2090.32	1160.88
31 March 2012	867.57	2542.51	1674.94
31 March 2013	950.49	3356.07	2405.58
31 March 2014	716.73	3516.09	2799.36

The banks charged (December 2014) a penalty of ₹0.59 crore on the Company for its CC exceeding the value of closing stock which was reversed (June 2015) by them.

Management while admitting the facts stated (August 2015) that this mismatch was due to non-reimbursement of various elements of cost by State Government/ GoI/ FCI and due to huge recoverable from defaulter millers. The reply is not acceptable as the gap arose due to Company taking into account its unconfirmed receivables for supporting its CC limits. The banks had taken cognizance of this gap and had accordingly requested (January 2015) the GoP to arrange for the payment of ₹20920.36 crore of all procurement agencies including the above gap of ₹2799.36 crore to regularise the cash credit account.

2.1.7.3 Reimbursement of Guarantee Fee

The CC limit was availed in accordance with requirement of funds assessed on the basis of minimum support price (MSP) of paddy, cost of gunny bags, transportation and other incidental charges etc. During 2010-14, the State

Government charged guarantee fee at the rate of 1/8 *per cent* from the Company for CC limit actually availed whereas GoI allowed guarantee fee subject to maximum of 1/8 *per cent* of MSP of quantity of paddy equivalent to rice delivered to FCI (Central Pool). The gap between these two remains unrecovered.

We noticed that:

- The Company paid guarantee fees of ₹ 8.96 crore to the State Government for the crop years 2010-14 whereas FCI reimbursed/ will reimburse guarantee fee of ₹ 7.22 crore only leaving a gap of ₹ 1.74 crore. The State Government reduced the guarantee fee to 1/8 *per cent* of MSP of paddy from KMS 2014-15. However, the Company had not approached the State Government for refund of the excess guarantee fee paid for the KMS 2010-14.
- During the scrutiny of seven selected district offices, we noticed that in five district offices⁴ there were instances of not claiming reimbursement of guarantee fee amounting to ₹ 0.34 crore for the crop years 2011-14. This indicated inadequacy of internal control to ensure timely raising and proper follow up of the claims lodged with FCI.

Management while admitting the facts stated (August 2015) that district offices are in touch with FCI for getting reimbursement of guarantee fee.

Procurement and Transportation of Paddy

2.1.8.1 Irregularities in distribution of additional relief bonus

The State Government declared (October 2010) an additional relief bonus to the farmers at the rate of ₹ 9.13 per quintal of paddy procured in crop year 2009-10. The Company received its share of ₹ 12.05 crore in November 2010/January 2011 for distribution to the farmers. The State Government directed (December 2010) all the State Procuring agencies to ensure⁵ that bonus was actually distributed among the farmers.

In audit of seven selected district offices, we noticed that while disbursing (December 2010) the bonus amounting to ₹ 6.18 crore for 67.69 lakh MT paddy procured during KMS 2009-10, six district offices, except Jalandhar, distributed bonus amounting to ₹ 5.28 crore to the *arhtias*⁶ for disbursement amongst farmers who did not give any documentary evidence in support of bonus disbursement to eligible farmers. Thus, the Company had no means to assure itself that the bonus was actually distributed among the farmers.

Management while admitting the facts (August 2015) assured to make inquiry into the matter.

⁴ Sangrur - ₹ 0.07 crore, Moga - ₹ 0.11 crore, Mohali - ₹ 0.09 crore, Ludhiana - ₹ 0.02 crore and Fatehgarh Sahib - ₹ 0.05 crore.

⁵ To ensure distribution of additional relief bonus to eligible farmers the Company was required to obtain the farmer-wise detail and receipt of bonus duly countersigned by joint committee of F&SD representatives, the Company and Secretary, Market Committee.

⁶ Arhtia – Middleman in the grain market

2.1.8.2 Abnormal variation in transportation rates

We noticed that the contracts for transportation of paddy from mandis to storage points were awarded after calling tenders by allowing certain *per cent* enhancement over the previous years' rates. The rates for transportation were fixed on per quintal basis and no weightage was given to the distance involved. We analysed the transportation rates paid in five⁷ selected district offices and found wide variations in the rates per quintal per kilometer (km) with reference to rates fixed on per quintal basis which ranged from ₹ 0.51 to ₹ 5.11 during 2010-14. Though the distance to be covered would be a key element in determining the cost of transportation, the Company never considered the desirability to fix the transportation rate on per quintal per km basis to bring uniformity in the transportation rates. Thus, there was a lack of sound basis for determining the rates for transportation of paddy thereby resulting in flawed bidding. This resulted in extra burden of ₹ 4.03 crore⁸ on the Company during 2010-14. It is worth mentioning that in the state of Haryana, the 'Schedule of rates' were fixed on the basis of per quintal per kilometer thus factoring in the distance element.

2.1.8.3 Non recovery of transportation charges from millers

While fixing the rates of custom milled rice (CMR) for the crop years 2010-2014, GoI did not fix any separate rates of transportation charges for transportation within eight kms and these were already included in the milling charges. In a meeting held in July 2013, GoI reiterated its orders that expenditure for transportation of paddy from purchase centre/ mandi to mills and also delivery of rice to FCI godowns upto eight kms was to be borne by millers as the same was inbuilt in the rates itself. Audit of seven selected district offices of the Company revealed that for transportation of paddy from purchase centres to rice mills within eight kms, expenditure of ₹ 20.71 crore incurred by district offices for crop years 2010-14 was not recovered from the millers.

Management while admitting the facts stated (August 2015) that transportation charges from the millers were not recovered as per the instructions of the State Government.

Milling of Paddy

2.1.9.1 Milling of paddy

The paddy procured from mandis was stored in the premises of millers under joint custody of the millers and the Company up to the year 2012-13. From 2013-14 onwards, paddy was stored in the sole custody of concerned rice miller. CMPs of the State Government for each crop year and standard terms of agreement between the rice millers and the Company, *inter alia*, provided that rice millers would deliver the custom milled rice to FCI within the stipulated/ extended period.

⁷ Sangrur, Ludhiana, Patiala, Jalandhar and Fatehgarh Sahib.

⁸ Rate per quintal per kilometer = Actual rate incurred per kilometer divided by distance in kilometers. Further, taking least rate as base and subtracting it from Rate per quintal per kilometer (calculated for each mandi). Extra burden of ₹ 4.03 crore was calculated by multiplying difference of rate per quintal per kilometer with the actual quantity transported in the five selected districts. Jalandhar – ₹1.67 crore + Ludhiana – ₹1.35 crore + Sangrur – ₹0.90 crore + Fatehgarh Sahib – ₹0.10 crore + Patiala ₹0.01 crore = ₹4.03 crore

The following table gives details of the paddy procured, rice due and rice delivered by the Company during the crop years 2010-15:

(Quantity in lakh MT)

Particulars	2010-11	2011-12	2012-13	2013-14	2014-15	Total
Paddy procured and stored	11.21	11.50	13.18	12.34	12.17	60.40
Rice due	7.51	7.71	8.70	8.19	8.12	40.23
Rice delivered	7.25	7.43	8.34	8.17	8.12	39.31
Rice not delivered	0.26	0.28	0.36	0.02	0.00	0.92
Rate of rice per MT (₹)	19,089.50	20,675.30	23,284.20	24,554.70	25511.40	-
Value of rice not delivered (₹in crore)	49.63	57.89	83.82	4.91	0.00	196.25
Stipulated dates ⁹	31 March 2011	30 June 2012	31 March 2013	31 March 2014	31 March 2015	-
Dates of extended period ¹⁰ (No. of months)	30 June 2012 (15 months)	31 December 2012 (6 months)	17 January 2014 (9.5months)	30 September 2014 (6 months)	30 June 2015 (3 months)	-

The above table shows that as against 40.23 lakh MT of rice due, the millers delivered only 39.31 lakh MT during crop years 2010-15. We observed that as against the weighted average period of two months allowed by GoI, in the CMPs the State Government, without compensating the Company, allowed weighted average period of 3.75 months in 2010-11, 4.70 months in 2011-12, 4.15 months in 2012-13 and 4.52 months in 2013-14 & 2014-15 to the millers for delivery of rice which resulted in loss of interest of ₹ 188.87 crore during crop years 2010-15.

We further observed that due to non-delivery of rice within stipulated period given in the CMP, the GOI, on requests made by the State Government extended the delivery period from time to time. The Company took weighted average period ranging between 4.89 months to 8.84 months during 2010-15 for delivery of rice.

- a) It was noticed that during crop year 2010-11, in case the millers failed to adhere to the schedule prescribed in CMP, there was a provision of payment of penal interest at the rate of 12 *per cent* of the cost of short delivered rice. However, the State Government dispensed with (October 2010) this clause for KMS 2010-11 and did not incorporate (September 2011) this clause in CMP for 2011-12. Hence, the loss of interest of ₹ 62.29 crore¹¹ (₹ 42.86 crore for 2010-11 and ₹ 19.43 crore for 2011-12) could not be recovered from the millers. The Company also did not take up

⁹ Stipulated dates as per custom milling policy of the State Government.

¹⁰ Reasons on the basis of which the State Government requested GoI to extend the stipulated dates of delivery of rice were not made available to Audit.

¹¹ Calculation of penal interest has been made after the end of stipulated delivery date i.e. 31 March 2011 and 30 June 2012 respectively.

the matter for making a provision of compensation in lieu of waiver of interest for the extended/delayed period of milling of paddy with the State Government.

- b) Though there was a provision in the CMP for the year 2012-13 and 2013-14 for recovery of penal interest from the millers for delayed milling of paddy/delivery of rice, however, the Company did not impose penal interest on the millers. Audit calculated such penalties at ₹8.14 crore.

The Company thus ended up bearing the cost of decisions taken by the State Government to extend milling periods in excess of period allowed by FCI without any commitment of reimbursement of associated costs.

Management accepted the audit observation and stated (August 2015) that the extension was granted by the GOI on State Government request and the cost sheet does not permit the reimbursement of interest on delayed milling by the millers.

2.1.9.2 Non delivery of rice/ misappropriation of paddy by millers

Upto KMS 2012-13 the paddy stored in the premises of the millers remained in the joint custody of the millers and the Company. Both the parties were responsible for maintaining the quality and quantity of the paddy stored¹².

We observed that 1.36 lakh MT of paddy of crop years 2010-11 to 2013-14 was stored with 20 millers in eight districts offices¹³ (as per details given in **Annexure 3**). Of this, the millers short delivered/ misappropriated 0.48 lakh MT of rice valued at ₹ 120.82 crore during the above crop years and the security obtained from them as per the CMP was insufficient. The total amount recoverable from the millers as on March 2015 on account of short delivered/ misappropriated rice, cost of gunnies and other recoveries (after adjustment of amount deposited by millers and milling charges payable to them) was to the extent of ₹ 143.11 crore.

Misappropriation of rice/paddy was facilitated due to violation of CMP and other irregularities as given below:

- The Company failed to conduct timely physical verification of paddy stocks in accordance with the CMP during the years when paddy was stored in joint custody. 0.43 lakh MT paddy was found missing from 14 millers (Sl. No. 3 to 14, 18 and 20 of **Annexure 3**) of the crop years' 2010-11 to 2012-13. The Company filed FIRs against these millers.
- The millers who had not delivered requisite quantity of rice of previous crop years' were not to be considered for allotment of paddy yet the Company allotted 0.25 lakh MT of paddy to four such millers (Sl. No. 3, 14, 15 and 19 of **Annexure 3**) who had not delivered 0.12 lakh MT rice valuing ₹ 31.43 crore.

¹² For the year 2013-14 and 2014-15 paddy was in the custody of millers.

¹³ includes district office Mukatsar in addition to the seven selected district offices

- The Company stored 0.38 lakh MT paddy with 12 millers (Sl. No. 3 to 7 and 10 to 16 of **Annexure 3**) over and above the allotted capacity/permissible quantity. These millers did not deliver 0.38 lakh MT rice valuing ₹ 96.67 crore.
- The Company stored 1559.35 MT paddy of crop year 2010-11 with an unallotted miller (Sl. No. 1 of **Annexure 3**) without entering into an agreement who did not deliver 265.83 MT rice valuing ₹ 0.70 crore. The case was terminated (May 2014) by the arbitrator due to absence of written agreement with the miller.

Management in its reply stated (August 2015) that action against the defaulter millers was being taken as per the terms of CMP.

2.1.9.3 Undue favour to the defaulting millers

In case the miller fails to deliver rice by the due date, the recovery is to be made from the miller at the rates fixed by the State Government for recovery of unmilled paddy, considering various elements of cost along with interest. However, we observed that:

a) District office, Moga and Ludhiana stored 22945.97 MT of paddy of crop years 2010-11 and 2011-12 with five millers (as per detail given in **Annexure 4**) who were required to deliver 15358.31 MT rice as per outturn ratio. However, they delivered only 11117.01 MT rice. The balance 4241.30 MT rice was not delivered upto the extended period (June 2012/ December 2012) for which an amount of ₹ 11.45 crore was required to be recovered. However, we observed that district offices settled the millers' accounts for ₹ 7.92 crore, thereby favouring them to the tune of ₹ 3.53 crore¹⁴ and interest of ₹ 1.02 crore as on March 2015.

b) Similarly, district office, Moga stored 12988.07 MT paddy of crop years 2010-11 and 2011-12 with a miller who was required to deliver 8702 MT rice. However, the miller delivered only 7364.04 MT, a shortfall of 1337.98 MT rice equivalent to 1996.99 MT paddy valuing ₹ 3.65 crore. As on March 2015, an amount of ₹ 4.59 crore (₹ 3.65 crore + interest ₹ 0.95 crore) was recoverable from the miller.

Though a period of more than two years had elapsed since the last date of delivery of rice in these cases, the Company had neither raised any claim against the millers nor initiated any legal action for the recovery of due (September 2015).

Management replied (August 2015) that district offices have been directed to recover the amount as per terms of CMP.

2.1.9.4 Arbitration cases

As per the terms of agreement with the millers, all disputes are to be referred to the sole arbitrator, i.e. Managing Director of the Company or any other

¹⁴ Calculated @ 12 per cent penal interest as provided in CMPs.

person appointed by him. Award of the Arbitrator is to be final and binding on both the parties.

As on June 2015, the Company was pursuing 37 arbitration cases¹⁵ involving ₹ 190.11 crore on account of shortage of paddy/ short delivery of rice by millers. We observed that during 2010-11 to 2013-14, the arbitration proceedings were initiated with delays of upto 32 months from the extended date of milling.

Management accepted the audit contention and assured (August 2015) to inquire the reasons for the delay in each case

Delivery of Rice

2.1.10.1 Delayed raising of claims and receipt of payment

Audit noticed that the Company did not evolve a system at its head office to ensure and monitor that the district offices were raising claims timely. During test check of records of selected district offices during 2010-15, instances of delayed raising of claims were noticed:

a) Custom Milling Policy states that it will be the responsibility of the miller to supply 'Acceptance Note', 'weight check memo' and all other relevant documents to the concerned agency within seven days of delivery of rice for claiming payments from FCI. Despite Company issuing instructions (June 2008) that delayed raising of claims against rice delivered, will invite penalty of interest at the rate being paid on CC limit, there was no enabling provision in the agreements entered with the millers for penalty in case dispatch documents were not submitted within the stipulated time.

Audit observed, the Company raised claims in consolidated form with delays of upto 378 days (after allowing a margin of 10 days from the date of delivery of last consignment of rice) in 8202 sale bills (71 *per cent*) out of 11480 sale bills reviewed. Resultantly, an extra payment of interest of ₹ 1.72 crore on CC limit for the years 2010-11 to 2014-15 was incurred, but in the absence of details of date of submission of dispatch documents by the millers and receipt of dispatch documents the responsibility for delays could not be fixed.

b) Government of India (GoI) (July 2013) decided to pay the arrears on account of enhancement of VAT/purchase tax from 11 April 2011. In five district offices (Moga, Ludhiana, Patiala, Jalandhar and Fatehgarh Sahib) the supplementary claims of differential VAT for the crop year 2011-12 and 2012-13 were raised with delays ranging between three to 14 months resulting in delay in receipt of amount of ₹ 10.23 crore and excess payment of interest of ₹ 0.98 crore.

¹⁵ Prior to crop year 2010-11: 10 cases (₹ 13.62 crore), 2010-11: 5 (₹ 7.70 crore), 2011-12: 12 (₹ 33.26 crore), 2012-13: 8 (₹ 128.40 crore) and 2013-14: 2 (₹ 7.13 crore).

c) FCI issued (July 2013) instructions to release withheld gunny depreciation¹⁶ in respect of new gunnies utilised for procurement of paddy during crop year 2011-12 and started releasing depreciation in respect of crop year 2012-13. We noted that except in Ludhiana, supplementary claims of gunny depreciation in respect of new gunnies for the crop year 2011-12 amounting to ₹ 8.69 crore were raised by other selected district offices with delays ranging between 4 months to 14 months. Similar delays were noticed, for crop year 2012-13 in four district offices (Moga, Sangrur, Jalandhar, and Patiala) in raising the supplementary claim of gunny depreciation in respect of new gunnies amounting to ₹ 8.04 crore, between seven to 12 months. Two district offices (Mohali and Fatehgarh Sahib) had not raised (March 2015) the claim of gunny depreciation of ₹ 57.80 lakh for the crop year 2012-13 at all. This delayed or non claiming of gunny depreciation resulted in excess payment of interest of ₹ 1.52 crore upto March 2015.

d) The audit of selected district offices of the Company showed that the district offices received payments of sale bills from FCI after delays ranging from one to 268 days (after allowing a margin of three days after raising of sale bills) resulting in a loss of interest of ₹ 5.57 crore for the crop years 2010-15, for which no claim was raised on FCI.

2.1.10.2 Incorrect raising of claims

The provisional rates of CMR for the KMS 2011-12 and 2012-13 were issued by GoI on 21 December 2011 and 23 November 2012 respectively. However, the district offices of Ludhiana, Moga, Fatehgarh Sahib and Mohali continued (February to May 2012) to raise the claim for KMS 2011-12 at the rates of crop year 2010-11. As a result, supplementary claims of ₹ 12.11 crore on account of rate differential of crop year KMS 2011-12 were raised with delays ranging between two to 21 months. Further, district office Fatehgarh Sahib continued to raise the claim of rice delivered for KMS 2012-13 at the rate of KMS 2011-12. As a result, it raised a supplementary claim of ₹ 6.06 crore on account of rate differential of crop year KMS 2012-13 in April 2013 after a delay of five months, without any recorded reasons, though other district offices were raising the claim as per the cost sheet issued by the GoI. This resulted in a loss to the Company due to excess payment of interest of ₹ 1.39 crore.

2.1.10.3 Non recovery of cost of once used gunny bags

During audit of gunny records of the five¹⁷ selected district offices, we noticed that the district offices utilised 134.13 lakh once used gunny bags valuing ₹ 32.69 crore for the procurement of paddy in KMS 2010-11 to KMS 2014-15. The district offices recovered ₹ 19.62 crore as 60 *per cent* of depreciated cost of the once used gunny bags from the millers and remaining 40 *per cent* cost amounting to ₹ 13.07 crore was to be recovered from FCI. However, the Company neither preferred any claim for reimbursement of the

¹⁶ It is 40 *per cent* cost of new bags reimbursed by FCI which were used during paddy procurement and were retained by the miller after delivery of rice to FCI.

¹⁷ Jalandhar, Sangrur, Ludhiana, Mohali and Fatehgarh Sahib

remaining cost of bags from FCI as per the guidelines (May 2013) nor took up the matter with GoI for finalisation of rates for once used bags.

2.1.10.4 Non-reimbursement of interest on the cost of gunny bags and arhtia commission

In the CMR rates for 2010-11 to 2014-15, the Company paid arhtia commission and invested its funds in the purchase of gunny bags at the time of procurement of paddy out of the cash credit. These cost of bags and arhtias charges are reimbursed to the Company at the time of delivery of rice. The interest element on the amount invested by the procuring agencies on these elements of cost is not reimbursed. This resulted in a cost of ₹ 36.56 crore to the Company during 2010-15, out of which ₹ 16.76 crore¹⁸ was recoverable from FCI and ₹ 19.80 crore from the State Government in lieu of allowing longer period of milling as discussed in paragraph 2.1.9.1 supra.

2.1.10.5 Non-recovery against delivery of 'beyond rejection limit' rice

FCI deducted (April 2011 to June 2013) ₹ 4.09 crore in three district offices (Moga, Jalandhar and Sangrur) from sale bills of rice on account of 'beyond rejection limit' (BRL) rice supplied by rice mills. However, the Company could recover only ₹ 1.18 crore from the defaulting millers and ₹ 2.91 crore was still recoverable (March 2015). It was also observed that in district office, Moga, FCI deducted ₹ 0.13 crore against the millers which were not even allotted to the Company. The district office had not raised (March 2015) any supplementary claim with FCI against this deduction.

2.1.10.6 Non finalisation of millers accounts

We observed that the district offices had not recovered an amount of ₹ 11.73 crore for the crop years 2010-11 to 2012-13 from 205 millers due on account of gunny bags retained, quality cuts etc while finalising their accounts. The district offices had not finalised the accounts of 212 millers for the crop year 2013-14 though the extended delivery period of rice for the crop years 2013-14 had already expired in September 2014. Further scrutiny revealed that district offices had recovered the outstanding amount of ₹ 11.49 crore from 126 millers after delays ranging between one to 36 months from finalisation of accounts/completion of milling which resulted in loss of interest of ₹ 0.42 crore.

Management while admitting the facts stated (August 2015) that actions are being taken to curb the deficiency in future.

Internal Control

2.1.11.1 Internal control is a tool for efficient and effective management of the Company. An essential part of internal controls is an accounting manual but the Company has not prepared any accounting manual. We observed that

¹⁸ Interest calculated at CC rate for two months, the period for milling allowed by FCI

internal control system in the Company in relation to the activities covered in the performance audit were deficient. It lacked a reliable mechanism to ensure:

- Implementation of terms of CMP framed by State Government such as storage and physical verification of paddy, timely delivery of rice, etc.;
- Adherence of agreement terms with the millers and timely finalisation of their accounts;
- Timely raising of claims, differential/ supplementary claims and recovery thereof from FCI; and
- Rendering of information to the Management of activity wise working results etc.

2.1.11.2 The Company has an internal audit wing under the control of a General Manager (Monitoring/ Audit and Recovery). The Company has been appointing firms of chartered Accountants for conducting the internal audit. A review of the internal audit system of the Company revealed that:

- No internal audit manual defining the scope of work, duties and responsibilities of internal audit wing was devised;
- There was no prescribed system to prepare action plans for Internal Audit resulting in the audit of units being conducted without deciding the priorities; and
- Reports of Internal Audit were neither brought to the notice of the Board of Directors for perusal nor any monitoring system to take corrective remedial action on the reports was evolved.

Management while admitting the facts (August 2015) assured for future compliance.

Conclusion

The operations of the Company from the procurement of paddy to the delivery of rice to FCI were plagued by inefficiencies. As a result the Company continued to make huge losses. The cash credit limit availed by the Company was not backed by an equivalent value of stock of foodgrains. There was a lack of control in milling operations with the result that there was misappropriation of paddy. Non-recovery of costs from millers and delay in raising bills on FCI with consequential loss of interest were noticed. Similarly, there were costs associated with the CMR operations which are neither reimbursed by FCI nor compensated by the State Government which affected the Company adversely.

Recommendations

We recommend the Company:

- i. to evolve a mechanism to ensure that millers deliver due rice to FCI within the stipulated period;**

- ii. to recover claims of undelivered rice and transportation charges from millers;**
- iii. to prefer claims timely with FCI/ millers and effect and monitor timely recovery of its dues;**
- iv. to fix time limit for initiating arbitration cases; and**
- v. to strengthen internal controls such as implementation of terms of CMP, adherence of agreement with the millers, timely raising of claims.**

The matter was referred to the Government (July 2015), their replies were awaited.

Punjab State Power Corporation Limited

2.2 Purchase and Inventory Control

Executive Summary

Consequent upon unbundling of Punjab State Electricity Board, Punjab State Power Corporation Limited (PSPCL) was entrusted the business of generation and distribution of power and Punjab State Transmission Corporation Limited (PSTCL) was made responsible for transmission of power. The important findings noticed in PSPCL while conducting the performance audit on 'Purchase and Inventory Control' are as under:

Purchase of transformers in excess of requirement valuing ₹ 15.46 crore and excess stock of cables without required accessories worth ₹ 3.81 crore were noticed.

(Paragraphs 2.2.7 a and 2.2.7 b)

Inefficient tendering process resulting in failure to place purchase order within the original validity period resulted in extra expenditure of ₹ 16.58 crore.

(Paragraph 2.2.8.1)

Material valuing ₹ 5.45 crore remained un-utilised even after five years of the corporatisation of the two Companies, due to non-finalisation of modalities.

(Paragraph 2.2.9.2)

No MIS mechanism had been evolved to ensure timely rendering of material at site accounts and finalisation thereof within the stipulated period. Accounts of 4788 works, involving material worth ₹ 103.05 crore, had not been finalised.

(Paragraph 2.2.10.1)

Company had neither framed its own internal audit manual nor updated the internal audit manual of the erstwhile Board, which it had adopted, to match with the size and nature of its business.

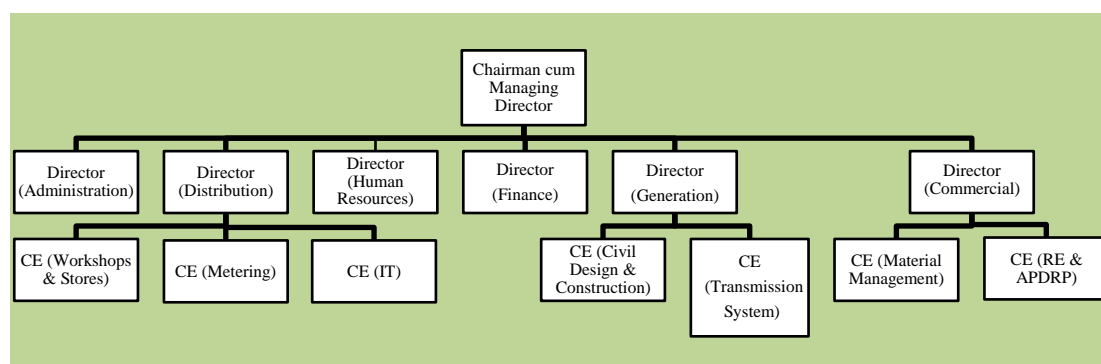
(Paragraph 2.2.10.5)

Introduction

2.2.1 Punjab State Electricity Board (PSEB) was unbundled on 16 April 2010 into two companies viz. Punjab State Power Corporation Limited (PSPCL) and Punjab State Transmission Corporation Limited (PSTCL). Consequently, business of distribution and generation of power was entrusted to PSPCL and PSTCL was made responsible for transmission of power.

Organisational set-up

2.2.2 The organisation hierarchy of PSPCL is given below:



Audit Objectives

2.2.3 The audit objectives of the performance audit were to ascertain whether;

- the regulatory framework for purchases has been framed and approved by the competent authority;
- purchase requirements were assessed on realistic basis and variance analysed;
- laid down criterion were followed for placing purchase orders and were executed as per terms and conditions of the contract/ purchase order; and
- internal control systems were commensurate with the size of the activities.

Scope of audit

2.2.4 Performance of activities of “Purchases and Inventory Control” in the erstwhile Punjab State Electricity Board (Board) were reviewed and included in the Report of Comptroller and Auditor General of India for the year 2007-08 (Commercial) - Government of Punjab. The Committee on Public Undertaking (COPU) of the State Legislature could not discuss this Report and had decided (June 2015) to send the whole Report, including the review, to the concerned Administrative Secretaries to take appropriate action at their own level. COPU is yet to be informed (September 2015) of the action taken.

The present performance audit of ‘Purchase and inventory control in PSPCL’ conducted during January 2015 to April 2015 covered the activities relating to

purchase of materials and inventory control during the period 2010-2015 in five¹ out of seven offices of Chief Engineers of PSPCL. During the last five years ending March 2015, these five Chief Engineers offices had placed purchase orders for materials worth ₹ 3993.91 crore. We examined 157 tender enquiries (31 *per cent*) out of 508 tender enquiries floated by these CEs, selected on the basis of Circular Systematic Sampling² and Judgemental Sampling technique. In addition to this, records of four³ central stores out of 12 central stores of PSPCL, selected on the basis of probability proportionate to size sampling technique, were examined.

We explained the audit objectives, methodology and criteria to the Management of PSPCL in an entry conference (February 2015). Audit findings were reported to them and the State Government (July 2015) and discussed in the exit conference (August 2014) which was attended by the senior management of PSPCL and the Government. The views expressed/ replies received by/ from the Management/ Government have been considered while finalising this performance audit report.

We acknowledge the co-operation and assistance extended by the staff and the Management of the PSPCL at the various stages of conducting this performance audit.

Audit Criteria

2.2.5 The audit criteria were sourced from:

- purchase regulations and instructions issued from time to time by the Board/ PSPCL;
- work plan/ basis for assessment of requirement of material;
- terms and conditions of purchase orders/ contracts/ agreements;
- norms fixed by the PSPCL for holding inventory; and
- procedure prescribed for receipt, issue and verification of stock.

Audit findings

Regulatory framework for purchases

2.2.6 Procurement of Material

2.2.6.1 Purchase procedure of Material Management organisation of PSPCL

The system, procedures, rules and regulations for purchase of materials in PSPCL are derived from its Purchase Regulations and the Commercial

¹ Chief Engineer (Material Management), Chief Engineer (Metering), Chief Engineer, (Workshop and Stores), Chief Engineer (Transmission System), Chief Engineer, (IT)

² One fourth of total tender enquires floated were selected through Circular Systematic Sampling technique and judgmental sampling. Judgmental Sampling was used to pickup interrelated tender enquires

³ Bathinda, Ludhiana, SAS Nagar (Mohali) and Verka (Amritsar)

Accounting System. Chief Engineer/Workshop & Stores (CE/W&S) intimates the requirements to CE/Material Management (MM) for initiating the purchase process. CE/MM determines the net annual requirement. The proposals for purchase of material worth upto ₹ four crore are decided by a Central Purchase Committee (CPC) and purchases above ₹ four crore are decided by a committee of Whole Time Directors (WTDs).

2.2.6.2 Non revision of Purchase Regulations

Erstwhile PSEB, exercising powers conferred by Clause (g) of Section 79 of the Electricity (Supply) Act 1948 had framed PSEB Purchase Regulations, 1981. These purchase regulations have been amended from time to time and a compilation printed (Oct 2005).

We observed that:

- Though Electricity (Supply) Act 1948 was repealed and the Electricity Act 2003 had come into force, the erstwhile Board and the PSPCL did not revise the Purchase Regulations by mapping it to the requirements⁴ of the Electricity Act, 2003.
- After unbundling of erstwhile Board, PSPCL adopted the PSEB Purchase Regulations, 1981 and had not framed its own purchase regulations as per its nature of business, requirements of the latest laws and best procurement practices.

Management replied (August 2015) that action has been initiated to frame purchase regulations.

2.2.6.3 Material Budget

An efficient material management system must have a proper estimate of material requirements, to be prepared in the form of a Material Budget. The actual purchases and utilisation thereof compared against estimates and variances analysed for taking corrective action.

We observed that an Annual Material budget for the ensuing year was not being prepared by PSPCL. The non-preparation of a comprehensive material budget led to funds for procurement of material being allocated on *ad hoc* basis in the annual financial budget.

Management accepted (August 2015) that no separate annual Material Budgets were being prepared and assured that the issue will be addressed.

⁴ Central Electricity Authority has made regulations acting on Section 55(1), 73(e), 177(2) of Electricity Act, 2003 for regulating the installation and operation of meters. These have not been included in the purchase regulation by the companies. Also guidelines issued by CVC from time to time regarding procurement, best practices as adopted by neighboring states have not been included in the purchase regulations

Assessment of requirement of material

2.2.7 Material Procurement Plan were not being prepared on a yearly basis or after consolidating requirements of different user departments. Purchase proposals were processed on receipt of requirements of individual items.

In PSPCL, consumption of material during previous three or four years, pending purchase orders and minimum stock level were being considered for preparing purchase proposals for individual items. Audit noticed, however, that the net requirements submitted by the MM organisation were being reduced/changed substantially by the WTDs at the time of approval of purchase proposal. Hence, the requirements of material were finalised by the WTDs on *ad hoc* basis and without considering these factors.

Audit observed the following, amongst other cases indicated in **Annexure 5**.

(a) Purchase of 10 KVA transformers in excess of requirement

PSPCL issued (October 2012) tender (Q 3901) for procurement of 43,000 numbers of 10 KVA distribution transformers (after considering residual quantity of 15900 nos. of an earlier tender), for meeting requirement of 'Accelerated Release of Tubewell Connections (ARTC) scheme'. The offers of all the 25 participating firms were valid upto 7 March 2013. During processing time of tender, residual quantity of the earlier tender enquiry was awarded and work of ARTC was decided to be executed on turnkey basis. In view of this, the Chief Purchase Officer (CPO) recommended to drop the tender enquiry (Q 3901). The Director (Commercial), however, directed to proceed with the tender enquiry citing forthcoming paddy season.

The price bids were opened on 31 May 2013 and the validity period of all the firms was extended upto 31 December 2013 as the purchase proposal could not be finalised within the validity period. The CPC in its proposal updated the requirement to 23,000 transformers⁵ for the period up to December 2014 but the committee of Whole Time Directors (WTDs), decided to continue with procurement of 43,000 transformers and allocated the same amongst 13 bidders at L₁ rate of ₹ 28,625.47 per transformer. The purchase orders were issued in January 2014 with deliveries up to January 2015. The CPO noticed (May 2014) that stock was 9766 numbers against minimum/ maximum level of 3000/ 6000 and another 2150 transformers were ready for inspection with the suppliers decided to defer further receipts. CPO again assessed (12 February 2015) the stock position at 11,400 transformers and deferred supplies up to 15 March 2015.

We observed that though the Director (Commercial) had advised to continue with the purchase in view of the forthcoming paddy season, the tender enquiry could not be finalised when the transformers were needed. We also observed

⁵ considering supplies in pipeline, minimum level, general requirements and additional requirements on previous consumption basis

that even after deferment of the supply, PSPCL had excess stock of transformers, which caused blockade of funds to the extent of ₹ 15.46 crore⁶.

Management replied (August 2015) that the agenda for procurement of transformers could not be finalised due to certain observations and introduction of advance tax by Government of Punjab. The reply is not acceptable as provisions of advance tax were introduced in October 2013 by GoP and were never the cause for non-finalisation of the purchase proposal. It was due to continuous change in the proposal of quantity that the purchase order was not finalised.

(b) Procurement of Aerial Bunched (AB) Cables without Accessories

CE (MM), PSPCL floated (September 2011) a tender enquiry (QQ-151) for procurement of 1280 kilometres (kms) of 11 KV XLPE Aerial Bunched (AB) cables of assorted sizes for erection of independent feeders. The WTDs after considering the purchase proposal decided (January 2012) to procure 450 kms⁷. Subsequently, due to very low consumption of these AB cables, the supply of the cables was deferred time and again. The deferment of supply of cable-1 was revoked in April 2013 considering increase in consumption of cable and the suppliers were asked to supply the remaining quantity. However, the supply of cable-2 remained deferred due to its low consumption and stock position in excess of minimum limit.

We observed that at the time of procurement of AB cables, the procurement of mandatory accessories was not considered due to non-availability of technical specifications. In the absence of required accessories and purchase in excess of requirements, 18.651 kms of cable-1 and 70.585 kms of cable-2 valuing a total of ₹ 3.81 crore⁸ remained excess in stock (January 2015), over and above maximum stock level of 55 kms and 35 kms of the cable -1 and cable-2 respectively.

Management replied (August 2015) that there is no requirement of specific accessories and no difficulty was being experienced by field staff. Also from 2013-14, consumption of cable-1 had increased. The reply is not acceptable because as per records of the Company difficulties were being faced by field staff in use of AB cables due to non-availability of accessories. Further, consumption levels regarding cable-2 were not commented in reply and audit has taken for valuation purposes, stock levels of cables in excess of maximum levels fixed by Company.

⁶ Figure worked out for 5400 transformers (11400 – 6000) @ ₹ 28,625.47 after giving maximum stock level margin of 6000 transformers.

⁷ 250 kms of 3Cx150+150 mm² (Cable-1) and 200 kms of 3Cx95+70 mm² (Cable-2)

⁸ 70.585 kms of 3Cx95+70mm² AB cable @ ₹ 398073.50 per Km and 18.651 kms of 3Cx150+150 mm² AB cable @ ₹ 5,38,208.53 per Km (After allowing margin for maximum level).

Tendering process and execution of tenders

2.2.8.1 Efficiency of tendering process

The Purchase Regulations mandate that all offers received from the bidders are to be valid for a period of at least 120 days. However, no time limit has been fixed within which tenders are to be finalised.

In many cases, PSPCL failed to finalise the purchase proposals within the original validity period of 120 days and had to get the validity of their offers extended. The delay in finalisation of tenders ranged between four and 170 days after the expiry of original validity period. There were also instances where L₁ bidders had refused to extend the validity of their offers and Company purchased the material at higher cost subsequently.

Management expressed (August 2015) that fixing of time frame was not feasible in view of time taken in getting clarifications on technical aspects and conducting work appraisal of new firms. However, they assured to address the issue.

Audit noticed delay in finalisation of purchase proposals with concomitant implication of higher cost to PSPCL:

(a) PSPCL invited (June 2013) online tenders (Q-3913) under three part bid system⁹ for procurement of 5000 numbers of 63 KVA distribution transformers. Seventeen firms participated in the tender and their offers were valid upto 6 November 2013. Part III of the bids of 14 eligible firms were opened on 19 September 2013 in which M/s Shree Balaji Industries, Baddi with offered quantity of 5000 transformers was L₁ with the equated rate of ₹ 52903.86 per transformer. However, PSPCL could not finalise the tenders within the validity period and approached the tenderers for extension of validity citing that GoP had notified (October 2013) imposition of advance tax on purchases from outside the State. All the firms except, M/s Shree Balaji Industries, Baddi (L₁) extended the validity of their offers.

On refusal of L₁ party to extend its offer, MM organisation proposed (January 2014) to the WTDs to procure the material at the L₂ rates. The WTDs observed (February 2014) that there had been inordinate delay in submission of the agenda after the finalisation of advance tax and decided to scrap tender Q-3913 and retender. Accordingly, the tender was cancelled and the quantity was associated with the subsequent tender Q-3926 which was finalised (July 2014) for procurement of 8,000 transformers at fresh L₁ rates of ₹ 67,488 per transformer quoted by M/s Hi-tech Transformers, Jammu.

⁹Three part bid system comprises of Part-I as Earnest Money Deposit; Part-II as Technical and Commercial bid; and Part-III as Price bid.

Thus, PSPCL had to incur extra expenditure of ₹7.29 crore¹⁰ due to delay in finalising the tender.

(b) PSPCL invited (June 2013) online tenders (Q-3914) for procurement of 5000 number of 100 KVA Distribution Transformers. After opening of Part I and II of the bids on 5 July 2013, Part III of the bids of all the 19 participating firms was opened on 3 October 2013. Shree Balaji Industries, Baddi emerged L₁ with equated¹¹ rate of ₹ 72093.86 per transformer. The difference between price of L₁ and L₂ was as high as ₹ 12697.39 per transformer. However, PSPCL did not place the Purchase Order within the validity period (1 November 2013) of price bid and L₁ firm also not agreeing to extend validity of their offer, the tender was scrapped (February 2014).

PSPCL invited (May 2014) on-line tenders (Q-3927), with enhanced requirement, for procurement of 10000 numbers of 100 KVA transformers which was finalised (July 2014) to at the rate of ₹ 90667.01 per transformer. Thus, the Company had to incur an additional expenditure of ₹9.29 crore¹² in procurement of 5000 DTs due to delay in placing the Purchase Order.

The Management replied (August 2015) to the above cases that L₁ firm had quoted unrealistically low rates and finalisation of tender enquiry was delayed due to introduction of Advance tax. The Management reply is not acceptable because each bidder quotes their own rates after checking their cost components. Further, due to any change in structure of payment of taxes etc., the purchase process should have not been delayed and that there was no change in total rates of taxes imposed, only the procedure of payment of taxes had been changed.

2.2.8.2 Splitting ordered quantity without valid reasons

As per Purchase Regulation 20(iv), the competent authority may distribute the quantity to be procured on more than one firm after recording reasons thereof. We noticed that allocated quantity was distributed amongst different bidders at L₁ rates without recording any reasons. There was no disclosure made in the NIT/ tender document of any pre-determined ratio for such distribution. The CVC had also issued instructions (March 2007) that the quantity being finally ordered should be distributed among the bidders in a manner that is fair, transparent and equitable.

A number of cases were noticed during the audit period 2010-15 where finalised quantity was split amongst different bidders without recording reasons and in the process L₁ bidder was awarded quantity lesser than the quantity offered. Instances of refusal by the other bidders to accept the counter offer at L₁ rate were also noticed leading to Company incurring higher costs for their purchase in subsequent tenders.

¹⁰5000 T/Fs x (₹67,488 – ₹52903.86) = ₹ 7,29,20,700

¹¹Equated rate is arrived at by adding applicable taxes and duties to ex-work rate quoted by the bidder.

¹²5000 DTs X (₹ 90667 - ₹ 72093) = ₹ 9,28,65,750

Management replied (August 2015) that distribution of quantity amongst bidders increase the reliability of supply. They also assured that internal guidelines would be framed.

A case of splitting the ordered quantity on *ad-hoc* basis and not taking up the full offered quantity with costly results is presented below as illustration:

Non-placement of purchase order on L₁ firm for full offered quantity

Against tender enquiry Q-3917 floated by CE (MM), PSPCL, for procurement of 13,000 distribution transformers, the WTDs decided (April 2014) to procure 2,000 transformers each from the L₁ firms (two) and 6,000 transformers from other next five firms in the merit list at the L₁ rates. Accordingly, Letter of Award (LOA) was issued to both the L₁ firms and Letter of Intent (LOI) to other five firms for the decided quantity at the L₁ rates. However, the other five firms (other than L₁) did not accept/ respond to the counter offer at L₁ rates. The purchase orders were placed (May 2014) for 4,000 transformers on both the L₁ firms at ₹ 63,728.20 against their offered quantity of 9000 transformers.

Due to not placing the purchase order (PO) for full offered quantity (9000 transformers) on L₁ firms, PSPCL had to purchase (July 2014) the balance quantity of 5000 transformers against a subsequent tender at the rate of ₹ 67,488 per transformer, which was higher than the L₁ rate of earlier tender enquiry by ₹ 3759.80 per transformer. This resulted in PSPCL incurring extra cost of ₹1.88 crore.

PSPCL stated (August 2015) that all the firms to whom counter-offers were made, refused the L₁ rates. Management reply is not acceptable because the Company did not place order on L₁ firms even for the full offered quantity which they were bound to accept.

2.2.8.3 Inaction against defaulting firms

The Committee of WTDs of PSPCL desired (August 2012) a memorandum from MM organisation alongwith the seniority list of firms who had defaulted in supply of material and directed that action of blacklisting be taken under Negligence & Default clause of Purchase Regulations, within one month.

(i) Audit noticed that a seniority list of 29 firms, who had defaulted in supply of material within contractual delivery periods (CDPs) up to 31 July 2012, was prepared and submitted belatedly to the WTDs in December 2014. Further, out of the 47 firms who had not supplied the material within CDP upto 31 December 2013, no action had been taken against 31 firms (April 2015). PSPCL, though added (December 2012) a new clause in its purchase regulation according to which the defaulter firm was not to be eligible for participation in any new tender enquiry for a period of two years from the date of issue of purchase order (PO) in which it had defaulted. We observed that reckoning the ineligibility from the date of placement of PO instead of from the date of default defeated the very purpose of addition of the clause as in most of the cases the CDP goes beyond one year.

(ii) PSPCL in pursuance of on-line tenders for procurement of Distribution Transformers (DTs) of various sizes, awarded M/s Shree Balaji Industries, Baddi (firm) contracts for supply of 800 nos. 25KVA capacity (Tender enquiry Q-3903); 3000 nos. 6.3 KVA capacity (Tender enquiry Q-3904); 2700 nos. 16 KVA capacity (Tender enquiry Q-3905) and 1500 nos. 63 KVA capacity (tender enquiry Q-3906) valuing ₹ 27.76 crore. The firm did not supply material in any of the said Purchase Orders except in case of TE Q-3904 wherein supplied only 466 DTs. Thus, the firm had defaulted in all the four POs.

The firm was to deposit a total security of ₹ 55.51 lakh against all the four Purchase Orders, which was not taken in terms of notice inviting tender (NIT). PSPCL made payments of ₹ 1.03 crore to the firm during the period September 2013 to November 2013 against 466 DTs delivered without deducting security amount. This non-enforcement of terms of NIT/ negligence on the part of the Company to obtain security led to non-forfeiture of Permanent Earnest Money deposit (PEMD) of ₹ 10 lakh and non-recovery of remaining ₹ 45.51 lakh from the bills of the defaulter firm.

PSPCL informed (August 2015) that the suggestions of Audit have been noted and suitable amendment in the clause is under consideration for making the defaulter clause more comprehensive and effective. The point states that the Management could not effect any recovery against the defaulter firm.

2.2.8.4 E- tendering system for procurement of material

PSPCL decided (August 2010) to select M/s (n) code Solutions, Ahmedabad, IT Division of Gujarat Narmada Valley Fertilizers Co. Ltd. (GNFC), Gujarat, deeming it to be a State Government Undertaking, for implementation of e-tendering in PSPCL. Accordingly, a work order cum contract agreement was entered into (September 2010) with (n) code Solutions and e-tendering was implemented in PSPCL with effect from 20 September 2010. The decision of the WTDs was ratified (December 2010) by the BoD of PSPCL. The agreement with M/s. (n) code was initially for one year which was extended time and again up to September 2015. At the time of grant of extension for the year 2014, WTDs discussed that e-tendering was part of MM module under SAP/ERP solution being implemented in PSPCL. Hence, extension was given to M/s (n) code up to 20 September 2014 and again up to 20 September 2015 for implementation of SAP/ERP in PSPCL whichever was earlier. However, SAP/ERP has not been implemented in PSPCL so far (September 2015). We observed that:

- PSPCL outsourced (September 2010) the work without inviting open competitive bids. This departure from the standard practice of inviting competitive bids deprived PSPCL from getting alternative competitive rates. The extensions were also granted without resorting to the process of open competitive tenders.
- M/s (n) code Solution, Ahmedabad which was considered a Gujarat Government undertaking/ agency was not even a deemed Government Company.

- As per agreement, (n) Code Solutions was to provide payment gateway integration for payment towards tender fees and EMD, free of cost. Though e-tendering is under implementation for four years, payments towards tender fee and EMD are being received manually in the form of bank drafts and the payment gateway has not been made operational so far.

PSPCL replied (August 2015) that open competitive bids have now been invited for hiring e-tender vendor.

2.2.8.5 Non-adoption of good practices for procurement of material

There was no mechanism in the PSPCL to research and adopt good procurement practices followed by other peer utilities. The following are some of the good practices adopted by some of the power utilities of neighboring States:

- In some power utilities¹³, there is a vendor rating mechanism. The philosophy of vendor rating¹⁴ aims to help a utility to procure equipment/stores from vendor who is able to deliver the products of good quality at competitive prices with deliveries at a stipulated pace for achieving planned and operational targets. The vendor getting the highest rating is regarded as V₁ (similar to L₁) and the others in the descending order of their rating for the purpose of distribution of quantities of equipment/material to be ordered. However, the ordering rate (price) for procurement is the lowest evaluated price out of the rates quoted by the vendors selected for ordering on Vendor Rating basis.
- In some utilities¹⁵, the purchase department has created vendor development cell (VDC). The VDC maintains item wise/ supplier wise details of quantity and rates and supplies the rates of items which are purchased by the various other utilities ensuring the reasonability of rates before placing orders.

Management of PSPCL while accepting the facts replied (August 2015) that there was no such formal mechanism but they had regulations for development of new firms and Punjab based firms.

Inventory Control

2.2.9 An efficient inventory control plays a key role in material management so as to avoid unnecessary holding of material leading to blockade of funds, more inventory carrying cost and lack of space etc.

¹³ Dakshin Haryana Bijli Vitran Nigam Limited and West Bengal State Electricity Distribution Company Limited.

¹⁴ Assessment of the qualifications of a vendor, on a single point scale, to help grading the performance of a vendor is called Vendor Rating.

¹⁵ Dakshin Haryana Bijli Vitran Nigam Limited and Rail Coach Factory, Rai Bareilly.

The inventory of PSPCL¹⁶ was ₹ 233.10 crore as on 31 March 2011 which increased to ₹ 365.03 crore at the end of March 2015.

We observed following deficiencies in the inventory control in the selected stores of PSPCL:

- Inventory items had not been segregated into critical and non-critical items.
- ABC analysis as per value of store items was not done.
- In PSPCL, the minimum and maximum levels of inventories were not fixed at the store level. Though the maximum and minimum levels had been fixed at head office level based on consumption of 2011-12 but there is need to revise the levels due to ever changing consumption patterns.

Management of PSPCL while accepting the facts replied (August 2015) that ABC analysis was being carried out on quarterly basis. The reply is not acceptable as no evidence was seen on records.

2.2.9.1 Non-adherence to inventory levels

Chief Engineer (Stores and Workshop), PSPCL had prescribed minimum and maximum levels of major store items which were fixed keeping in view the annual requirement for the year 2011-2012 and no revision in these inventory levels had been made thereafter considering actual consumption of these major store items.

A review of the stock position ending March 2015 of the Central Stores of PSPCL revealed that out of total 53 major store items, prescribed inventory levels were not adhered to in as many as 26 items (49 *per cent*) like ACSR, Stay sets, Earth rods, Cables and transformers, etc. The maximum level had exceeded in case of 9 items and stock level of 17 items was below the minimum level fixed. The excess of material ranged between 16.93 *per cent* and 717.62 *per cent* of the maximum level fixed and shortfall of material ranged between 4.74 *per cent* and 97.33 *per cent* of the minimum level fixed.

Management replied (August 2015) that heavy stock of distribution items had to be maintained in summer due to heavy demand in paddy season. The reply is not supported by facts as in 17 out of 26 items, the stock level were below the minimum level.

2.2.9.2 Lack of co-ordination between PSPCL and PSTCL

After unbundling, PSPCL was made responsible for procurement of transmission equipment and sub-stations up to 66 KV and PSTCL for above 66 KV.

¹⁶ In respect of three Chief Engineer i.e. Chief Engineer/Transmission Systems, Chief Engineer/Stores & Workshop and Chief Engineer/Metering

We observed that material valuing ₹ 11.77 crore relating to 66 KV transmission lines and Grid Sub-stations was lying in PSTCL store, which was of no use to it. The PSTCL decided (March 2014) to ask PSPCL to lift the material at the offered price or at PSPCL recent procurement price with a rebate of 10 *per cent*, whichever was lower. Out of the material worth ₹ 11.77crore, PSPCL after scrutiny of the material at stores, identified suitable material valuing ₹ 2.10 crore. Similarly, material worth ₹ 3.35 crore relating to 132 KV and 220 KV transmission lines and sub-stations was lying in PSPCL stores.

We further observed that PSPCL and PSTCL could not finalise the modalities for transfer of this material to each other and resorted to fresh purchases instead. Resultantly, material valuing ₹ 5.45 crore remained un-utilised even after five years of the corporatisation of the two Companies, with further chances of its deterioration, misappropriation and lapse of warranties.

Management replied (August 2015) that they have now finalised the modalities for transfer of materials and action would be taken for transfer the materials.

2.2.9.3 Non return/ non-lifting of transformers damaged within warranty period

In PSPCL, we noticed that at the end of March 2015, 488 transformers valuing ₹ 1.92 crore¹⁷ which were damaged within warranty period, were not lifted by the suppliers even after lapse of three months¹⁸ of intimation of their damage and 2,393 transformers valuing ₹ 9.42 crore were lying with suppliers for more than three months but not returned. The timely repair of these damaged transformers within the warranty period and recycling of these for operation within reasonable period could have reduced the fresh purchases of transformers to that extent.

Management replied (August 2015) that this was a continuous process and interest was chargeable for period of delay. Reply is not acceptable because recycling of these transformers could have reduced the fresh purchase of transformer to that extent.

2.2.9.4 Non-disposal of irreparable transformers

Damaged distribution transformers are sent to Central Store for repair in Transformer Repair Workshops of PSPCL. The healthy parts of irreparable transformers are extracted and irreparable portion is surveyed off for sale.

¹⁷ 488 T/Fs x ₹ 39376.61 (Average cost of transformer) = ₹ 1.92 crore

¹⁸ The warranty clause of the purchase orders for transformers provides that the supplier shall be responsible to replace free of cost, the whole or any part of the transformer which gets damaged within twelve months from the date of commissioning or 18 months from the date of dispatch whichever is earlier, within three months of intimation of failure/damage.

We noticed that in PSPCL 16,765 irreparable transformers valuing ₹ 27.92 crore were lying un-disposed at various Central Stores at the end of March 2015 and no mechanism had been evolved for disposal of such transformers. We also noted that parts valuing ₹ 0.41 crore extracted from damaged transformers were lying at the end of March 2015.

Management of PSPCL replied (August 2015) that accumulation of irreparable transformers was due to not receiving bids for whole lot. Management reply is not acceptable as PSPCL should make concrete efforts for disposal of irreparable transformers.

2.2.9.5 Blockade of funds due to slow moving/ non-moving items

The Controller of Stores, PSPCL (now CE/ Workshop and Stores) issues directions from time to time to all its Central Stores regarding issue of slow moving/non-moving items to other offices of PSPCL where these items can be used or consider these items for disposal if these are not required any more.

We noticed that as on 31 March 2015, 304 slow moving and non-moving items valuing ₹ 0.65 crore were lying in 12 central stores of PSPCL since long. No action had been taken to identify these items for disposal or issue to other organisations for their utilisation.

Management of PSPCL while accepting the facts replied (August 2015) that list of usable slow moving/ non-moving items have been circulated for identification and early utilisation. Audit also noticed that the Company had circulated the list only in August 2015.

Internal Control System

2.2.10 Internal control is a management tool used to provide reasonable assurance that objectives are being achieved in an economical, efficient and orderly manner.

The following points indicating weak internal control have been noticed:

2.2.10.1 Non rendering/ finalisation of material at site (MAS) accounts

The Company (erstwhile Board) had issued instructions from time to time that concerned JEs should render the accounts of material-at-site (MAS) within one month from the completion of work. The accounts rendered were to be finalised in the divisional office within three months of the completion of works.

We observed that no MIS mechanism had been evolved by PSPCL to ensure timely rendering of accounts and finalisation thereof within the stipulated period. At the end of March 2015, accounts of 4,788 works completed up to March 2014 involving material worth ₹ 103.05 crore had either not been submitted by the concerned JEs or had not been finalised by the concerned

divisions. It was observed that the works completed as early as 1998 had not been closed. The breakup of MAS accounts, not rendered by JEs and those awaiting finalisation at the divisional offices, was not available with the head office of PSPCL.

Management while accepting the facts replied (August 2015) that it reviews the position of pending MAS accounts through Management Information Reports (MIR) and instructs the officers to clear the pending MAS account at the earliest. However, it was observed that MIR were deficient as they did not depict the executing units to which these pending MAS accounts pertain.

2.2.10.2 Physical verification of stock

Materials Accounting Manual prescribes continuous stock taking by stock verifier so that all the material items are covered at least once in a year and random checks by the Sub – divisional officer/ officer in-charge of the store.

We observed that in selected stores of PSPCL, stock verifiers did not conduct physical verification of stock during the period under audit as prescribed and were not conducting verifications so as to be able to cover all materials at least once a year. There was no provision for annual physical verification of stock on the closing date of accounting year to depict correct picture of inventories in the financial statements. The consolidated position of shortages/excesses detected during physical verifications by stock verifier/the Sub-divisional officer/ Divisional officer was not being compiled and analysed at head office level.

Management while accepting the facts stated (August 2015) that instructions have been issued to get the 100 *per cent* physical verification of all stock items. However, it was observed that the orders were only iterating the existing instructions of verification of all stores at least once a year and continues to be silent about institutionalising a system of year end stock verification.

2.2.10.3 Reconciliation of store ledger with financial accounts

We observed in selected Central Stores of PSPCL that value ledger cards as per Materials Accounting Manual were not being maintained, in the absence of which reconciliation of store ledger with financial accounts could not be ensured. The difference of inventory of ₹ 13.56 crore between control ledger and trial balance upto 2013-14 had not been reconciled.

2.2.10.4 Inter-unit transfer

During the scrutiny of records of CE/W&S, PSPCL, Ludhiana it was noticed that 583 number Inter Unit Transfer (IUT) bills valuing ₹ 51.55 crore were pending for adjustment at the end of March 2015. Out of these, bills of ₹6.62 crore pertained to the year 2010-11. Thus, PSPCL did not have adequate

means to ensure that the materials issued from one store to other store were acknowledged in time by the recipient stores.

Management replied (August 2015) that pending IUT bills up to March 2014 have been cleared except the bills of ₹ 6.62 crore pertaining to year 2010-11.

2.2.10.5 Internal audit manual

We observed that PSPCL had adopted the Internal Audit Manual (2004) of erstwhile Board and neither had framed its own Manual nor updated it as per the nature and size of its business, requirements of the latest corporate laws and best auditing practices.

In PSPCL, Office of Chief Auditor is responsible for internal audit. The internal audit of CE/MM and CE/IT had been conducted upto 2013-14. At the end of December 2014, 1648 paras relating to the period 1973-2014 were outstanding in respect of these CEs.

The Statutory Auditors of the PSPCL also reported that internal audit system of the PSPCL was not commensurate with the size of the company and the nature of its business.

Management stated (August 2015) that the internal audit was being strengthened.

Conclusion

The system of Purchases and Inventory control in PSPCL was found deficient. The requirements of material were finalised on *ad hoc* basis. There were delays in finalisation of tenders in original validity period leading to subsequent purchases at higher rates. The basis for distribution of purchase quantity amongst various bidders were not disclosed and transparent. Instances of non-initiation of action against defaulter firms were also noticed. Inventory items had not been segregated into critical and non-critical items. The minimum and maximum levels of inventories were not fixed at the store level. Material at site accounts were not rendered/ closed timely after completion of works. Internal Controls were weak.

Recommendations

We recommend PSPCL:

- i. to update procurement procedures for proper assessment of requirement of materials, timely finalisation of tenders and allocation of quantity amongst various bidders.
- ii. to review inventory levels periodically considering past consumption trend of material, review re-order levels and evolve mechanism to ensure adherence to the inventory levels.

- iii. to adopt good procurement practices of peer utilities.**
- iv. to strengthen internal control systems to ensure timely rendering of materials at site accounts, periodic physical verification of stock and reconciliation of stock ledger with financial accounts.**