PAPERS LAID ON THE TABLE
OF THE RAJYA SABHA
ON 25 AUG 2000

Report of the Comptroller and Auditor General of India

for the year ended March 1999

Union Government (Commercial)

Public Sector Undertakings

Hindustan Antibiotics Limited

No. 6 of 2000

PAPERS TO BE LAID ON THE TABLE OF RAJYA SABHA.

AUTHENTICATED.

NEW DELHI
DATED:- 21-8-2000

[RAMESH BAIS]
MINISTER OF STATE IN THE MINISTRY OF
CHEMICALS & FERTILIZERS.

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PREFACE

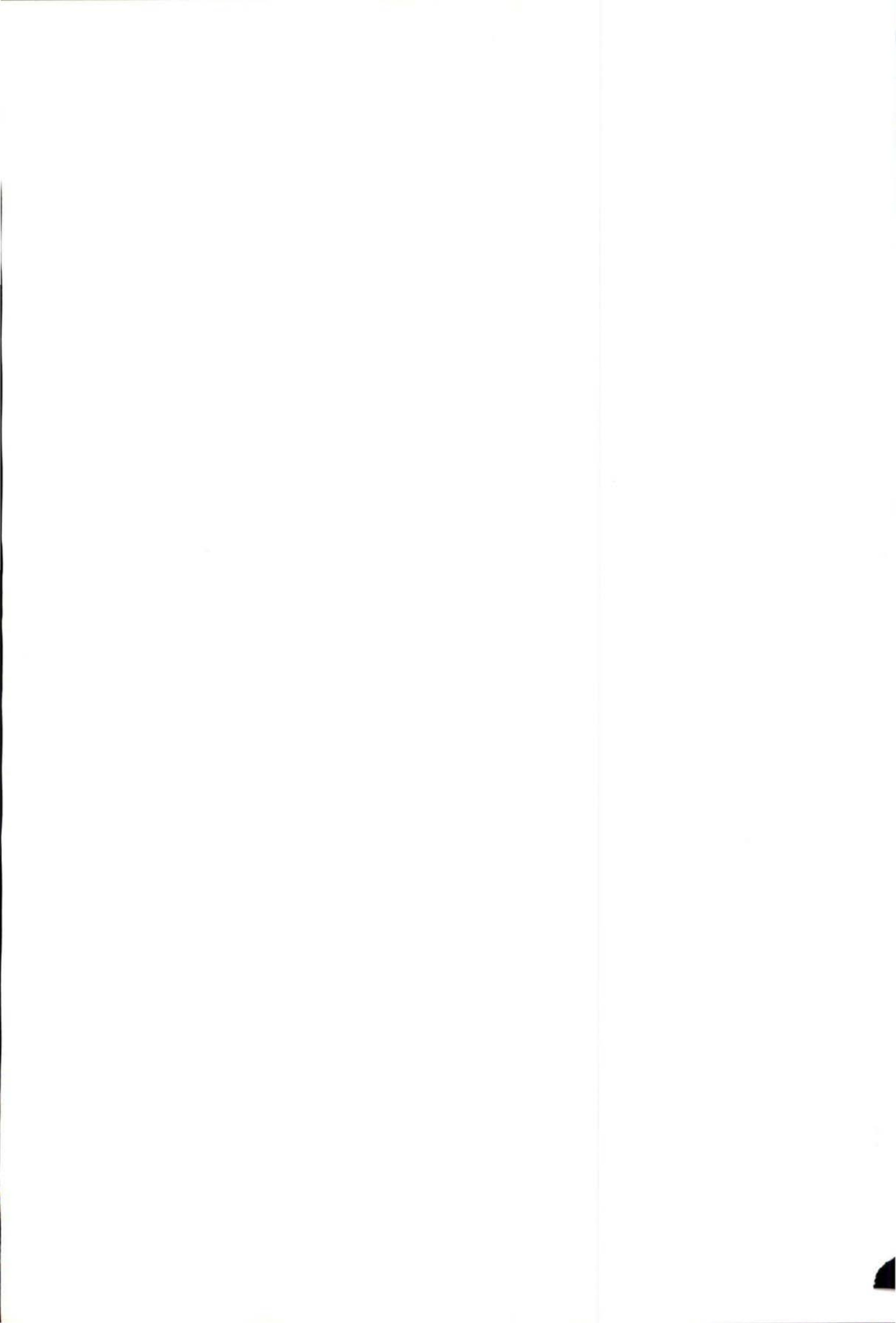
1. Audit Boards are set up under the supervision and control of the Comptroller & Auditor General of India to undertake comprehensive appraisals of the performance of Government Companies and Corporations.

2. The report on **Hindustan Antibiotics Limited** was finalised by the Audit Board consisting of the following members:

1. Shri Samir Gupta	Chairman, Audit Board and Deputy Comptroller & Auditor General (From January 1996 to December 1997)
2. Shri A.K.Chakrabarti	Chairman, Audit Board and Deputy Comptroller & Auditor General (From January 1998)
3. Shri B.B.Pandit	Principal Director (Commercial) & Ex-Officio Member Secretary, Audit Board
4. Shri Sanjeev Saluja	Principal Director of Commercial Audit & Ex-Officio Member Audit Board–I, Mumbai (upto July 1998)
5. Shri P.Sesh Kumar	Principal Director of Commercial Audit & Ex-Officio Member Audit Board–I, Mumbai (From July 1998 onwards)
6. Ms. Vijaya Moorthy	Principal Director of Commercial Audit & Ex-Officio Member Audit Board–I, New Delhi
7.Dr. Kalyan Banerjee	Part-time Member
8.Dr. M.C.Srinivasan	Part-time Member

3. The part-time members were appointed by the Government of India (in the Ministry of Fertilizers & Chemicals, Department of Chemicals & Petro-chemicals) with the concurrence of the Comptroller & Auditor General of India.

4. This report as set out in the succeeding chapters is based on studies, made by the Audit Board, of various aspects of the functioning of the Company and the discussions held with the Secretary, Department of Chemicals & Petro-chemicals and the Management of the Company



OVERVIEW

I. Introduction

Hindustan Antibiotics Limited was incorporated on 30 March 1954 for production of Penicillin. The Company produced Penicillin and streptomycin sulphate etc. in bulk and in the form of capsules, tablets, syrups and fluids. The Company is also presently marketing products like Hemax, Isabgol, Renax, etc. produced by other Companies.

(Paras 1.1 to 1.1.1)

II. Objectives and Corporate plan

Most of the micro objectives of the Company like introduction of five new products per annum, introduction of products in new fields, becoming a market leader in two or three products etc. were not achieved.

(Paras 2.1.1 to 2.1.4)

The performance of the Company in comparison to targets set in the Memorandum of Understanding (MOU) signed with Government during 1995-96 and 1996-97, was rated poor. In view of this no further MOUs were signed by the Company.

(Para 2.3)

III. Financial performance and Working results

The Company incurred loss during all the years under review i.e. 1993-94 to 1998-99.This was due to increased input costs, competition in the market, excess consumption of raw materials and power, excess manpower and delay in revision of prices. The accumulated loss of the Company as on 31 March 1999 was Rs.154.72 crore. However, the Company earned an operating profit of Rs.12.97 crore during 1998-99 due to introduction of cost control measures, leasing out idle pilot plant facilities, implementation of voluntary retirement scheme and alignment of production of formulations with market requirements.

(Paras 3.1.1, 3.2.1 and 3.2.3)

IV Capital structure

The paid up capital of the Company as on 31 March 1999 was Rs.44.84 crore. This has, however, been fully eroded as the net worth of the Company has become negative to the extent of Rs.128.58 crore. In spite of the interest holiday and subsidy of Rs.39.63 crore given on three different occasions between 1983 and 1994, the financial position of the Company failed to improve. In 1997 the Company was declared sick by Board of Industrial Finance and Restructuring (BIFR). The Rehabilitation plan submitted by the

Operating Agency nominated by BIFR and involving infusion of Rs.110.64 crore was awaiting approval of Government (December 1999).

(Paras 3.2.4, 3.3.1 and 3.3.4)

As on 31 March 1999, the Company had invested Rs.2.05 crore as equity capital in its three subsidiaries and provided them loan of Rs.12.15 crore. Two of these subsidiaries had also become sick and were referred to BIFR.

(Para 3.6)

V. Joint Venture Agreement with Max –GB

As the production of Penicillin with the existing technology was inadequate the Company floated a Joint Venture Company (JVC) with Max-GB, an associate of Gist Brocades of Netherland sharing equity on 50:50 basis. Existing Penicillin production facilities having an assessed profitability of Rs.31.68 crore per annum, was leased out to the JVC as per the directives of Ministry at a rental of Rs.17 crore per annum, a sum which was without any rational and verifiable basis. The deliberations leading up to the signing of JVC agreement were characterized by controversy and lack of transparency. The JVC accumulated a loss of Rs.86.99 crore upto 1998-99. It also owed Rs.23 crore to the Company on account of lease rent and cost of other services rendered (August 1999).

(Paras 4.1.1, 4.2.1 to 4.2.8)

VI. Project implementation

During the period from 1982-83 to 1998-99 the Company invested Rs.91.22 crore in 10 projects, of which 9 projects estimated to cost Rs.87.61 crore were completed and one (Rs.3.61 crore) was abandoned. There was time overrun ranging from 3 to 45 months in all the projects completed. Six of these projects also entailed cost overrun which varied between Rs.0.31 crore to Rs.13.61 crore.

Interesting features noticed in implementation of some of the delayed projects were as under:

(Paras 5.1 and 5.2.1)

(i) Intravenous fluids plant

Scope of the project sanctioned (October 1989) by Government for Rs.4.79 crore was widely altered during execution, without the approval of Government/Board. The project was completed at a cost of Rs.18.40 crore with a time overrun of 11 months.

(Paras 5.3.1 and 5.3.2)

(ii) Gentamycin Sulphate

A plant set up in 1982 at the cost of Rs.3.63 crore to produce Gentamycin with Hungarian Technology could not be utilised fully resulting in high cost of production. Being

uneconomical, production was suspended in 1986-87. Upgradation carried out (1991) with Bulgarian Technology at a cost of Rs.2.80 crore also failed to give desired results and production was completely stopped from 1992, rendering the entire expenditure of Rs.6.43 crore infructuous.

(Paras 5.4.1 to 5.4.4)

(iii) Starch Hydrolysate project

Change in the scope of work, delay in taking managerial decisions and in delivery of equipment by suppliers resulted in time overrun of 21 months in setting up (October 1986) of this Plant (Rs.1.91 crore). Till March 1990 production (of raw material for Streptomycin) was less than 10 per cent of the installed capacity. This was due to fall in demand for the end product whereafter production was altogether stopped as new technology was adopted for this purpose.

(Paras 5.5.1 to 5.5.3)

(iv) Penicillin expansion phase- III

The project taken up for the enhancement of penicillin capacity at an estimated cost of Rs.3.23 crore, was actually completed at a total cost of Rs.8.41 crore with a time overrun of 3 months. Many items of cost like interest, salary, power etc. had not been included in the project at the initial stage. Availability of fund, had also not been ascertained.

(Paras 5.6.1 and 5.6.2)

(v) New Non-parenteral facilities

Establishment of facilities for manufacture of non-parenteral drugs* to comply with the requirement of Food & Drug Authority of Maharashtra at a cost of Rs 2.5 crore, was delayed by 28 months. The final cost of the project exceeded the revised cost (Rs 4.02 crore) by 231 per cent resulting in diversion of scarce working capital and indicating poor project formulation.

(Paras 5.7.1 to 5.7.5)

(vi) Packing facilities for Erythropoietin (EPO)

Project for setting up packing facilities for EPO, approved in January 1993 for Rs.7.78 crore, was actually completed in June 1998 at a cost of Rs.13.80 crore. The final cost included a sum of Rs.9.56 crore on account of lease rent as well as interest on borrowed funds necessitated by the time overrun of 45 months. The delay was due to paucity of funds, lack of budgetary support from Government and erosion of profitability on

* *"Non Parenteral Drugs" = Drugs administered orally i.e., other than injectibles.*

account of devaluation of Rupee in 1991. The facilities created were, however, lying idle (December 1999)

(Paras 5.8.1 to 5.8.5)

VII. Project abandoned:

(i) Cephalosporin project

For transfer of technology required in production of cephalosporin the Company entered into an agreement with M/s JCP Martin, U.K. at a total technical know-how fees of US $ 0.9 million, though the firm neither owned the technology nor had a laboratory of its own. The first instalment of US $ 0.3 million was released even though the collaborator had failed to prove the technology at the laboratory level. Consequently the project could not take off and the Company had to write off Rs.3.61 crore spent on the project during 1997-98.

(Paras 5.9.1 to 5.9.6)

VIII. Production performance

(a) Streptomycin Sulphate

Production of Streptomycin decreased from 75 tonnes in 1993-94 to about 18 tonnes in 1998-99 due to fall in demand caused by arrival of more potent and convenient drugs in the market and fall in prices. Company incurred a loss of Rs.9.11 crore on this product in the last six years up to 1998-99.

(Paras 6.4.1 to 6.4.3 and 6.4.5.)

(b) Semi-synthetic penicillin drugs

Facilities for manufacturing this drug were grossly underutilised before production was altogether stopped in 1994-95. This was due to high cost of production as compared to market price. Loss due to idle capacity during years 1994-95 to 1998-99 was Rs.1.15 crore.

(Para 6.5.2)

(c) Formulations

Company incurred a loss of Rs.69.13 crore on production of various formulations (i.e. bulk drugs, vials, capsules, tablets and syrups) during the six years period ended 1998-99.

(Paras 6.6.1 and 6.6.2)

(d) Machine utilisation

Recommendations of the Committee on Public Undertakings (COPU) seeking reporting of idle machine hours to management/Board and critical examination of such reports by Internal Audit for proper follow up action were not implemented.

(para 6.9.1)

IX. Energy conservation

Energy consumption norms of the Company were not fixed on a scientific basis. Loss due to excess consumption of fuel and power between 1992-93 and 1998-99 was Rs.11 crore. The Company had not conducted any energy audit to assess the impact of major energy conservation measures adopted during the above period at a cost of Rs.5.77 crore.

(Paras 7.2.2 to 7.2.5)

X. Research and Development

The Company spent Rs.21.40 crore on 25 R & D projects between 1983-84 to 1998-99. This was 1.2 per cent of the sales revenue whereas in the industry norm was 10 per cent. Out of these seventeen projects costing Rs.11.57 crore were abandoned on the ground that technologies were either non-viable or unsuccessful. However, seven projects involving an expenditure of Rs.9.41 crore were completed and put to use. The remaining one project was under progress.

(Paras 8.3.1 and 8.3.2)

XI. Credit control

The Company has evolved no definite credit policy. Sundry debtors in 1998-99 (Rs.27.23 crore) were 24.04 per cent of the total sales and the percentage of doubtful debts to total book-debts increased from 7.20 per cent in 1993-94 to 19.79 per cent in 1998-99.

(Para 10.3.1)

XII. Export

In the six year period ended 1998-99 the Company incurred total loss of Rs.7.42 crore on the export of its products.

(Paras 10.4.1 & 10.4.2)

XIII. Other topics of interest

The Company paid Rs.19 lakh to an agent to get waiver of delayed payment charges levied by the Maharashtra State Electricity Board on the overdue payment of electricity

bills leading to registration of a case by Central Bureau of Investigation against the then Managing Director and other employees.

(Paras 12.1.1 and 12.1.2)

Failure of the Company to meet the delivery target in an export contract resulted in a loss of Rs.1.86 crore by way of carrying costs of inventory, non-recovery of production cost, loss of interest on unrealised dues and extra expenditure on air freight. Company also suffered an additional loss of Rs.1.46 crore because the export agent offered lower prices than what he had received from the foreign importer.

(Paras 12.2.1 to 12.2.4)

An interest free advance of Rs.1 crore was sanctioned by the Managing Director to a private firm (from September 1993 to July 1994) without prior approval of the Board at a time when the Company faced severe cash crunch. Case for recovery of Rs.4 crore due from the firm was under arbitration (August 99).

(Paras 12.3.1 and 12.3.3)

1. INTRODUCTION

1.1 Hindustan Antibiotics Limited (HAL) was incorporated on 30 March 1954 to take over control and management of the factory set up at Pimpri by the Government of India for production of Penicillin with the assistance of United Nations International Children Education Fund (UNICEF) and World Health Organisation (WHO). The Company is a Government of India enterprise under the administrative control of the Ministry of Chemicals and Fertilizers, Department of Chemicals and Petrochemicals.

1.1.1. Presently the Company produces bulk drugs like Fortified Procaine Penicillin, Benzyl Penicillin Sodium Salt and Streptomycin Sulphate. It also prepares formulations in the form of capsules, tablets, syrups, fluids of Penicillin, Streptomycin Sulphate and Ampicillin. A portion of its production of Streptomycin is also vialled. From the year 1991, 1992 and 1995, respectively, the Company started marketing products like Hemax, Isabgol, Renax, etc., of other companies, purely on trading basis. The Company leased (October 1995) its Penicillin-G first crystals manufacturing facility to a Joint Venture Company (JVC) set up with Max-GB Limited. The prices of some of the products of the Company such as Streptomycin Sulphate, Pen G sodium, Pen G Procaine, Benzathine Penicillin and 6 Amino Pencillinic Assay (6 APA) are determined/fixed by Government of India under Drugs (Price Control) Order (DPCO) which was introduced in 1970 with the intention to check the profit earned by pharmaceutical companies and to ensure availability of common drugs at reasonable prices. Maximum sales price of a bulk drug is fixed by the Government in a manner so as to yield a post tax return of 14 per cent on the net worth or 22 per cent return on the capital employed, whichever parameter is chosen by the manufacturer. DPCO has revised the prices thrice in the past i.e. in 1979, 1987 and 1995.

1.2 Organisational Structure

1.2.1 The Managing Director (MD) is the Chief Executive of the Company and works under the overall control of the Board of Directors (Board). Besides, there is only one post of functional Director, viz. Director (Finance) which is lying vacant since March 1998. Two officials of the Ministry of Chemicals and Fertilizers represent the Government on the Board of Directors. In addition, one representative of the BIFR also sits on the Board of Directors, since 31 March 1997. The Company has its manufacturing plants at Pimpri, (near Pune). It also has twelve regional sales offices (March 1999) located throughout the country.

1.3 Scope of Audit and main audit findings

1.3.1 The working of the Company was last reviewed and reported upon by the Comptroller and Auditor General of India (CAG) vide Part XI of the Union Government (Commercial) Audit Report 1970-71 and by the Committee on Public Undertakings (COPU) in their 80th Report (Fifth Lok Sabha 1975-76) and again in their 67th Report (Seventh Lok Sabha 1982-83). The COPU had recommended (April 1983) that the idle machine hour details should be reflected in the monthly/quarterly reports to the Management/Board. It had also suggested that internal audit should critically examine such reports to enable proper follow up action. These recommendations have, however, not been implemented as discussed in Chapter 6.9. Similarly, another recommendation of COPU calling for qualitative strengthening of the R&D and closer co-ordination amongst all drugs and

pharmaceutical manufacturing companies in the Public Sector in relation to their R&D activities, remain unimplemented, as detailed in Chapter 8.

1.3.2 The present appraisal covers a period of 6 years from 1993-94 to 1998-99. It brings to light the following significant observations related to the functioning of the Company for the period of 6 years ending 31 March 1999:

- The Company had been incurring loss for the last five year ended 1998-99. Accumulated loss of Rs.115.28 crore as on 31 March 1997 increased to Rs.154.72 crore by the end of 1998-99 and had eroded its equity of Rs.41.84 crore many times over. Due to this development the Company on 31 March 1997, had been declared by BIFR to be a sick Company. IDBI which had been appointed as the operating agency had submitted (July 1998) to BIFR a proposal for its revival. This was pending for consideration with Ministry (August 1999). The Company was beset with problems like idle investment, underutilised capacity, high costs of production, product obsolescence, high interest burden, weak marketing strategy, wide product portfolio etc.

- The Company went through major capital restructuring in March 1994. Concessions given in the relief package included, (i) conversion of outstanding Government loans of Rs.42.37 crore into equity, (ii) conversion of interest of Rs.17.79 crore accrued on outstanding loans into interest free loan and (iii) conversion of interest liability of Rs.9.15 crore accruable in future years into interest free loan.

- The efforts of the Company in the last decade to diversify into new products and to effect expansion of its existing capacities had not yielded the expected results. In fact, the negative returns on these investments were threatening the survival of the Company. With the liberalisation of the economy, the Company had lost the advantage of price preference, it used to get from Government departments/public sector. Hence it was unable to compete with private sector units which had lower overheads and also enjoyed tax benefits. Further, with the leasing of its only profit making production facilities i.e., Pen G plant, to JVC, the Company had been left with only loss making products.

- The Ministry while accepting many of the limitations/weaknesses in the functioning of the Company as pointed out by Audit, stated during the Audit Board Meeting (December 1997) that specific cost centers had been identified and that only such products would be produced as would be economically viable. Marketing set up would be tightened. It was also stated that the Company had taken steps to reduce costs by bench marking them with comparable costs of other companies. It was seen that the Company earned an operating profit of Rs.12.97 crore during 1998-99 due to introduction of cost control measures, leasing out idle pilot plant facilities, implementation of voluntary retirement scheme and alignment of production of formulations with market requirements.

2. OBJECTIVES

2.1 Objects:

2.1.1 The main objects of the Company as laid down in the Memorandum of Association were to produce, buy, sell, export, import and deal in penicillin and penicillin preparations, all other antibiotics, sulpha drugs and preparations, anti malarials of all kinds and any other medicines. The Company's production predominantly consists of antibiotics like penicillin and streptomycin sulphate. There has been very little diversification into other medicines.

The Company failed to achieve most of its Micro-objectives.

2.1.2 The micro objectives, which the Company had set before itself, in accordance with Bureau of Public Enterprise guidelines, were approved by the Ministry in August 1988. Some of the important micro objectives were:

a) To increase turnover to Rs.100 crore by 1990-91 and Rs.150 crore by 1994-95;

b) To increase trade sales by 33.33 per cent of total sales by 1990-91 and to maintain the same ratio thereafter;

c) To become a market leader in at least two or three products by 1994-95;

d) To introduce at least five new products every year;

e) To achieve 15 per cent return on capital employed by 1994-95;

f) To introduce products in anti-diabetic, anti-malarial and anti-blindness therapeutic groups, which were not then covered;

g) To improve level of finished goods inventory to 10 per cent of net sales;

h) To reduce debtors to the level of 16 per cent of sales by 1994-95;

i) To diversify into other fields like cosmetics, food products and synthetic drugs;

j) To increase the efficiency of existing operations to provide maximum returns on investment and to generate more internal resources; and

k) To promote the sale of Hamycin formulation and to reach a sale of Rs.3 crore by 1994-95.

2.1.3 None of the above mentioned objectives except (a) and (b) was achieved by the Company. During a meeting (17 December 1997) of the Audit Board, the Ministry stated that :

a) the Company could not achieve its basic objectives due to the nature of drugs and pharmaceutical industry in the country which was characterised by difficult trade practices and cut throat competition.

b) Multinationals exerted pressure to influence pricing decisions while chemists played an influential role in determining the magnitude of retail sales of formulations.

c) Advertisement and sales promotion practices determined the brand preference. The choice before the Company was to incur huge selling expenses in promoting brand sales or to sell the basic formulations in bulk at lower prices.

d) Company also lost the assured market of Government departments because most of the departments had switched over to tendering system for effecting purchases. Consequently, private sector and multinational companies were able to outprice the Company.

2.1.4 The explanation by the Ministry for the failure of the Company in meeting micro objectives underlines the inadequacies of Management as well as the Ministry which did not prepare the Company for meeting the challenges of operating outside the umbrella of Government patronage. There was failure in controlling excess consumption of raw materials and energy, and overheads, which rendered the Company's products unremunerative. Besides, there was no review of the product mix of the Company in the light of the changing market conditions, as a result of which products of the Company like Streptomycin lost their importance, efficacy and utility due to introduction to the market of more effective drugs by competitors. The Company did not keep pace with its competitors in bringing out new drugs. This was due to its inadequate R&D effort resulting mainly from paucity of funds. Two projects implemented by the Company to introduce new drugs viz. Cephalosporin C and Erythropoietin also did not fructify due to faulty project formulation as discussed in paras 5.8 and 5.9. Though the Ministry had representatives on the Board of Directors of the Company, no proper guidance/assistance which could have helped the Company overcome its problems was given at any stage. Ministry agreed (December 1997) that the Company was mismanaged in the past.

2.2 Corporate Plan

2.2.1 The COPU in its 67th Report (Seventh Lok Sabha 1982-83) had recommended formulation of a Corporate Plan. The Company had agreed to submit the same by March 1984. The first Corporate Plan covering the period 1991-2000 was submitted to the Government only in November 1991 in spite of its commitment to COPU to formulate the same by March 1984. The impetus for preparing Company's first ever Corporate Plan was external because without a Corporate Plan Government was not prepared to sign the Memorandum of Understanding (MOU) with the Company. The Company, therefore, worked without a Corporate Plan for 7 years. Unproductive capital investment in projects, borrowed at commercial rates, during the period 1982-83 to 1998-99 (as discussed in subsequent chapters) led to an increase in the interest burden and repayment of loan which eventually affected the financial health of the Company. Consequently, the Company failed to achieve the planned targets in spite of Corporate Plan having been

formulated, as shown in the table below:

(Rs. in crore)

Particulars	**1993-94**	**1994-95**	**1995-96**	**1996-97**	**1997-98**	**1998-99**
Production (Plan)	287.58	344.32	372.71	419.81	465.22	519.23
Actual	206.73	183.31	181.32	116.82	98.12	118.64
Achievement (%)	**72**	**53**	**49**	**28**	**21**	**23**
Sales (Plan)	262.34	310.21	331.62	370.87	406.83	452.74
Actual	199.37	197.82	169.82	134.71	105.75	113.26
Achievement (%)	**76**	**64**	**51**	**36**	**26**	**25**
Profit before tax (Plan)	15.21	21.71	27.85	37.09	40.68	45.27
Actual	3.60	(- 15.95)	(- 21.51)	(- 31.07)	(- 26.08)	(-12.93)
Achievement (%)	**24**	---	---	---	---	---

Production declined steadily during 1993-94 to 1997-98 but picked up in 1998-99. Similarly sales showed a continuous declining trend from 1993-94 to 1997-98 and slightly picked up in 1998-99. There was a reduction in loss in 1998-99.

2.3 Memorandum of Understanding (MOU)

The overall performance grading of the Company decreased from "GOOD" in 1993-94 to "POOR" in 1996-97.

2.3.1 The Ministry and the Company had been signing MOUs since 1991-92. The MOU aimed at modernisation and development of the Company for meeting the health care needs of the country by manufacturing and marketing antibiotics, drugs and other products related to health care and Agrovet* of high quality at reasonable prices. Based on the targets laid down in the MOU signed by the Company for the years 1992-93 to 1997-98, the overall performance grading of the Company decreased from "Good" in 1993-94 to "Poor" in 1996-97. The performance of the Company was poor in respect of major indicators such as production, trade sales, sundry debtors, gross margin, and finished goods during 1995-96 and 1996-97. Keeping in view the overall poor rating of the Company during 1996-97, the Government did not sign with it any MOU for the years 1997-98 and 1998-99.

** Agrovet - Agricultural and veterinary product*

3. FINANCIAL POSITION AND CAPITAL STRUCTURE

3.1 Financial Position

3.1.1 The table below summarises the financial position of the Company for the last six year ended 1998-99:

(Rs. in crore)

Years	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99
LIABILITIES						
a) Share Capital i) Paid up capital ii) Deposits awaiting allotment of shares	 39.91 0.43	 *39.91 0.43	 39.91 0.43	 40.91 0.93	 42.91 0.43	 43.41 1.43
b) Reserves and Surplus i)Capital Reserve ii) Committed Reserves	 0.01 1.48	 0.01 1.47	 0.01 4.21	 0.01 4.07	 - 3.92	 - 3.02
c) Borrowings i) From Government of India ii) From others iii) Interest accrued and due	 76.38 109.63 15.15	 78.22 8.33 119.79	 80.05 121.41 10.58	 83.38 123.34 16.36	 84.88 117.14 34.26	 86.38 113.19 50.78
d)Trade dues and current liabilities (including provisions)	53.43	48.26	79.69	61.68	70.52	74.71
TOTAL	**296.42**	**296.42**	**336.29**	**330.68**	**354.06**	**372.92**
ASSETS						
e)Gross Block	126.43	131.51	149.27	155.03	155.53	169.59
f)Less : Depreciation	48.66	53.51	59.04	64.71	70.65	77.10
g)Net Block	77.77	78.00	90.23	90.32	84.88	92.49
h)Capital work-in-progress	14.54	23.27	17.08	12.58	13.59	0.28
i)Investments	2.05	2.05	7.05	7.05	7.05	7.05
j)Current assets, loans and advances	138.58	108.72	117.00	85.51	81.68	99.68
k)Capitalised expenditure (to the extent not written off)	23.39	22.00	21.76	19.94	22.83	18.70
l)Accumulated loss	**40.09**	**62.38**	**83.17**	**115.28**	**144.03**	**154.72**
TOTAL	**296.42**	**296.42**	**336.29**	**330.68**	**354.06**	**372.92**
****Capital employed (g+j-c(iii)-d)**	**147.78**	**130.14**	**116.96**	**97.79**	**61.80**	**66.68**
*****Net worth (a+b(i)-k-l)**	**(-)23.14**	**(-)44.04**	**(-)64.60**	**(-)93.37**	**(-)123.53**	**(-)128.58**
Debt Equity Ratio	**4.61:1**	**4.90:1**	**4.99:1**	**4.94:1**	**4.66:1**	**4.45:1**

3.1.2 The accumulated loss of Rs.40 crore in 1993-94 was the culmination of two decades of continuous losses (Since 1973-74) which could not be reversed and led to complete erosion of its net worth by 1992-93. As of 31 March 1999, the net worth had turned negative to the extent of Rs.128.58 crore.

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* *Does not include the conversion of loan into equity of Rs.42.37crore pending completion of formalities.*

** *Capital employed represents net fixed assets plus working capital.*

*** *Net worth represents paid-up-capital plus free Reserves less intangible assets less accumulated losses.*

3.2 Working Results

3.2.1 The working results of the Company from 1993-94 to 1998-99 were as follows:

(Rs. in crore)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99
i. **Total income** (after adjustment of stock)	216.07	193.50	205.67	140.01	123.60	148.87
ii. Consumption of Raw Materials	88.82	75.68	93.77	44.64	32.61	37.76
iii. Power and Fuel	32.41	34.08	33.49	39.60	40.08	44.34
TOTAL (ii + iii)	**121.23**	**109.76**	**127.26**	**84.24**	**72.69**	**82.10**
iv. Expenses :						
a. Salary and Wages	18.95	21.77	23.74	18.66	20.31	18.86
b. Other expenses	48.73	55.34	53.16	40.11	33.24	34.94
c. Depreciation	4.74	4.86	5.56	5.78	5.96	6.46
d. Interest on Loan	18.82	17.72	17.46	22.29	17.48	19.43
TOTAL	**91.24**	**99.69**	**99.92**	**86.84**	**76.99**	**79.69**
v. Net Profit (+)/ Loss (-) (i-(ii+iii+iv))	3.60	-15.95	-21.51	-31.07	(-)26.08	(-) 12.92
Add: Provision and Reserves not considered necessary	--	1.08	--	--	-	-
TOTAL	**3.60**	**- 14.87**	**- 21.51**	**- 31.07**	**- 26.08**	**- 12.92**
Less : Net Prior Period expenditure	16.33	7.43	+0.56	1.18	2.83	+1.34
PROFIT (+) / LOSS(-) BEFORE TAX	**- 12.73**	**- 22.30**	**- 20.95**	**- 32.25**	**- 28.91**	**- 11.58**
Operating Profit (+) /Loss (-) before interest and depreciation (iv (c) + iv (d) + v)	27.16	6.63	1.51	- 3.00	- 2.64	12.97

3.2.2 Though the Company earned a modest profit of Rs.3.60 crore during 1993-94, prior period adjustments on account of provision of interest on non plan Government loan turned it into a loss of Rs.12.73 crore. Increase in input cost, consumption of raw materials, power and fuel in excess of norms, led to sharp decline in its operating profits and loss mounted during the next two years viz. 1994-95 and 1995-96. This position worsened due to transfer of the profit making Pen-G production facilities to JVC during October 1995. The overall production of the Company fell in the subsequent two years viz. 1996-97 and 1997-98.

3.2.3 Inadequacy of working capital caused by continuous loss in the previous years, competition in the market, delay in revision of prices by the Government of India under Drugs (Price Control) Order (DPCO) and excess manpower also contributed to losses in all these years as indicated in the table above. During 1998-99, however, the Company, for the first time in the preceding last five years, earned significant operating profit of Rs.12.97 crore. This was attributed to cost control measures, leasing out of pilot plant facilities which were lying idle earlier, implementation of Voluntary Retirement Scheme (VRS) (387 employees had retired), control over administrative expenditure like

telephone charges and subsidy to schools, alignment of formulation production within market requirements, etc.

3.2.4 Since its accumulated loss of Rs.115.28 crore, as on 31 March 1997, had eroded paid-up capital and free reserves by 2.5 times, the Company was declared sick by BIFR. Industrial Development Bank of India (IDBI) was appointed as the Operating Agency to prepare and submit a rehabilitation plan for the revival of the Company. Based on the rehabilitation plan submitted by IDBI (July 1998), the Ministry had sent to the Cabinet Committee of Economics Affairs (CCEA) a note seeking relief of Rs.110.64 crore. The proposal had not been approved so far (December 1999).

3.3 Capital restructuring

3.3.1 The authorised capital of the Company was Rs 45 crore. The paid up capital up to 1995-96 was Rs 39.91 crore, besides which shares worth Rs.0.43 crore were pending allotment. In the next three years the paid up capital of the Company as well as share pending allotment went up by an aggregate sum of Rs 4.5 crore. Consequently, at the end of 1998-99, the paid up capital of the Company was Rs.43.41 crore and shares worth Rs 1.43 crore were pending allotment.

<u>As on 31 March 1999</u>

(Rs. in crore)

- ***Paid up Capital:*** ***44.84***
- ***Accumulated Loss:*** ***154.72***
- ***Deferred revenue Expenditure:*** ***18.70***
- ***Net worth:*** ***(-) 128.58***

3.3.2 It was observed in audit that from 1982-83 onwards the Company had received an aggregate interest subsidy of Rs.39.63 crore. Apart from this, the Government on three different occasions restructured and rescheduled the debt of the Company as indicated in the table below:

(Rs. in crore)

Mile Stones	January 1983	October 1988	March 1994
Loan outstanding	-	61.02	201.16
Outstanding treated as fresh loan	35.38	44.02	12.60
Interest added to loan	8.64	4.55	26.94
Interest waived	-	-	0.04
Period of Interest holiday	5 years	3 years	5 years

3.3.3 Despite these measures the financial position of the Company had not improved. Consequently, by 1992-93, it again defaulted in payment of interest. The loss was attributable to "excess consumption of raw material, energy, excess deployment of manpower, and inability of the Company to operate in a competitive market" as detailed in paras 6.8, 7.2 and 10.1.

3.3.4 The Ministry stated (June & December 1997) that the price control which affected the viability of majority of the products marketed by the Company as well as competition from the private sector units had affected the profitability of the Company. According to the Ministry the Company should have been vigilant right from 1980-85 and restructured its objectives and strategies to ensure better product mix, objective pricing and

appropriate selling mechanism. It further added that the Company should have resorted to aggressive marketing and developed new products and modernised the plants and machinery. The Ministry also admitted that requisite support from the Government was not made available to the Company at the appropriate time.

3.4 Cash Management

3.4.1 During 1989 to 1995 the Company obtained short term and long term loans from various Financial Institutions (FIs) but failed to repay either the principal or interest on due dates. As a result, the Company had to pay huge penalties and incur additional financial burden due to increase in interest rates. The precarious financial condition of the Company can be gauged from the fact that in March 1994, it could not even afford to pay registration fees that was required for conversion of loans of Rs.42.37 crore into equity as agreed to by the Government. Thus, the Company lost a good opportunity to reduce its interest burden. The Company had also failed to pay loan installments of Rs.3.89 crore each during 1997-98 and 1998-99. Based on the recommendation of IDBI the Company had been pursuing the FIs for grant of relief from the burden of interest and penal interest amounting to Rs.8.14 crore. However, the Company was unable to get any relief till August 1999 and the rehabilitation package recommended by IDBI was yet to be approved by BIFR.

3.4.2 Although the Company was facing acute working capital shortage it opened (1995) an exclusive current account to facilitate timely payment to a private party (i.e. Hindustan Antipests Private Limited, Hyderabad) despite the fact that it was not contractually bound to do so (as detailed in Para 12.3 of this appraisal). Thus the Company had exhibited extraordinary sensitivity to the financial interests of a private company when its own financial condition was in doldrums.

3.5 Borrowings

3.5.1 As on 31 March 1999, the Company had borrowed short-term and long-term loans from (i) Government of India (Rs.86.38 crore), (ii) FIs, Public Sector Undertakings (PSUs) and others (Rs.59.23 crore). Total interest accrued and due on various such loans as on 31 March 1999 was Rs.36.53 crore. Consequent on restructuring of capital approved by the Government in March 1994 no interest was due on Government loans. As on 31 March 1999 the Company had also availed of Cash Credits (CC) of Rs.68.22 crore to meet its working capital requirements. This exceeded the CC limit of Rs.35 crore by 94 per cent. In addition the Company had also borrowed (August 1989) Rs.35 crore at coupon rate of 13 per cent per annum through issue of bonds by private placement with Canbank Financial Services. The bonds matured in November 1996 but had not been redeemed so far (September 1999).

3.5.2 Loan From Oil and Natural Gas Commission (ONGC).

The Company obtained (December 1988) a loan of Rs.10 crore from ONGC at the rate of 14.5 per cent per annum to meet its working capital requirement. As the Company failed to repay the principal and interest, ONGC increased (December 1991) the rate of interest to 22 per cent resulting in additional interest burden of Rs.75 lakh per annum.

3.6 Investments in Subsidiaries

3.6.1 As on 31 March 1999, the Company had invested Rs 2.05 crore as equity capital in its three subsidiaries and provided to them a loan of Rs.12.15 crore. The Ministry stated (April 1998) that the loan was provided to enable the subsidiary companies to carry out their day to day operations. The reply is not tenable, as the Company was paying interest to State Industrial Investment Corporation of Maharashtra Limited (SICOM) while getting no returns from the above loans to subsidiaries. Though one of the subsidiaries viz. Karnataka Antibiotics and Pharmaceuticals Limited, was earning moderate profits, the other two subsidiaries viz. Maharashtra Antibiotics and Pharmaceuticals Limited and Manipur State Drugs and Pharmaceuticals Limited had turned sick since November 1996 and June 1997, respectively. The BIFR to which both the subsidiaries had been referred to, had, however, not approved any relief package for their revival (September 1999).

3.7 Goa Antibiotics and Pharmaceuticals Limited (GAPL)

3.7.1 At the instance of Government of India the Company divested (1987-88) its shareholding (Rs.43.35 lakh) in GAPL, a subsidiary, by selling shares to Economic Development Corporation, Goa, for a sum of Rs.16.57 lakh. A loss of Rs.26.78 lakh (43.35 lakh – Rs.16.57 lakh) was incurred in this transaction. The resultant loss suffered by the Company had not been reimbursed by the Government of India for the last six years despite a claim having been lodged by the Company.

4. JOINT VENTURE AGREEMENT

4.1. Background

4.1.1 In December 1994 the total production of Penicillin (Pen G) within the country was sufficient to meet only 45 per cent of requirement. Balance requirement was met through imports. Price of Penicillin, which is controlled under DPCO 1995, was Rs.1021/Billion Units (BU). This was 57.07 per cent higher than the landed cost of imported Penicillin (Rs.650/BU.) Main reasons for the high cost of indigenous Pen G were low yield and low extraction efficiency.

4.2 Technology Upgradation

4.2.1. In its efforts to improve the quality and yield of Pen G strain, the Company switched (1989) from Filamentous Toyo Jozo strains imported from Japan to Pellety strains available from Pan lab Inc., USA. The Company acquired the strain from Pan lab and tried to achieve the yield at pilot and commercial plant level. An expenditure of Rs.2.12 crore was incurred on this effort over five years up to 1996-97. The Company could, however, obtain only 31000 u/ml of Pen-G against the yield of 55000 u/ml expected at broth level. Its failure to achieve high yield from the imported strains of penicillin and anticipated addition of three new production units in the private sector, each capable of producing 1000 million mega units of penicillin, made it imperative for the Company to improve productivity through a collaborator. In January 1994 Gist Brocades of Netherlands (GB), the leading producers of penicillin in the world was chosen as the collaborator.

A joint Venture agreement was signed with Indian associates of Gist Brocades of Netherlands under controversial circumstances. The handling of the matter by the Government and the Board of Directors was inept and non-transparent.

4.2.2 Accordingly, the Company, on 20 June 1994, signed a joint venture agreement (JV) with Max-GB, an Indian associate of Gist Brocades of Netherlands. Joint venture provided for:

- Equity participation in the ratio of 50 per cent share for each party.
- Transfer of existing facilities for manufacture of Pen-G to the Joint venture on a lease rent of Rs.17 crore per annum.
- Production of penicillin using GB technology.

4.2.3 The new Joint Venture Company (JVC) called Hindustan Max-GB Limited was approved by the Cabinet Committee on Economic Affairs (CCEA) a year later (June 1995) and started functioning from 8 October 1995.

4.2.4 By the end of 1998-99 the JVC had incurred a total loss of Rs.75.55 crore. This excluded unadjusted deferred revenue expenditure of Rs.11.44 crore. An amount of Rs.23 crore was due from the JVC to the Company as on August 1999, on account of lease rent as well as cost of services and utilities provided.

4.2.5 Audit examination of the circumstances and the process leading to the setting up of JVC revealed certain unusual features as indicated below:

- Though the MD of the Company had proposed to visit Holland for the express purpose of finalising the Memorandum of Understanding (MOU) with GB, the Government while allowing the visit during August 1993, debarred the MD from making any commitment in the matter. It is unclear why the MD was allowed to undertake the journey at all when Government was unwilling to repose confidence in his negotiating skills.

- The MD after return from Holland in (September 1993) proposed an MOU with GB in preference to offers for a similar MOU by Ranbaxy and Pharmaceutical Business Group (PBG) citing urgent need for enhancement of penicillin production in the country. Board of Directors in its meeting on 26 October 1993 differed with the proposal and directed the former to obtain proposals from other potential collaborators.

- Though various proposals were received, the sub committee of the Board (here after sub-committee) set up for evaluating such proposals found only the proposal from Max-GB complete and acceptable. The terms offered by Max-GB including lease rent of Rs.13 crore per annum for transfer of Pen-G plant to the JVC was the same as had been discussed by the MD with Max-GB five months earlier during his visit to Holland. This makes it clear that Ministry's action in allowing the MD to visit and discuss the terms of JVC agreement had compromised the ability of the Board to negotiate better terms.

- Prompted by letters from certain Member of Parliament, the Government directed the sub-committee to look into, interalia, the reasonability of the lease rent being offered by Max-GB. Though the sub-committee had concluded that a minimum lease rent should be fixed on the basis of assessed minimum profitability of the plant at Rs.31.68 crore per annum, the Company neither accepted this recommendation nor reworked as desired by the Board the lease rent after taking into account depreciation, interest on the proportionate lease rent (to be borne by the Company) and income tax liability. No reasons were on record for overlooking the views of the Sub-committee.

- The Company instead referred (May 1994) the question of lease rent to one Prof. M.M.Sharma, Director, Department of Chemical Technology, Bombay University who opined that lease rent of Rs.13 crore per annum offered by GB was reasonable without explaining the basis on which such opinion had been formed. The credentials of Professor Sharma for expressing an opinion on an accounting matter were never brought on record and were, therefore, susceptible to doubt.

- Pursuant to a directive by the Minister for Chemicals and Fertilizers on 20 June 1994 asking for conclusion of the agreement between the Company and Max-GB without further loss of time and determination of lease rent at any sum between Rs.13 crore per annum (recommended by Prof. Sharma) and Rs.16.38 crore per annum (calculated by Department), a Presidential directive was issued to the Company on the same day asking it to enter into an MOU at a lease rent to be negotiated by a committee comprising of MD, HAL, a part time official Director on the Board of the Company, the Joint Secretary and Financial Advisor, Ministry of Chemicals and Fertilizers and Joint Secretary in the Department of Chemicals and Petrochemicals. The Company management complied with this directive with utmost promptness and

entered into an MOU with GB on 20 June 1994 itself. The MOU provided for payment of lease rent of Rs.17 crore per annum by the JVC.

- No calculations were available on record or produced to audit to indicate the basis on which the lease rent of Rs.16.38 crore or Rs.17 crore per annum as recommended by the Department had been determined.
- Similarly no records of discussion or minutes relating to the question of lease rent or negotiations with Max-GB were maintained either by the MD or by the negotiation committee.

4.2.6 Justifying the acceptance of lease rent of Rs.17 crore per annum without taking into account the minimum profitability of the plant at Rs 31.68 crore per annum as recommended by the sub-committee, the Ministry stated (June 1997) that the assumptions made by the sub-committee were based on incorrect figures of installed capacity and cost of production whereas Prof. Sharma's evaluation was based on the latest cost cum technical study report of Bureau of Industrial Costs and Prices (BICP). The Ministry's averments were unacceptable in the absence of any definite set of calculations in support of lease rent recommended by Prof. Sharma. In his report Prof. Sharma had merely stated that lease rent of Rs.13 crore per annum was 'reasonable' which at best was a vague statement and hence did not constitute sufficient evidence of the correctness of this assessment. In accepting this amount as a benchmark, the Ministry was, at the least, being gullible.

4.2.7 As regards the justification for issuing a Presidential directive to the Company, the Ministry replied (June 1997) that the issue of a directive in the affairs of the Company which included the commercial matters, was a right conferred upon the President of India by Memorandum and Articles of Association of the Company. The Ministry further stated (July 1998) that as the signing of the MOU was taking a long time, they had advised the Company to negotiate the lease rent in such a manner that the negotiations did not drag on. Ministry's directive in a normal business matter, as well as the undue haste with which the Company complied with it on the same day and the fact that no records of negotiations or profitability calculations, were maintained would indicate that Company was rushed into clinching a deal with the Indian associate of GB. Thus interference on the part of the Ministry had rendered the decision making process non-transparent besides depriving the Company an opportunity to negotiate better terms in the deal.

4.2.8 The Ministry attributed the loss of Rs.86.99 crore accumulated by the JVC up to 31 March 1999 to crash in the prices of Pen-G which were prone to fluctuations and competition from private sector firms. This explanation, however, is not convincing because the JVC suffered heavy loss during the initial years 1995-96 (Rs.18.26 crore) and 1996-97 (Rs.24.37 crore) as its cost of production was very high at Rs.51.45 lakh/MMU and Rs.10.67 lakh/MMU in comparison to the selling price of Rs.8.90 lakh/MMU and Rs.7.36 lakh/MMU, respectively, during these years. Though the JVC brought down its cost of production to Rs.6.48 lakh/MMU by 1997-98 and Rs.6.29 lakh/MMU by 1998-99, it did not derive much benefit because the selling price also crashed to Rs.5.18 lakh/MMU and Rs.5.10 lakh/MMU, respectively, during these years.

5. PROJECT IMPLEMENTATION

5.1 Projects undertaken

During 1982-83 to 1998-99 Company took up 10 projects in which Rs.91.22 crore were invested as detailed below:

		No. of projects	Investment for creation of new/additional capacities (Rs. in crore)
(i)	Projects completed	9	87.61
(ii)	Projects written off	1	3.61
	TOTAL	**10**	**91.22**

5.2. Completed Projects

- ***Nine projects completed from 1982 to 1999.***

Total cost: ***Rs.87.61 crore***

Cost overrun: ***ranging from Rs.0.31 crore to Rs.13.61 crore.***

Time overrun: ***ranging from 3 months to 45 months.***

5.2.1 During 1982-83 to 1998-99 the Company had completed nine major projects as detailed in Annexure-I, at a total capital cost of Rs.87.61 crore. Time over-run in implementation of these projects ranged from 3 to 45 months. In 6 out of the 9 projects there was cost over-run ranging from Rs.0.31 crore to Rs.13.61 crore which worked out to 16 to 284 per cent of the original project cost.

5.2.2. Reasons for cost and time overrun were: (i) difficulties in installation of equipment in the existing plants, (ii) change in the scope of work, (iii) price escalation, (iv) variation in customs duty, taxes, excise duty, etc., (v) non-availability of steel and cement, (vi) delay in getting import license, (vii) strike at the Company, and (viii) late arrival of foreign experts.

5.2.3 Important aspects noticed in examination of six out of the nine projects wherein the cost and time overrun were considerable, are discussed in the succeeding paragraphs:

5.3 Intravenous Fluids Plant

Completed at a cost of Rs.18.40 crore against the estimated cost of Rs.4.79 crore with a time overrun of 11 months.

5.3.1 The Government approved (October 1989) 'intravenous fluids' project with latest, fully automatic and sophisticated 'blow-fill-seal system'* at an estimated cost of Rs.4.79 crore. The scheduled date of completion was April 1991. But the project

* *Name of the plant*

was completed in March 1992 and the total expenditure incurred on it was Rs.18.40 crore. Time overrun of 11 months and increase in cost was due to acquisition of certain equipment which were originally proposed to be leased (Rs.2.48 crore), doubling of production capacity from 66 lakh bottles per annum to 132 lakh bottles per annum (Rs.9.49 crore) which included installation of second Rommelag machine and manpower/interest cost (Rs.1.64 crore) not included in the original estimates. The scope of the project was thus completely changed by doubling the production capacity and changing the mode of financing for certain equipment. Though this had the effect of increasing the cost four fold, the approval of the Board/Ministry was not obtained till May 1993 after the irregularity was pointed out by audit (February 1993). Besides, the project formulation was defective, as the scope of the work was not estimated realistically.

5.3.2. Although the plant was making profit its capacity utilisation duirng 1992-93 to 1998-99 fluctuated between 39.85 per cent and 66.57 per cent. Thus the additional capacity created at an investment of Rs.9.49 crore was utilised partially (9 per cent to 33 per cent) during the initial 4 years till 1995-96, and was not utilised at all during the next two years. During 1998-99 the Company undertook manufacturing of the item for Fresenius Mafatlal Medicals Limited, Pune on loan licence basis, thereby utilising the additional capacity up to 27 per cent. Company had not made efforts in earlier years to utilise the additional capacity despite the fact that the product was generating profit.

5.4 Gentamycin Sulphate

Production facilities with Hungarian and Bulgarian technologies completed with a cost overrun of Rs.1.99 crore and a time overrun of 35 months and both proved to be uneconomical

5.4.1 In February 1982 the Company set up a facility with technology obtained from M/s Medimpex and M/s Chinoin from Hungary for production of 1000 Kgs of Gentamycin Sulphate per annum at a cost of Rs.3.63 crore. The expenditure had exceeded the estimated cost by Rs.1.09 crore as a result of time overrun of 35 months in its completion. Reasons for time overrun in implementation of the project were delay in supply of equipment by the suppliers, labour problems, delayed receipt of power supply from Maharashtra State Electricity Board (MSEB) etc.

5.4.2 Immediately after commissioning the facility it was observed that Gentamycin'C' strain, a component of the final product, was not of desired potency and resulted in low capacity utilization i.e 51 per cent. Consequentially, the cost of production was high. Thus the Hungarian technology, which was neither tested at the collabortor's laboratory nor at pilot plant proved to be uneconomical. The problem culminated in suspension of production during 1986-87.

5.4.3 To overcome the situation another agreement for transfer of Gentamycin technology was executed (July 1987) with M/s Pharmachim of Bulgaria at a cost of Rs.1.90 crore. In addition a sum of Rs.0.90 crore was spent to make the Plant & Machinery compatible with Bulgarian technology. The new production facility was commissioned in October 1991. However, the new technology also turned out to be uneconomical resulting in suspension of production once again (April 1992). The Company incurred a loss of Rs.1.97 crore due to high cost of production of Gentamycin during 1987-88 to 1991-92.

Management failed to get any safeguard in the agreements for transfer of technology against commercial failure of the technology.

5.4.4 It was observed that neither of the two agreements for transfer of technology contained a clause guaranteeing the commercial viability of the technologies, in absence of which loss suffered due to high cost of production could not be claimed from the suppliers of technology.

5.4.5 The Ministry admitted (July 1998) high cost of production of Gentamycin under both the technologies. Another reason cited by it for the loss suffered by the Company was sluggish sales resulting from availability of Gentamycin, permitted to be imported under open general license.

5.4.6 The Ministry's reply is not acceptable because Bulgarian Technology was introduced in spite of its projected cost of production i.e. Rs.18,000 per Kg being 71.42 per cent higher than the ruling international price. Hence, the Company should not have gone in for replacement of an economically unviable technology with another losing proposition.

5.4.7 Ministry also stated that two fermentors meant for production of Gentamycin were shifted to Aureofungin plant and the downstream processing facilities in the Gentamycin plant were being used for production of Carbendazim. However, these measures had no significant impact on the loss being incurred in the Gentamycin plant because only a meagre quantity of Aureaofugin was produced during 1994-95 to 1996-97 and in other years up to 1998-99 production was 'nil'. Similarly, Carbendazim production had decreased from 55.94 per cent in 1994-95 to 6.31 per cent in 1996-97 and became 'nil' from 1997-98 onwards. The Gentamycin Sulphate plant, thus, remained idle incurring an idle cost of Rs.65 lakh per annum.

5.4.8 Thus, the entire investment of Rs.6.43 crore (Rs.3.63 crore + Rs.2.80 crore) became infructuous.

5.5 Starch Hydrolysate Project

5.5.1 The Government approved (December 1982) establishment of a plant capable of producing 3465 Tonnes of Starch Hydrolysate (SHP) at a cost of Rs.2.54 crore. The feasibility report envisaged that the project would be completed and commissioned by November 1984 i.e., within 24 months from the date of approval by Government, and was expected to :

(i) provide captive raw material for Streptomycin fermentation; and

(ii) reduce loss in the Streptomycin production and fetch an internal rate of return of 39.7 per cent with a pay back period of 2 years and 8 months.

5.5.2 During execution the scope of the project was reduced by utilizing some existing equipment instead of acquiring new ones, thus, reducing the actual cost to Rs 1.91 crore. However, the project was completed in October 1986 with a time overrun of 21 months which was due to delay in finalising the type of boiler to be used in the plant, delay in delivery of equipment by suppliers and changes in the location of equipment.

5.5.3 The objectives of the project remained unachieved, as the average utilisation of the plant during 1985-86 to 1989-90 was less than 10 per cent of its installed capacity. This was due to reduced demand for the end product which could not be envisaged by the Management primarily due to insufficient R&D backup. Commercial production was finally discontinued with effect from 31 March 1990 as the requirement became nil due to adoption of new technology for Streptomycin production. The plant and machinery was transferred in 1990 for use in production of Pen-G. and the same had since been leased (June 1994) to JVC.

5.6 Penicillin Expansion (Penx) Phase III

Capacity enhanced with a cost overrun of Rs.3.42 crore and time overrun of 3 months.

5.6.1 Enhancement of Penx-Phase III capacity was taken up by the Company at an estimated cost of Rs.3.23 crore. The scheduled date of its completion was 31 December 1992. The cost was revised to Rs.4.99 crore due to fluctuation in exchange rate. The project was completed (March 1993) at a total cost of Rs.8.41 crore with a cost overrun of Rs.3.42 crore (68.58 per cent).

5.6.2 Ministry attributed (July 1998) the cost overrun to non-inclusion of interest, salary, power allocation in the earlier cost estimate. The Company had undertaken the project without fully estimating cost and without ascertaining the availability of funds. Both the factors led to cost and time overrun. This plant was also transferred to JVC on lease on 8 October 1995.

5.7 New Non-Parenteral Facilities

- ***Cost overrun: Rs.9.28 crore***
- ***Time overrun: 28 months***
- ***Delay in establishing facilities necessary for quality control in manufacture of non-parenteral drugs***

5.7.1 The Company in December 1991 conceived a project to integrate all facilities for manufacture of non-parenteral drugs and formulations. The project was expected to cost Rs.15 crore. Owing to insufficiency of funds and greater priority associated with manufacture of non-penicillin tablets, the Board of Directors approved a limited facility for this purpose at a cost of Rs.2.5 crore. The scheduled date of completion of the facility was March 1993.

The existing non-penicillin facilities were being carried out under conditions of severe congestion which constrained provision of many essential sub-activities and convenience required in the manufacturing lines as per the report of the Commissioner, Food & Drug Administration, Maharashtra. Since these activities were being carried out in different buildings situated at undesirable distances from each other supervision and control over the quality of products was inadequate. The Management expected to overcome these problems with implementation of the limited facilities referred to above.

5.7.2 The project was completed in July 1995 after a time lag of 28 months during which cost had exceeded the revised estimate of Rs.4.02 crore (January 1994) by 231 per cent. The final cost of the project was Rs 13.30 crore. It was observed in audit that non-availability of funds, change in scope of work by increasing the area and height of the building and installation of sub-station, resulted in time and cost overrun. The Company had

thus failed to implement a high priority project with due expedition and also ended up diverting scarce working capital to meet the cost overrun. Considering the fact that the integrated facility for manufacture of non-parenteral drugs was not taken up in its entirety for lack of funds, cost overrun was particularly undesirable.

5.7.3 The Ministry stated (April 1998) that overhead costs like power, interest, salary, etc were not considered while arriving at the revised project cost, which worked out to Rs.9.85 crore. It is evident from the reply of the Ministry that the Company took up the new project without fully estimating the costs involved. Moreover, time overrun resulting from revision of cost would inevitably have resulted in extra costs, which could not be worked out for want of necessary details. Thus the Company had exposed itself to financial burden at a time when it was going through a resource crunch.

5.8 Packing Facilities for Erythropoietin (EPO)

EPO Packing facility lying idle since its completion (June 1998)
Estimated cost: Rs.7.78 crore
Actual cost : Rs.13.80 crore
Cost Overrun: Rs.6.02 crore
Time overrun: 45 months

5.8.1 The Company entered into an agreement (October 1991) with M/s. Elanex Pharmaceuticals Inc., USA for marketing their product 'Hemax RHU EPO' in India. Domestic demand for the drug was estimated to be around 1.50 lakh vials per annum. The viability of the project was worked out on the basis of prevailing market price of the product. It was estimated that at a price of Rs.1378 per vial of 4000 IU, the Company could earn a margin of Rs.137.80 per vial.

5.8.2 While negotiating the distribution agreement, the foreign Company (July 1991) advised the Company that for better profitability it should set up a formulation and packing facility at its premises. Accordingly, the Company formulated (January 1993) a proposal to set up facilities for processing and packing of one lakh vials per annum at a cost of Rs.7.78 crore. The scheduled date of completion was September 1994.

5.8.3 The Company had assessed (January 1993) the profitability and the amount payable to the supplier at an exchange rate of Rs.19.97 per US $ prevailing in July 1991. The exchange rate prevailing in January 1993 when the proposal was given concrete shape was, however, Rs.30.78 per US$. Though the change in the dollar-rupee exchange rate was material and warranted reassessment of the project's profitability, Management went ahead with its implementation unmindful of this important and adverse development. It was observed in audit that with the change in exchange rate, the cost of production per unit worked out to Rs.1436.48 as against estimated selling price of Rs.1378, thus indicating a negative rate of return. Had the Company reassessed the profitability consequent to the devaluation of Rupee in 1991, which was very much possible as the project was given shape only in 1993, imprudent investment amounting to Rs.13.80 crore could have been avoided.

5.8.4 Although M/s Elanex had also proposed to buy back the product from the Company for export to South East Asian countries, no such agreement with them was executed. Along with paucity of funds, lack of budgetary support from Government and erosion of profit margin due to successive devaluation of Rupee, contributed to delay in completion of the project. The project was finally completed only in June 1998 with a time overrun of 45 months. The total cost incurred was Rs.13.80 crore which worked out to 177 per cent of original cost inspite of a saving of Rs.4.83 crore on purchase of plant and

machinery, margin money and other fixed assets. The main reasons for cost overrun of Rs.10.85 crore were interest borne on borrowed funds and lease rental (Rs.9.56 crore) over an extended period, power (Rs.0.48 crore), manpower (Rs.0.71 crore) and construction of building (Rs.0.10 crore). The facilities created at considerable cost had remained idle so far (May 2000). The Company stated (December 1998) that a committee had been appointed to examine alternate use of EPO packing facility. The committee, however, was yet to give its report (April 2000) and the facilities continued to remain idle.

5.8.5 The expenditure of Rs.13.80 crore has been, thus, rendered infructuous due to Management failure in reassessing the profitability of the project in the wake of devaluation of Rupee, and due to its negligence in not securing a firm buy back commitment from M/s Elanex and finally in pursuing the project without assured availability of funds.

5.9 Project abandoned

5.9.1 Cephalosporin Project

5.9.2 The Company entered (September 1989) into an agreement with JCP Martin and Partners, U.K. for manufacture of Cephalosporin 'C' Sodium Salt and its conversion into 7 Amino Cephalosporanic Acid (ACA) and Cefazol in Sodium Sterile. The total technical know-how fees payable to the other party in three equal installments was US $ 0.9 million. The agreement envisaged that the Company would undertake trials in laboratory and pilot plant within six months from the receipt of strains and know-how and in a commercial scale plant within 6 months thereafter. The collaborators would provide technical assistance only if the Company was unable to achieve process guarantees on its own. As per agreement, the foreign collaborator was required to successfully demonstrate in its laboratory the fermentation process of Ceph 'C' Sodium Salt and its conversion into above mentioned derivatives. Though a team of experts from the Company visited in June 1990, the facilities of the collaborators in Taiwan, the latter failed to prove the guaranteed extraction norms at laboratory level. Inspite of that, the Company decided (December 1991) to create manufacturing facilities for 7 ACA and Injectable Cephalosporin (cephazolin sodium) with an annual capacity of 10 MT and 15 MT, respectively, at an estimated aggregate cost of Rs.18.05 crore.

An expenditure of Rs.3.61 crore towards creation of facilities for manufacture of Ceph 'C' did not yield any results and was written off during 1997-98.

5.9.3 In April 1992, the Company again planned to send its team to the collaborators' laboratory in Taiwan who informed that process demonstration was possible only in respect of Ceph 'C' fermentation and recovery. The collaborator, however, advised (May 1992) the Company to omit enzymatic splitting of the Ceph-C strain into 7 ACA from the purpose of the visit. The Company's team visited the collaborator's laboratory in Taiwan in July/August 1992. During this visit the collaborators provided only the strain and technical documents relating to fermentation and recovery of Ceph 'C'. The guaranteed extraction norms at laboratory level could, however, not be proved by the collaborator. While sending its team to Taiwan the Company also opened a Letter of Credit (L/C) for US $ 0.3 million but instructed the bank (August 1992) to pay to the collaborator only the first installment of US $ 0.15 million, on production of proof relating to demonstration of the process technology of Ceph.'C' fermentation. However, due to failure on part of Company's bankers in conveying the above condition to the bankers of the Taiwanese firm

the latter released the entire amount of US $ 0.3 million. Efforts of the Company to recover the excess amount of US $ 0.15 million drawn by the collaborator have not succeeded so far (August 1999).

5.9.4 The Ministry replied (June 1997) that legal action against banker/collaborator was being taken. However, the Company issued legal notice to the collaborator only in March 1998 i.e. five years after the date of payment. No suit has been filed against the defaulting party so far (August 1999).

5.9.5 It was also observed that the Company had overlooked the offers made by Pan Lab Inc., USA and Pharmacin Ind, Italy for transfer of similar technology on the ground that both possessed technical know-how only up to Ceph 'C' stage. Yet it entered into collaboration with JCP Martin and Partners, a firm which neither owned the technology nor possessed any laboratory of its own. The contract for transfer of technology was signed with JCP Martin and Partners merely on the basis of an agreement it had executed with Industrial Technology Research Institute of Union Chemical Laboratories, Taiwan to undertake laboratory demonstration of the process.

5.9.6 Thus, the expenditure of Rs.3.61 crore made by the Company towards creation of facilities for manufacture of Ceph 'C' which included the payment of technical know-how fee to the collaborator up to the end of March 1997, had become infructuous. The Company agreed with this perception of Audit and informed (November 1997) that the expenditure of Rs.3.61 crore had been written off during 1997-98.

6. PRODUCTION PERFORMANCE OF BULK DRUGS

6.1 Penicillin

6.1.1 Production of Penicillin and other antibiotics begins with biological fermentation. The fermentation process consists of three steps viz. (i) seed growth, (ii) production fermentation, and (iii) harvesting the fermented broth. From the fermented broth, Mycelium is separated and Penicillin is recovered from the filtrate by the solvent extraction process. As on 31 March 1995, the Company had twelve 80 KL fermentors and four 23 KL fermentors for manufacture of Penicillin. However, these fermentors were leased out with effect from 8 October 1995 to Hindustan Max-GB, a joint venture formed for production of Pen G as discussed in chapter 4.

6.2 Titre Yield and Broth Obtained

Despite an expenditure of Rs.2.12 crore on up-scaling the technology of producing Pen-G the desired yield could not be achieved.

6.2.1 The Company acquired a new strain from Pan Lab, USA during 1989-90 with the expectation that the 'titre' yield would be around 55,000 u/ml in a time cycle of 240 hours. The company paid Rs.72.13 lakh towards fees for supply of the strain and Rs.57.55 lakh towards the fees for participation in the foreign company's ongoing programme of up scaling the shake-flask level yields to plant level. But despite spending Rs.2.12 crore on Pan Lab technology the Company could achieve not even the lower yield of. 40,000 u/ml fixed as the standard by the company. Pan Lab could, however, not be made liable for its failure to achieve standard yield because the collaboration agreement executed with it by the Company provided a guarantee for achieving the yield at the shake flask level only. The Ministry stated (June 1997) that in a process stiff targets for upscaling the technology were kept deliberately so as to reach at least the minimum expected yield.

6.2.2 The standard yield fixed by the Company per harvested batch of Pen-G was 2 mmu. As against this, the actual average yield per harvested batch obtained during 1990-91 to 1994-95, varied from 1.66 mmu to 1.87 mmu thus resulting in a total shortfall of 767.94225 mmu as detailed in the table below:

Year	Actual average yield penicillin-G (in mmu/batch)	Shortfall (2.00 mmu–Col..2)	Number of batches actually harvested (in mmu)	Total shortfall in production (in mmu) (3x 4)	Per-centage of short fall
(1)	(2)	(3)	(4)	(5)	(6)
1990-91	1.669258	0.330742	481	159.08690	16.54
1991-92	1.668554	0.331446	528	175.00349	16.57
1992-93	1.726705	0.273295	528	144.29976	13.67
1993-94	1.868320	0.131680	570	75.05760	6.58
1994-95	1.669500	0.330500	649	214.49450	16.53
			TOTAL	**767.94225**	

6.2.3 While admitting (June 1997), that the yield was less than the target on an average, the Ministry stated that Pan Lab strain was very sensitive and reacted to little fluctuations in temperature and air pressure causing high drop in 'titre' yield. The reply is not tenable for the following reasons:

i) though the plants of the Company were designed for filamentous strains, the Pan Lab strains of pellety nature, which were delicate and required very fine tuning of fermentation parameters, had been specifically selected by the Company, in preference to the filamentous strains also offered by Pan Lab. Apparently, the adverse implications of this strain had been overlooked;

ii) the factors mentioned in the reply could have been foreseen and proper and timely steps taken to overcome the same; and

iii) the guarantee under the agreement with Pan Lab should have been extended to cover commercial production in Indian conditions rather than confined up to only the shake flask level in Taiwan.

6.2.4 The capacity utilisation of Pen G plant during 1990-91 to 1994-95 was as under:

Year	Installed capacity (MMU)	Budgeted Production (MMU)	Actual production (MMU)	Value of production (Rs. in crore)	Percentage utilisation/ achievement of	
					Installed capacity	Budgeted production
1990-91	600	700	547.837	32.37	91	78
1991-92	780	840	642.051	44.79	82	76
1992-93	780	800	714.807	56.27	91	89
1993-94	900	900	821.930	64.62	91	91
1994-95*	900	900	837.790	75.57	93	93

6.2.5 It is evident that till 1992-93 budgeted production was more than the installed capacity . The Ministry replied (June 1997) that the installed capacity of Pen-G plant was based on Toyo Technology and even though 30 per cent higher yield was expected in the context of Pan Lab Technology its exact installed capacity could not be fixed because yield from this technology was not consistent. This would indicate that the Company did not have any realistic yard stick for measuring its productivity.

6.3 Streptomycin

6.3.1 Fermentation

6.3.2 The Company has 10 fermentors, each with a capacity of 70,000 litres. One fermentor was allotted for preventive maintenance and the remaining 9 having a total fermentation capacity of 6,30,000 litres were available for normal production. During 1988-89 and 1989-90, five fermentors in the Streptomycin Plant were converted for Penicillin production with a view to enhance Penicillin production capacity. Assuming 320 hours

* *Production stopped after 1994-95*

cycle time per batch and 330 working days in a year for the balance fermentors available in the Streptomycin Plant it was assessed (1990-91) by the Company that 120 batches in a year could be seeded. However, number of batches harvested by the Company ranged between 113 in 1993-94 to 1 in 1997-98 due to fall in demand for the end product as discussed in succeeding paragraphs.

6.4 Final Product

6.4.1 Actual production of bulk Streptomycin during 1992-93 to 1998-99 vis-à-vis the installed capacity of 85 tonne is given below:

Year	Actual production * (Tonnes)	Per centage of capacity utilisation
1993-94	74.80	88
1994-95	37.19	44
1995-96	63.17	74
1996-97	40.09	47
1997-98	2.68	3
1998-99	18.38	22

6.4.2 It may be seen from the table that the installed capacity was underutilised in all the years from 1993-94 to 1998-99, and during 1997-98 the production was negligible. The Ministry explained (June 1997) that the demand of Streptomycin Sulphate as an anti-TB medication had fallen due to introduction of more potent drugs like Rifampicin and Ethambutol in convenient dosages. Banning of such widely used combination drugs as 'chlorostrep' had also contributed to the slackness in demand. The Ministry further stated (April 1998) that in view of low demand and drastic fall in the market prices, production of Streptomycin had been virtually stopped. The production during 1997-98 was 2.68 tonnes against installed capacity of 85 tonnes. However, owing to its higher in house consumption in manufacture of the Agrovet products, the over all production of streptomycin during 1998-99 again increased to 18.38 tonnes.

6.4.3 Actual value of production of bulk Streptomycin during 1993-94 to 1998-99 and the cost of production vis-à-vis sales price are detailed below:

Year	Production value (Rs. in crore)	Cost of production per Kg.* (Rs.)	Average sales price per Kg (Rs.)	Profit (+)/Loss (-) (Rs. in crore) (Production (4-3)
1.	2.	3.	4.	5.
1993-94	14.93	1658.86	1854.00	(+) 1.46
1994-95	11.13	2636.73	1839.45	(-) 2.97
1995-96	14.46	2813.74	1905.44	(-) 1.59
1996-97	7.74	3220.55	1930.97	(-) 4.28
1997-98	0.56	2804.48	**	(-)0.19
1998-99	4.37	2839.70	**	(-) 1.54

** As per Cost Audit Reports*

***** There was no sale during 1997-98 and 1998-99 and the entire production was captively used realising Rs. 0.37 crore and Rs. 2.83 crore during 1997-98 and 1998-99, respectively.***

6.4.4 Cost of production was thus higher than the sale price resulting in recurring loss except during 1993-94. Reasons for excess cost of production in comparison to sales price were increase in power tariff, fuel cost and delayed revision of sale prices of Streptomycin under DPCO. The increase in sale price did not improve profitability because of uneconomical level of production on account of lack of demand.

6.4.5 The Company stated (September 1993) that the main reason for high cost of production was regular increase of cost of inputs compared to which increase in the fair selling price fixed by the BICP, that too only after 3 to 4 years was less. It was further stated that the last cost-cum-technical study had been conducted by BICP in the year 1988 where after no such study was made though relevant cost data was submitted to the Bureau in October 1992 as well as in January 1993. Though the prices were subsequently fixed by BICP at Rs.1810 per Kg with effect from September 1994 and Rs.2100 per Kg in December 1996, the Company continued to incur loss during the years 1994-95 to 1998-99. The cumulative loss of the Company during the six years up to 1998-99 was Rs.9.11 crore. It was observed that fixation of price by BICP was based on cost data of past years and did not take into account likely increase in the future. This was one of the main reasons for loss in Streptomycin plant. Audit Board is of the view that there should be more frequent revision of prices by BICP and that such revisions should be based on more current data.

6.4.6 The Ministry replied (April 1998) that production of Streptomycin has been stopped due to high costs. The Company has, however, taken a decision (April 1999) to lease out these facilities to M/s RPG Life Science Limited for producing vitamin B2 & B12 at a lease rental of Rs.2.25 crore per annum. In addition, the lessee would also reimburse the salary and other expenses of 137 employees to be seconded to them for operation and maintenance of the facilities. BIFR had given its clearance, to this proposal on 16 August 1999. This plant is yet to be leased out (May 2000).

6. 5 Semi-Synthetic Penicillin Drugs

6.5.1 The Company expanded (1983) the plant at a cost of Rs.2.90 crore thus, increasing its capacity to produce 6APA, Ampicillin Anhydrous and Ampicillin Trihydrate to 35000 kg per annum. No separate capacities were fixed for each product. The necessary facilities were set up after considerable delay resulting in extra cost of Rs.1.46 crore.

6.5.2 Examination in audit revealed that the production capacities in the above plant were grossly underutilised as the actual production was only 22.80 per cent of installed capacity in 1992-93 and merely 3.65 per cent of the capacity in 1993-94. There was no production from 1994-95 onward as the cost of production for these two drugs was Rs.2817/Kg and Rs.3663/Kg as against which the ruling market price at Rs.1800/Kg for each product was low and hence uneconomical. It had, therefore, been decided to go in for 6 APA production as per the market demand. However, there has been no production of 6 APA since the year 1994-95. Loss due to idle capacity for the years 1994-95 to 1998-99 worked out to Rs.1.15 crore. Such vast difference between the cost of production and ruling price is indicative of the fact that Management's decision to go for expansion was not based on scientific projection of the future market trend.

6.6 Formulations - Working Results

The Company incurred a cumulative loss of Rs.69.13 crore in production of formulations during 1993-94 to 1998-99.

6.6.1 During the six years ended on 31 March 1999, the Company had incurred a heavy cumulative loss of Rs.69.13 crore in the production of various formulations as detailed below:

(Rs. in crore)

Year	Bulk Drugs	Vials	Capsules	Tablets	Syrups	Total
1993-94	0.52	0.16	1.52	1.04	0.28	3.51
1994-95	2.72	2.87	2.01	1.37	0.17	9.15
1995-96	9.39	4.56	3.70	1.71	-	19.35
1996-97	5.07	6.58	3.78	3.08	0.22	18.73
1997-98	-	2.71	3.79	5.43	-	11.93
1998-99	4.16	2.30	-	-	-	6.46
Total	**21.86**	**19.18**	**14.80**	**12.63**	**0.67**	**69.13**

6.6.2 The Company stated (March 1994) that (i) it was incorporated with the social objective of making available life saving medicines to common man at cheaper prices and hence it could not discontinue a number of products even as these resulted in loss to the Company; (ii) most of their products (formulations) were covered under DPCO under which prices were fixed on the basis of cost of production assuming an efficient industry; and (iii) being a Government Company, social overheads of the Company were very high. Moreover due to its negative capital structure, the entire requirement of funds was met from borrowed capital resulting in higher interest charges, which, in turn, had resulted in loss in the last few years. Ministry added (September 1999) that low availability of working capital, competition in the market and withdrawal of price preference by Government departments/ institutions also contributed to the loss. The Company could not even recover the variable cost of its products during 1996-97 and 1997-98.

6.6.3 The Ministry further stated (June 1997) that since there was no restriction on the Company to continue with the existing product profile it could have opted for newer products to remain competitive in the market. But, since the Company was facing a liquidity crunch, chances of its opting for newer products were remote.

6.7 Vitamin-C

6.7.1 The Vitamin-C plant was set up in 1973 at a cost of Rs.2.15 crore. The technology was obtained from National Chemical Laboratory, Pune. The layout of the plant was however, defective and the technology also did not yield satisfactory results. The Company, therefore, invited (1982) Roche Products Limited to provide technical assistance in rehabilitation of the plant. Even after repeated attempts, the production did not improve and was suspended thus rendering the expenditure incurred on the plant infructuous.

6.7.2 The Company stated (May 1993) that the idle facilities in Vitamin-C Plant had been utilised for producing Carbendazim, Pen G Acylace Enzyme and Aureofungin. Reply of the Company is not factually correct as there was no production of Aureofungin in 1994-95, 1997-98 and 1998-99 and during 1995-96 and 1996-97 such production was nominal. Production of Carbendazim had also decreased from 75518 Kg. in 1994-95 to 8524 Kg. in

1996-97 and there was no production during 1997-98 and 1998-99. Production of Pen G Acylace Enzyme also declined from 306 Kg in 1993-94 to 80 kg in 1998-99.

6.7.3 During the Audit Board Meeting (February 1996), the Management stated that full capacity of Carbendazim was not utilised due to fund constraints. It was suggested that full potential in respect of Pen-G Acylace Enzyme could be exploited by adopting a more innovative working technique. Although the Ministry stated (June 1997) that production and sale of enzyme during 1997-98 would be better than 1996-97, the actual production of the Pen G Acylace Enzyme in subsequent years was lower due to non-availability of working capital and sluggish market conditions.

6.8 Raw Material Consumption

Excess consumption of raw material during 1992-93 to 1996-97 in production of penicillin and its clinical products amounted to Rs.3.26 crore.

6.8.1 No scientific norms had been fixed for consumption of raw materials. Hence realistic targets for assessing the performance could not be laid down. Contrary to this the annual consumption targets were taken as a standard and actual consumption of raw materials of each year compared there against.

6.8.2 The Ministry stated (June 1997) that norm for consumption of raw materials were fixed on the basis of past consumption. The reply is not tenable as past consumption cannot be considered to be a scientific basis for fixation of norms. Such norms should have been fixed with reference to the technology adopted, taking into account process loss, etc.

6.8.3 It was noticed that actual consumption of raw material was excessive even in comparison to norms adopted for preparation of budget. Percentage of actual consumption to the norms adopted for preparation of budget varied from 2 per cent in 1996-97 in respect of Procaine HCL to 62 per cent during 1995-96 in respect of cotton seed meal. The value of excess consumption of raw materials in production of Penicillin and its clinical products during 1992-93 to 1996-97 (details in Annexure II) worked to Rs.3.26 crore.

6.8.4 The Company stated (March 1994) that Pan Lab technology involved frequent withdrawals and each withdrawal took away some amount of material (sugar and cotton seed meal) which needed to be replenished from time to time. The reply is not tenable because the standards of consumption were also revised upwards after the adoption of Pan Lab technology.

6.9 Machine Utilisation

6.9.1 The COPU in its 80th Report (Fifth Lok Sabha 1975-76) recommended that the information regarding idle machine hours should be reflected in the monthly/quarterly reports to the Management/ Board. The Committee also suggested that internal audit should critically examine the records of idle machine/man hours and report to the Management/Board so as to enable them to take conclusive follow-up action. Neither any report relating to idle machine hours were submitted to the Board nor were there any positive efforts by Company's Internal Audit Department to implement COPU's recommendations. The Ministry stated (July 1998) that in future information on idle machine

hours would be submitted to the Board, as suggested by Audit. However, this assurance has not materialised so far (August 1999).

6.9.2 It was further noticed in audit that idle machine hours were being computed only in respect of Fermentation (Penicillin and Streptomycin) and Filling sections but not in respect of utility department. Details of idle hours and their proportion to total available hours in respect of Penicillin, Streptomycin and Formulation plants during 1993-94 to 1998-99 were as detailed below:

(In machine hours)

Product	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99
1. Penicillin	6455 (6.70)	4601 (4.84)	4754 (9.84)	*	*	*
2. Penicillin fermentation in STPT Plant	2111 (4.82)	2919 (6.76)	548 (2.32)	*	*	*
3. Streptomycin Plant	5230 (5.97)	7682 (17.35)	4417 (11.09)	12170 (41.91)	--	--
4. Formulation Plant I	769 (7.51)	735 (8.69)	249 (4.55)	287 (4.32)	299 (8.40)	473 (9.01)
5. Formulation Plant II	483 (12.78)	400 (14.65)	503 (13.05)	499 (16.86)	448 (15.42)	675 (20.67)

(Figures in brackets indicate the percentage of idle hours to the available machine hours.)

6.9.3 The facilities in Streptomycin plant (5 fermentors) remained idle during 1996-97 to the extent of 41.91 per cent and were not utilised thereafter. This was attributed to low demand. The Company estimated (November 1995) that operations of this plant had been resulting in an annual loss of Rs 65 lakh. Further, the Company estimated that had these 5 fermentors been leased out, an annual profit of Rs 9.38 crore would have accrued to the Company apart from the lease rent. Though the Company decided, in April 1998, to lease out the fermentors to M/s. Searle (India) Limited no action had been taken thereafter (August 1999). Thus, due to delay in leasing out 5 fermentors, Company incurred loss of Rs.65 Lakh in each of the years 1996-97, 1997-98 and 1998-99, which was avoidable. Besides, the Company also threw the prospect of earning revenue on account of lease rent away.

Delay in leasing out fermentors caused avoidable loss of Rs.65 lakh in each during 1996-97, 1997-98 and 1998-99.

* *The plant was in operation upto September 1995; from October 1995 the facilities were transferred to Hindustan Max-GB Limited (India), a Joint Venture Company*

7. ENERGY MANAGEMENT AND CONSERVATION

7.1 The production processes of the Company depend upon two energy inputs viz electricity and fuel oil. The electricity generated/provided by the Electrical Department is used by the Utilities Department to generate compressed air and chilled water, both used in Penicillin and streptomycin plants. Fuel oil is used by Utilities Department for generation of steam necessary for various process heating operations in different production plants.

7.2 Power and Fuel Oil Consumption

Fuel and power valuing Rs.11 crore consumed in excess of norms during 1992-93 to 1998-99.

7.2.1 In 1992-93 the Company switched over from Japanese technology (Toyo-Jozo) to American technology (PAN LAB) for producing penicillin. Consequently, the Company relaxed the norms of consumption per unit of power and fuel as indicated in the table below:

Normative consumption of energy:

Sl. No.	Name of Product	Power consumption Norms			Fuel consumption Norms		
		Unit	1992-93	1993-94	Unit	1992-93	1993-94
1.	Penicillin First Crystals	LKWH/ mmu	0.67	0.68	Te/ mmu	10.00	14.00
2.	Streptomycin	LKWH/ Te	1.74	2.09	Te/Te	23.00	25.00

7.2.2 The actual consumption before and after the revision of norms was as indicated below :

Actual consumption of energy:

Sl. No.	Product	Unit	1992-93	1993-94	1994-95	1995-96	1996-97	1998-99
(A) Power Consumption :								
1.	Penicillin First Crystals	LKWH[@] / mmu	0.70	0.69	0.66	0.80	NA[#]	NA
2.	Streptomycin	LKWH/ Te[*]	1.96	1.96	1.89	2.06	2.30	2.83
(B) Fuel Oil Consumption:								
1.	Penicillin First Crystals	Te/ mmu[**]	13.26	12.67	12.64	13.59	NA	NA
2.	Streptomycin	Te/Te	30.15	28.71	29.32	31.46	28.54	27.86

[*] 'Te' denote tonne

[**] 'mmu' denotes million mega units.

[#] 'NA' facilities were leased out to Hindustan Max – GB Limited in October 1995.

[@] 'LKWH' (Lakh Kilo Watt Hours) represents units of electricity consumed in lakh.

7.2.3. In 1995-96 actual consumption of power in production of Penicillin and fuel oil in production of Streptomycin went even beyond the revised norms. Energy consumption in excess of norms resulted in extra expenditure of Rs.11 crore (Fuel: Rs.6.48 crore; Power: Rs.4.52 crore) during the period 1992-93 to 1998-99.

7.2.4 The Ministry replied (June 1997) that the standards fixed in 1991-92 were based on theoretical calculations of mass and energy and were too stringent to be achieved because of (i) deviation of standard operating time cycle, (ii) deviation due to manual operation, (iii) contamination, (iv) low productivity due to unpredictable fermentation, and (v) deviation in efficiency of utility services etc. The Ministry further stated that change in the standard of Penicillin was necessitated by adoption of Pan Lab strain and that after 1993-94 standards had remained unchanged. The reply is not tenable because:

(i) neither the old nor the new standards were based on any scientific study and did not relate to industry standards;

(ii) the new standard adopted for power consumption for Streptomycin and fuel oil consumption for penicillin from 1993-94 onwards was much higher than that actually achieved in the previous year; and

(iii) excess consumption and variation in consumption level continued even after upward revision of norms.

7.2.5 The Company had adopted various energy conservation measures by incurring an expenditure of Rs.5.77 crore during 1992-93 to 1998-99. However, it did not conduct any energy audit to assess the effect of these measures. The Ministry stated (June 1997/ July 1998) that it would not be possible to quantify the savings derived from various schemes as plant load was never constant and there were no meters attached to steam and chilled water etc. The reply of the Ministry is not tenable because, as is evident from para 7.2.2 above, the intended benefit of reduction of steam and electricity could not be achieved in case of Penicillin and Streptomycin plants. Since the Company did not maintain details of energy consumption in plants other than Penicillin and Streptomycin it was not possible to assess the impact of investment on energy saving in the other plants.

8. RESEARCH AND DEVELOPMENT (R & D)

8.1 The R & D Division of the Company was established in 1955 and its activities fell into two categories viz. (i) Development Research (ii) Basic Research.

8.2 Recommendations of COPU

8.2.1 The COPU in their 67th Report (Seventh Lok Sabha 1982-83) had observed that the R & D efforts of the Company had not borne any fruit and the strains developed or being developed were either commercially unviable or had no market demand. The Committee had further observed that the R & D centre of the Company required qualitative strengthening and emphasised the need for close co-ordination of R & D activities of not only the Company but also of all the drugs and pharmaceutical manufacturing companies in the Public Sector. However, no steps were taken to co-ordinate the R&D efforts of the Drugs & Pharmaceutical companies in the Public Sector. The R&D activity within the Company had also not taken off as desired by the COPU, as brought out in the next paragraph.

8.2.2 The Ministry stated (June 1997) that while it agreed that greater emphasis on R & D activities was absolutely necessary for survival of pharmaceutical industry, it had to be recognised that fundamental research was fraught with the risk of high expenditure, often with no tangible results. The Ministry during the Audit Board meeting clarified (December 1997) that obsolescence in pharmaceutical industry was very common because of time overrun, which in turn led to cost overrun. It was added that most of the projects were funded from internal sources, which affected the working capital. The Ministry further stated (April 1998) that the Company might seek assistance/funds from normal R & D funding given by Department of Science and Technology. However, when the Company submitted a proposal (February 1999) for a project for 'Development of Lyposanal Drug Delivery system' at a cost of Rs.33 lakh, only a sum of Rs.7 lakh was sanctioned by Ministry.

8.3 Implementation of R & D Projects

Expenditure on R&D projects far below industry norm.

Expenditure of Rs.11.57 crore on 17 abandoned projects proved to be infructuous.

8.3.1 The Company spent Rs.21.40 crore on 25 major R&D projects between 1983-84 and 1998-99 which worked out to 1.2 per cent of the sales revenue. This was far below norm of 10 per cent prevalent in the pharmaceutical industry.

8.3.2 The details of the projects undertaken, completed successfully, ongoing and abandoned, are given in the table below.

(Rs. in crore)

PROJECTS TAKEN UP		PROJECTS COMPLETED		PROJECTS ONGOING		PROJECTS ABANDONED	
No.	Amount	No.	Amount	No.	Amount	No.	Amount
25	**21.40**	**7**	**9.41**	**1**	**0.42**	**17**	**11.57**

8.3.3 Out of 25 projects taken up, 7 projects completed at a cost of Rs.9.41 crore were commercialised and put to use. The abandonment of 17 project was attributed to (i) lack of commercial viability; (ii) failure of technology; (iii) lack of facilities; and (iv) financial constraints. The only ongoing project was related to 'soil screening for newer microbials.'

8.3.4 The Ministry stated (April 1998) that the question of further pursuing the R&D projects abandoned for want of funds can be addressed only after the financial position of the Company improved.

8.4 Diversion of Funds

8.4.1. The Department of Bio-technology (DBT) sanctioned Rs.3.46 crore in two phases (March 1990 and March 1991) for undertaking 7 R & D Projects over a period of 5 years from March 1990 subject to the condition that the grant should be exclusively spent within the stipulated time on the projects for which it was sanctioned. Accordingly, DBT released Rs.2.89 crore up to 31 March 1995.

8.4.2 A review of the records relating to the grant received from DBT revealed that a sum of Rs.1.40 crore received between April 1990 and April 1991 was temporarily diverted towards working capital requirements. This became possible because no separate bank account was operated to ensure utilisation of the grant exclusively for the specified projects. This caused delay of 8 - 10 months in importing, two numbers each of 15 litres and 72 litres laboratory fermentors required for R & D projects, during 1991-92. In the same project the Government, fearing diversion of funds did not release the second installment of grant amounting to Rs.57 lakh. Consequently, there was cost overrun of Rs.83 lakh on the completion of the R&D projects funded by DBT.

8.4.3 The Ministry replied (June 1997) that as per the conditions of the grant it was not necessary to maintain a separate account and that the Company's Bankers, in order to facilitate payment, did not allow it to open a current account while a cash credit account was still in operation. The reply of the Ministry is not tenable since the Company had opened a current account during 1994-95 without the consent of its Bankers in order to facilitate payment to a private party (refer para 12.3). Moreover, conditions of the grant clearly stipulated that it should be exclusively spent on the projects for which it was sanctioned, within the stipulated time and that any unspent part of the amount must be surrendered.

9. MATERIAL MANAGEMENT AND INVENTORY CONTROL

9.1 Inventory Holdings

9.1.1 The value of the inventory of raw materials, stores and spares, stock under process and finished stock in terms of the number of months consumption/production/ sales for the last six years up to 1998-99 are given below:

(Rs. in crore)

Particulars	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99
Raw materials	13.54	13.02	11.04	7.93	5.90	5.47
General stores, spares and tools	7.24	8.05	4.96	3.76	3.57	4.25
Stock under process	9.97	9.65	9.78	7.10	4.59	4.86
Finished stock	31.33	17.18	28.50	14.19	9.07	14.18
Total	**62.08**	**47.90**	**54.27**	**32.98**	**23.14**	**28.76**
Value of production	206.73	183.31	181.32	116.82	98.12	118.64
Total inventory in terms of monthly production	3.60	3.14	3.59	3.38	2.83	2.91
Stores and spares in terms of monthly consumption	30.58	31.02	22.49	25.91	29.98	37.67
Finished goods equivalent to monthly sales	1.89	1.04	2.01	1.26	1.03	1.50

- ***Norms for stock holding level for stores & spares not fixed***
- ***3296 items of stores valued at Rs.1.93 crore were lying unused for 3 years or more***

9.1.2 While inventory holding of stores and spares in terms of monthly consumption increased from 22.49 in 1995-96 to 37.67 in 1998-99 that of finished goods in terms of monthly sales fluctuated between 1.03 to 2.01. No norms were prescribed to have adequate control over the excess provision of stores and spares. As on 31 March 1999, 3296 items of stores (2646 insurance stores) valued at Rs.1.93 crore had not moved for 3 years or more. Ministry stated (July 1998) that norms for stock level of Stores and Spares had not been yet finalised.

10. SALES PERFORMANCE AND CREDIT CONTROL

10.1 Appointment of Clearing and Selling (C&S) Agents

10.1.1 For increasing sales through better execution of orders and for follow-up on collections, the Company appointed C&S agents throughout the country. The agreement between the Company and the C&S agents provided that the latter would (i) store the Company's products for the purposes of onward despatch to stockists and hospitals; and (ii) ensure execution of all orders received, the Company in turn would pay them 4 per cent commission on net invoice value and additional 1.5 per cent commission for payments received within 45 days, 1 per cent for payments received between 45 and 60 days and 0.5 per cent for payments received between 60 and 90 days.

10.1.2 The number of C&S agents appointed and total value of orders executed through them in absolute sum and as a percentage of overall sales during 1993-94 to 1998-99, are given below:

(Rs. in crore)

Paticulars	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99
a) No. of Agents	22	21	25	25	25	16
b) Value of orders executed	84.30	86.36	96.11	84.03	48.00	NA
c) Commission paid	3.51	3.02	3.55	3.77	1.34	1.14
d) Total sales	199.37	197.82	157.84	97.41	61.92	68.87
e) Percentage of achievement ('b' to 'd')	42	44	61	86	77	NA

10.1.3 It can be seen from the table above that the declining trend in sales could not be arrested with the introduction of the scheme. The Company attributed (July 1998) payment of commission to the C & S agents disproportionate to the volume of sales effected through them to inclusion therein of the element of interest which would have accrued on the advance collections made from them during the period July 1996 to March 1997. Such collections were being made by the Company to tide over shortage of working capital. However, since the scheme of advance collection by C & S agents itself did not have the approval of Board and its extension beyond October 1996 had been strongly objected to by it, these payments were unauthorised and resulted in avoidable extra expenditure of Rs.37.92 lakh.

Unauthorised appointment of C&S agents and advance collections from them resulted in loss of Rs.37.92 lakh.

10.2 Avoidable Appointment of C & S Agents.

10.2.1 It was noticed that the Company was appointing C&S agents even in places where they had their own depots/offices. The staff of the Company had requested (May 1992) that the appointment of C&S agents be cancelled on the grounds that: (i) while the employees were toiling hard to keep the Company in good working condition and earn a goodwill in the market, the Company was spending huge amount by creating special posts of

Managers and by hiring costly office accommodation on rental basis for maintaining the depot and godowns at Calcutta and (ii) the Company had appointed C&S agents by paying them commission @ 5.5 per cent on sales while the employees were made to sit idle.

10.2.2 The Ministry stated (June 1997) that the appointment of C&S agents was part of Company's efforts to strengthen its marketing activities. The reply is not tenable, as the Company had terminated the services of 9 C&S Agents during 1997-98 and 1998-99 after reviewing their performance. This indicated that appointments of C&S agents in these places were avoidable, *ab initio.*

10.2.3 As per the terms of the appointment, one per cent of trade sales was to be retained by the C& S agents to promote sales of the Company as per the advice of the Marketing Division. However, out of sums thus retained an amount of Rs.52.64 lakh had remained unutilised since September 1994. Ministry stated (July 1998) that the system of allowing 1 per cent on trade sales was stopped from 1 October 1994 and the balance unspent amount had been adjusted towards commission due to C&S agents, during June 1998. The fact, however, remained that the sales promotion activities have not been effectively monitored which had hampered the market share of the Company. Simultaneously, on the sum of Rs.52.64 lakh remaining unutilised with the agents for 4 years, loss of interest of Rs.32.37 lakh @ 18 per cent per annum had also been incurred.

10.3 Book Debts

10.3.1 The following table gives the value of sales and book debts at the end of each year from 1993-94 to 1998-99.

(Rs. in crore)

Year	Sales during the year	Book debts	Percentage of book debts to sales	Amount of provision for doubtful debts	Percentage of doubtful debts to total debts
1993-94	199.37	41.52	20.83	2.99	7.20
1994-95	197.82	36.54	18.47	2.86	7.82
1995-96	169.82	38.64	22.76	3.34	9.45
1996-97	134.71	29.95	22.23	4.06	15.65
1997-98	105.75	27.11	25.64	4.78	17.63
1998-99	113.26	27.23	24.04	5.39	19.79

10.3.2 While bulk drugs were sold against advance payment/Letter of Credit, the Company extended credit up to 60 days, for formulations and trade sales. Out of the total debts of Rs.27.23 crore as on 31 March 1999 debts worth Rs.7.52 crore (27.62 per cent) were more than 3 years old. Against this, the Company had already provided Rs.5.39 crore in the accounts for the year ended 31 March 1999. Following deficiencies were also noticed:

(a) letters of confirmation were invariably not obtained from the debtors;

(b) the Company did not have a system of recording and pursuing separately the debts due from Government departments and trade sector;

(c) supplies continued to be made to some parties even though large balances had remained un-recovered from them; and

(d) no proper assessment as to the realisabilty of the debt was made with the result that the adequacy of the provisions made for bad and doubtful debts could not be assessed.

10.3.3 The Ministry stated (June 1997) that a new system had been introduced to ensure follow up of outstanding and analysis of old outstanding and fixation of targets for Medical Representatives and Divisional Managers. Consequently, the book debts had come down from Rs.29.95 crore in 1996-97 to Rs.27.23 crore in 1998-99.

10.4 Export Sales

Loss of Rs.7.42 crore on export of three drugs during 1993-94 to 1998-99.

10.4.1 The Company exported during 1993-94 to 1998-99 Tetracycline capsules, Procaine Penicillin, Benzathine Penicillin and earned Rs.37.85 crore in foreign exchange. The Company was awarded "CHEMEXIL AWARD" for Excellence in exports during 1992-93 to 1996-97 and "INTERNATIONAL EXCELLENCE AWARD" during 1997-98 by Indian Council for Small and Medium Exporters. However, these exports resulted in a loss of Rs.7.42 crore to the Company because, to win export orders the Company had quoted rates even lower than the variable cost.

10.4.2 The Ministry stated (June 1997) that in future, export would be undertaken only in those areas where a positive contribution was expected. During 1998-99 Company exported goods amounting to Rs.8.03 crore and earned a contribution of Rs.1.01 crore.

10.4.3 The Company imported during 1991-92, 34596 Kg of Tetra bulk at a total cost of Rs.1.65 crore and availed concession of Rs.1.36 crore in payment of custom duty. The concession was availed under Advance License Scheme, which was accompanied by an obligation to export 1358 lakh capsules of Tetracycline (250 mg). In order to comply with this obligation the Company exported 1403 lakh capsules worth Rs.2.15 crore during 1995-96 and incurred a loss of Rs.97.78 lakh.

10.4.4 The Ministry stated (June 1997) that the loss was due to delay in opening of Letter of Credit (LC) by the buyer, low international price of Tetracycline and ban on export of tetra capsules during 1994-95. The reply is not tenable, as the Company had not taken any action against the buyer for not opening LC in time, as there was no clause in the purchase order to that effect.

11. INTERNAL AUDIT

11.1 Internal Audit Department was set-up to conduct the audit of Head Office and to review the work of firms of Chartered Accountants (CAs) also appointed for internal audit work. The Internal Audit Department was headed by a Deputy Manager, working under the control of Manager, Finance and Internal Audit, who in turn was reporting to the Deputy General Manager (Finance) till September 1994. However, from September 1994 Internal Audit, department was directly reporting to Director (Finance)/MD.

11.1.2 Firms of CAs were appointed at a cost of Rs.4.78 lakh during 1998-99 to conduct internal audit of the accounts of Depots and sales and marketing records at Head Office, besides conducting pre-audit of payments exceeding Rs.25,000 and all purchases over Rs.1 lakh. The scope of their audit was defined and conveyed to them in their appointment letters. Major observations of internal audit related to discrepancies in postings in ledger and subsidiary books and writing back of liabilities no longer required.

11.2 Deficiencies in Internal Audit System

11.2.1 In spite of deteriorating production performance and financial position of the Company, Internal Audit had not carried out any critical appraisal of systems, procedures and operations till 1993-94 except in Transport and Marketing areas.

11.2.2 Consolidated Internal Audit Report containing the important observations were not placed before the Board. These were, however, placed (June 1997) before Director (Finance) and Managing Director.

11.2.3 The Audit Manual prepared in June 1974 had not been updated. The Company stated (March 1994) that the process of incorporating latest procedures, critical and sensitive areas requiring close attention in the Audit Manual was in progress. The Company further stated (August 1997) that the updating of the Manual would be completed within one year. The work had been awarded to a firm of CAs who were also conducting internal audit of the Company's operations. But, no concrete progress had been made in this regard till August 1999.

12. OTHER TOPICS OF INTEREST

12.1 Default in Payment of Energy Bills

12.1.1 Owing to liquidity problems, the Company was irregular in payment of power bills since January 1991. Hence the Company on many occasions sought extension of time from Maharashtra State Electricity Board (MSEB) for payment of bills. Consequently, as per rules, MSEB levied delayed payment charges (DPC) and interest on outstanding dues. The Company sought (October 1992) the waiver of DPC and interest and for this purpose engaged a firm and though hiring the services of the firm was without authorisation and paid it Rs.18.83 lakh towards service charges. MSEB, waived (May 1994) the entire DPC of Rs.106.19 lakh as well as interest of Rs.40.64 lakh there upon.

12.1.2 The Ministry stated (June 1997) that the matter regarding payment of service charges had been referred to CBI. It further stated (April 1998) that CBI had registered a case against Shri A.K. Basu, the then MD, and other employees. The final outcome of the case was awaited (August 1999).

12.2 Failure to Meet Delivery Schedule in Export Order

12.2.1 The Company accepted (April 1995) from its Agent M/s Trinity Pharma Limited (TPL) in Nairobi an export order for supply of certain dispensary kits to Ministry of Health, Government of Kenya at a value of Rs.2.45 crore (US $ 773733). As per the terms of the purchase order the Company was to deliver the stocks by 27 May 1995; but due to delay in production, the Agent refused (July 1995) to accept the stock. As a result, stock worth Rs.2.22 crore was lying idle till April 1997.

12.2.2 In May 1997, the Company revived the order through the same Agent for the same Government at a value of Rs.1.86 crore and despatched (June 1997) the stocks by incurring an extra expenditure of Rs.29.70 lakh towards air freight. The Company also agreed to pay commission at 20 per cent. This was 7.5 per cent higher than the maximum commission of 12.5 per cent permitted under the RBI Rules. The Agent had also offered to the Company lower prices (US$ 520000) than what (US $ 927000) the Government of Kenya had agreed to pay to him. In this manner he had made a profit of Rs.1.46 crore (US$ 407000) at the cost of the Company in addition to the commission received by him.

12.2.3 The Company had issued (October 1997) a legal notice to the agent for which no response was received. Thereafter, the Company invoked the arbitration clause and sent a legal notice to the agent (June 1998). The case is still pending (August 1999) and the balance amount was yet to be realised.

12.2.4 Thus, due to its failure in meeting the delivery schedule, the Company suffered a loss of Rs.1.86 crore (Rs.70 lakh on inventory carrying cost, Rs.36.10 lakh due to non-recovery of production costs, Rs.29.70 lakh extra on air freight and Rs.50.22 lakh interest loss for delay in realisation of sale proceeds). Apart from this, Company was also deprived of revenue to the tune of Rs.1.46 crore as the agent passed on lower prices than what he received from Government of Kenya.

12.2.5 The Company replied (June 1997) that the export order could not be executed mainly due to budgetary constraints and non-availability of funds with Government of Kenya. The reply is not tenable as order dated 13 April 1995 received from the Ministry of Health, Government of Kenya had clearly stated that "Funds were available and commitment had been noted in Vote Book".

12.3 Unintended Benefits to a Firm

12.3.1. The Company gave (September 1993 to July 1994) an interest free advance of Rs.1 crore to a firm for ensuring long term supply of certain Agrovet products. The supplies required to be made at the production cost of the firm during 1994-95 to 1996-97 had become disputable due to higher prices, delayed supplies, unacceptable terms of payment and supply of damaged goods. The Company in October 1997, made a claim of Rs.2.53 crore on the firm.

12.3.2 It was observed in Audit that firm had been extended an unjustifiably favourable treatment as indicated by the following:

(i) reasonableness of product price charged by the firm was not ascertained as no comparisons were made with the product cost of other manufacturers;

(ii) allowing increased prices even as it was a fixed price purchase order;

(iii) opening a separate bank account to facilitate smooth payments to the party which was contrary to the normal practice; and

(iv) payment of interest free advance of Rs.1 crore to the firm without the prior approval of the Board.

12.3.3. The Company replied (June 1997) that the MD of the Company had been delegated authority by the Board to sanction up to Rs.1 crore for purchase of materials on a single tender basis. It was also stated that the transaction with the firm had been undertaken with the intention of entering into the agro-market in a big way and whatever concessions were allowed to the firm were justified in view of Company's overall objective of accelerating the selling activity. The reply of the Company is not tenable as the transactions with the firm finally ended up in claims and counter claims leading to the firm serving a legal notice (September 1997) on the Company for recovery of disputed claims aggregating Rs.68.05 lakh. Since the matter had not been settled, the Company had invoked the arbitration clause and filed against the firm a claim (July 1998) for Rs 4 crore. The arbitration award was awaited (August 1999).

(A.K.CHAKRABARTI)
Deputy Comptroller and Auditor General
Cum Chairman, Audit Board

New Delhi
Dated : 4 August 2000

Countersigned

(V.K. SHUNGLU)
Comptroller and Auditor General of India

New Delhi
Dated :

ANNEXURE-I

[Refer Para 5.2.1]

Statement showing details of Major Projects completed during 1982-83 to 1997-99.

Project	Date of approval by Government/Board	Original estimated cost (Rs. in lakh)	Revised cost (Rs. In lakh)	Actual cost (Rs. in lakh)	Scheduled date of completion	Actual date of completion	Cost overrun (Rs. in lakh)	Time overrun (No. in months)
1	2	3	4	5	6	7	8	9
1. 400 mmu Pen. Expansion PENX -PHI PENX -PHII	Board/ 28.2.1989 Govt./ 18.10.1989	1980.00	1922.00	1729.00	28.2.1990 31.10.1991	15.2.1992 15.2.1992-	- -	24 4
2. IV Fluid Plant	Govt./ 25.10.1989	479.00 - PH.I - PH.II	727.29 949.22	1840.00	30.4.1991	March 1992	1361 (284%)	11
3(a) Gentamicin Plant.	Government/26.02.97	254.09	279.00(I) 309.22(II) 343.15(III)	363.36	26.2.1979	6.2.1982	109.27 (43%)	35
(b) Gentamycin Technical Upgradation Plant.	Board/22.8.1987	190.10	--	279.82	21.3.1990	26.4.1990	89.72	--
4. Starch Hydro- lysate Project	Govt./ 27.12.1982	253.58	--	191.33	31.12.1984	October 1986	-	21
5. 3.3 KV Project	Board/ January 1982	196.00	170.00	226.57	13.1.1986	10.12.1987	30.56	23
6. PENX-PH III (Capacity Enhancement of Pen.Ist Crystals 135 mmu/p.a.)	Board/ December 1991	323	499.00	841.20	31.12.1992	22.3.1993	342.00 (68.58%)	3
7.New Non Parenteral Facilities	Board/19.12.91 Board/24.1.1994 (202.11)	250.15	402.00(I) 1000.00(II)	1330.42	March 1993	31.7.1995	928.00 (231%)	28
8. Packing facilities for EPO	January 1993	777.85	--	1380.02	September 1994	June 1998	602.17 (77.41%)	45
9.PEN.Expansion Scheme (840 MMU to 955 MMU) (PEN I-IV)	17.5.1993	829.42	--	578.81	June 1994	15.11.1996	--	42
TOTAL				**8760.53**				

Note: .Figures in brackets indicate percentage of increase over original estimates.

ANNEXURE – II

[Refer Para 6.8.3]

Statement showing the details of Actual Consumption vis-a-vis Standards in respect of Penicillin and its Clinical Products during 1992-93 to 1996-97.

[QUANTITY : in Kgs/mmu \ VALUE : Rs. in lakh]

Sr. No.	Process/raw material	1992-93			1993-94			1994-95			1995-96			1996-97			TOTAL
		Std. Qty.	Act. Qty.	Value of excess Consum -ption	Std. Qty.	Act. Qty.	Value of excess Consum -ption	Std. Qty.	Act. Qty.	Value of excess Consum -ption	Std. Qty.	Act. Qty.	Value of excess Consu m-ption	Std. Qty	Act. Qty.	Value of excess Cons-umpt-ion	
1.	**Pen. Ist Crystals**																
a)	**Fermentation:**																
i)	Sugar	6982	8655	109.80	6982	6086	-	6982	6347	-	6982	7800	32.43	*	-	-	142.23
			(24)									(12)					
Ii)	Cotton seed meal	1100	1312	14.38	1100	1250	1.70	1100	1314	26.87	1100	1780	37.15	-	-	-	80.10
			(19)			(14)			(19)			(62)					
Iii)	Phenyl Acetic Acid	443	456	14.01	443	433	-	443	427	-	443	503	26.47	-	-	-	40.48
			(3)									(14)					
b)	**Extraction Acetone**	400	501	19.84	450	423	-	450	384	-	450	522	7.66	-	-	-	27.50
			(25)									(16)					
2.	**Pen.G.Sodium Butanol**	-	-		1750	1983	7.98	1750	2221	4.05	1750	1622	-	1750	1483	-	12.03
						(13)			(27)								
3.	**Clinical Products Procaine HCL**	525	581	11.64	535	545	6.14	535	549	2.67	535	551	2.10	535	545	0.93	23.48
			(11)			(2)			(3)			(3)			(2)		
	TOTAL			**169.67**			**15.82**			**33.59**			**105.81**			**0.93**	**325.82**

*Note : * - No production from Oct. 1995 and their was no excess consumption during 1997-98 & 1998-99.*

Figures in bracket indicate percentage of excess consumption over norms