Report of the Comptroller and Auditor General of India

for the year ended March 2005

Union Government (Commercial)

Transaction Audit Observations

No. 12 of 2006

(Regularity Audit)

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PREFACE

1. The accounts of Government Companies set up under the provisions of the Companies Act (including Government Insurance Companies and Companies deemed to be Government Companies as per provisions of the Companies Act) are audited by the Comptroller and Auditor General of India (CAG) under the provisions of Section 619 of the Companies Act, 1956. The accounts certified by the Statutory Auditors (Chartered Accountants) appointed by the CAG under the Companies Act are subject to supplementary or test audit by officers of the CAG and the CAG gives his comments or supplements the report of the Statutory Auditors. The Companies Act, 1956 empowers the CAG to issue directions to the Statutory Auditors on the manner in which the Company's accounts shall be audited.

2. The statutes governing some Corporations and Authorities require their accounts to be audited by the CAG and reports to be given by him. In respect of five such Corporations viz. Airports Authority of India, National Highways Authority of India, Inland Waterways Authority of India, Food Corporation of India and Damodar Valley Corporation, the relevant statutes designate the CAG as their sole auditor. In respect of one Corporation viz. Central Warehousing Corporation, the CAG has the right to conduct a supplementary or test audit after audit has been conducted by the Chartered Accountants appointed under the statutes governing the Corporation.

3. Reports in relation to the accounts of a Government Company or Corporation are submitted to the Government by the CAG under the provisions of Section 19-A of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971, as amended in 1984.

4. Annual reports on the accounts of the Central Government Companies and Corporations are issued by the CAG to the Government. These are

Regularity Audit (Yellow Series)

Report No.10 - Review of Accounts: This gives an overall appreciation of the performance of the Companies and Corporations as revealed by their accounts and information obtained in Audit.

Report No.11 - Comments on Accounts: This contains extracts from the important comments of the CAG on the accounts of the Companies and Corporations and a resume of the reports submitted by the Statutory Auditors (Chartered Accountants) on the Audit of the Companies in pursuance of the directions issued by the CAG.

Report No.12 - Transaction Audit Observations: This contains the observations on individual topics of interest noticed in the course of Audit of the Companies and Corporations other than Companies under the Telecommunications Sector.

Report No.13 - Transaction Audit Observations: This contains the observations on individual topics of interest noticed in the course of Audit of the Companies under Telecommunications Sector.

Performance Audit (Blue Series)

Report No.8 : This contains reviews on some of the activities of the Companies and Corporations other than Companies under the Telecommunications Sector.

Report No.9 : This contains reviews on some of the activities of the Companies under the Telecommunications Sector.

5. The existing Audit Board mechanism was revamped during 2005-06. The restructured Audit Board for Central PSUs is set up under the supervision and control of the CAG. The Board examines the selection of topics based on strategic audit plan of the Department and approves the topics recommended for performance audit. It also approves the guidelines, audit objectives, criteria and methodology for conducting performance audits which are reported through stand alone volumes in Reports No.8 and 9. The Board finalises the stand alone performance audits with the representatives of the Ministry and Management. The Board, which is permanent in nature, consists of the Chairperson (Deputy Comptroller and Auditor General-Commercial), Director General (Performance Audit), Economic Advisor and three Principal Directors of Audit under the CAG as members and two technical experts as special invitees, if necessary, in the area of performance of the Company or Corporation. The Principal Director (Commercial) of the CAG's Office is the Member Secretary of the Board.

6. The cases mentioned in this Report are among those which came to notice in the course of audit during 2003-2004 and 2004-2005 as well as those which came to notice in earlier years but could not be covered in previous years.

7. All references to 'Government Companies/ Corporations or PSUs' in this report may be construed to refer to 'Central Government Companies/ Corporations' unless the context suggests otherwise.

OVERVIEW

I Introduction

1. This Report includes important audit findings noticed as a result of test check of transactions of Central Government Companies/Corporations, conducted by the officers of the CAG of India under Section 619(3)(b) of the Companies Act, 1956 or the statute governing the particular Corporations. The results of Information Technology (IT) Audit are also included in this Report.

2. The Report contains 145 paragraphs and two IT reviews relating to 63 PSUs. The draft paragraphs and IT reviews were forwarded to the Secretaries of the concerned Ministries/Departments under whose administrative control the PSUs are working to give them an opportunity to furnish their replies/comments in each case within a period of four weeks. Replies to 71 paragraphs/reviews were not received even as this report was being finalised in December 2005. Earlier, the draft paragraphs were sent to the Management of the PSUs concerned - in respect of six paragraphs, they failed to respond despite being reminded.

3. The paragraphs/reviews included in this report relate to the PSUs under the administrative control of the following Ministries/Departments of the Government of India:

Ministry/Department (Total number of PSUs/ **PSUs involved here)**	**No. of Para-graphs/ IT Reviews**	**Financial Implication under the Paragraphs/ IT Reviews (Rs. in crore)**	**Number of Paragraphs/IT Reviews in respect of which Ministry reply was awaited**
1. Atomic Energy (5/**1**)	1	3.40	0
2. Banking (8/**1**)	1	4.13	0
3. Chemicals and Petrochemicals (16/**1**)	1	18.17	0
4. Civil Aviation (10/**3**)	7	22.27	5
5. Coal (10/**7**)	8	139.82	1
6. Commerce (10/**2**)	2	10.81	1
7. Consumer Affairs, Food and	12	50.58	6

Public Distribution (3/**2**)			
8. Defence (10/**5**)	5	8.92	0
9. Development of North Eastern Region (2/**1**)	1	14.30	0
10. Fertilizers (10/**2**)	5	45.51	2
11. Finance (9/**5**)	21	87.33	13
12. Heavy Industries (47/**5**)	13	41.11	8
13. Non-conventional Energy Resources (1/**1**)	1	3.18	1
14. Petroleum and Natural Gas (20/**8**)	29	293.70	17
15. Power (14/**3**)	3	23.48	3
16. Department of Public Enterprises (♣/♦)	2	46.73	1
17. Railways (9/**2**)	2	4.24	0
18. Road Transport (2/**1**)	2	6.39	1
19. Science and Technology (1/**1**)	1	0.91	0
20. Shipping (7/**3**)	5	12.18	3
21. Social Justice and Empowerment (6/**1**)	1	0.52	1
22. Steel (15/**6**)	19	218.46	8
23. Tourism (8/**1**)	3	11.40	0
24. Urban Development and Poverty Alleviation (2/**1**)	2	79.64	0
Total (235/**63**)	**147**	**1147.18**	**71**

The audit observations/IT reviews included in this report highlight deficiencies in the management of PSUs, which resulted in serious financial implications. The irregularities pointed out are broadly of the following nature:

- Overpayments, wasteful, excess, avoidable expenditure and undue favour to contractors etc. amounting to Rs.679.86 crore in 72 paras.

♣ *All the PSUs are under the Department of Public Enterprises*

♦ *PSUs covered in the paras are appearing in the respective Ministries*

- Idle investment, non-achievement of objectives, delay in commissioning of projects and blocking of funds etc. amounting to Rs.221.31 in 26 paras.
- Loss of Rs.81.85 crore due to fraud, inadequate internal controls, improper storage of material etc. in 13 paras.
- Loss of Rs.85.34 crore due to shortloading of insurance premium, under charging of premium, lacuna in the policies/procedures in 19 paras.
- Non recovery of dues from customers, delay in leasing, deficiency in debtor control etc. resulted in loss of Rs.59.69 crore in 14 paras.
- Rs.12.38 crore were recovered at the instance of Audit in one para.
- Financial implication of Rs.6.75 crore in two IT reviews

II Highlights

Gist of some of the important paragraphs and IT reviews included in the Report is given below:

- **New India Assurance Company Limited (NIA) and National Insurance Company Limited (NIC)** issued group policies to Golden Trust Financial Services (GTFS)/Golden Multi Services Club (GMSC) on irregular terms and conditions, inadmissible discounts and ambiguous group definitions. The entire business of NIC was booked with one agent who was the wife of an ex-officer of NIA (later became a partner in GMSC). In the process, NIA and NIC incurred loss of **Rs.21.57 crore and Rs.5.59 crore** respectively from **2001-01 to 2004-05**.

  (Para 11.3.1)

- Lapse on the part of **Power Finance Corporation Limited** in not incorporating the enabling clause in the agreement for foreign currency loan and restructuring of rupee term loan in **April 2005** in relaxation of its policy resulted in undue benefit to a private party and loss of **Rs.13.48 crore** to the Company.

  (Para 15.2.1)

- **Balmer Lawrie & Company Limited** contributed **Rs.15.07 crore** in **December 2003** to a superannuation fund required to be maintained solely by its officers and in which the company did not have any legal or contractual obligation to contribute, resulting in extension of undue benefit to a group of employees.

  (Para 14.1.1)

- **Oil India Limited** purchased a project of petroleum properties from ONGC Videsh Limited without adequate assessment of its prospects. The project turned out to be unsuccessful due to absence of commercial gas zones leading to loss of **Rs.31.55 crore** during the period **March 2003 to April 2004**.

  (Para 14.8.1)

- Injudicious investment of **Rs.38.83 crore** made by **Brahmaputra Valley Fertiliser Corporation Limited** in revamping of the ammonia plant became unfruitful as the plant was shut down from **September 2002** after running for four months since the operations became uneconomical.

  (Para 10.1.1)

- **Indian Oil Corporation Limited** could not recover an amount of **Rs.13.69 crore** from Dabhol Power Company due to absence of system for timely flow of documents between its various departments and consequent delay in raising final bills against supplies of high speed diesel/naphtha during **September 1999 to May 2001,** and non-collection of 'C' forms in advance during **2001-02.**

  (Para 14.6.2)

- Agra unit of **GAIL (India) Limited** sold natural gas as well as re-gasified liquid natural gas to various consumers in Agra and Firozabad. Due to tampering of meter skids by consumers, gas valuing **Rs.10.10 crore** was not billed during **January 2004 to February 2005.**

  (Para 14.4.1)

- Due to shifting of bottling plant away from its refinery, **Hindustan Petroleum Corporation Limited** incurred an extra expenditure of **Rs.70.60 crore** between **2000-01** and **2004-05** on transportation of bulk Liquified Petroleum Gas from Mumbai to bottling plant at Usar and its re-transportation to Mumbai for sale to consumers.

  (Para 14.5.1)

- **Rashtriya Ispat Nigam limited** could not recover the value of its Imported Coking Coal amounting to **Rs.34.70 crore** supplied to Indian Iron and Steel Company Limited during **March 2003 to January 2004**. It also failed to invoke the risk purchase clause to recover an additional expenditure of **Rs.18.49 crore** which it incurred on procurement of Blast Furnace Coke during **February 2004 to June 2004** when Indian Iron and Steel Company Limited failed to complete the supplies.

  (Para 22.5.1)

- **Rashtriya Ispat Nigam Limited** procured US coal from **July 2004 to August 2004** without a correct assessment of its requirement and incurred an extra expenditure of **Rs.35.73 crore**.

  (Para 22.5.2)

- **Oil and Natural Gas Corporation Limited** incurred an avoidable expenditure of **Rs.42.77 crore** during **October 2000 to March 2004** due to delay in award of contract for logging services and subsequent injudicious termination of the contract.

  (Para 14.7.1)

- Non-compliance of the Government of India instructions resulted in unauthorised reimbursement of Hill Transport Subsidy by **Food Corporation of India** to the Government of Arunachal Pradesh during **July 2003 to March 2004**, resulting in loss of interest of **Rs.20.34 crore.**

  (Para 7.2.1)

- **Kudremukh Iron Ore Company Limited** set up Vertical Shaft Pelletising Furnace Plant with defected technology resulting in non achievement of objective of expansion of the existing capacity. The Company wrote off the residual value of the Plant of **Rs.31.65 crore** in **2004-05.**

  (Para 22.2.1)

- **Steel Authority of India Limited incurred** a loss of **Rs.30.84 crore** in procurement of silico manganese and ferro silicon during the procurement cycle **2003-04** due to not enforcing quantity tolerance of plus 25 *per cent* at buyer's option in terms of the contract

  (Para 22.6.1)

- Despite being aware of the scarcity of hard coke due to price rise, **Steel Authority of India Limited** delayed advance payments resulting in an extra expenditure of **Rs.2.32 crore** during the period **September 2003 to February 2004** on account of production of saleable steel **upto March 2004**.

  (Para 22.6.2)

- Due to adoption of 26 days as a month instead of 30 days for computation of encashment of leave **Hindustan Aeronautics Limited, Bharat Electronics Limited, Bharat Earth Movers Limited and Kudremukh Iron Ore Company Limited** made excess payment of **Rs.34.35 crore** to their employees **up to March 2005**.

  (Para 16.1.1)

- Due to not retaining a call option in its infrastructure bonds issue, in spite of expert advice, **Housing and Urban Development Corporation Limited** incurred an avoidable interest expenditure of **Rs.30.46 crore** from **April 2002 to October 2005** and would further incur expenditure of **Rs.18.52 crore** till the maturity of the bonds in **April 2007.**

(Para 24.1.1)

- **Central Coalfields Limited** incurred an avoidable expenditure of **Rs.37.05 crore** for the unused energy from **1999-2000 to 2004-2005** as two Captive Power Plants commissioned by DLF Power Supply Company Limited at Rajrappa and Giddi in **July 1999** and **April 2000** respectively, to meet acute shortage of power, could not be synchronised with the grid of Damodar Valley Corporation.

(Para 5.2.2)

- **Housing and Urban Development Corporation Limited** did not consider the downward trend of interest rates and accepted over subscription of Rs.137.51 crore at higher rates of interest. Consequently, it incurred extra expenditure of **Rs.13.29 crore till October 2005** and committed future liability of **Rs.17.37 crore** towards interest over the remaining tenure of bonds.

(Para 24.1.2)

- **Central Coalfields Limited** invested **Rs.80.24 crore** for commissioning two Captive Power Plants at Kathara to ensure uninterrupted power supply. The plant, commissioned in **May 1995**, failed to give the desired output and remained completely idle since **May 2000** rendering investment on this project unfruitful.

(Para 5.2.1)

- **Eight PSUs** recovered **Rs.12.38 crore** during **2004 and 2005** out of Rs.13.82 crore pointed out by Audit.

(Para 16.2.1)

- **New India Assurance Company Limited and The Oriental Insurance Company Limited** lost premium of **Rs.12.26 crore** due to charging incorrect rate on the insurance of the compressors and terminals of GAIL (India) Limited during **April 2003 to March 2005**.

(Para 11.5.1)

- **Northern Coalfield Limited** incurred an avoidable expenditure of **Rs.14.34 crore** towards payment of excess statutory dues from **1998-99 to 2004-05.**

(Para 5.5.1)

- **Oil and Natural Gas Corporation Limited** suffered loss of **Rs.19.61 crore** between **October 2001 and October 2002** due to delay of 13 months in submission of application to Gujarat Electricity Board for wheeling of surplus power from its Hazira plant to Mehsana unit.

(Para 14.7.2)

- **Bharat Heavy Electricals Limited** suffered a loss of **Rs.12.40 crore** on account of payment of liquidated damages and penal interest because of delay in supply of equipment and spares during **1995 to 2001**, caused due to incorrect assessment of shop floor needs.

(Para 12.2.1)

- **Oil and Natural Gas Corporation Limited's** failure in arrangement of gas compression facility at the Group Gathering Station-II at Ankleshwar, resulted in avoidable flaring of gas valued at **Rs.10.65 crore** during the period from **April 2000 to April 2003**.

(Para 14.7.3)

- Lapse on the part of **Hindustan Organic Chemicals Limited** to implement the polyurethane project without making adequate arrangements for the major raw material rendered the investment of **Rs.18.18 crore** in PU system production facilities idle since **April 2004**.

(Para 3.1.1)

- **Airports Authority of India** did not synchronise its activities relating to planning, coordinating and execution of all related activities such as finalisation of site, acquisition of land, carrying out civil and electrical works etc. before placing orders for Doppler Very Frequency Omni Range in **July 2001 and July 2002,** which resulted in non-utilisation of navigational equipment of **Rs.11.75 crore** and loss of interest of Rs.86.81 lakh.

(Para 4.2.1)

- **Indian Oil Corporation Limited** installed Sulphur Recovery plant with unrealistic capacity and assumed higher sulphur content in High Speed Diesel feed stock. As a result the unit remained idle for two and a half years due to insufficient feed with

lower sulphur content and an investment of **Rs.13.05 crore** remained fruitless apart from loss of interest of **Rs.1.63 crore** during the period **January 2003 to June 2005.**

(Para 14.6.1)

- **North Eastern Development Finance Corporation Limited** financed a project in **April 2001** for setting up a call center at the time of recession in Information Technology industry, without any detailed investigation of the promoters' past record and technical feasibility of the project. As a result the finance of **Rs.9.07 crore** in DSS e Contract Limited became wasteful. Further, the Corporation could not recover the interest on the above loan and other charges amounting to **Rs. 5.23 crore** for the period **upto March 2005.**

(Para 9.1.1)

- Due to acceptance of supply order without price escalation clause, **Steel Authority of India Limited** suffered a loss of **Rs.10.15 crore** in the sale of steel blooms during the year **2003-04.**

(Para 22.6.3)

- **United India Insurance Company Limited** suffered a loss of **Rs.7.05 crore** during the period from **2000-01 to 2003-04** due to providing tailor made mediclaim policies in violation of its own guidelines.

(Para 11.7.1)

- **Oriental Insurance Company Limited** erroneously granted group discount at higher rate on the Group Mediclaim policy issued to the employees of Larson and Toubro Limited, which resulted in loss of premium of **Rs.6.62 crore** during the period from **February 2000 to December 2004.**

(Para 11.6.1)

- **United India Insurance Company Limited** issued tailor made group mediclaim policies in violation of its guidelines to cover the existing and retired employees of Bharat Electronics Limited during the period from **September 2002 to March 2005** which resulted in a loss of **Rs.5.53 crore.**

(Para 11.7.2)

- Wrong application of driage percentage by **Food Corporation of India** resulted in undue benefit of **Rs.5.45 crore** to the millers during the period **2000-01 to 2003-04**.

(Para 7.2.3)

- **State Trading Corporation of India Limited** paid to the Associates the cost of sugar without restricting the same to the actual cost of procurement. It also paid freight in the export of rice, wheat, tea and sugar to the Associates without relating the same to the actual. This resulted in undue favour of **Rs.6.11 crore** during **2002-03 and 2003-04** at the cost of the Government.

(Para 6.2.1)

- On account of its failure to exercise freight option in time, **Rashtriya Ispat Nigam Limited** incurred an avoidable extra expenditure of **Rs.8.77 crore** in importing limestone from a foreign supplier during **November 2003 to March 2004.**

(Para 22.5.3)

- Though **Bharat Heavy Electricals Limited** had obtained a contract below cost in **November 2000**, it could not adhere to the delivery schedule so as to avoid levy of liquidated damages. By taking advance manufacturing action, it could have avoided loss to the extent of Rs.1.32 crore on account of liquidated damages imposed by the customer. Overall, the Company incurred loss of **Rs.7.66 crore** in the execution of the contract.

(Para 12.2.2)

- Incorrect estimation of taxable income and consequent short payment of advance income tax by **General Insurance Corporation of India** resulted in avoidable payment of interest to the tune of **Rs.7.10 crore** in respect of the financial year **2003-04.**

(Para 11.1.1)

- **Bharat Heavy Electricals Limited** failed to assess the advance tax liability correctly, which resulted in avoidable payment of interest of **Rs.6.14 crore** under section 234C of the Income Tax Act on short-payment of advance tax for **Assessment Years 2003-04 and 2004-05.**

(Para 12.2.3)

- The placement of the order in **March 2004** of additional dredger for National Waterways–2 by **Inland Waterways Authority of India** without adequate justification resulted in avoidable expenditure of **Rs.3.16 crore** besides future liability of **Rs.2.59 crore.**

(Para 20.2.1)

- **Oil and Natural Gas Corporation Limited** approved the Food Grade Hexane/Special Boiling Point solvent project without giving due consideration to the current demand situation and unauthorised use of these products and awarded the contract for the project without studying the impact of the Government's 'Solvent Control Order' of 2000 on the consumption pattern of these products, which led to wasteful expenditure of **Rs.9.05 crore** between **1998-99 and 2001-02.**

(Para 14.7.4)

- **Oil and Natural Gas Corporation Limited's** failure to obtain prior clearance from forest authorities for drilling at a location forming part of 'Desert National Park' and non-provision of an alternative drilling location in its Annual Drilling Plan, led to idling of rig for 292 days in **2002** and wasteful expenditure of **Rs.7.21 crore.**

(Para 14.7.5)

- **NTPC Limited** could not recover interest on the excess funds blocked in coal stocks and suffered an avoidable interest loss of **Rs.9.20 crore** during three years ending **2003-04,** due to overstocking of coal beyond norms of Central Electricity Regulatory Commission.

(Para 15.1.1)

- Failure to implement the orders, issued in **March 2002** by the excise authority, in time due to inability to manage the software led to blockade of **Bharat Petroleum Corporation Limited's** fund of **Rs.7.67 crore** during **April 2002 to September 2002** and unnecessary litigation.

(Para 14.2.1)

- Flats purchased by **Central Warehousing Cor**poration for staff at Jawaharlal Nehru Port, Navi Mumbai in **May 1998** could not be utilised and resulted in idle investment of **Rs.6.07 crore.**

(Para 7.1.1)

- **Food Corporation of India** failed to file complete claims of input tax for exports made during the years **2003-04** resulting in loss of interest of **Rs.5.67 crore.**

(Para 7.2.2)

- Failure of **India Tourism Development Corporation Limited** to follow its own credit policy, for recovery of debts coupled with ineffective recovery action resulted in accumulation of debtors of **Rs.6.68 crore.**

(Para 23.1.1)

- **GAIL (India) Limited** did not coordinate with ONGC and the Government of Tripura for laying and use of its Konaban-Rokhia pipeline resulting in a loss of revenue of **Rs.9.12 crore** during **April 1998 to February 2002.**

(Para 14.4.2)

- Due to lack of planning and commercial appreciation by **GAIL (India) Limited** and the Ministry of Petroleum and Natural Gas in investment of surplus funds from Gas Pool Account, there was a loss of interest of **Rs.6.72 crore** to Gas Pool during **March 1999 to March 2005.**

(Para 14.4.3)

- **PNB Housing Finance Limited** had not observed the basic checks in the sanction of individual housing loans amounting to Rs.2.89 crore during **September 2001 to November 2001**. Due to lack of proper verification of documents and inadequate monitoring, loans and interest amounting to **Rs.4.13 crore** including interest of Rs.1.24 **crore** had become doubtful of recovery.

(Para 2.1.1)

- **Food Corporation of India** incurred a loss of **Rs.2.63 crore** due to inadequate internal control and failure to conduct proper physical verification leading to misappropriation of stock at Food Storage Depot, Kokrajhar during **2002-2003**

(Para 7.2.1)

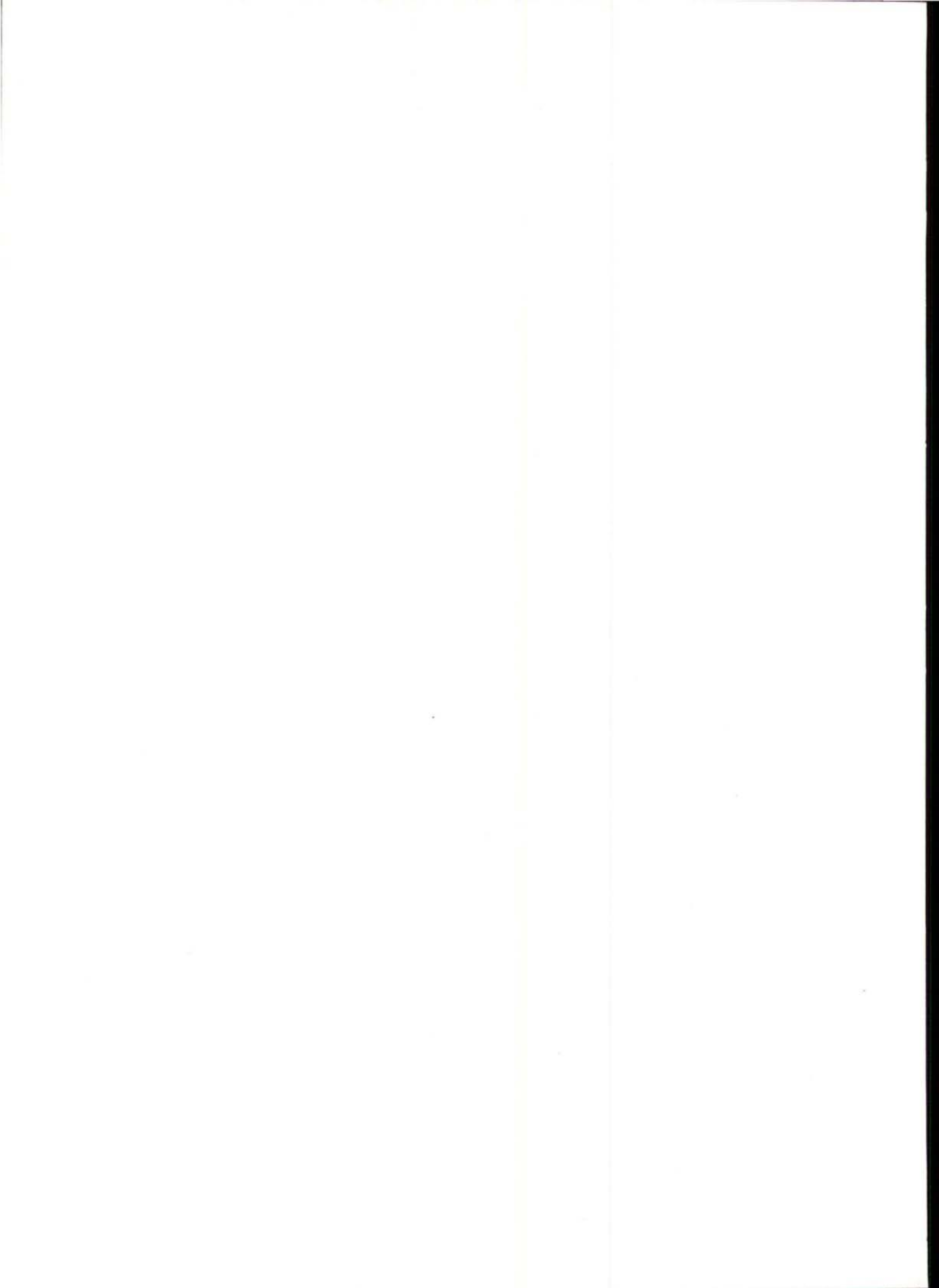
- Information Technology Report on the General Insurance System (GENISYS) Software in **National Insurance Company Limited:** Under GENISYS software introduced in **2001**, books were allowed to be kept open up to seven days after transactions. This is fraught with the risk as back dated entries can be made and policies with back date can also be generated. Some of the cheques entered in the 'Inward Remittance Register' of Division XI were not accounted for in GENISYS and no policy was issued against such cheques. Cheques and cash were held for periods ranging from one day to 343 days in 20,488 cases. In 111 cases cheque date was later than the Scroll date. GENISYS software does not have appropriate validation controls to ensure cancellation of the policy when claims were disbursed on 'Total Loss' basis leaving scope for further claim under the policy. In some cases effecting change in recovery of service tax at higher rate was delayed and the difference in collection amounted to **Rs.1.24 crore up to 31 May 2003**. There was no check, either manually or through computer system to see whether all the Cover Notes were accounted for and policies issued.

(Para 25.1)

- The absence of a structured information technology plan in **National Highways Authority of India Limited** resulted in a non coordinated approach in development and implementation of systems most suitable to its business needs. The systems were developed for the purpose of monitoring and evaluation on an on going basis, in accordance with the indicators satisfactory to the World Bank and not borne out of any cost benefit analysis undertaken by the Authority. In one case, where the preparation of Information Technology package was half way through, the Authority realised that the information was to be hosted on servers located in a foreign country and consequently the idea of developing the information solution had to be abandoned resulting in wasteful expenditure of **Rs.5.07 crore** upto **December 2005**.

(Para 27.1)

SECTION I
TRANSACTION AUDIT OBSERVATIONS



CHAPTER I: DEPARTMENT OF ATOMIC ENERGY

Electronics Corporation of India Limited

1.1.1 Additional cost of Rs.3.40 crore due to failure in ensuring the source of interfacing data and consequential delay in execution of the project

The Company failed to ensure availability of interfacing data, which was essential for execution of the project and had to incur an extra expenditure of Rs.1.05 crore for obtaining it during execution. This resulted in delay of the project on account of which an amount of Rs.2.35 crore could not be recovered from the customer.

The Company received two orders (April 2001 and August 2001) valuing Rs.7.75 crore and Rs.8.26 crore respectively from Airports Authority of India Limited (AAI) for supply of hardware and software for Flight Data Processing System (FDPS) and for its integration with the Radar Data Processing System (RDPS) which had been supplied by one Northrop Grumman Overseas Services Corporation (NGOSCO), USA directly to AAI. The orders were to be executed by September 2001 and February 2002 respectively. Any delay in completion would have attracted liquidated damages at a rate of one *per cent* per week of the value of the undelivered stores subject to a maximum of 10 *per cent* in case of the first order and 0.5 *per cent* per week subject to a maximum of five percent of the value of the undelivered stores in case of the second order.

For integration of FDPS with RDPS, the Company planned to prepare the interface specification after decoding the message format by tapping output from the RDPS with the co-operation of AAI. But after trying for 12 months, the Company realised that the message formats and the protocols were propriety to NGOSCO and could not be decoded without violating Intellectual Property Rights. Consequently, it had to procure (May 2004) the required interfacing data from NGOSCO at a cost of Rs.1.05 crore, which it could not claim from AAI. In the process, the project also got inordinately delayed on account of which the customer withheld an amount of Rs.2.35 crore. As the Company failed to realise this amount it wrote off the same in the accounts of 2003-04.

The Management stated (May 2005) that the expenditure of Rs.1.05 crore on interface data was met from the amount of Rs.3.12 crore available against application software for FDPS. In another reply (June 2005), it informed that the matter would be taken up subsequently with AAI for compensating the unforeseen cost. The Ministry stated (August 2005) that the Company presumed the availability of interfacing data with AAI. However, when it could not be obtained, the same was purchased from NGOSCO. It further added that the amount spent was being considered as an investment for securing future business. It also stated that as against the amount of Rs.2.35 crore, the Company would approach AAI to get waiver of the liquidated damages of Rs.1.19 crore and collect the remaining amount of Rs.1.16 crore after installation of the system at remaining airports, which was under demonstration at Chennai.

The reply is not tenable because if the amount available for application software for FDPS already provided for the cost of accessing interface data, the question of claiming it

separately from the customer as unforeseen cost would not arise. Moreover, in the absence of a clause for making claim for unforeseen cost, the admissibility of such a claim is also questionable. As regards considering the amount spent as investment, the same is not tenable as no new order was received till date (October 2005). As regards liquidated damages and other withholdings, the Company itself would have assessed it as non-realisable as an amount of Rs.2.35 crore was written off as bad debt in the accounts of 2003-04.

Thus, failure in ensuring availability of interfacing data required for integration of software and consequential delay in execution of the project resulted in an additional cost of Rs.3.40 crore to the project.

CHAPTER II: DEPARTMENT OF BANKING

PNB Housing Finance Limited

2.1.1 Fraud in sanction and disbursement of loans

Due to lack of proper verification of documents and inadequate monitoring, loans and interest totalling Rs.4.13 crore had become doubtful of recovery.

The NOIDA branch (branch) of PNB Housing Finance Limited (Company) sanctioned (September 2001 to November 2001) individual housing loans amounting to Rs.2.89 crore to 32 employees of 'Vigilance to City Crimes'*, a private office engaged in journalism.

Audit scrutiny of these 32 cases revealed that the branch had not observed the basic checks in the sanction of individual housing loans and had sanctioned and disbursed the loans without proper verification of documents. In this connection, the following deficiencies were noticed:

(i) Post-dated cheques with the same account numbers on the same bank had been issued under signatures of different borrowers and the same had been accepted by the branch without raising any objections or doubts in this regard.

(ii) The Company did not obtain any independent proof of income, like salary slips, income tax returns, statement of bank accounts in all the cases with the result, inflated fake salary certificates were accepted.

(iii) The Company did not verify the independent proof of residence and the correctness of the individual residential addresses given in the loan applications.

(iv) There was no report of site visit of the branch officials on record, in the absence of which it was not ascertainable whether any site visit was made to establish the status of the site, the flats etc.

(v) The branch did not obtain financial data of the private office to ascertain its credit worthiness and financial background.

(vi) The Company did not verify the means and income of the guarantors to ensure that the same was sufficient to cover the loan amount.

As a result of inadequate scrutiny of credentials of the individual borrowers before disbursement of loans, the loan accounts became non-performing assets (NPA) in terms of prudential norms of National Housing Bank due to non-recovery of even a single instalment of principal from the borrowers. Accordingly, the entire principal amount of

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* *registered with Registrar, Newspapers of India, Ministry of Information and Broadcasting*

Rs.2.89 crore and interest of Rs.1.24 crore[♣] aggregating Rs.4.13 crore could not be recovered by the Company for more than four years (September 2005).

The Company filed (March 2002) individual suits in Delhi High Court against the fraud committed by the borrowers and removed (June 2005) two staff members of the branch. For taking possession of the flats under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act), the Company issued (April/December 2004) demand notices and possession notices to the borrowers, which were received back undelivered. Constructive Possession (an act of pasting the notice on door of the resident borrower) of two flats had been taken by the Company in December 2004 and in respect of other 30 borrowers the notice was published in the newspapers in January 2005.

The Management/Ministry accepted (November 2005) that it was a case of non-adherence to the system of checkpoints because of which loans were sanctioned flouting procedures for financing. There was criminal intent of cheating the Company in connivance with borrowers and agents. In the instant case, agents in collusion with the incumbent of the branch and the borrowers manipulated the system for sanction of loans. Stating that the Company had initiated action for recovery of dues through civil suits as well as SARFAESI Act 2002, the Management added that the present system had been strengthened to avoid recurrence of such fraud.

Thus, due to lack of proper verification of documents and inadequate monitoring, the entire amount of Rs.4.13 crore (including interest of Rs.1.24 crore) had become doubtful of recovery.

[♣] *The Company could receive interest of Rs.7,102 only from one borrower till March 2005.*

CHAPTER III: DEPARTMENT OF CHEMICALS AND PETROCHEMICALS

Hindustan Organics Chemicals Limited

3.1.1 Idle Investment

Lapse on the part of the Company to implement the polyurethane project without making adequate arrangements for the major raw material rendered the investment of Rs.18.18 crore in PU system production facilities idle.

To take advantage of favourable market environment available for polyurethane product, the Company entered into a formal license agreement in October 1995 with M/s. Baxenden Chemicals Limited (BCL) for the implementation of polyurethane (PU) system project. The Board of Directors of the Company approved (November 1996) investment of Rs.12.08 crore for creation of installed capacity of 10,000 MT of polyurethane under the PU project. Accordingly, the project was implemented at a total cost of Rs.18.18 crore and commercial production started in March 1998.

As raw material constituted 80 *per cent* of the cost of production in high value PU systems, the sourcing of raw materials with adequate alternatives had to be tied up with a view to maintain profitability. Methylene Di-Phenyl Di-isocyanate (MDI) was the major raw material for the production of polyurethane and the Company had to import the entire requirement of MDI of the required specifications as recommended by M/S. BCL. The Company conceived (December 1995) the MDI project in joint venture with M/s. Chematur Engineering AB (CEAB), Sweden but the project could not take off, as project viability due to higher input cost and lower sale price was not established. Due to non-implementation of its MDI project, the Company had to import the same for the production of PU systems. The imported MDI raw material prices were high as compared to the finished product prices, which got reduced due to severe competition.

As against the installed capacity of 10,000 MT of PU system per annum, the actual production ranged between 2.53 MT and 541.24 MT during the six years ending March 2004 with the highest production of 541.24 MT in 1999-2000 and the lowest of 2.53 MT in 2003-04. The Company in the production of PU systems made cash profit of Rs.87.00 lakh only during the year 1998-99 and from 1999-2000 onwards, started incurring cash losses. The total cash losses incurred by the Company during the years 1999-2000 to 2003-04 worked out to Rs.1.08 crore.

The committee constituted by the Company to study the scenario and to work out the profitability of PU system operations noticed (July 2001) that if the Company ran the PU plant at its full capacity it would incur a loss of Rs.26.00 crore per annum at the then prevailing market price. The Board of Directors of the Company considering the above position decided (January 2002) to discontinue the operation of PU plant after consuming the raw materials available in the Rasayani unit of the Company. Accordingly the production facilities of PU plant continued upto March 2004 and thereafter lay idle.

Simultaneously, the Board of Directors of the Company decided in principle (January 2002) to lease out the PU system plant but it had not been leased out till October 2005.

Thus, lapse on the part of the Company to implement the PU system project without making adequate arrangements for the major raw material i.e. MDI, rendered the investment of Rs.18.18 crore in the PU plant idle.

The Management while accepting the facts stated (September 2005) that considering the bleak prospects of making any profit, the Company decided to look for other options of putting the facility to use and discussions were held for renting the facilities during 2002. However, decision of leasing out PU facilities could not be taken as the Company was under active mode of disinvestment. The new policy decision of the Government in July 2004 for restructuring of Public Sector Enterprises had opened up the possibility of leasing out the facilities once again. The Ministry endorsed (September 2005) the reply of the Management.

The above contention of the Management/ Ministry is not tenable, as even after the opening up of the possibilities of leasing out in July 2004, the Company had not been able to lease out the PU system production facilities so far (November 2005).

CHAPTER IV: MINISTRY OF CIVIL AVIATION

Air India Limited

4.1.1 Avoidable expenditure due to wrongful termination of agency

Air India incurred avoidable expenditure of Rs.2.26 crore, during the years 1999 to 2002, due to wrongful termination of agency.

Air India Limited (Air India) appointed M/s. G.C. Nanda and Sons as consolidator in Hong Kong in 1978, without entering into any written agreement, for issue of air tickets on market fares at agreed levels of incentives. In December 1997, the consolidator issued Concessional Group Fare tickets to 18 passengers for travel to India ex-Hong Kong. Air India alleged that the passengers, to whom these tickets were issued, were not group travellers but individuals who travelled independently and hence should have been charged normal fare. It viewed that as four Indian members of the group were not returning with the rest of the group on the same day, Group Fare regulations were violated. The matter was taken up with the consolidator and, as the explanation of the consolidator was considered unsatisfactory, the Manager, Air India at Hong Kong terminated the arrangement, withdrew (January 1998) all special fares offered to the consolidators and imposed restrictions regarding sale of tickets etc. with immediate effect. An amount of Hong Kong Dollars (HKD) 10,510 being the alleged difference in fares between the Group fare and Economy class fare was also recovered by Air India from the consolidator in June 1998.

The consolidator filed a case in the High Court of Hong Kong (July 1998) seeking compensation, *inter alia*, for wrongful termination of contract. The consolidator argued that as they were in business association with Air India since 1978, there was an express agreement by which their services were not to be terminated without giving six months' notice period. On receipt of its counsel's opinion (December 1998) that its case was weak, Air India tried for an out of court settlement but could not arrive at a mutually acceptable full and final solution.

The High Court of Hong Kong in its order observed (November 2002) that there were two categories within the Group fare i.e. Group Visitors (GV) and Group-Inclusive Tours (GIT). The requirement of returning with the group was under GIT category but there was no specific endorsement on the tickets to suggest that the tickets were issued on GIT basis and also there was no evidence to suggest that GIT fares were paid as opposed to GV fares. The Court while observing that three months' notice would have been reasonable in the circumstances of the case, dismissed the allegation of Air India that the group was fictitious and held that there was no breach on the part of the consolidator to justify the letter of termination. The judgment was awarded for payment of compensation for wrongful termination of contract, refund of recovered difference in fare, refund of disputed productivity linked incentive, profit cost (being loss of commission etc.), disbursement cost (legal expenses incurred by the consolidator) and interest on all the above till the date of payment to the consolidator. After considering its counsel's

recommendation and huge additional legal cost, Air India decided not to appeal against the judgment.

Thus, wrongful termination of the agency with the consolidator resulted in an avoidable expenditure of Rs.2.26 crore*.

The Board of Directors appointed a one-man committee in November 2002 to enquire into this matter. The committee sent its report directly to the Ministry and a copy of the same was not available with Air India.

The Management stated (November 2005) that all the 18 tickets had reflected the tour code indicating that the group was traveling on GIT fare and, therefore, conformed to the applicable Fare Rules. The Management reply is not tenable as it failed to establish its argument before the High Court under the Rules that existed at the time of issue of the tickets. Moreover, the Management admitted that, as per its solicitor's opinion, Air India did not have a good case in view of the prevailing market practice in respect of the GV fares.

Thus by terminating the agency on wrongful grounds, Air India incurred an avoidable expenditure of Rs.2.26 crore.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

4.1.2 Loss due to delay in sub lease of surplus space

Air India at New York suffered loss of revenue of US$ 0.25 million (equivalent to Rs.1.16 crore) due to (i) delay in signing a new agreement for sub lease of surplus space in cargo warehouse and (ii) not renting out aircraft parking space during the years 2003 and 2004.

Air India, New York has a cargo warehouse measuring 20,062 square feet and truck dock area of 1,22,188 square feet leased from Port Authority of New York and New Jersey for an annual rent of US$ 0.46 million. Part of the cargo warehouse was in excess of Air India's needs and was sub leased from September 2000 to M/s. North American Aviation Services (NAAS) who also handled cargo on behalf of Air India under a common agreement.

Air India signed the agreement with NAAS for sub lease of surplus space in the cargo warehouse as well as for the cargo handling in June 2001. It was valid for a period of one year effective from September 2000 and was extended in February 2002, till September 2002. However, NAAS was allowed to continue with the use of warehouse facilities and handle the cargo beyond September 2002, without a valid agreement. In September 2003, Air India, New York initiated tender procedure for awarding a new contract valid for the period October 2003 till September 2006. NAAS remained the best bidder and in September 2004 signed a new agreement accepting the revised terms of payment with

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* *Includes payment of Rs.1.32 crore towards compensation for wrongful termination, profit cost, disbursement cost, court fee and interest, besides the legal expenses of Rs.93.51 lakh incurred by Air India in defending the case*

retrospective effect from October 2003. Air India, New York signed the agreement in January 2005, after obtaining approval from their Headquarters. It was observed in Audit that an amount of US$ 0.11 million (equivalent to Rs.50.27 lakh) remained unrecovered from NAAS for the period October 2003 to September 2004, being the difference between the old and new rates. The Management stated in September 2005 that NAAS had expressed their inability to pay the amount citing the following reasons:

(i) The contract was signed in September 2004 accepting the revised terms with retrospective effect from October 2003 on the understanding that the retrospective effect was only for continuity on record and would not involve any financial liability for the past period;

(ii) NAAS had filed their Financial Tax Returns without providing any liability and to pay for the periods in question,

(iii) NAAS was unable to accept any liability at the belated stage.

Air India added that the matter was under negotiation with NAAS.

Thus, delay in inviting tenders and signing the new agreement, led to a situation whereby the amount of US$ 0.11million (Rs.50.27 lakh) could not be recovered as of September 2005.

Further, it was observed in Audit that the aircraft parking space in the truck dock area was rented out to other airlines as and when requested by them for which Air India earned revenue of US$ 0.08 million in the calendar year 2002. However, after 2002 no revenue was earned as the space was not rented out. On this being pointed out by Audit in June 2005, the Management stated in September 2005 that offers had since been invited for sub leasing the aircraft parking space and an agreement would be finalised in consultation with their Headquarters. The Management added that there was no demand for this space after 2002. The Management's contention was not borne out by the available records which could indicate that earnest efforts were made by Air India to rent out this space after 2002. The fact remained that Air India, New York failed to gainfully utilise this surplus space after 2002 and suffered loss of potential revenue of US$ 0.14 million (equivalent to Rs.65.46 lakh) in 2003 and 2004[♣].

Thus, delay in the Management's action in finalising the sub lease agreement for the surplus space in cargo warehouse resulted in loss of Rs.50.27 lakh. Further, by not pursuing renting out of aircraft parking space in the truck dock area after 2002, Air India lost potential revenue of Rs.65.46 lakh during the years 2003 and 2004.

The matter was reported to the Ministry in November 2005, its reply was awaited.

[♣] ***Based on the revenue earned in 2002 less 10 per cent of the revenue payable as fee to the Port Authority***

Airports Authority of India

4.2.1 Locking up of funds due to delay in installation of equipment

The Authority did not synchronise its activities relating to planning, coordinating and execution of related activities, which resulted in non-utilisation of navigational equipment of Rs.11.75 crore and loss of interest thereon.

The Airports Authority of India (Authority) placed a purchase order (July 2001) for the supply of 21 Doppler Very High Frequency Omni Range (DVOR) for installation at various airports maintained by the Authority and a repeat order for supply of 9 DVORs (July 2002) for additional stations.

On a review by Audit (February 2005) on the installation of commissioning of these equipment, it was noticed that out of above 30 DVORs, 10 DVORs received between March 2003 and August 2003 remained in stores without installation (June 2005) due to various reasons such as delays in site survey, land acquisition, pre construction activities award, execution of civil and electrical works etc.

It was observed that the Authority did not synchronise its activities relating to planning, coordination and execution of all related activities such as finalisation of site, acquisition of land, carrying out civil and electrical works etc. before placing orders for the equipment. The non-installation/commissioning of these equipment within the specified period defeated the purpose and objective of providing accurate specific directional navigational facilities in the specified airports, for which the equipment were purchased. It also resulted in locking up of funds amounting to Rs.11.75 crore for periods ranging from 21 to 26 months with consequential loss of interest amounting to Rs.86.81 lakh. Moreover as the guarantee/warranty period of the non-installed equipment was already over, the Authority lost the right to claim defects liability from the supplier.

The Management stated (June 2005) that the equipment procured could not be installed due to delay in land acquisition and narrated the events that led to the delay in land acquisition. It also stated that some of the equipment was being shifted to other stations.

The fact, thus, remains that absence of synchronisation of related activities in the procurement and installation of equipment resulted in defeating the objective of providing accurate navigational facilities and resulted in blocking up of Rs.11.75 crore, with consequential loss of interest of Rs.86.81 lakh.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

4.2.2 Delay in recovery of Rs.3.63 crore

The decision of the Authority to repay the loan amount without recovering the amount due from MIADS resulted in overpayment of Rs.3.63 crore.

The Airports Authority of India (Authority) signed (October 1995) a Memorandum of Understanding (MoU) with Malabar International Airport Development Society

(MIADS) for financing the project of expansion and development of Calicut airport. The terms and conditions of MoU included, *inter alia,* the following:

(i) MIADS would raise a loan of Rs.60 crore and provide the same to the Authority, interest free, in instalments. The Authority would repay the first part of the loan of Rs.30 crore on completion of 66 months from the date of drawal of each instalment and the balance Rs.30 crore on completion of 60 months from the date of drawal of each instalment.

(ii) The interest would be paid by MIADS for the loans raised by imposing User Development Additional Fee (UDAF) from international passengers embarking at Calicut airport.

(iii) The UDAF would be collected by MIADS till the completion of the project.

(iv) The excess of UDAF collected by MIADS over the interest paid on the loan amount would be remitted to the Authority.

(v) MIADS would furnish quarterly statement of account of the UDAF collected and interest paid.

The expansion of the project was taken up by the Authority on the funds provided by MIADS (Rs.54.32 crore), which were borrowed from HUDCO. The project was completed in March 2001. Meanwhile, the Ministry of Civil Aviation (MOCA) in December 2000 reduced the UDAF from Rs.500 to 375 per embarking passenger and directed that UDAF would be in force till the interest was required to be paid by MIADS to HUDCO.

The Authority had, upto April 2003, repaid an amount of Rs.43.89 crore (excluding Rs. five crore paid directly by MIADS to HUDCO towards principal amount from the excess UDAF collection). After adjusting Rs. five crore out of the surplus amount of collection of UDAF, the last two instalments payable by the Authority were to the extent of Rs.5.43 crore only (Rs.2.50 crore due in July 2004 and Rs.2.93 crore due in October 2005 respectively).

Meanwhile, due to public protest at Calicut and suits filed by some of the users, it was decided to withdraw the collection of UDAF at Calicut airport and it was stopped with effect from August 2003. The MOCA, based on a proposal by the Authority, directed (August 2003) it to pre-pay the loan taken from HUDCO. The Authority paid Rs.6.33 crore to MIADS to enable it to settle the loan raised from HUDCO without adjusting the surplus amount available with MIADS. It also did not insist on production of statement of accounts as per MoU before prepayment of the loan.

Audit noticed that MIADS during the period upto August 2003 had generated excess UDAF of Rs.10.49 crore, but remitted (March 2003 and May 2003) Rs.2.75 crore only to the Authority after adjustment of Rs. five crore towards settlement of the principal amount with HUDCO and kept the balance amount of Rs.2.74 crore. MIADS also failed to remit the interest amount of Rs.89.10 lakh earned on surplus UDAF invested by them.

The Authority failed to adjust this amount of Rs.3.63 crore at the time of prepayment of the loan.

The Management while confirming the facts stated (May 2005) that the matter was being pursued with MIADS and reconciliation was pending.

The reply of the Management is not tenable as the Authority possessed the relevant details regarding surplus in UDAF to be recovered from MIADS at the time of releasing Rs.6.33 crore. The Authority failed to protect its financial interest and failed to adjust the amount due from MIADS before repaying the full amount.

Thus, the decision of the Authority to repay the loan amount without recovering the amount due from MIADS resulted in overpayment of Rs.3.63 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

4.2.3 Loss due to avoidable payment of power factor surcharge

The Authority failed to monitor and maintain required power factor at the substations resulting in avoidable payment of penalty of Rs.1.73 crore.

The Netaji Subash Chandra Bose International Airport, Kolkata of Airports Authority of India (Authority) draws its power requirements from Calcutta Electric Supply Company (CESC). The Authority installed ten sub-stations, two for intake of 33 KV of power and eight for distribution to various consumers within the airport premises. The Authority is required to maintain monthly average power factor (PF) of 0.85 being categorised as high voltage commercial consumer by CESC.

The Authority did not install automatic capacitor banks/automatic power factor control equipment at its distribution sub-stations other than at one sub-station. As a result, the overall average monthly PF of the Authority varied from 0.77 to 0.84 during the period February 1997 to July 2004. The Authority consequently paid PF surcharge of Rs.1.73 crore over this period. Further levy of PF surcharge was avoided from August 2004 due to installation of another correction apparatus at one more substation. Existing static type capacitor banks were subsequently converted (November 2004) to auto mode in four substations.

Thus, the failure to monitor and maintain the power factor and non-installation of automatic power factor correction equipment in time resulted in avoidable payment of penalty of Rs.1.73 crore.

The Authority while confirming the facts and figures stated (October 2004) that in most of the other sub-stations, static type capacitor banks were installed (six during 1995-96) which did not work due to erratic load characteristics of airport. Also, various other consumers drawing power from the Authority's sub-stations took no corrective action. Further the surcharge on low power factor had been imposed on the consumers for which bills (Rs.1.78 lakh) had been sent to Indian Airlines Limited, Airport Hotel and Indian Oil Corporation Limited for the period from April 2004 to June 2004 and for the remaining period, action for raising the bills for surcharge on low power factor was in

process. It added (May 2005) that non-installation of automatic power factor equipment was not intentional, but due to lack of experience and confidence with newly introduced equipment. The Ministry endorsed (July 2005) the Management's reply.

The reply is not tenable as despite being aware of the importance of maintaining monthly average power factor and its consequences, Authority failed to take remedial measures of installing automatic power factor correction equipment in time and had not raised any bills for imposition of surcharge for the period February 1997 to March 2004 (September 2005). Again, as against Rs.18.73 lakh actually paid by the Authority, for the period April 2004 to July 2004, bills amounting to Rs.1.78 lakh only had been raised and the amount was yet to be recovered. The bills for the balance amount could not be raised against low voltage consumers, as there was no provision of imposition of surcharge on them.

Thus, due to not maintaining the required power factor at the substations, the Authority had to pay penalty of Rs.1.73 crore.

4.2.4 Extra expenditure of Rs.1.02 crore on electricity charges at Agartala airport

Failure on the part of the Authority to take immediate action to surrender the old connection and to detect billing arrears in time resulted in avoidable extra energy charges of Rs.1.02 crore.

The Agartala airport of Airports Authority of India (Authority) was drawing power of 515 KVA for its Old Power House from the Department of Power, Tripura Government. Consequent upon taking up the project for construction of a new terminal building, it was estimated by the Consultant (August 2000) that the power requirement of the Airport would be 1,507.5 KVA.

The Authority applied (October 2000) to the Department of Power for a total connected demand of 1,250 KVA in a phased manner i.e., 750 KVA from December 2000, 1,000 KVA from June 2001 and 1,250 KVA from December 2001. The Department of Power, however, informed the Authority (February 2001) that electricity charges for bulk supply would be made on the basis of the installed capacity of the transformer, considering 80 *per cent* load factor and not as per the phased requirements of the Authority. Accordingly the Authority obtained an additional connected load of 1,600 KVA (July 2001), thus, taking the total connected load to 2,115 KVA. The Authority failed to surrender immediately the 550 KVA of the connected load of the Old Power House.

It was noticed in Audit that even after completion of all the works related to new terminal building in August 2002, the maximum requirement of power ranged between 900 KVA and 1,100 KVA only as against the total installed capacity of 2,115 KVA. The Department of Power also incorrectly billed the Authority to the extent of Rs.31.89 lakh for 100 *per cent* of the total installed capacity of the transformer as against 80 *per cent* required to be billed from July 2001 till November 2004. After this was pointed out by Audit in November 2004, the same was revised to 80 *per cent* of the installed capacity from December 2004 onwards. The Authority also surrendered the Old Power House connections in March 2005. The incorrectly billed amount of Rs.31.89 lakh was, however, yet to be recovered (July 2005).

Thus, the Authority not only failed to surrender the connected load of Old Power House connection but also failed to notice the wrong billing by the Department of Power in respect of the New Power House connection. This resulted in avoidable payment of energy charges of Rs.1.02 crore.

The Management stated (May 2005) that the new connection with transformer capacity of 1,600 KVA was necessary due to the modernisation project and it was not feasible to surrender the old connection in view of future projects, which were under planning stage.

The reply of the Management is not tenable in view of the following:

(i) The consultant had assessed the total power requirement as 1,507.5 KVA only at Agartala airport taking into account the future demand.

(ii) The Authority also had assessed that it had enough spare capacity to feed the whole airport.

(iii) The Airport surrendered the old connection (March 2005), which proves Audit's contention.

(iv) The Authority also delayed in taking up the issue of incorrect billing with Department of Power for 40 months.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

Indian Airlines Limited

4.3.1 Delayed decision to construct a booking office at Chandigarh resulted in loss of Rs.72.04 lakh

Delayed decision by Indian Airlines Limited to construct a booking office on its plot resulted in loss of Rs.72.04 lakh.

Indian Airlines Limited (Company) was allotted a plot measuring 472 square meter on lease in Chandigarh (April 1985) by the Estate Officer, Union Territory of Chandigarh, at a cost of Rs.33.88 lakh for the construction of booking office. The lease agreement stipulated completion of construction within three years, failing which a penalty of Rs.37,759 per annum was payable. The Company decided in December 1988 to construct an office at a cost of Rs.74.50 lakh. However, no concrete steps were taken in this regard for 13 years and the booking office continued to function from a rented building. A Committee was formed in August 2001 and a cost benefit analysis was done for the proposed construction of booking office. The Committee found the project to be financially and commercially viable. Accordingly, financial sanction of Rs.1.25 crore was accorded in March 2002. The work was awarded in December 2004 for Rs.1.06 crore after a delay of 33 months to M/s. Evam Construction Private Limited. The construction is under progress and the Company presently operates its booking office in a rented building for which it pays a rent of Rs.75,000 per month.

Audit noticed (February 2005) that during the period December 1990 to March 2005, the Company made a total payment of Rs.72.04 lakh (penalty Rs.5.66 lakh and rent of Rs.66.38 lakh).

The Ministry stated (December 2005) that Audit while assessing the amount of loss had not taken into account the estimated expenditure on upkeep of building and other incidental expenditure. It further stated that the commercially non-viable conditions in the early stages coupled with acute financial crunch were instrumental in the Company's inability to carry out the construction.

The reply of the Ministry is, however, not tenable because the Audit computed the loss on the basis of the actual rent and penalty paid duing December 1990 and March 2005. The estimated cost of maintenance and incidental expenditure were not considered in view of the projected rental earnings of Rs.1.50 lakh per month for the surplus area of the construction. As the cost benefit analysis made by the Company indicated that the construction was financially viable even with borrowed funds, there was no justification for delaying the construction till November 2004.

Thus, the delayed decision on the part of the Management for construction on the plot has cost the Company Rs.72.04 lakh (upto March 2005). Moreover, the loss of revenue that could have been generated by letting out space for commercial purposes cannot be ignored as this was one of the items taken into account in the feasibility analysis of the project.

CHAPTER V: DEPARTMENT OF COAL

Bharat Coking Coal Limited

5.1.1 Avoidable revenue loss due to consumption of steel grade coal for boiler

Failure in arranging transportation for cheaper 'C' grade coal and continued injudicious use of steel grade coal for boiler consumption resulted in revenue loss of Rs.51.20 lakh and wastage of resources.

Coal is required for the purpose of firing the boiler to generate electricity for the collieries' consumption. Bharat Coking Coal Limited (Company) in its two collieries, Victoria West and Begunia in Chanch Victoria area used substantial quantity (19,085 MT) of steel grade coal worth Rs.3.66 crore in their boilers during the period from April 2000 to March 2004. The scarce and costly steel grade coal was meant for consumption only in steel plants. During this period the price of steel grade coal was higher by Rs.583 to Rs.1,788 and ranged between Rs.1,307 per MT and Rs.2,676 per MT as against the price of 'C' grade coal that ranged between Rs.724 per MT and Rs.888 per MT. The cheaper 'C' grade coal was available in sufficient quantity from nearby Dahibari and Basantimata collieries situated at a distance of 30 to 32 Km. While the production in Victoria West colliery was suspended from the end of November 2001, the Company instructed (January 2002) Begunia colliery Management to use 'C' or 'D' grade coal from Basantimata colliery and termed (May 2002) use of steel grade coal for boiler firing a criminal offence of wasting national property. To facilitate transportation of 'C' or 'D' grade coal, a tipper was also allotted to Begunia colliery in February 2002. The tipper could not be used as it was defective. The Project Authorities proposed (November 2002) transport of 'C' grade coal contractually from Basantimata colliery. The tenders floated in January 2003 were cancelled in January 2004 on the grounds of unreasonable rates quoted by the transporters. As a result, till March 2004 neither departmental serviceable tipper was made available nor private transport was arranged and Begunia colliery continued with the consumption of steel grade coal.

It was observed in Audit that the rate agreed by the lowest tenderer was Rs.215 per MT and departmental transportation cost was Rs.186 per MT as estimated by the Management whereas the difference in the rate of steel grade and 'C' grade coal varied between Rs.1,326 per MT and Rs.1,788 per MT from February 2002 to March 2004. Thus, by deploying a workable departmental tipper or by using private transportation, the Management could have saved 5,318 MT of precious steel grade coal at Begunia colliery during this period.

On this being pointed out by Audit (April 2003), the Management stated (March 2004) that with the availability of tippers, the consumption of steel grade coal for boiler use had been totally stopped. It further stated (March 2005) that the monthly consumption of 344 MT of Steel grade coal in boiler was equivalent to 444 MT of 'C' grade coal taking into account the comparative 'useful heat value' of the two categories of coal. The Ministry endorsed (November 2005) the views of the Management.

The reply of the Management/Ministry is not tenable as even after considering the useful heat value, 1.29 MT of 'C' grade coal would have been equivalent to one MT of steel grade coal used and taking into account the variable departmental transportation cost and differential royalty, the value of 'C' grade coal consumed would have been cheaper than steel grade coal by Rs.51.20 lakh for the coal consumed during February 2002 to March 2004.

Central Coalfields Limited

5.2.1 Unfruitful investment of Rs.80.24 crore on captive power plant at Kathara

To ensure uninterrupted power supply, Central Coalfields Limited placed an order on BHEL in March 1987 for commissioning of 2x10 MW Captive Power Plant at Kathara with completion date by September 1990. The plant, commissioned in May/June 1995, failed to give the desired output and remained completely idle since May 2000 rendering investment of Rs.80.24 crore on this project unfruitful.

In order to ensure uninterrupted power supply at Kathara Area of Central Coalfields Limited (Company), the Management on the basis of a Feasibility Report (May 1980) decided to install 2 x 10 MW Captive Power Plant (CPP) at a total capital investment of Rs.30.02 crore which was revised to Rs.49.20 crore (October 1986) at the time of approval of the project. The orders for supply of equipment and installation and commissioning of CPP were placed (March 1987) on Bharat Heavy Electricals Limited (Contractor) with phase-wise scheduled commissioning dates fixed as May and September 1990. The work on the project commenced in April 1987. However, the project could not be completed within the scheduled period leading to revisions in cost to Rs.58.80 crore (March 1991) and Rs.85.20 crore (September 1996). The scheduled dates of completion were finally fixed as December 1992 and February 1993. The CPP was partially commissioned in May/June 1995 at a total cost of Rs.80.24 crore. The CPP worked at sub optimal capacity till May 2000 and has been idle thereafter (October 2005).

The CPP could not be optimally utilised and the expenditure incurred has become largely unfruitful as is evident from the following:-

(i) The decision for installation of CPP was taken in 1980 and the plant was partially commissioned in March 1995 i.e. after a lapse of 15 years. The Management attributed such abnormal delay, *inter alia*, to resource crunch, local law and order problems and slow progress of work by the sub contractor. The contractor finally left the site in June 1997 without properly handing over the Plant and left a number of jobs unattended. The Management also failed to revalidate the performance bank guarantee (expired in May 1995) of the contractor and initiate recovery of liquidated damages of Rs.31.98 crore due to non fulfillment of contractual obligations. However, a sum of Rs.8.73 crore was withheld for non-execution of work. The contract was terminated in June 2003.

(ii) The CPP was not duly commissioned and the productivity was very poor ranging from 112.85 lakh KWH to 2 lakh KWH per year from the year 1995-96 to 2000-01 as against the planned output of 1,300 lakh KWH per year. As a result, the

CPP could generate on an average only 41.64 lakh KWH per year during this period. This was mainly due to the fact that the contractor left several jobs incomplete.

(iii) Due to various deficiencies in the installation of CPP, it could not run on full load for commercial generation of power and could achieve only 3.20 *per cent* of the planned output. Thus, low generation of power increased the average unit cost of power to Rs.34.21 per KWH whereas the purchase cost of power from Damodar Valley Corporation was ranging from Rs.2.83 per KWH in 1998-99 to Rs.2.95 per KWH in 2002-03. Thus, power generated by CPP was significantly more expensive.

The Management stated (June 2004) that teething problems faced during the trial run could not be solved due to the obstructions by local people and ultimately contractor left the work unfinished. Due to some reason or the other contractor did not resume the work. It was further stated that letter of intent had been issued to M/s. Imperial Fasteners Private Limited for leasing of the CPP on 15 April 2005. The Ministry endorsed (May 2005) the views of the Management.

The above contention of the Management is not convincing as the fact remains that the huge investment of Rs.80.24 crore had been blocked and remained unproductive. Even when CPP was commissioned after 15 years, it could not be utilised gainfully. Further, no progress had been achieved in leasing out the CPP till October 2005.

5.2.2 Avoidable expenditure of Rs.37.05 crore due to non synchronisation of Captive Power Plants

DLF Power Company Limited built and commissioned two Captive Power Plants (CPPs) at Rajrappa and Giddi in July 1999 and April 2000 respectively to meet acute shortage of power for Central Coalfields Limited. But the CPPs could not be synchronised with DVC grid and as a result, the Company incurred an avoidable expenditure of Rs.37.05 crore for the unused energy from 1999-2000 to 2004-2005.

In view of acute shortage of power experienced in the eastern region, it was decided by Coal India Limited (CIL) Board to increase national power generation capacity through Captive Power Plants (CPPs) by utilising washery rejects. Accordingly, CIL entered into a 30 years contract with M/s. DLF Power Company Limited (DPCL) in February 1993 to construct Fluidised Bed Combustion (FBC) technology based power plants at Rajrappa and Giddi (10 MW each) of Central Coalfields Limited (Company), under the 'Built Own and Operate' (BOO) principle, for supply of power. The Company was bound to purchase the guaranteed power generated by CPPs. Further, if DPCL was able to feed more power from the station the same was also to be evacuated and paid for by CIL.

The CPPs were conceptualised on the principle of optimum utilisation of power that required synchronisation of the plant with the Damodar Valley Corporation (DVC) grid to ensure that all the power generated by the CPPs was fed into DVC grid. The power so drawn was to be deducted from the power drawn by CCL from DVC. The Ministry of Coal took up (January 1996) the matter with the Ministry of Power for using the grid of DVC for wheeling out the power from the CPPs. It was also emphasised that operation of

CPPs would be highly uneconomical in case the evacuation was not allowed. DVC issued 'no objection' in June 1996 for setting up CPPs in its command area without committing to the synchronisation proposal of the Company.

It was noticed in Audit that power situation improved subsequently in the eastern region necessitating review of the setting up of the CPPs in 1996 itself. However, no such review was conducted by the Company and Memorandum of Understanding (MOU) was signed with DPCL in July 1997. Two CPPs at Rajrappa and Giddi were commissioned in July 1999 and April 2000 respectively without obtaining the approval from DVC for synchronisation. As per the agreement with DPCL, the Company was required to consume a minimum of 58.40 lakh KWH per month per plant otherwise penalty in the form of 'Deemed Energy Charges' (DEC) was to be paid for the unconsumed energy. The Company continued taking power from DVC in view of periodical maintenance, breakdown etc. of CPPs for which it had to pay Minimum Guaranteed Energy (MGE) charges for not consuming energy as per the contract demand. There was a series of meetings and correspondence at different levels between DVC and CIL to resolve the issue of synchronisation and feeding of power generated from CPPs to DVC grid. DVC time and again refused synchronisation and clearly stated in June 2001 that in view of expected surplus power position and high frequency scenario in Eastern Regional Grid it would not be possible for them to allow CIL for synchronisation of the CPPs with their grid.

As per the contract, the Company was required to pay Rs.54.39 crore to DPCL for unused energy of 3,163.26 lakh KWH on account of DEC from the date of commissioning of the CPPs at Rajrappa and Giddi to March 2005. Out of this, the Company had already paid Rs.40.79 crore to DPCL, being the interim payment of 75 *per cent* of total payable amount. At the same time the Company also paid Rs.11.08 crore to DVC towards MGE charges for drawing less energy than the Contract Demand at Rajrappa area from July 1999 to March 2005. Thus, an amount of Rs.65.47 crore was incurred in respect of the energy not consumed by the Company.

The Management contended (April 2005) that had the power been taken from DVC only, the cost would have been more or less the same and that there would not be any extra expenditure for taking power partially from DPCL. It was further stated that arrangements had been made to utilise more power from Giddi CPP and there was no further scope to utilise excess power at present from Rajrappa CPP. The contention of the Management is not tenable in view of the fact that if power was taken from DVC only in the absence of CPP, the differential cost would work out to Rs.28.42 crore[*] and net avoidable expenditure would work out to Rs.37.05 crore for the period July 1999 to March 2005. Further, considering the 30 year contract with DPCL, the Company would continue to sustain recurring loss towards payment of DEC to DPCL as it has been doing since the commissioning of CPPs till either these are synchronised with DVC grid or creation of its own grid as an alternative.

[*] ***the difference of cost of power drawn from DPCL as if drawn from DVC by applying average rates (Rs.95.77 crore minus Rs.67.35 crore)***

The Ministry stated (September 2005) that the matter of synchronisation is under active consideration by the DVC Management. Once the synchronisation is done, the DLF plant will be fully utilised.

Thus, setting up the CPPs without obtaining firm commitment from DVC for synchronisation with their grid resulted in an avoidable extra expenditure of Rs.37.05 crore. Further, the Company did not avail the opportunity to review the projects in 1996 when power situation improved and therefore, would continue to incur an extra expenditure in future also.

Central Mine Planning and Design Institute Limited

5.3.1 Avoidable payment of interest due to short payment of advance income tax

Incorrect estimation of taxable income and consequent short payment of advance income tax by the Company resulted in avoidable payment of interest of Rs.72.42 lakh in respect of the financial years 2001-02 to 2003-04.

Under Section 208 read with Section 211 of the Income Tax Act, 1961 (Act), each Company is required to pay advance tax at the prescribed rates on due dates in quarterly instalments in a financial year in case the amount of income tax payable by the Company during that year exceeds Rs.5000. In the event of short payment of advance tax, the Company is liable for payment of interest under the provisions of the Act. According to Section 234 (B) of the Act, if the advance tax paid is less than 90 *per cent* of the assessed tax, simple interest at the prescribed rate is leviable for every month or part thereof, from first April of the assessment year to the date of determination of income under the Act, on the amount by which the advance income tax paid falls short of the assessed tax. Section 234(C) of the Act also provides for payment of interest at the prescribed rate on the amount of short paid instalments of advance tax for a period of three months.

A review of records of Central Mine Planning and Design Institute Limited (Company) relating to assessment of income tax revealed that it paid less advance income tax during the financial years 2001-02 to 2003-04. As a result, the Company had to pay interest of Rs.41.61 lakh under Section 234(B) and Rs.30.81 lakh under Section 234(C) of the Act totalling Rs.72.42 lakh due to incorrect estimation of taxable income during the above financial years.

While admitting the fact the Management stated (November 2004) that the estimated profit and actual profit would always vary and therefore the calculation of advance income tax and actual income tax payable would also vary. The reason for shortfall in payment of advance income tax was mainly attributed to wide variations in estimated and actuarial valuation of gratuity and leave encashment, budgeted and actual profit and minor variations in estimated and actual rate per Engineering Day (ED) and per meter of drilling which were available much beyond March of the respective years. Other factors viz. provision for bad and doubtful debts and obsolete items etc. were also causing variance between estimated advance income tax and actual income tax.

The above contention of the Management is not tenable as the Company's inability to make self-assessment of income and advance income tax accurately indicated poor

financial management. The Management had the opportunity to review the abnormal variation in actuarial valuation and other factors and revise their estimated taxable income while paying the quarterly instalments of advance income tax due in September, December and March of the respective years by closely monitoring its actual income and expenditure *vis-a-vis* the estimates, thus reducing the difference to the minimum as was done for the financial year 2004-05. Moreover, provisions for gratuity and leave encashment are not admissible and are added back to the book profit by the Income Tax Department and only actual payments on account of gratuity and leave encashment are allowed as deduction.

The Ministry stated (September 2005) that though efforts were made to minimise the variation between budgeted and actual income, the difference could not be eliminated due to abnormal and irregular variation in actuarial valuation of gratuity and leave encashment.

Thus, due to failure in making correct assessment of taxable income, the Company had to pay avoidable interest of Rs.72.42 lakh to the Income Tax Department on account of short payment of advance income tax during the financial years 2001-02 to 2003-04.

Eastern Coalfields Limited

5.4.1 Loss due to incorrect assessment of power requirement

Against the actual maximum demand of 750 KVA for power of Kalidaspur Project, the Management reduced the contracted power load from 1,500 KVA to 1,000 KVA (to be increased by 100 KVA in every succeeding year) with effect from April 1998 resulting in payment of Rs. 63.47 lakh towards unconsumed power during April 1998 to June 2004.

Eastern Coalfields Limited (Company) entered into an agreement with West Bengal State Electricity Board (WBSEB) in July 1981 for supply of electricity to its Kalidaspur Project. As the production of Kalidaspur Project did not come upto the desired level, the Company entered into a fresh agreement with WBSEB in April 1998, for a period of five years reducing the maximum contract demand from 1,500 KVA to 1,000 KVA for the first year with the provision to increase it by 100 KVA in each subsequent year till the fifth year (2002-03) when the contract demand was to be 1,400 KVA.

Audit observed (January 2004) that though the actual maximum demand was within 750 KVA before entering into the agreement in April 1998 the Management did not take any initiative to revise the contract demand to 750 KVA at the time the agreement was concluded in 1998. The reasons for providing for yearly increase in the contract demand were also not on record. During the period 1998 to 2003, the actual demand also never exceeded 750 KVA. As a result, Rs.63.47 lakh was paid towards penalty to WBSEB for drawing power less than the contracted demand during the period April 1998 to June 2004. In May 2004, the Management further intimated the load forecast for the next five years to the WBSEB as 750 KVA with an increase of 50 KVA per year despite the project being foreclosed by the Ministry in August 2003. The revised agreement was executed in July 2004 for a period of five years.

The Management stated (August 2004/June 2005) that cent *per cent* correct assessment of demand of power in respect of a new upcoming project was not possible. The Ministry endorsed (November 2005) the views of the Management.

The contention of the Management/ Ministry is not tenable as the demand never exceeded 750 KVA as reported to WBSEB in November 1997 itself. Further, there was no justification for an annual increase in demand of power when the provision to increase the demand by giving one-year notice existed in the agreement.

Thus, due to unrealistic assessment of power requirement the Company suffered an avoidable loss of Rs.63.47 lakh during April 1998 to June 2004 towards unconsumed power.

Northern Coalfields Limited

5.5.1 Avoidable extra expenditure of Rs.14.34 crore towards payment of excess statutory dues

The Company preferred sales bills without considering subsequent adjustments on account of excess moisture and thereby had to absorb an extra expenditure of Rs.14.34 crore on account of excess statutory dues.

Northern Coalfields Limited (Company) preferred sales bills on the very next day against daily dispatch of coal from its Nigahi, Amlohri and Jayant projects and deposited statutory dues viz. Royalty, Stowing Excise Duty (SED) and Sales Tax on the billed amount to the appropriate authorities. Clause 10.2 of the Coal Supply Agreement with NTPC Limited (NTPC), *inter alia*, stipulated that the Company would make adjustment (reduction) in quantity of coal on account of excess total moisture noticed in joint sampling on monthly basis. Otherwise, NTPC would make payment of bill after making due adjustments.

It was observed in Audit that the Company issued credit notes in favour of NTPC in respect of excess moisture noticed on the basis of joint sampling only for the basic price of coal and sales tax thereon. The Company, however, did not make any adjustment for other statutory dues namely Royalty and SED paid in respect of moisture content beyond the permissible limits. Consequently, NTPC deducted, on its own, from the original bills for the period 1998-99 to 2004-05 an amount of Rs.14.34 crore towards excess Royalty (Rs.10.24 crore), SED (Rs.3.55 crore) and Sales Tax (Rs.0.55 crore) in proportion to the excess quantity of moisture, as per joint sampling. However, the Company did not issue revised sales bills considering excess moisture content (reduction) and as a result did not claim refund of the above amounts from the appropriate authorities. The Management admitted (November 2004) that the Company was not entitled to any payment including statutory levies from NTPC on account of excess moisture. Therefore, the statutory dues paid on account of excess moisture were absorbed by the Company. Thus, the Company incurred avoidable expenditure of Rs.14.34 crore.

The Management (May 2005) accepted the Audit observation and stated that necessary steps had been taken for adjustment of excess moisture beyond permissible limit as per analysis report, from monthly dispatch bills, as suggested by Audit. An instruction in this

regard was issued to the concerned project authorities on 31 March 2005 for implementation. Thus, as the Company did not have a mechanism for timely adjustment of excess weight due to moisture in the invoice, it had to bear the extra expenditure of Rs.14.34 crore apart from showing inflated production figures as a result of taking gross dispatched quantity in the bills preferred without considering the adjustment (reduction) due to excess quantity of moisture.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

South Eastern Coalfields Limited

5.6.1 Wasteful expenditure of Rs.1.06 crore and blocking of funds of Rs.2.30 crore

The Company did not ascertain the feasibility of coal dispatches from Pali siding through Coal Handling Plant before starting construction, which resulted in wasteful expenditure of Rs.1.06 crore and blocking of funds of Rs.2.30 crore for more than five years.

The project report for Pali underground mine of South Eastern Coalfields Limited (Company) provided for a Coal Handling Plant (CHP) for loading coal into wagons of Madhya Pradesh Electricity Board (MPEB) for transportation to Sanjay Gandhi Thermal Power Station of MPEB. Accordingly, the Company constructed CHP and electronic weighbridge at a cost of Rs.3.36 crore and it was commissioned in October 1995. However, it could be utilised for a limited period of five months only from January to May 2000 and was lying un-utilised since then as MPEB stopped taking coal from Pali mine.

It was observed in Audit that the dispatch of coal was stopped since the Railways did not allow (April 2000) transportation of coal from Pali siding as it affected the running of regular railway pilots. This indicated that the Company did not ascertain the feasibility of dispatching coal from Pali siding through CHP before starting construction of CHP. Further, though CHP remained idle since April 2000, the issue of possible utilisation of steel items on dismantling of CHP was put up to Board of Directors only in September 2003. The Company is yet to complete the dismantling of CHP (September 2005).

The Ministry stated (March 2005) that the Railways had accorded temporary permission on trial basis subject to the condition that if it affected running of regular railway pilots, the same would be withdrawn. They added that almost all the items except steel structures and electronic weighbridge of CHP had been dismantled and used.

The Management subsequently informed (September 2005) that the dismantling of CHP was yet to be completed. In fact, even after retrieval of steel items on dismantling of CHP, the expenditure of Rs.1.06 crore incurred on civil works would still be wasteful.

Thus, the Company's failure to ascertain the feasibility of coal dispatches from Pali siding through CHP resulted in wasteful expenditure of Rs.1.06 crore as well as blocking of funds of Rs.2.30 crore for more than five years.

Western Coalfields Limited

5.7.1 Avoidable loss of Rs.2.96 crore due to delay in installation of weighbridges

The Company delayed the installation of weighbridges and incurred a loss of Rs.2.96 crore on account of avoidable payment of penalty for underloading and overloading of coal wagons over a period of five years from 2000-01.

Pench Area of Western Coalfields Limited (Company) had no weighbridge for weighment of coal wagons at its two sidings [Broad Gauge (BG) and East Donger Chikhli (EDC)] and the wagons were to be weighed at Junnardeo, about 22 kms from the loading point. As a result, the Company had to suffer losses on account of payment of penalty for underloading and overloading of wagons.

A proposal for installation of rail weighbridge at BG siding of Pench Area was under the consideration of the Company since 1998-99. As the Railway authorities had not approved installation of 'in motion' weighbridge because of insufficient space, the Company decided (August 2001) to install two static weighbridges one each on both rail tracks at BG siding and awarded (July 2002 and April 2003) work orders for the same. The weighbridges were commissioned at an expenditure of Rs.27.13 lakh and became operational from January 2004.

Though the Company was paying heavy underloading charges at EDC siding also, it initiated proposal for installation of rail weighbridge at this siding in April 2004 only. The work order for the same was yet to be awarded (August 2005).

It was observed in Audit that even though the Company had been paying underloading charges, the Company took more than 43 months in awarding the orders for installation of the weighbridges at BG siding, while even the work order was yet to be awarded for the installation of weighbridge at EDC siding (August 2005). No urgency was shown by the Company and an inordinate time was taken by its various agencies in deciding the type of weighbridge. Further, though one weighbridge was installed at BG siding in March 2003, the same was not put to use till the installation of the second weighbridge in January 2004. The Company in the process had to pay underloading charges of Rs.2.96 crore[♣] at BG and EDC sidings during the period from 2000-01 to 2004-05.

While accepting that the underloading of wagons took place due to transit loss and pilferage, the Management/Ministry stated (May/October 2005) that although there was insufficient space, the Company explored the possibility of 'in motion' weighbridge for fast movement of wagons, which caused delays in taking decision and implementation. Further, commercial use of the first weighbridge could not be started in March 2003 as only half the number of wagons in a rake would have been weighed. They added that loss due to under or overloading of wagons at EDC siding could not be controlled by 'in motion' weighbridge and static weighbridge could not be installed as there was no arrangement for chute loading.

[♣] *Rs.1.25 crore at BG siding for the period 2000-01 to 2003-04 and Rs.1.71 crore at EDC siding for the period 2000-01 to 2004-05 (upto December 2004)*

The reply is not acceptable as the Company took an inordinate time of 33 months in deciding the type of weighbridge at BG siding and further 10 months in awarding the works, while in the case of EDC, even the proposal for installation of weighbridge was initiated only in April 2004 and the work order was yet to be awarded. This was despite the fact that there were recurring incidences of overloading/underloading charges and the same were being regularly pointed out by Audit since 1990-91. The Management's contention that loss at EDC siding could not be controlled by 'in motion' weighbridge, is also not correct as even by installing 'in motion' weighbridge, the Company could have avoided transit losses/pilferage.

Thus, inordinate delay in installation of weighbridges at BG siding and non-installation of weighbridge at EDC resulted in loss of Rs.2.96 crore to the Company upto December 2004, which would further increase till installation of weighbridge at EDC siding.

CHAPTER VI: MINISTRY OF COMMERCE AND INDUSTRY

India Trade Promotion Organisation

6.1.1 Loss of revenue due to non enhancement of licence fee and doubtful recovery of overdue amount

The Company lost revenue of Rs.2.76 crore due to not enhancing the licence fee from two licencees. An amount of Rs.1.94 crore was also outstanding from these licencees, which was doubtful of recovery due to inadequate security taken by the Company.

India Trade Promotion Organisation (Company) decided (May 1998) to operate Food and Beverages (F&B) outlets in Pragati Maidan by appointing F&B operators and accordingly allotted (July 1999) a restaurant in Kiosk K-11 to M/s. Gulati Restaurant Private Limited for 10 years (First licensee). The area allotted was 148.64 square meter (sqm) of covered area and 139.35 sqm of open area, at an annual licence fee of Rs.15.00 lakh (July 1999) with an increase of 10 *per cent* in the licence fee over the previous year.

Simultaneously another operator viz. M/s. Gulati Caterers (P) Limited (Second licensee) was allotted (July 1999) Woodland restaurant (Aader Satkar) with covered area of 226.59 sqm and an open area of 170 sqm for 10 years. The annual licence fee fixed was Rs.25.54 lakh with an annual increase of seven *per cent* over the previous year. The agreements with these licensees were entered into after a lapse of 16 months (November 2000) and in the meanwhile the licensees were operating on the basis of allotment letters. Apart from the payment of licence fee, the licensees had to pay for electricity, water, and conservancy charges to the Company. Besides, as per clause A-1 of the agreement, the licensees had to obtain prior permission from the Company for any improvement in the existing structure.

In violation of the above clause, Audit observed that while the first licensee had constructed an extra area of 148.60 sqm, occupied 448.41 sqm of open area and converted 250 sqm of green area. into open paved area, the second licensee was allowed by the Company (September 2002) to utilise 645 sqm of constructed area for which no proportionate additional licence fee was enhanced and collected by the Company. The licence fee leviable for the constructed area alone worked out to Rs.2.76 crore (Rs.1.16 crore for the first licensee and Rs.1.60 crore for the second licensee respectively). The licensees were also irregular in the timely payment of licence fee and other charges from the year 2000-01 onwards and an amount of Rs.1.94 crore (Rs.0.69 crore and Rs.1.25 crore respectively) was overdue as on 31 March 2005.

Audit noticed that the selection of these two licensees was made without assessing their financial strengths to pay the licence fee and other charges and agreements entered into with the licensees did not contain the clauses for (i) providing Bank Guarantee by the licensees and (ii) assets to be mortgaged in favour of the Company. Other undue benefits extended were as below:

(i) Important clauses binding the parties to consult the Company about the rates to be charged for their range of items and prohibiting barat, wedding ceremonies etc., were deleted at the time of signing of agreements.

(ii) The agreements provided that non receipt of licence fee within the time schedule would be treated as non compliance to the agreed terms and conditions and penalty for the same would be imposed by the Company. However, the quantum of penalty was neither pre-determined in the agreements nor levied by the Company.

(iii) Gulati Caterers (Second licensee) who opted for termination of contract in October 2001, was on its request allowed extension of notice period to enable it to exploit the business opportunity during the Annual India International Trade Fair in November 2001 inspite of non-settlement of its outstanding dues. Subsequently, it was not only allowed to continue beyond the extended date but also its plan for reconstruction of restaurant was approved (July 2002).

(iv) Three cheques amounting to Rs.14 lakh (Rs. four lakh, Rs. five lakh and Rs. five lakh) received from Gulati Caterers (Second licensee) were dishonoured during October 2002 and October 2003 by their bank but no legal action under the Negotiable Instruments Act was initiated.

The Management accepted the above facts (May 2005) but did not furnish any reasons for not initiating action against the licensees.

Thus, the Company extended undue benefits to these two licensees for which no responsibility had been fixed. As a result, it not only lost licence fee of Rs.2.76 crore but also accumulated outstanding dues of Rs.1.94 crore, recovery of which was doubtful as the Company had a security of Rs.0.04 crore only.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

The State Trading Corporation of India Limited

6.2.1 Loss to exchequer in supplying humanitarian aid to the Governments of Tajikistan and Ivory Coast - Rs.6.11 crore

The State Trading Corporation of India Limited paid to the Associates the cost of sugar without restricting the same to the actual cost of procurement. It also paid freight in the export of rice, wheat, tea and sugar to the Associates without relating the same to the actual. This resulted in undue favour of Rs.6.11 crore to the Associates at the cost of the exchequer.

The Ministry of External Affairs (MEA) made an enquiry with the State Trading Corporation of India Limited (Company) to furnish the consolidated quotation for supply of rice, sugar, wheat and tea to be exported to Tajikistan (November 2001) and Ivory

Coast (April 2003) on CIF[♣] basis, as humanitarian assistance. The Company invited quotations from its branches and based on the prices quoted by the Associates, the Company intimated (March 2002 and April 2003 respectively) its estimated offer price to the MEA for the above commodities. The prices quoted included cost of material, freight, insurance etc. Against the aforesaid quotation, the MEA accorded approval (March 2002 and June 2003 respectively) for supply of sugar, wheat, tea and rice. The Company in turn directed its branches to formalise the arrangements. Accordingly, the contracts were entered into with two Associates (April 2002 and June 2003) one from Bangalore for supply of wheat, rice and sugar at the prices quoted by them inclusive of service charges of 2.5 *per cent* on FOB[♠] value and another from Kolkata for supply of tea at the price quoted by them.

As per contracts with the Associates, they were required to procure the sugar and tea from the open market and wheat and rice from Food Corporation of India's godowns. While the Associate at Kolkata purchased tea from the open market, the Company helped the Associate from Bangalore in procuring sugar at the rate of Rs. 11,000 per MT from sugar mill through Directorate of Sugar under Ministry of Consumer Affairs. The basic price of sugar as quoted by the Associate was Rs.13,900 and the market rate was Rs.13,685 (January 2002). However the Company paid to the Associate at the rate of Rs.13,900 per MT for 3,633.50 MT of sugar instead of restricting the payment to Rs.11,000 per MT being the actual cost paid by them. This resulted in overpayment of Rs.1.05 crore to the Associate.

The Company also failed to analyse and restrict the payment of freight to the actuals incurred by the two Associates in respect of all commodities and consequently, released payment of freight amounting to Rs.11.65 crore, as against the actual freight of Rs.6.59 crore paid by the Associates, resulting in excess payment of Rs.5.06 crore. .

Thus, failure of the Company to analyse the rates before entering into contracts and/or failure to incorporate a clause in the agreements for the payment on actual basis resulted in extension of undue benefit of Rs.6.11 crore to the Associates at the cost of the Government.

The Ministry of Commerce and Industry, Department of Commerce stated (September 2005) that the Company had agreed to follow the procedure suggested by Audit so that such a situation did not arise in future and undue gains did not occur to the Associates.

The matter was also referred to the Ministry of External Affairs in October 2005; its reply was awaited (November 2005).

[♣] *Cost, insurance and freight*

[♠] *Free on board*

CHAPTER VII: MINISTRY OF CONSUMER AFFAIRS, FOOD AND PUBLIC DISTRIBUTION

Central Warehousing Corporation

7.1.1 Blocking of funds on purchase of flats for staff at JNP, Navi Mumbai

Flats purchased for staff as quarters at Jawaharlal Nehru Port, Navi Mumbai from City Industrial and Development Corporation, Mumbai could not be utilised and resulted in idle investment of Rs 6.07 crore.

The Board of Directors (BOD) of Central Warehousing Corporation (CWC) approved (June 1997) the proposal for purchase of 86 flats at an estimated cost of Rs 7.45 crore at Jawaharlal Nehru Port (JNP), Navi Mumbai from City Industrial and Development Corporation (CIDCO) on the ground that additional residential accommodation was required as its activities were expanding. The Government of India (GOI) agreed in principle (May 1998) to the purchase of these flats.

The estimated cost of the flats increased to Rs 8.65 crore due to inclusion of stamp duty and other miscellaneous charges. The CWC released the differential cost of Rs 1.20 crore to CIDCO even before the approval of BOD (August 1999). In addition, Rs 0.68 crore was spent for fixture and fittings thus raising the total cost of flats to Rs 9.33 crore.

Out of the 86 flats, 55 flats purchased at the cost of Rs 6.07 crore, remained vacant since the date they were taken over and only 31 flats were allotted during the period June 2000 to August 2002. Of these 31 flats only four flats were occupied as on date (May 2005). The period of occupancy of the remaining 27 flats varied from less than one year (two flats) to upto five years (three flats).

The Management to whom the matter was referred, in its reply (May 2005 and August 2005) stated that it was necessary to purchase the flats due to proposed expansion of activities, likely posting of additional manpower in JNP region and orders for vacation of flats allotted by JNP Trust to the CWC staff members. Further a number of builders came offering attractive flats at reasonable rates and banks liberalised housing loans resulting in decline in the demand of flats owned by the CWC. The BOD in principle approved the proposal to dispose of these flats. The Committee constituted to fix the reserve prices of these flats decided to put up the flats for sale only by the end of 2005 as price escalation was anticipated. The Ministry endorsed (September 2005) the views of the CWC.

The replies of the Ministry and Management are not tenable in view of the non-occupancy/low occupancy of the flats. The decision (December 2004) to dispose of these flats showed that the decision to procure them initially was not grounded on the needs as expressed. The Management's contention of increase in the value of the flats is not backed by any analysis and making profits on sale/purchase of property is not an activity of the CWC as per its Articles and Memorandum of Association.

Thus the non-occupancy of 55 flats showed that the purchase of flats was done on insufficient grounds and resulted in blocked of funds to the tune of Rs 6.07 crore.

7.1.2 Irregular payment of Productivity Linked Incentive of Rs.3.86 crore

Payment of Productivity Linked Incentive in contravention of DPE guidelines resulted in excess payment of Rs.3.86 crore during the last five years ended 31 March 2004.

Central Warehousing Corporation (CWC) Employees Productivity Linked Incentive Scheme was notified in September 1998 and brought into effect from April 1996. The Department of Public Enterprises (DPE) vide its OM dated 25 June 1999 provided that performance related payments to the employees should not exceed five *per cent* of the distributable profit in an enterprise. DPE further clarified (12 September 2000) that distributable profits represented the profit after tax after providing for transfer to Statutory Reserves.

It was noticed in Audit that during the period 1999-2000 to 2003-04 (except 2001-02) CWC paid Productivity Linked Incentive (PLI) of Rs.13.23 crore against the admissible amount of Rs.9.37 crore *i.e.* five *per cent* of distributable profits of Rs.187.36 crore. This resulted in excess payment of Rs.3.86 crore in contravention of the DPE directives.

The Management replied (June 2004 and June 2005) that five *per cent* norms prescribed by DPE's circular in June 1999 related to payment of perks and allowances exceeding 50 *per cent* of pay and was not applicable to CWC where such payment was 28 *per cent* only. This is not tenable as the payment of perks and allowances are additions to salary and are payable even if the enterprise runs into losses but the payment under PLI scheme is a performance related payment and cannot exceed five *per cent* of the distributable profits.

The Management further stated that the provisions of the Companies Act 1956 are not applicable to it, as it had been set up under Section 3 of the Warehousing Corporations Act, 1962. The contention of the Management is not tenable because DPE's instructions are applicable to all Central Public Sector Enterprises. Further Section 30 (2) of the Warehousing Corporations Act, 1962 provides that the Corporation may, out of net profits, declare a dividend after making all provisions for bad and doubtful debts, depreciation on assets and all other matters which are usually provided by companies under the Companies Act, 1956.

Thus, the irregular and excess payment of PLI amounting to Rs.3.86 crore to the employees was in contravention of DPE's instructions.

The matter was reported to the Ministry in May 2005; its reply is awaited (November 2005).

7.1.3 Irregular upgradation of posts

Irregular upgradation of posts by Central Warehousing Corporation under central dearness allowance pattern resulted in additional financial commitment of Rs.45.00 lakh.

The Department of Public Enterprises (DPE) directed (June 1990) the Public Sector Enterprises (PSE) to revise the scales of pay of officers and staff under central dearness allowance (CDA) and industrial dearness Allowance (IDA) scales of pay as per the recommendations of High Power Pay Committee set up by the Government of India (GOI). The GOI directed (August 1991) that no new posts be created on CDA pattern by any PSE on or after 1 January 1989 and upgradation of posts would be deemed as creation of posts.

The Board of Directors of Central Warehousing Corporation (CWC), in their meeting held in July 2001, approved the upgradation of employees who had completed 12 years of service in the same scale to the next higher grade/post as a one-time measure. Of the 2,406 posts which were upgraded, 99 posts were on CDA pattern and the rest were on IDA scales of pay. The upgradation of 99 posts resulted in creation of new posts under CDA scales in contravention of the DPE's directions. This irregular upgradation resulted in additional financial burden of Rs.45.00 lakh (approximately) from July 2001 to March 2005.

On being pointed out by Audit in February 2004, the Management replied (March 2004 and July 2005) that the Corporation had promoted only those employees to the next higher grade/scale who had completed 12 years of service as on 1 July 2001, as per guidelines of Assured Career Progression (ACP) Scheme. The Ministry while endorsing (December 2005) the views of the Management stated that the Board of Diecctors was competent for creation of any post below the level of Board as per amendments in February 1991 in CWC Regulations, 1986.

The reply of the Management/Ministry is not tenable as the ACP scheme was applicable only to Government employees and DPE had not issued any guidelines on the subject of application of ACP to PSE employees. Further, as per GOI directions no new post can be created on CDA pattern by any PSE on or after January 1989.

Thus irregular upgradation of posts under CDA pattern resulted in recurring additional financial burden every month with Rs.45.00 lakh (approximately) incurred upto March 2005.

Food Corporation of India

7.2.1 Loss of interest on excess payment of Hill Transport Subsidy

Non-compliance of instructions resulted in unauthorised reimbursement of Hill Transport Subsidy to the Government of Arunachal Pradesh resulting in loss of interest of Rs.20.34 crore.

The transportation charges of foodgrains incurred by the North Eastern States (NE States) for moving stocks from Food Corporation of India (FCI) Base Depots to the Public Distribution Centres (PDCs) approved by the Government of India (GOI) were to be reimbursed on actual basis to the State Governments as Hill Transport Subsidy (HTS). In terms of the Ministry of Food and Civil Supplies's instructions, the claims of the Governments for reimbursement were to be supported with the five points prescribed

certificate from the appropriate authority of the State Government receiving the foodgrains. The Ministry of Food (November 1995) further laid down that in the state of Arunachal Pradesh, reimbursement of HTS would be allowed even in such cases where the foodgrains were off-loaded at Distribution centers/ Fair Price Shops other than the PDCs or enroute to PDCs. The reimbursement of HTS upto the off-route distribution points/Fair Price Shops would not under any circumstances exceed the amount that would have become reimburseable, had the stocks been moved to the PDCs. The State Government while submitting their claims on fortnightly or on monthly basis, were required to give full details with supporting documents so that FCI could scrutinise and pass the same for payment in the shortest time possible.

FCI (May 1998) prescribed another three point mandatory certificate, for claims relating to Arunachal Pradesh, in addition to the five-point certificate to be given by the appropriate authority of the State Government, wherein the truck numbers transporting the stocks were to be mentioned against each HTS claim for reimbursement.

The additional three-point certificate led to a deadlock as the claims from the Government of Arunachal Pradesh (GoAP) were all received without the three-point certificate resulting in huge accumulation of bills.

The pendency of settlement of HTS bills by FCI was discussed in the meetings between FCI and GoAP from time to time during May 1999 to December 2001. The GoAP informed that foodgrain was being carried on head load in many centers and State Government was not paying advance to carrying contractors and as such they were not able to provide certain information as required by FCI.

It was observed in one such meeting (December 2001) that the figure of claims quoted by the State Government (Rs.5.87 crore) and FCI (Rs. three crore) showed wide variation. The State authorities were directed by the GOI to reconcile the differences with FCI and review pending claims for early settlement. It was also decided that as the funds received by the GoAP were not reflected in the budget, the GoAP should create a new budget head from 1 April 2002, so that all funds received by it under HTS would be deposited in this head of account. A sum of Rs. three crore was placed at the disposal of the GoAP to be deposited under this Budget Head as *ad-hoc* settlement against outstanding claims. The GoAP in February 2002 confirmed to the GOI that a new budget head had been opened.

As the HTS claims of the GoAP accumulated to Rs.34 crore as on 31 March 2002, GOI directed (June 2002) that FCI should pay an advance equivalent to this amount to the GoAP. Later, however, (August 2002) the FCI was ordered to place a Revolving Fund of Rs.10 crore at the disposal of the GoAP. As the position of settlement of the HTS claims of the GoAP was not satisfactory, the GOI decided (June 2003) to allow an advance in the form of an 'on account payment' of Rs.10 crore to the GoAP to be released by FCI on the claims submitted by the GoAP. On release of the 'on account payment' the GoAP was to settle its claims in a time-bound manner in a cycle of 15 days and forward further claims for the next round of 'on account payment'.

Examination in Audit showed that 'on account payments' totalling Rs.340.60 crore were released to the GoAP during the period July 2003 to March 2004 for HTS claims of the GoAP for the period April 2001 to November 2003 in contravention of the GOI

instructions of June 2003. Besides, 'on account payments' for reimbursement were released in excess of the amount admissible as per the limits laid down by the GOI instructions (November 1995) regarding restriction in reimbursement of HTS in case of off-route distribution points. In the three districts viz., Tezpur, North Lakhimpur and Dibrugarh it was observed in Audit that such excess amounted Rs.185.76 crore, resulting in blockage of funds till the bills are finally settled. This resulted in loss of interest of Rs.20.34 crore calculated on the basis of cash credit rates.

It was further observed in Audit that:

(i) Before release of the instalments of the 'on account payment' during the period July 2003 to March 2004, FCI did not insist on proof of deposit of the same in the Government account, leading to breakdown of internal control.

(ii) The instalments of 'on account payments' were released continuously by the FCI despite the utilisation certificates furnished by the GoAP not being complete and claims not submitted against the 'on account payment.' These certificates did not mention the date of deposit to the Government account or payment to contractor.

(iii) No details of payments made from this amount of Rs.340.60 crore were furnished by the GoAP to FCI.

(iv) An amount of Rs.80 crore of HTS received by the GoAP (in 2002-03) was routed through a Savings Account by the Director Civil Supplies, GoAP. The Crime Branch Arunachal Pradesh is currently investigating the transactions.

(v) FCI had no role in finalising the transportation rates. The rates were fixed arbitrarily by the GoAP and were subject to frequent revisions. The road transport rates, which were Rs.2.90 per quintal per km (September 2002) were increased to Rs.5.50 per quintal per km during April 2003. Similarly, head load charges of Rs.125 per quintal per km were increased to Rs.250 per quintal per km during April 2003. These rates were reduced back to Rs.2.90 per quintal per km and Rs.125 per quintal per km respectively from 1 September 2003. Also, for the same period, different rates were fixed in respect of different transport contractors operating in the same area.

The GOI had also reiterated (March 2005) that all advances beyond Rs.10 crore at any point of time were irregular and decided to undertake a special audit of all HTS bills settled in case of the GoAP relating to the period 2003-04 and beyond. The GOI had also instructed to adjust any excess payment against pending and future bills.

On the instructions of FCI Headquarters Regional office, Guwahati intimated FCI Headquarters that the excess paid to the GoAP was adjusted from the outstanding and future bills from March 2004 onwards. Even considering that the adjustments are fully accepted by the GoAP, FCI entailed an interest loss Rs.20.34 crore on the blockage of funds of Rs.185.76 crore due to excess release of HTS.

The matter was reported to the Management/Ministry in November 2005, their replies were awaited.

7.2.2 Failure to file claims

Failure to file complete claims for refund of input tax resulted in loss of interest of Rs.5.67 crore to the Corporation.

Under the Haryana Value Added Tax (HVAT) Rules 2003, any amount representing input tax relating to the goods which have been sold in the course of export out of the territory of India shall be refunded in full to the exporting dealer. A VAT dealer can lodge a provisional claim for refund of input tax quarterly by submitting the required documents. Accordingly, the input tax paid on wheat exported by FCI is refundable.
During the four quarters of 2003-04 the Regional Office Haryana (ROH) of Food Corporation of India (FCI) exported wheat valuing Rs.840.10 crore. A refund claim of Rs.13.79 crore for the period April to September 2003 in respect of three districts was submitted by ROH to the assessing authority in March 2004. It was returned (April 2004) by the assessing authority stating that the claim was incomplete and not in accordance with the provisions of Rules. In July/August 2004, ROH submitted final claim for the year 2003-04 for refund of Rs.59.74 crore. The assessing authority intimated (July/August 2004) that the application was incomplete as the original documents were not enclosed and claim could not be processed as the financial year was over and as such the refund could be determined only in yearly assessment. Due to incomplete submission of claims for refund, FCI could not avail the benefit of quarterly refund of input tax. Thus, FCI blocked its funds of Rs.59.74 crore and incurred a loss of interest of Rs.5.67 crore (upto March 2005) worked out at the rate at which cash credit was availed by the Corporation.

The Management stated (August 2005) that the export transactions carried out by it were deemed export sales under section 5(3) of the Central Sales Tax Act and the claims were regularly exhibited in the quarterly returns filed with the assessing authority. The quarterly provisional claims of input tax could not be filed, as the exporters who were allowed 45 days for submission of documents did not furnish the required documents.

The reply of the Management is not tenable as the HVAT was introduced with effect from 1 April 2003 and the claims for refund of input tax were made under this Act. The exhibition of claims in quarterly returns did not serve any purpose. FCI did not take steps to obtain the export documents from the exporters within 45 days and could not file the complete quarterly provisional claims.

Thus, incomplete submission of claims for refund of input tax resulted in a loss of interest of Rs.5.67 crore (upto March 2005) to the Corporation.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

7.2.3 Inadmissible driage allowance to millers

Wrong application of driage percentage resulted in benefit of Rs.5.45 crore to millers.

The Food Corporation of India (FCI), State Government of Haryana and its agencies procure paddy and get it milled from private millers. The resultant Custom Milled Rice (CMR) is delivered directly to the FCI godowns.

The final rates for CMR fixed by the Government of India (GOI) to be reimbursed to State Government and its agencies by FCI, include three components viz. Minimum Support Price (MSP), statutory charges and non-statutory charges and make up the cost of paddy. Driage is a component of non-statutory charges and was admissible at the rate of one *per cent* of MSP as per orders issued from time to time. The GOI also prescribed that for every quintal of paddy received, the millers were to return 67 kg of rice (64 on URS[♣] paddy during 2000-01) to FCI.

In contravention of the GOI orders, Haryana region of FCI and State Government of Haryana and its agencies allowed one *per cent* driage on the gross quantity of paddy issued to millers instead of one percent of MSP. FCI, thus, obtained 66.33 kg (63.36 kg for URS paddy during 2000-01) in place of 67 kg (64 kg for 2000-01) of CMR against every quintal of paddy supplied to millers. Based on the admissible driage of one *per cent* of MSP the difference worked out to Rs.1.53 to Rs.1.90 per quintal of CMR supplied to FCI during the years 2000-01 to 2003-04.

On receipt of 30.66 lakh MT of CMR in Haryana region of FCI (2.42 lakh MT through FCI and 28.24 lakh MT through agencies), the total undue and inadmissible benefit amounting to Rs. 0.43 crore and Rs.5.02 crore respectively, was extended to millers with corresponding loss to the Central and State exchequers respectively.

The Management (December 2005) accepted the Audit observations in respect of the paddy procured by FCI but in respect of paddy procured for milling by the State Government and its agencies no comments were given. It, however, stated that, if required, the GOI could confirm the position from the State Government. The Management further stated that it had decided to direct FCI Haryana region to recover the differential amount towards excess expenditure incurred by FCI due to non-regulation of driage allowance at one percent of MSP.

Thus, wrong application of GOI's orders resulted in inadmissible benefit of Rs.5.45 crore to millers.

The matter was reported to the Ministry in March 2005, its reply is awaited (November 2005).

7.2.4 Inadequate internal control and improper physical verification

Misappropriation of stock due to inadequate internal control system and failure to conduct proper physical verification resulted in loss of Rs.2.63 crore.

The Storage and Contract Manual of Food Corporation of India (FCI) stipulates that physical verification (PV) of stocks should be conducted annually and quarterly as per instructions of Stock Division of Headquarters (HQrs), 100 *per cent* weighment of

[♣] ***Under relaxed specifications***

baby/small stacks should be carried out and District Managers (DMs) should periodically inspect every depot. Zonal Managers (ZMs) and Senior Regional Managers (SRMs) are required as per existing instructions to inspect at least one depot and two depots respectively every month under their jurisdiction.

Food Storage Depot (FSD), Kokrajhar, one of the three depots under District Office Kokrajhar in Assam region has two hired godowns♣. SRM Assam, during inspection of the depot observed (February 2002) that there was huge shortage and discrepancy in the physical existence of the stock. Accordingly, he suggested to DM (Quality Control) and DM (Kokrajhar) to conduct 100 *per cent* PV of stock immediately.

Despite the serious observation and suggestion of 100 *per cent* PV by the SRM, only special PV was conducted by DM Bongaigaon (April 2003) after a lapse of 14 months. DM Bongaigaon also observed huge discrepancies and suggested 100 *per cent* PV.

The suggested 100 *per cent* PV of the stock was done in September 2003. Based on this, a shortage of 40,512 bags weighing 21,362.48 quintals was detected at this depot. The loss to FCI due to this shortage worked out to Rs.2.63 crore at the economic cost of Rs.1,230 per quintal.

The SRM referred (September 2003) the matter to FCI, HQrs and recommended entrusting the case to CBI. Three officials were placed under suspension and investigation was entrusted to a retired officer in December 2003. In his report (March 2004), it was indicated that quarterly and annual PVs, were reduced to a routine exercise and no endorsement to the effect that shortages were found in the stock was made in the ledger.

Zonal Management in its reply (February 2004) stated that there was a failure on the part of SRM in not endorsing a copy of his report to the Zonal office and Regional Vigilance Wing despite the seriousness of the matter and as such no action could be taken. The Corporate Management (May 2005) accepted the shortages and stated that the case was under investigation by CBI and further action, as deemed fit would be taken. The Ministry (May 2005) endorsed Management's view.

Thus, inadequate internal control system and failure to carry out proper physical verification led the Corporation to suffer a loss of Rs.2.63 crore.

7.2.5 Tender sale of 'D' category rice

Violation of tender terms resulted in non-recovery of Security Deposit of Rs.68.60 lakh and a loss of Rs.1.38 crore due to sale of rice below the floor price.

The Regional Office of Food Corporation of India (FCI) at Tamil Nadu (ROTN) floated a tender (September 2000) for disposal of 'D' category rice lying at different centres of the region. Nine tenderers participated and the centre-wise highest rate quoted (September 2000) ranged from Rs.10 per MT to Rs.4,545 per MT. The FCI Headquarters (HQs) fixed (October 2000) floor price of 'D' category rice at Rs.5,250 per MT for Tamil Nadu State

♣ *'Assam Industries' and 'Agriculture Refinancing and Development Corporation, Kokrajhar'*

and advised ROTN to obtain counter-offers from all tenderers who had quoted rates less than this. Only one tenderer M/s. Venkata Koli Setty Commercial Corporation (VKSCC), who had earlier quoted a rate of Rs.522 per MT, agreed on the rate of Rs.5,250.60 per MT for the entire quantity of 'D' category rice. This was accepted (November 2000) by the ROTN for the available quantity of 14,518 MT. The tenderer was directed to remit the security deposit (SD) of Rs.76.22 lakh i.e. 10 *per cent* of the total cost as per the tender terms.

VKSCC did not remit the SD but pleaded for reduction of the SD from 10 to one *per cent*. In violation to the tender terms and with the approval of Zonal Manager, South Zone, ROTN agreed to the request to reduce the SD to one *per cent*. VKSCC remitted the reduced SD of Rs.7.62 lakh (February 2001) but failed to remit the cost of stock of Rs.7.62 crore within the validity period (April 2001). Instead, VKSCC requested to issue the stock at its initial quoted rate of Rs. 522 per MT. The FCI, however, forfeited the SD (May 2001) and sold the available quantity of 14,518 MT through re-tender (January 2002) at the risk and cost of VKSCC for Rs.6.17 crore (average rate Rs.4,247 per MT). FCI, thus, suffered a loss of Rs.1.38 crore due to sale of stock at a price below the floor price. The FCI HQs decided (November 2003) not to file a money suit for recovery of the amount as enquiries made to ascertain the whereabouts and solvency of VKSCC revealed that they were not in business for quite a long time and had no property.

The Management in its reply (September 2005) stated that non-receipt of response to tender enquiries, prolonged storage and need for augmenting storage space to cater to preservation of bumper procurement were the reasons that forced the administrative decision to offer an incentive by way of agreeing to the request of the tenderer for reduction of the SD from 10 to one *per cent*.

The reply of the Management is not tenable as the decision to reduce the SD was in violation of the tender terms. It had resulted in non-recovery of an amount of Rs.68.60 lakh (nine *per cent* SD), which could have been forfeited for non-performance of contract by VKSCC.

Thus, the violation of tender terms resulted in non-recovery of Rs.68.60 lakh and a loss of Rs.1.38 crore due to sale of rice below the floor price.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

7.2.6 Non-recovery of rentals from Delhi State Civil Supplies Corporation Limited

Non-realisation of rent of Rs.70.85 lakh and loss of interest of Rs.66.63 lakh for the space occupied by the Delhi State Civil Supplies Corporation Limited.

Delhi State Civil Supplies Corporation Limited (DSCSC) had occupied an area of 3,357 square feet in six Food Storage Depots (FSDs) of FCI since July 1984. However, no agreement was entered into between DSCSC and FCI for the rent, water and electricity charges. In 1993, for the first time, FCI assessed details of arrears of rent for the space occupied at its three FSDs, (Ghevera, Narela and Shaktinagar) and in December 2003 raised a bill for Rs.28.82 lakh.

After Audit pointed out in August 2004 the Regional Office, FCI, Delhi raised a consolidated bill for Rs.68.54 lakh (October 2004) for the period from July 1984 to July 2004 on DSCSC for utilisation of the total space in all the six FSDs. The matter regarding rent recovery was pursued with DSCSC, who agreed to pay for electricity and water charges on proportionate basis as per the area occupied by it and requested for waiver of the rent. This was not acceptable to FCI and it directed its field offices to raise the pending rent claims including the electricity and water charges. No payment was, however, received till March 2005. This resulted in short recovery of rent amounting to Rs.70.85 lakh besides loss of interest of Rs.66.63 lakh* (approximately) till March 2005.

The Management stated (August 2004) that there was no financial loss since this facility was extended to the State Government (Delhi Government) for close liaison with FCI for smooth operation of Public Distribution System work. The Management further stated (August 2005) that DSCSC had started paying rent against the current demand for the space in occupation (1,297 square feet) with effect from April 2005. The Ministry endorsed (November 2005) the views of the Management.

The reply of the Management/Ministry that there was no financial loss, thus, goes against facts as DSCSC agreed to pay the rent with effect from April 2005.

Thus, the sum of Rs.70.85 lakh towards rent, rates and taxes upto March 2005 was yet to be recovered from DSCSC. In addition FCI had already incurred a loss of interest of Rs.66.63 lakh.

7.2.7 Avoidable loss due to improper storage

Improper storage of wheat in bins in silo resulted in loss of Rs.1.17 crore due to damage and storage loss.

The Quality Control Manual (QCM) of FCI recognises that wheat can be held in bulk storage in bins without affecting quality for over 40 years and has laid down in detail, the operational requirements to be complied with to retain the quality. The QCM lays down that regular inspection of the stocks are to be carried out by the technical personnel with regard to moisture content, heat development, relative humidity and insect infestation.

In the District Office, Mayapuri of FCI, 18,520 MT of 'A' category wheat, pertaining to crop years 1998-99 and 1999-00, was stored in bins of the silo system during the period from January 1998 to March 2000. The wheat stock was liquidated through Public distribution system/Open sale and after complete evacuation of the silos (November 2003), 597.50 MT and 1,155.50 MT of the above stock was declared as storage loss and damaged stock respectively.

Examination of records in Audit revealed that the storage loss occurred as the empty bins were not cleaned before filling in the new grain during January 1998 to March 2000 and some of the stock of grain had moisture content beyond the permissible limit of 13 *per cent* when fed initially into the silo. No hygrometers and in-built thermocouples were fitted in the silo bins to check the heat and humidity level in the silos. The stock got

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* ***Interest calculated at the rate of 9.10 per cent (approximately)***

infected due to high moisture content, heat development and relative humidity resulting in damage and storage loss.

The Regional Management in its reply (April 2005) was silent about the damaged stock and stated that the storage loss was on account of silo dust, loss of moisture and prolonged storage of five years. It further stated that due to non-availability of required equipment, QC officials could not know the damage and it was only known at the time of evacuation of silos. In reply FCI Headquarters (October 2005) however, denied the fact that the loss was because of non-installation of in-built thermocouples in the silo bins and stated that it was due to negligence and human failure for which action had been taken against erring staff. The reply of Management is not tenable as wheat stock can be held in bins without affecting its quality for over 40 years provided proper aeration, temperature and humidity are maintained. The Regional Management had admitted that quality control devices were not fitted in the bins and thus, the fortnightly and monthly inspection of the stocks with regard to moisture content, heat development, relative humidity and insect infestation were not carried out.

The loss of 1753 MT was finally written-off in March 2004. This write-off of stock because of laxity in implementation of quality control standards resulted in loss of Rs.1.17 crore to FCI.

The matter was reported to the Ministry in June 2005, its reply is awaited (November 2005).

7.2.8 Locking up of funds toward bank guarantee

Excess margin money was kept in term deposit towards bank guarantee resulting in loss of interest of Rs. 81.90 lakh.

Food Corporation of India (FCI) has been availing the facility of Firm Credit Notes (FCNs) from Railways for payment of railway freight by furnishing a bank guarantee (BG) to the Railways for 15 days' freight based on transactions of previous 12 months. The FCI is required to deposit an amount equivalent to BG value as "term deposit" with the bank towards margin money for obtaining BG. As the FCI is availing cash credit facility from the banks for its working capital and other purposes, the differential interest between the cash credit availed and term deposit rate is an additional cash outflow to the FCI.

The Northern Railway (January 2000) allowed the FCI to furnish BG equivalent to seven days average freight of peak month's transactions instead of 15 days, subject to fulfillment of certain conditions. Subsequently, the Railway Board extended (July 2003) this facility to all organisations across all railways upto 30 June 2004 (since extended till further advice from Railway Board). However, FCI Headquarter communicated this relaxation to its Zonal Offices only in March 2004. As the communication to the field units by FCI Headquarters was issued after a gap of seven months, FCI South Zone could not avail the benefit and continued to obtain BG based on the old formula during the period July 2003 to March 2004. This resulted in loss of interest of Rs.72.57 lakh on excess margin money kept in term deposit for BGs during the period July 2003 to

February 2005 and Rs.9.33 lakh on the unexpired period of all term deposits towards BGs as on February 2005.

The Management/Ministry stated (June/July 2005) that the issue was actively being pursued by them with the Railway Board whereby no BG would be required to be deposited by FCI. The Railway Board, however, did not agree (February/March 2004) to the Ministry's proposal. They added that FCI South Zone could not implement the scheme, as the Southern Railway did not agree to extend the same, pending verification of some facts.

The reply is not acceptable, as despite instructions of July 2003, FCI could not avail the facility till March 2004, as it did not convey the instructions to its zonal offices in time. Further, FCI South Zone had informed in April 2004 that the facility could not be availed because of delayed communication from the headquarters.

Thus, delay in implementation of the Railway Board's instructions resulted in avoidable loss of interest of Rs.81.90 lakh on locking up of funds.

7.2.9 Avoidable subsidy on the disposal of barley at lower cut off rate

Barley was disposed of at a lower cut off price fixed without considering market rates resulting in avoidable subsidy of Rs.67.66 lakh in Rajasthan Region.

The Government of India (GOI) directed (June 2001) the Food Corporation of India (FCI) to auction the barley procured by the Government of Rajasthan and its agencies in the rabi marketing season 2001-2002. Accordingly, Regional Office (RO), Jaipur invited (October 2001) open tender for sale of 60944 MT of barley. Forty-eight offers were received in response at rates ranging from Rs.241 per quintal to Rs.460 per quintal.

Based on the offers received, the inter-ministerial High Level Committee (HLC), which was authorised to fix the rates for disposal of stock, decided (November 2001) to accept the rates quoted at Rs.351 and above per quintal for each lot/stack. A quantity of 48,946 MT was sold at the rate of Rs.351 and above per quintal. However, for the balance quantity 11,998 MT, with quoted rate less than Rs.351 per quintal, HLC directed that a counter offer may be made to all tenderers to accept the barley at cut off rates of Rs.351 per quintal. The Regional Office, Jaipur informed (December 2001) that as the demand of barley was high, the balance quantity might be sold at competitive rates obtained through limited tender invited only from the existing parties rather than at the cut off rate of Rs.351 per quintal. FCI Headquarters neither considered this aspect nor referred the matter to HLC but informed RO Jaipur (December 2001) to sell the balance quantity at Rs.351 per quintal only. Accordingly the remaining quantity was disposed of at the rate of Rs.351 per quintal.

It was observed in Audit, that while fixing the cut off rate the prevailing rates and the market trend had not been properly analysed. Audit observed that the market rate of barley was Rs.380 per quintal at the time of finalisation of tender. FCI had also received higher rates (between Rs.380 per quintal to Rs.455 per quintal) for more than 58 *per cent* (35,577 MT) of the total quantity offered for sale. Based on the market rate above, even without taking into account the cost of procurement, as well as the higher rate obtained

for more than 58 *per cent* of the quantity, the minimum rate of Rs.380 per quintal should have been fixed, thereby reducing the additional subsidy burden to the extent of Rs.67.66 lakh on the sale of 25,367 MT of barley.

In reply, the Ministry and Management stated (June 2005) that HLC had decided to accept the rate of Rs.351 per quintal and above considering the various locations from where barley was procured and the prices prevalent in the various markets of Rajasthan. They further added that re-tendering was not advisable because of the short shelf-life of coarse grain.

The replies of the Ministry and Management are not tenable in view of the fact that the market price was higher than the cut off price of Rs.351 per quintal and even the rates offered by some parties (for more than 58 *per cent* quantity) were higher than the market price. Keeping in view the market trend, the cut-off price should have been fixed at a more realistic level. Further the FCI plea that re-tendering was not advisable because of short shelf-life of coarse grain doesn't hold good as FCI had disposed of another 400 MT of storage gain of barley, observed after disposal of 60944 MT of barley, at prices ranging from Rs.615 to 787 per quintal in August 2002, *i.e.* after one and a half years of its procurement.

Thus, by fixing a lower cut off rate without consideration of market trend of barley, the FCI caused an additional subsidy burden to the GOI to the tune of Rs.67.66 lakh in the disposal of barley.

CHAPTER VIII: MINISTRY OF DEFENCE

Bharat Earth Movers Limited

8.1.1 Avoidable payment of liquidated damages

The Company incurred liquidated damages of Rs.1.19 crore due to avoidable delay in supply of Rope Shovels to Coal India Limited beyond the scheduled delivery period of April 2003.

Bharat Earth Movers Limited (Company) received (August 2002) a purchase order from M/s. Coal India Limited (Customer) for supply of six Rope Shovels[♠] valued at Rs.88.30 crore, of which two were to be supplied by October 2002 and the balance four by March/ April 2003. As per the terms of the contract, any delay in supply attracted liquidated damages (LD) equivalent to a sum not less than 0.5 *per cent* of the price of Rope Shovels not supplied for each week limited to five *per cent*. The Company supplied four Rope Shovels before 31 March 2003. The fifth and sixth Rope Shovels were dispatched on 31 May 2003 and 19 July 2003, i.e. after delays of 31 and 79 days respectively. On the request (April 2003) of the Company, the Customer extended (May 2003) the delivery of the fifth and sixth Rope Shovels upto June 2003, subject to their right for imposition of LD. The request of the Company for extension of delivery schedule without LD was not accepted (May 2003) and an amount of Rs.1.19 crore was deducted by the Customer towards LD.

The Management/Ministry attributed (November 2005) the following reasons for the delay in supply:

(i) delay in providing Project Concessional Duty (PCD) documents by two months by the Customer and consequent delay in import of components,

(ii) possible blow holes latent[♣] in castings procured but detected during machining requiring a lead time of four to five months,

(iii) delayed placement of order by the Customer for the Rope Shovels by 10 months.

The reply of the Management/Ministry is not acceptable on the following grounds:

(i) One of the delayed Rope Shovels was to be supplied under Normal Customs Duty[♦] which should not have been delayed due to delay in providing documents under PCD. PCD documents were provided to the Company on 20 December

[♠] *Three Rope Shovels were to be supplied under Normal Customs Duty and three under Project Concessional Duty.*

[♣] *Possible blow holes latent means that the raw castings contain inherent holes which are not visible during visual inspection but become noticeable when the castings are machined further.*

[♦] *The import of components under Normal Customs Duty implies the import of goods by paying applicable customs duty at normal rate.*

2002 and two Rope Shovels out of three to be supplied by the Company under PCD were also supplied within the original scheduled date of March/April 2003.

(ii) Placing orders in November 2002 for castings for use in Shovels scheduled for delivery in March/April 2003 was injudicious as the expected lead time for manufacture of Rope Shovels was four to five months from the date of receipt of defect free castings.

(iii) The delivery schedule indicated by the Customer was accepted by the Company.

Thus, due to delay in production and supply of Rope Shovels the Company incurred LD of Rs.1.19 crore.

Bharat Electronics Limited

8.2.1 Avoidable payment of interest due to short payment of advance income tax

Incorrect estimation of income and consequential short payment of advance income tax during 2000-01 to 2003-04 by the Company resulted in avoidable expenditure of differential interest of Rs.3.05 crore.

In terms of Section 234 (B)(1) of the Income Tax Act, 1961 an assessee who fails to pay advance tax or the advance tax paid is less than 90 *per cent* of the assessed tax, shall be liable to pay simple interest at one *per cent* per month for every month or part thereof on the amount by which the advance income tax paid falls short of the assessed tax. Section 234 (C)(1) of the Income Tax Act, 1961 also provides for payment of interest by the assessee at one *per cent* per month on the amount of short paid instalments of advance tax for three months.

Bharat Electronics Limited (Company) had paid interest of Rs.1.23 crore under Section 234 (B)(1) and Rs.2.87 crore under Section 234 (C)(1) of Income Tax Act 1961 due to incorrect estimation of income for the financial years 1997-98 to 1999-00. This was reported in para 8.2.1 of the Report of the Comptroller and Auditor General of India No.3 (Commercial) of 2002. The Ministry in their Action Taken Note stated (September 2002) that the Company was making efforts to bridge the gap between the advance tax payable and advance tax paid and was taking expert advice from consultants on various related matters to derive maximum benefit.

A review of records relating to assessment of income tax, however, revealed that despite taking the advice of experts on issues relating to tax twice in 1999-2000 and once each in 2000-01 and 2001-02, the Company paid less advance income tax during the financial years 2000-01 to 2003-04 due to incorrect estimation of income and paid interest of Rs.1.12 crore under Section 234 (B)(1) and Rs.4.35 crore under Section 234 (C)(1) of Income Tax Act, 1961.

The Management/Ministry stated (August 2005) that incorrect estimation of income and consequent short payment of advance tax was due to the following reasons:

(i) Many of the orders considered as executable at the beginning of each of the years under consideration could not be executed and the shortfall was met out of the orders to be obtained during the course of the year.

(ii) Material consumption varied widely from around 40 *per cent* to 85 *per cent* depending on the product mix.

(iii) The profits of the Company were reviewed every quarter at the time of payment of advance tax based on actual sales upto the quarter and the profit turned out to be higher than the estimated profit mainly due to the healthy growth of the Company.

The reply of the Management/ Ministry is not tenable due to the following reasons:

(i) Having executed the orders during the year which were not planned at the beginning of the year, the Company could estimate the profit on the changed product mix with reasonable accuracy.

(ii) The variation of 40 *per cent* to 85 *per cent* in material consumption as stated by the Company related to certain products executed by the Company. However, overall actual consumption of material was around 50 *per cent* to 60 *per cent* only during the period.

(iii) Even though the profits were reviewed periodically as stated by the Company, the Company was not able to assess the profits with reasonable accuracy as the estimates of profits furnished by the units were based mostly on original and revised budgets but not on subsequent changes in the product mix. Moreover, the increase in profit due to healthy growth was not an unforeseen phenomenon but was gradual and as such should have been taken into account while estimating the profits.

Thus, the Company could not bridge the gap between the advance tax payable and advance tax paid and had incurred avoidable expenditure of Rs.3.05[♦] crore, being the differential interest during the years 2000-01 to 2003-04.

Garden Reach Shipbuilders & Engineers Limited

8.3.1 Loss due to inordinate delay in ship repairing

Due to inordinate delay in indenting, coordinating and executing and failure to monitor the job, the Company suffered an avoidable loss of Rs.2.61 crore.

Garden Reach Shipbuilders & Engineers Limited (Company) received (March 2000) a work order for medium refit of a Coast Guard Ship at a total price of Rs.12.02 crore. The work order stipulated submission of a PERT[♣] Chart prior to commencement of the work. The work had to be completed within 240 days and in case of delay beyond 15 days of

[♦] ***Interest paid Rs.5.47 crore and interest saved Rs.2.42 crore***

[♣] ***Programme Evaluation and Review Technique***

quoted time, liquidated damages (LD) at the rate of half *per cent* was to be levied for every week's delay subject to maximum of five *per cent* cost of refit. The Company submitted a Bar Chart, scheduling major activities, in September 2000 after a delay of four months from the date of start of refit work. The Chart indicated that the refit work would be completed by January 2001 and sea trial would be conducted in February 2001.

It was observed that though the refit work started (May 2000), due to non-availability of the PERT Chart, difficulties were experienced in monitoring progress and pursuing critical activities resulting in slow progress of work. The progress of plating work for hull which was to be completed by December 2000, was poor as the Company could not start 70 *per cent* of the jobs till September 2000 thereby delaying the related works like insulation, paneling, cabling etc. The Company also delayed the submission of the final spares indent for imported items, which were critical for shafting work. It placed the order in November 2000 for Gear Box spares and opened letter of credit (LC) under the contract, which was just two months ahead of the scheduled completion date of the work even though it was known that a lead time of four months was required for delivery after opening the LC. Finally, the refit work was completed in January 2002 after a delay of one year. Though the Company received (during 2004-05) Rs.84.00 lakh additional sanction for extra expenditure incurred on refit work, the cost incurred for this work was Rs.14.79 crore out of which the Management could recover only Rs.12.18 ♥crore (March 2005) resulting in a loss of Rs.2.61♠crore after deduction of LD of Rs.45.00 lakh on the entire job.

The Ministry/Management attributed (August 2005/May 2005) the delay in completion of the job *inter alia* to delay in assessment of quantum of work, non-availability of spares and to the nature of the job. While accepting the loss Management further stated (November 2005) that such work execution gave the Company the opportunity to assess its capabilities and improve and this perhaps helped them to earn profit in a later repair work. The reply of Management clearly indicates that the Company had failed to assess the magnitude of the job and could not efficiently coordinate the various components of the job even though they were engaged in shipbuilding/repairing jobs from the outset. The Coast Guard was not convinced that the delays were beyond the Company's control and therefore imposed liquidated damages.

Thus, due to inordinate delay in indenting, coordinating and executing and failure to monitor the job as per the work plan, the Company had to suffer an avoidable loss of Rs.2.61 crore.

Hindustan Aeronautics Limited

8.4.1 Short billing of material cost to the customer

Failure of the internal audit/ internal control system in the Company to detect short billing of material resulted in loss to the extent of Rs.64.62 lakh.

♥ *(Sales value: Rs.12.02 crore and Rs.0.84 crore) minus (LD: Rs.0.45 crore plus non supply of spares Rs.0.23 crore)*

♠ *Cost Rs.14.79 crore minus amount recovered Rs.12.18 crore*

The Overhaul Division of Hindustan Aeronautics Limited (Company) undertakes major servicing of Kiran Mark – I aircraft. The pricing is based on Indian Air Force (IAF) approved pricing system. The material required for major servicing is issued from customer's stores (HAL-held IAF stores) free of cost. It was further agreed between the Company and the IAF that if materials were to be drawn from the Company's stores, the same would be charged on 'actual cost plus profit basis'.

On a review of invoices raised by the Division for materials used from the Company's stores during the years 2002-03 and 2003-04 and their booking in the cost ledger, Audit observed that in 15 out of 44 cases, the claim preferred by the Division towards material cost and profit margin thereon was less by Rs.64.62 lakh. The internal audit of the Company failed to point out this short billing.

On being pointed out in Audit (April 2005), the Management while conceding the short billing, stated (June 2005) that the supplementary claims had been lodged (June 2005) with the Deputy Controller of Defence Accounts and the same would be followed up for early settlement. The Ministry also concurred (August 2005) with the views of the Management.

However, the Deputy Controller of Defence Accounts did not admit (November 2005) the claims stating that invoices towards final payment were already paid and there was no provision existing towards supplementary bills.

Thus, failure of the internal audit/ internal control system in the Company to detect short billing of material resulted in loss to the extent of Rs.64.62 lakh.

Vignyan Industries Limited

8.5.1 Avoidable loss due to excess rejection of steel castings

The Company incurred an avoidable loss of Rs.1.42 crore due to abnormal rejections of steel castings.

Vignyan Industries Limited (Company), a subsidiary of M/s. Bharat Earth Movers Limited is engaged in the manufacture and supply of steel castings to its holding Company and to other customers like Integral Coach Factory (ICF), HMT etc. The main raw material used in the manufacture of castings is iron and steel scrap. Scrap is melted in furnaces and the liquid metal obtained is poured into moulds to get castings of required specifications. After the required cooling period, castings are removed from the moulds by a process called 'shake-out', after which the finished castings are dispatched to customers.

The steel castings manufactured were rejected internally as well as by customers due to manufacturing defects like dimensional deviations, cracks, hot tears etc. The rejections of steel castings ranged between 5.89 *per cent* and 9.64 *per cent* during 2001-02 to 2004-05 (major portion of which was due to rejections by the customers) which was significantly more than the industry norm of four *per cent*.

The Management/Ministry stated (October 2005) that (i) rejections could be avoided by procuring quality control equipment at an estimated cost of Rs.25 lakh, however, due to financial constraints the investment could not be made and (ii) corrective action was taken to bring down rejections in the form of process improvements.

The reply of the Management/ Ministry shows lack of financial prudence as by making an investment of Rs.25 lakh the Company could potentially save Rs.35 lakh (approximately) annually. Even the corrective measures stated to have been taken could not bring down the percentage of the customer end rejection to the level of industry norm.

Thus, the Company lost Rs.1.42 crore towards rejections during the last four year period ending 2004-05 due to its failure to procure quality control equipment.

CHAPTER IX: MINISTRY OF DEVELOPMENT OF NORTH EASTERN REGION

North Eastern Development Finance Corporation Limited

9.1.1 Injudicious investment in call center Project

The Corporation financed a project for setting up a call center at the time of recession in IT industry, without any detailed investigation of the promoters' past record and technical feasibility of the project. As a result the finance of Rs.9.07 crore in DECL became wasteful. Further, the Corporation could not recover the interest on the above loan and other charges amounting to Rs. 5.23 crore.

North Eastern Development Finance Corporation Limited (Corporation) invested (April 2001) Rs.66.00 lakh as equity capital♣ and extended financial assistance of Rs.7.34 crore as loan (term loan -Rs.6.60 crore and bridge loan -Rs.0.74 crore) at an interest rate of 15 *per cent* per annum to M/s. DSS e Contact Limited (DECL), a newly incorporated (January 2001) Company, to set up an International call center of 200 desks. The loan disbursement was made between August 2001 and July 2002 against hypothecation of plant and machinery, equipment etc., and collateral security of escrow on receivable and corporate guarantee of the promoters. An additional term loan of Rs.1.07 crore was also disbursed (July 2002) to meet the additional cost of taking redundant connectivity. Further, the Corporation sub-leased (June 2001 and June 2002) a major part (17,330 square feet) of its property 'IT Park' on a monthly rent of Rs.25 per square feet per month to DECL to set up the call center.

The trial operation of the call center was started in August 2002 with 65 desks but due to poor connectivity and lack of business mobilisation, the operation came to a halt in January 2003. Consequently DECL failed to honour the commitment to repay the instalments due on bridge loan and term loan (including additional term loan) due from April 2003 and October 2003 respectively. The Corporation also could not recover the lease rentals of Rs.73.33 lakh (January 2004) and electricity charges of Rs.11.35 lakh (December 2003).

As DECL continued to default in payment of dues, the Corporation recalled (February 2004) the outstanding amounts of Rs.10.84 crore including interest due of Rs.2.43 crore (January 2004) and filed (March 2004)) a recovery proceeding with Debt Recovery Tribunal, Guwahati for recovery of the dues. The Corporation also took possession of the first and third floors of the IT Park alongwith miscellaneous assets of DECL. The possibility of recovery of dues was remote as the hypothecated assets were customs bonded and there was no equitable mortgage of immovable properties in favour of the Corporation.

♣ *6,60,000 Equity Shares of Rs.10 each valuing Rs.66 lakh*

Audit observed the following major weaknesses/deficiencies while sanctioning and disbursing the loan: (i) DECL was promoted by DSS Mobile Communication Limited, New Delhi (DSSMCL) whose net-worth had eroded and which had no experience in International call center business. Further, loan was sanctioned without investigating the credibility of the directors, two of whom were in defaulters' list of Reserve Bank of India since September 2000. (ii) The Corporation was aware of the recession/slowdown in IT industry especially in the USA at the time of sanction/disbursement of loan but went ahead with the Project. (iii) The Corporation relaxed the disbursement conditions regarding obtaining the banker's opinion about credit worthiness of the promoter. (iv) The Corporation entered into the project without enquiring into essential details of connectivity / link available to set up call center Project. (v) International Private Leased link circuits (IPLC) through optical fibre connection (OFC) was taken for the project due to cost consideration and without ensuring an alternate route.

The Management stated (May 2005) that the promoter (DSSMCL) was the largest paging service provider and was on the path of revival at the time of approval of the project. It also stated that the Corporation wanted to leverage its experience in international call center business, which had started booming at that time. The Ministry endorsed (October 2005) the Management's views.

The contentions of the Management are not acceptable as the Corporation evaluated the promoter on the basis of estimated /provisional data for future instead of authenticated historical data and also ignored the fact of disassociation of the only profitable Group Company from the project before approval of loans. The Management's contention regarding boom in IT industry during project appraisal is also not tenable as the issue of recession in the USA was highlighted by the Corporation itself during appraisal (January/April 2001) of the project. Besides, the Corporation did not make any provision for redundant connectively even though it is a general practice in call center business to have a redundant connection for smooth operation of the business. Further, instead of going for a satellite-based link, they opted for an IPLC link on cost considerations, which was unreliable.

Thus, the decision to venture into a new project during recession with a new Corporation, which was promoted by an inexperienced company whose net-worth had eroded and without a detailed investigation about the promoter's past record and technical feasibility of the project, was injudicious. Consequently, the finance of Rs.9.07 crore[♣] of the Corporation to DELC became unproductive and was in jeopardy with remote possibility of recovery of dues. The Corporation could not also recover the interest on the above loan and other charges amounting to Rs.5.23 crore[♦] (March 2005).

[♣] ***Rs.7.34 crore loan plus Rs.66 lakh equity plus Rs.1.07 crore additional loan***

[♦] ***Rs.4.01 crore interest upto 31 March 2005 plus Rs.1.22 crore lease rent (including interest on lease rentals)***

CHAPTER X: DEPARTMENT OF FERTILIZERS

Brahmaputra Valley Fertiliser Corporation Limited

10.1.1 Unfruitful investment of Rs.38.83 crore in ammonia plant

Even after revamping of the ammonia plant at a cost of Rs.38.83 crore, production cost of ammonia was high due to old design of the plant, selective revamping and very high-energy consumption. As a result, the plant was shut down from September 2002 after running for four months, being uneconomical and the fate of the plant remained undecided thereafter.

Based on a rehabilitation scheme formulated by ICICI Limited, the Operating Agency appointed by Bureau of Industrial and Financial Reconstruction (BIFR) for unit wise rehabilitation of Hindustan Fertiliser Corporation Limited (reconstituted as Brahmaputra Valley Fertilizer Corporation Limited with effect from April 2002), a proposal for rehabilitation of Namrup unit plants was approved by the Government in October 1997 at a total cost of Rs.350 crore, revised to Rs.509.40 crore by the Government in September 2001. The rehabilitation scheme, *inter alia,* included Rs.42.27 crore for revamping of Namrup-I plant for production of ammonia. According to the approved Detailed Project Report, Namrup-I plant, having revamped capacity of 132 MT of ammonia per day, was to supply 87 MT of ammonia per day to Namrup-III plant and the balance to Namrup-II plant for conversion to urea.

The work for rehabilitation of Namrup-I plant started in November 1998 with completion schedule of 30 months, subsequently revised to 39 months. After partial completion at a cost of Rs.38.83 crore, the production of ammonia started by the end of May 2002. However, the plant was shut down midway by the middle of September 2002 for further revamping works. During May to September 2002, the plant produced a meagre quantity of 1,402 MT ammonia against 16,236 MT expected to be produced as per the rated capacity. The Management observed (September 2003) that operation of the plant was not economical due to high-energy consumption and high cost of production. Uneconomical operation of the plant was attributed to the following factors:

(i) Design of Namrup-I Plant was of 1960s origin where energy consumption was high.

(ii) The plant operating pressure was high and required high manpower deployment for operation as well as for maintenance.

(iii) The revamp of the plant was done selectively which resulted in high maintenance cost.

(iv) Actual energy consumption was much higher than what was envisaged in the rehabilitation scheme.

Further, in the rehabilitation scheme, economy in specific energy consumption was mistakenly projected from the pre-revamping level of 19.5 GCAL[♥] per MT of ammonia to 15.96 GCAL per MT of ammonia instead of to 19.42 GCAL per MT of ammonia. In fact, actual specific energy consumption in 2002-03 was much higher at 69.57 GCAL per MT of ammonia produced. Thus, decision of investment in Ammonia Plant-I was not based on sound grounds *ab initio.*

In the mean time, a new pricing policy was adopted by the Government of India effective from April 2003 which *inter alia* required fixation of retention price of urea for a group of plants instead of an individual plant. The Management, after closure of the plant in September 2003, opined that substantial reduction in cost of production at downstream urea plants was possible by not utilising ammonia from this plant. This coupled with other foreseeable contributing factors viz. risks arising out of 1960s vintage design of the plant, selective replacement of the parts, high energy consumption etc. led (September 2003) to discontinuance of the operation of the plant, which was proposed to be converted to manufacture of methanol. This proposal was also found techno-economically unviable, thus, rendering investment of Rs.38.83 crore unfruitful.

The Management stated (May 2005) that a high power Technical Committee was constituted for detailed study of revamping of the plant and also to assess viability in respect of balance erection/commissioning and operating the plant in the overall perspective.

The Ministry, while accepting the facts and figures, stated (November 2005) that the high power Technical Committee identified various factors *e.g.* incompleteness of FEDO[♣]/ICICI Report, slackness of the Management, limitation of the availability of natural gas, high cost of purchased power etc. which contributed towards the unviability of the plant.

Thus, in spite of foreseeable and perceptible uneconomic factors, the unviable revamping scheme of the plant was carried through, resulting in unfruitful investment of Rs.38.83 crore.

The Fertilisers And Chemicals Travancore Limited

10.2.1 Avoidable expenditure

Despite having firm commitment from indigenous supplier, the Company procured 30,150 MT phosphoric acid through imports at higher rates resulting in avoidable expenditure of Rs.4.34 crore.

The Fertilizers And Chemicals Travancore Limited (Company) manufactures complex fertilizers and phosphoric acid (acid) is one of the key inputs. The Company has two plants to produce acid for captive use. However, due to low productivity of the aging captive plants, the Company used to outsource the acid from domestic market as well as

[♥] *Gega calorie i.e.10^6 Kilo calorie*

[♣] *Fact Engineering and Design Organisation*

through imports. Fertilizer Association of India (FAI) centrally arranged import of acid based on the indent of purchasing companies.

The Company planned (March 2002) to meet the entire shortfall in captive production of acid during 2002-03 through purchases from its indigenous supplier. In the annual forecast for that year procurement of 'nil' quantity of imported acid was projected. The Company even obtained a firm commitment (January/February 2002) from Sterlite Industries (India) Limited, Tuticorn (SIIL) to supply to it a minimum of 72,000 MT (+/- 10 *per cent)* acid during the year 2002-03. However, the Company simultaneously intimated its requirement of 25,000 MT to FAI in January 2002, which subsequently necessitated corresponding reduction in procurement from SIIL. Finally, a purchase order for procurement of 49,500 MT was placed on SIIL in May 2002. The Company through FAI also imported 30,150 MT acid at an average landed cost of Rs.17,349 per MT and procured the left over quantity of 49,504 MT from SIIL at the much cheaper rate of Rs.15,909 per MT. The procurement of acid through imports was, thus, costlier and also avoidable.

The Ministry stated (November 2005) that import of acid offered more flexibility than contracting with SIIL for indigenous acid as schedule of shipments for imported acid could be given from time to time based on actual requirement.

The reply is not tenable as the delivery of acid from indigenous supplier could have been scheduled as per the Company's requirement, particularly when the Company had already procured substantial quantity during the previous year from the same supplier. The indigenous supplier had given a firm commitment for meeting the entire supply even before the Company approached FAI. Even then, the Company did not plan the procurement from the indigenous supplier available at a lower price.

Thus, unjustified deviation from the original procurement plan despite having firm commitment from indigenous supplier caused avoidable expenditure of Rs.4.34 crore[♣] on imports of phosphoric acid at higher cost.

10.2.2 Avoidable extra expenditure

The Company had to procure materials through re-tendering at an avoidable extra expenditure of Rs.1.14 crore due to its failure to promptly place purchase orders within the validity period of the bids.

The Fertilisers And Chemicals Travancore Limited (Company) failed to act promptly to seal contracts for procurement of sulphur and muriate of potash within the validity period of the bids and incurred an avoidable extra expenditure of Rs.1.14 crore in two cases discussed below:

CASE - A

The Company sent (1 June 2004) tender enquiry to its pre-qualified suppliers for supply of 45,000 MT (+/-five *per cent*) sulphur. The bids were opened on 8 June 2004 and M/s. Transammonia AG, Switzerland (vendor) emerged the lowest bidder, who offered firm

[♣] ***30,150 MT x Rs.1,440 per MT (Rs.17,349 minus Rs.15,909) = Rs.4.34 crore approximately***

supply of 30,000 MT sulphur (+/-10 *per cent*) in two shipments of 15,000 MT each and additional 15,000 MT at their option. The vendor also stressed that written confirmation of the acceptance of offer should reach them by 1500 hours IST 10 June 2004.

Audit scrutiny revealed that the Standing Sales Purchase Committee (SSPC)[♠] of the Company took up the matter only on the day of expiry of the offer i.e., 10 June 2004. Although, SSPC recommended placement of order on L1 basis, which were approved by the Chairman and Managing Director the same day, the Company sent its acceptance to the offer only after the expiry of the validity period. The vendor was also requested to confirm the supply of third shipment to enable the Company to place order for it. The vendor rejected Purchase Order (PO) due to communication of acceptance after the validity period.

As a result, the Company had to procure (July - September 2004), the material from another supplier at a higher rate (US$ 90.75 per MT) in comparison to the rate offered by the vendor (US$ 84.45 per MT) and incurred an avoidable extra expenditure of Rs.73.14 lakh[♦] on procurement of 30,000 MT sulphur.

The Management admitted (January 2005) that PO was not sent within the validity period. They further alleged that the vendor was actually not inclined to execute PO even if the Company's confirmation in writing had reached within the stipulated time on the grounds that the PO was not in line with their offer.

The reply is not tenable as SSPC took up the matter only on the last day of the validity period and continued to negotiate the price with the vendor till noon on the same day. This ultimately resulted in delay in sending the express acceptance of the offer within the validity period. The Company's request for seeking confirmation of the additional third shipment only gave an added reason to the vendor to reject the offer.

Thus, delay in processing the tender enquiry and failure to communicate the acceptance of the offer within the validity period resulted in an avoidable extra expenditure of Rs.73.14 lakh in procurement of 30,000 MT sulphur from another supplier.

CASE - B

The Company invited (March 2003) limited tenders for the supply of 25,000 MT of muriate of potash (MOP). The rate quoted by Madras Fertilizers Limited (vendor) at US$ 119.80 per MT CFR[♦] was the lowest. Accordingly, a PO was placed on the vendor on 16 April 2003 with a delivery period of 30 days from the date of issue of PO. While accepting the PO, the vendor agreed to the terms and conditions including levy of liquidated damages (LD) to compensate for loss due to possible delay in supplies. The vendor also asked (24 April 2003) the Company to establish a confirmed irrevocable and workable letter of credit (LC) in the format provided by them in favour of their principal suppliers, viz., International Potash Co (UK) Limited, London (IPC) and confirmed that the shipment would be arranged within 30 days from the date of establishment of LC.

[♠] *comprising of Director (Marketing), Director (Finance) and Director (Technical) of the Company*

[♦] *after forfeiture of Earnest Money Deposit of Rs.13.80 lakh*

[♦] *cost and freight*

The Company, however, deviated from the LC format provided by the vendor and established (7 May 2003) an LC on IPC with specific LD clause of its own, thereby binding them for delayed shipments. The vendor objected to the LD clause incorporated in the LC as it was not acceptable to IPC and insisted (8 May 2003) that the Company establish the LC exactly as per the format proposed by the vendor. Thereupon, the Company took more than two weeks' time to rectify the defect and forwarded the fresh LC on 26 May 2003. The vendor expressed (27 May 2003) its inability to supply the order as IPC had withdrawn their offer citing belated response by the Company as the reason. Thereafter, the Company procured the material by re-tendering involving an avoidable extra expenditure of Rs.40.91 lakh.

The Management stated (June 2005) that they incorporated the LD clause in the LC on IPC since the vendor had already agreed for the LD clause rendering them liable for delay in shipment and the LC was opened at the vendor's behest. They further added that the vendor objected (8 May 2005) to the inclusion of LD clause and requested for unconditional LC, which was forwarded on 26 May 2003.

The reply is not acceptable since the Company unilaterally imposed an LD clause on IPC with whom the Company had no direct contractual relationship. Further, the contract with the vendor itself provided adequate safeguard by way of LD clause. Even after realising the mistake, there was inordinate delay of more than two weeks on the part of the Company to rectify the mistake.

Thus, establishment of an inappropriate LC and delay in rectifying the defect led to procurement of MOP through re-tendering, which resulted in an avoidable loss of Rs.40.91 lakh to the Company.

The matter was reported to the Ministry in February/July 2005; its reply was awaited (November 2005).

10.2.3 Payment of higher rate of interest on Trade Deposits

The Company did not reduce the rate of interest on trade deposits in line with interest on public deposits and suffered a loss of Rs.66.29 lakh during April 2003 to March 2005.

The Fertilisers And Chemicals Travancore Limited (Company) released goods to dealers on cash as well as credit basis. The credit sales terms, *inter alia* included a facility to the dealers to deposit cash with the Company in addition to bank guarantee submitted for obtaining additional credit. During the years 2003-04 and 2004-05, interest was paid by the Company on these trade deposits (TD) at the rate of 10 *per cent* per annum.

It was observed in Audit that the Company had been simultaneously raising Public deposits (PD) under Public Deposit Scheme since 1993 at interest rates ranging from 13 *per cent* in 1993 to seven *per cent* in 2003. Though, the Company reduced the rates on PD to seven *per cent* effective from April 2003, it did not simultaneously reduce the rate on TD. Only on being pointed out by Audit (July 2004) the Company amended the credit terms with effect from April 2005 and brought the rate on TD down to seven *per cent*.

Thus, failure of the Company to reduce the rates on TD to match with the rates of PD resulted in additional cash outflow of Rs.66.29 lakh during the period April 2003 to March 2005, being the differential of interest paid.

The Management stated (September 2005) that there was vast difference between PD taken under the Companies Act, 1956 (Act) and the deposits taken from its own customers. According to the Management, TD were in the nature of security towards credit supplies and a source of finance for working capital. They added that the TD were more liquid than the bank guarantee obtained from dealers. The Company further maintained that the Public Deposit Scheme under the Act had a lot of legal restrictions and procedures. The Ministry endorsed (November 2005) the views of the Management.

The Management's view in support of allowing higher interest rate on TD in the past was untenable as both PD and TD are a source of finance the cost of which is influenced by the same factors. TD as well as PD for one-year term co-existed at the same interest rates from early 1993 to August 1997. During August 1997 to March 2003, the PD rates for one-year deposits progressively declined and the TD rate followed closely with maximum excess interest of one *per cent* given on TD except for a brief period of six months between October 2001 and March 2002 when the difference was three *per cent*. However, between 2003-2005 while the PD rate was reduced twice, first to seven *per cent* and then to six *per cent*, the TD rate remained unchanged. Thus, the Management's decision to allow higher rate of interest on TD as compared to PD rates lacked justification.

10.2.4 Avoidable extra expenditure

Despite product shortage and rising prices in the international market, the Company failed to place the purchase order within the validity period and subsequently procured sulphur at higher prices resulting in avoidable extra expenditure of Rs.53.86 lakh.

The Company issued a limited tender enquiry (November 2002) to pre-qualified vendors for the procurement of 45,000 MT sulphur in three consignments of 15,000 MT (+/- five *per cent*) each with a delivery schedule from January 2003 to February 2003. The Company received (December 2002) three valid bids of which the offer from M/s. Swiss Singapore Overseas Enterprises Pte. Limited Dubai (vendor) was the lowest and valid till 7 December 2002 at US$ 79.50 PMT[♣] CFR, Cochin. The Company requested (4 December 2002) the vendor for maximum reduction in quoted price and freight margin but they intimated their inability on the same day to offer any further discount in the quoted prices. The vendor even cautioned the Company that there was continuous rising trend and product shortage in the international market.

The Material Procurement Committee (MPC) of the Company after careful consideration of price trends, demand and supply position in the international market recommended (6 December 2002) for placing the order on the vendor. The Company, however, compared the quoted rates with the rate of US$ 73 PMT CFR offered to Paradeep Phosphates Limited (PPL) for December 2002 shipment by the same vendor. The Company again

[♣] *per metric tonne*

requested (7 December 2002) the vendor to either offer maximum discount in the quoted rates or match the rates offered to PPL and it also sought extension of validity of the offer to 14 December 2002. The vendor did not accept this (7 December 2002) mainly on the ground that all the refineries in the middle east changed their prices on monthly/quarterly basis and that while old price was for December 2002 shipments, new prices were applicable for shipments due in January - February 2003. The vendor also expressed its inability to extend further the validity of the offer. Subsequently, the Company decided to go for re-tender (December 2002) for the same delivery period and procured (January - February 2003) 28,022 MT sulphur from two other vendors at the rate of US $83.50 PMT involving an avoidable extra expenditure of Rs.53.86 lakh.

The Management stated (April 2005) that PPL had contracted sulphur at lower rates from the same vendor for January 2003 arrival. However, the vendor refused to match the rates offered to PPL and they decided to go in for re-tender in anticipation of the prices coming down in view of procurement at lower rates by PPL.

The reply is not tenable as MPC in its deliberations considered reports published on price trends in an international monthly business publication (November 2002 issue) regarding rates finalised by the suppliers with MMTC Limited, total volume of sulphur procurement by China in excess of its previous year procurement and the impending price rise of US$ 20 PMT for contract shipments from January 2003 along with the rates finalised by PPL. After considering all these factors, it had apprehended stiffness in the market owing to poor response against the tender enquiry. Only after considering all these factors, the MPC had recommended placing the order. However, the Company instead of placing the order on the vendor continued to negotiate the prices and allowed the offer to expire. The Company ultimately procured the sulphur through re-tendering resulting in avoidable extra expenditure of Rs.53.86 lakh.

The matter was reported to the Ministry in April 2005; its reply was awaited (November 2005).

CHAPTER XI: MINISTRY OF FINANCE

Insurance Division

General Insurance Corporation of India

11.1.1 Avoidable payment of interest

Incorrect estimation of taxable income and consequent short payment of advance income tax by the Corporation resulted in avoidable payment of interest to the tune of Rs.7.10 crore in respect of the financial year 2003-04.

Under Section 208 read with Section 211 of the Income Tax Act, 1961 (the Act) the Corporation is required to pay advance tax at the prescribed rates on due dates in quarterly instalments in a financial year in case the amount of income tax payable by the Corporation during that year exceeds Rs.5,000. In the event of short payment of advance tax, the Corporation is liable for payment of interest under the provisions of the Act. According to Section 234 (B) of the Act, if the advance tax paid is less than 90 *per cent* of the assessed tax, interest at the rate of one *per cent* per month or part thereof on the amount by which the advance tax paid falls short of the assessed tax is leviable from April 2001 of the assessment year to the date of determination of income under the Act. Section 234 (C) of the Act also provides for payment of interest at the rate of 1.25 *per cent* (revised to one *per cent* effective from September 2003) per month or part thereof on the short paid instalments of advance tax for a period of three months.

A review of records of the General Insurance Corporation of India (Corporation) relating to assessment of income tax revealed that it paid less advance income tax during the financial year 2003-04 due to incorrect estimation of taxable income and had to pay interest of Rs.7.10 crore under Section 234 (B) and Rs.6.16 crore under Section 234 (C) of the Act totalling Rs.13.26 crore.

In reply the Management stated (March 2005) that the payment of interest was one off instance as the actual profits were higher than the projected profit for the first time in the year 2003-04 owing to qualitative improvement in the business underwritten, higher investment income following boom in the market and reduction in reserve strain on account of transfer of crop insurance business to another company viz. Agriculture Insurance Company of India Limited. The Ministry endorsed (June 2005) the reply of the Management.

The above contention of the Management/Ministry is not tenable as in earlier years also, the Corporation was unable to make accurate self-assessment of their income and advance income tax liability, indicating poor financial management. During the financial years 1999-2000 to 2002-03 the Corporation paid advanced tax of Rs.135.50 crore, Rs.103.13 crore, Rs.81.00 crore and Rs.90.65 crore against the actual tax liability of Rs.76.00 crore, Rs.55.42 crore, Rs.29.00 crore and Rs.28.94 crore respectively. The Corporation was, thus, unable to realistically assess its advance tax liability in the year

2003-04 when it actually made under payment of tax with consequent penal interest liability. The Corporation's inability to assess the impact of improvement in the business underwritten and investment income from the boom in the market also indicated the absence of an effective internal control mechanism to monitor and review its financial results periodically.

Thus, due to failure in making correct assessment of taxable income and to deposit 90 *per cent* of the assessed tax liability by 15 March 2004, the Corporation had to pay avoidable interest of Rs.7.10 crore under section 234 (B) to the Income Tax Department on account of short payment of advance income tax during the financial year 2003-04.

National Insurance Company Limited

11.2.1 Loss of revenue due to under-charge of premium

The Company lost premium of Rs.2.41 crore due to application of rates lower than tariff rates in respect of the Special Contingency Policies issued by the Company.

According to Section 64U of the Insurance (Amendment) Act, 1968, Tariff Advisory Committee (TAC) shall control and regulate the rates, advantages, terms or conditions of the tariff that may be offered by insurers in respect of general insurance business. As such Insurance Companies are required to follow the rates, advantages, terms or conditions for these risks as provided in tariff.

It was noticed in Audit that Bhubaneswar Divisional Office of the Company devised a Special Contingencies Policy (SCP) to cover various risks to properties owned by power supply distribution companies in Orissa, including risk relating to machinery break down, which were governed by tariff. Between May 2000 and May 2001, four such policies insuring different sums were issued to three power distribution and supply companies viz. Northern Electricity Supply Company of Orissa Limited (NESCO), Western Electricity Supply Company of Orissa Limited (WESCO) and Central Electricity Supply Company of Orissa Limited (CESCO). While calculating the premium, the Division considered the tariff rates for machinery break down risks for transformers and cables/transmission lines as 0.15 *per cent* each instead of the regular rates of 1.25 *per cent* for transformers and 0.50 *per cent* for cables/transmission lines, to arrive at a composite package rate of 0.30 *per cent* on sums insured for both tariff and non-tariff covers under the SCP. In violation of TAC guidelines, Head Office/Regional Office accorded approval to the composite rate which resulted in breach of tariff rates. The policy was renewed for the second year also in case of WESCO. Application of premium rates lower than the tariff rates in these SCPs resulted in undercharge of premium of Rs.2.41 crore.

The Management contended (June 2005) that alleged breach of tariff had occurred due to unclear directive from TAC and that the breach was not intentional. The reply of the Management is not convincing as in the guidelines issued in February 1998, the Company itself had categorically instructed the field offices to protect the tariff requirement both in respect of rate and cover in a package issued as SCP.

Thus, the Company suffered loss of Rs.2.41 crore because of application of lower tariff rates in violation of the Company's own guidelines.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

11.2.2 Loss of revenue due to charging incorrect premium

The Company suffered a loss of Rs.1.54 crore due to charging incorrect premium under Group Personal Accident Policy issued to Government of Haryana.

The Company issued a Group Personal Accident Policy to Government of Haryana for the period October 2003 to October 2004 covering 24,66,666 beneficiaries below poverty line in Haryana for a sum insured of Rs. one lakh per person.

The Company decided (May 2003) to charge premium at the rate of Rs.10 per person after allowing discount of Rs.35.10 (including discount of Rs.16.65 for excluding rail road accidents) on the basic rate of Rs.45 per person as below:

Usual rate of Table 1A for Normal risk persons	**Rs.45 per lakh**
Less:	
Group Discount – 30 *per cent*	13.50
Discount for not covering rail/road accident – 37 *per cent*	16.65
Discount for excluding children education fund – 6 *per cent*	2.70
Discount for excluding funeral expenses – 5 *per cent*	2.25
Total discount 78 *per cent*	**35.10**
Premium to be charged Rs.45.00 less Rs.35.10 = Rs.9.90 Say Rs.10 per lakh	

Subsequently, on a request from the Government of Haryana to cover rail/road accidents also, the premium rate was revised (August 2003) to Rs.15 per person after loading the decided rate of Rs.10 by 37 *per cent* (Rs.3.70) for coverage of rail/road accidents and adding the additional (Rs.1.30) for a cushion for negotiations with the Government. The revised rate of Rs.15 per person was not correct because the discount of Rs.16.65 allowed earlier for excluding rail/road accidents should have been added back for fixing the rate instead of adding only Rs.3.70.

The Management in their reply (August 2005) stated that

(i) The details of computation of Rs.15 were not indicated in approval note of August 2003 but Audit observed that the rate of Rs.15 was arrived at after loading earlier approved rate of Rs.10 by 37 *per cent* (Rs.3.70) for coverage of Rail/Road accident and adding the rest (Rs.1.30) for a cushion for negotiation.

(ii) After approval of the rate of Rs. 10 per person some further negotiation would have taken place with the Government of Haryana when the amount of compensation was reviewed and the benefits under the policy were restricted to almost 50 *per cent* for two out of four contingencies involving loss to limbs/eyes. Accordingly, the premium was recast to Rs.15 after allowing truncated cover discount of 25 *per cent* as below:

Usual rate of Table 1A for Normal risk persons	**Rs.45 per lakh**
Less:	
Group Discount – 30 *per cent*	13.50
Discount for truncated cover – 25 *per cent*	11.25
Discount for excluding children education fund – 6 *per cent*	2.70
Discount for excluding funeral expenses – 5 *per cent*	2.25
Total discount **66 *per cent***	**29.70**
Premium to be charged Rs.45.00 less Rs.29.70 = Rs.15.30 Say Rs.15 per lakh	

The Ministry endorsed (September 2005) the reply of the Management.

The reply of Management/Ministry is not tenable because

(i) The working of Rs.15 per person is not an Audit calculation but was a clear proposal of the Regional office of the Company (August 2003) which was approved by the Company.

(ii) Neither the proposal of the Regional office nor the approval of the Company contained the element of truncated cover discount as stated now. The Company's Head Office did not approve the truncated cover discount even *ex-post facto*. The reply of Management is, thus, not borne out by facts.

(iii) The truncated cover discount of 25 *per cent* stated to have been allowed was also not justified because only two out of four contingencies were truncated by fifty *per cent*. Even if the Company had truncated the cover fully by the three contingencies and limited it to death only, the rate chargeable would have been Rs.40 per person (Table 1 of the Insurer's Premium Guide of the Company) as against the rate of Rs.33.75 (Rs.45 less 25 *per cent* truncated cover discount) charged by the Company.

Even if the contention of the Company regarding truncated cover is accepted, it allowed an extra discount of atleast Rs.6.25 per person and charged incorrect premium resulting in loss of Rs.1.54 crore.

11.2.3 Non-compliance with directives of Tariff Advisory Committee

The Company failed to collect 10 *per cent* surcharge towards terrorism risk amounting to Rs.1.22 crore in violation of TAC's directives.

Tariff Advisory Committee (TAC) directed (September 2001) the Insurance Companies to collect a surcharge of 10 *per cent* towards terrorism risk on the net premium on all fire and engineering policies issued fresh or renewed on or after 1 October 2001 and to collect the surcharge on the existing policies on pro-rata basis for the un-expired period of the policy. TAC also clarified (December 2001) that the surcharge so levied would be treated as premium and no option was to be given to the insured to opt out of terrorism cover. Further, TAC intimated (March 2002) that the premium would be charged

separately in respect of terrorism cover for industrial and non-industrial risks with effect from 1 April 2002 at the rate of Re.0.50 per Mille* and Re.0.30 per Mille

A test check of policies issued by some units of National Insurance Company Limited (Company) in the Southern Region revealed that the pro-rata surcharge of 10 *per cent* was not collected. Further, for policies issued and renewed after 1 April 2002, premium at revised rates was also not collected in certain cases. The total amount thus foregone was Rs.1.22 crore.

The Management stated (April 2005) that most of the clients objected to imposition of additional premium for covering the risks of terrorism in the existing policies for which the insurer had already worked out and obtained consideration of relevant premium. The Management further stated that the issue was finally sorted out and TAC issued (March 2002) revised terms with effect from 1 April 2002 making the terrorism cover optional and the surcharge towards terrorism for the period from October 2001 to March 2002 was left uncollected due to legal reasons.

The reply is not tenable as the problem in collection of pro rata surcharge was discussed in the meeting of the Underwriting Committee of Indian Insurers' Pool for Terrorism Risk Insurance held on 23 March 2002 wherein it was decided to exclude the cover for terrorism risk from 1 October 2001 if any client refused to pay the surcharge of 10 *per cent*. Further, TAC's directive (September 2001) was categorical and the Company had no alternative but to negotiate the terms afresh with the existing policyholders and collect the pro-rata surcharge on the above-referred policies also during the intervening period.

Thus, the Company's failure to comply with TAC's directives resulted in loss of revenue of Rs.1.22 crore.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

The New India Assurance Company Limited and National Insurance Company Limited

11.3.1 Undue favour to a customer by extending group discount exceeding norms

The New India Assurance Company Limited and National Insurance Company Limited issued group policies on undue and irregular terms and conditions to Golden Trust Financial Services, thereby, incurring loss of Rs.21.57 crore and Rs.5.59 crore respectively.

11.3.1.1 Introduction

Group Insurance constitutes an important activity of Insurance business and the group schemes offered by the Insurance Companies provide certain specified classes of individuals the advantage of a beneficial coverage at a moderate cost. Most of the Group Insurance schemes pertain to employer-employee groups, but Group Insurance is also

* ***Per thousand of sum insured***

sold to organisations where there is some commonality of interest. There are various relevant aspects connected with Group Insurance such as definition of the group, the market conduct to be adopted by the insurers in canvassing group insurance schemes, etc.

Reimbursement of hospitalisation and/or domiciliary hospitalisation expenses for illness/diseases contracted or injury sustained is covered under Mediclaim Insurance Policy. Death, partial or total disablement due to accident is covered under Janata Personal Accident (JPA) Policy for sums insured upto Rs. one lakh. If the sum insured is above Rs. one lakh, the same is covered under the Personal Accident (PA) Policy. All these policies can be issued to an individual or to a group and can cover a period of a year or more. Group discount and long term discount are allowed based on group size and the period of cover.

11.3.1.2 Scope of Audit

From 1998 onwards, The New India Assurance Company Limited (NIA) and National Insurance Company Limited (NIC) conducted substantial Group Insurance business in personal line, with Golden Trust Financial Services (GTFS), a partnership firm which also floated (April 1999) a service club called Golden Multi Services Club (GMSC). A test check of the records relating to Group Insurance business with GTFS/GMSC of NIA and NIC was conducted in Audit for the period 1998-99 to 2004-05. The irregularities noticed are discussed in the succeeding paragraphs.

CASE -A New India Assurance Company Limited (NIA)

Golden Trust Financial Services (GTFS), a partnership firm, constituted to carry on various commercial activities, entered into two separate Memoranda of Understanding (MOU) with NIA for extending group Mediclaim and group Janta Personal Accident cover in favour of their investors and their family members, field workers and their family members and friends. As per the terms of MOU, the policies were to be renewed every year till the last insured person was in the books of NIA and the scheme was to continue for a period of at least four years. In so far as Group Janata Personal Accident Policy (GJPAP) was concerned, full coverage for a long term/ short term period was required to be extended from the date of entry of new entrants even subsequent to the issue of the policy. Accordingly, Howrah Divisional office of NIA issued Group Mediclaim Policy (GMP) (August 1998) and a long term GJPAP (January 1999).

After experiencing the adverse claim ratio in the first year, NIA referred the matter to General Insurance Company Limited, its holding company. NIA sent (May 1999) notice to GTFS for cancellation of MOU as the latter had redefined a group to include *inter alia* service clubs and stated that further premium through endorsements under both the policies would not be accepted. Aggrieved by the decision, GTFS moved the court to obtain (July 1999) an interim order/stay from Hon'ble High Court, restraining NIA in giving effect to the notice, though by the same order, the court also directed GTFS not to collect any premium from members under the category of 'friends'. NIA failed in its efforts to get the order vacated and consequently had to accept renewal premium and its liability for coverage continued. Two other Divisional offices (Siliguri and Kolkata-17) of NIA also conducted similar business with GTFS, albeit at a lesser volume as compared to Howrah Divisional Office.

Audit scrutiny of the records relating to GMP and GJPAP in Howrah Divisional Office revealed the following:

(i) Group discount allowed was 50 *per cent* in GMP and 75 *per cent* in GJPAP to a heterogeneous group consisting of investors of GTFS, field workers, agents and their family members and friends. Premia were being collected from thousands of people, spread all over the country and the net premium amount was deposited by GTFS at periodical intervals through a consolidated cheque with a list of persons covered till the Kolkata High Court order of July 1999 which directed GTFS not to collect any premium from the categories of friends as the group had become highly heterogenous.

(ii) The discounts were allowed on the basis of anticipated group size. As a result, the group size formed to avail of group discount subsequent to the inception of the policy did not fall in any of the group size categories. Hence, GTFS was allowed an arbitrary rate of discount on the higher side.

(iii) The sums insured for individual and maximum time limit under GJPAP were upto Rs.10 lakh and 15 years respectively. The 15 year period offered in the cover was inordinately long and the Company subsequently restricted it to five years.

(iv) While the Group policies were issued to GTFS alone, the insured were being issued certificates. Blank certificates that were not pre-numbered, bearing facsimile signatures of the officials of the divisional offices of NIA, were handed over to GTFS for issue to the insured. There was no control or reconciliation of the certificates issued. This led to issue of duplicate certificates.

(v) NIA apprehended that discount was not being passed on to the insured as certificates issued neither contained the amount of the premium paid nor the amount of discount offered.

(vi) Procurement of business and collection of premium were done with lakhs of unauthorised agents in violation of the provisions of the Insurance Act, 1938, which prohibited employment of unlicensed agents.

(vii) The entire business was booked under the business code of a particular development officer of NIA who later became a partner of GTFS.

The Management while admitting the above facts, stated (November 2005) that besides administrative steps, action against erring officials had also been initiated; policies and MOUs were cancelled and now group policies were being finalised with the approval of Head Office.

Thus, NIA allowed financial benefit to GTFS by way of group discount amounting to Rs.28.71 crore and suffered a loss of Rs.21.57 crore (GMP Rs.2.75 crore; GJPA Rs.18.82 crore) till 31 March 2005 on paid and outstanding claim basis.

CASE- B National Insurance Company Limited (NIC)

Chairmen cum Managing Directors (CMDs) of Government Insurance Companies in consultation issued various directions on Group Insurance in the line of personal covers and the decision of CMDs with certain modifications was made effective by General Insurance Corporation of India (GIC) from November 1999. These instructions *inter alia* included:

(i) Service clubs were identified as one of the seven eligible groups for availing group discount. However, the definition of service club, its compositions etc. were not defined.

(ii) Group discount was to be considered on the number of persons in the group at the inception and amalgamation of independent identifiable groups for the purpose of forming a larger group to earn higher discount was not permitted. The maximum group discount limit was fixed at 30 *per cent* and the discount benefit was to be passed on to the individuals insured in a group.

(iii) No JPA group or individual policy was to be issued for sum insured for more than Rs. one lakh per person. Whenever the insured sum was higher, the same would be covered under PA policy.

(iv) The group policies were not to be issued through intermediaries and the maximum period of the policy was to be five years.

Meanwhile, GTFS floated a service club named Golden Multi Services Club (GMSC) in April 1999 and reduced substantially its business with NIA. Subsequently, GMSC entered into two MOU (January 2001) with NIC to take GMP and GJPAP for the members of its club. NIC issued a GMP and a GJPAP in January 2001 covering the first group of 246 and 1481 members, under each policy, respectively. Subsequently, new groups of members were covered on various dates by issuing endorsements under these two policies.

Audit scrutiny revealed the following:

(i) NIC did not make any change in discount rate, sum insured and long term limits and agreed to extend a cover to GMSC on lines similar to the one earlier extended by NIA to GTFS. This was despite NIA experiencing a high claims ratio and the group becoming very large and heterogeneous. Thus, NIC failed to gain anything from the experience of NIA.

(ii) The cover had been extended to 35.45 lakh persons and 14.35 lakh persons (April 2005) scattered over a wide geographical area with no common interest, through numerous endorsements under GJPAP and GMP respectively. In this process, instead of having a definite date of expiry of cover under a normal group policy, the policy became a perpetual, never-ending policy.

(iii) GMSC got 75 *per cent* and 50 *per cent* discount benefit in GJPAP and GMC, respectively by treating the policy as renewal in continuation.

(iv) The sole official intermediary between NIC and GMSC for procurement of business from GMSC was the wife of the ex development officer of NIA who later became a partner in GTFS. This was done against consideration of substantial amount of agency commission payable to the wife (agent). The commission of the agent was increased from five *per cent* to 15 *per cent* in August 2003 and agency commission amounting to Rs.13.88 crore was paid till December 2004.

Thus, NIC extended insurance cover to GMSC in gross violation of the existing rules and regulations. Between January 2001 and December 2004, NIC allowed financial benefit of Rs.196.70 crore to GMSC by way of group discount and incurred a loss of Rs.5.59 crore upto March, 2005 as calculated on the basis of claims paid and outstanding by the actuary appointed by NIC. This was despite the fact that a special team of Internal Audit and Inspection Department of NIC had critically examined the various issues involved in the business and had reported serious irregularities in July 2001.

In the face of criticism from various quarters including Internal Audit of the Company, Statutory Auditors, Government Audit, vigilance etc., NIC appointed an actuary for pricing the policy and determining various terms and conditions in order to keep control over Claim Premium Ratio (CPR) in the long term policies. The actuary concluded (March 2004) that NIC would suffer a total loss of Rs.23.11 crore under the existing GJPAP at the end of the year 2018 i.e. the last expiring policy year of long term policy and the present value of the loss was Rs.18.86 crore. Besides, under provisioning of outstanding claims was also apprehended as there was no time limit clause for reporting claims in the earlier MOU. The actuary advised that NIC should consider decreasing the term of the policy, increasing the premium rate, decreasing the discount, reducing the sum assured, reducing commission, taking reinsurance protection etc. under a new long term policy. In view of the actuary's recommendations, NIC discontinued the old GMP and GJPAP and entered into two fresh MOUs with GMSC (the club was converted into a company in February 2003) in April 2004 to introduce a new GMP and GPAP with modified terms in place of the old policies.

IRDA issued instructions in December 2004 to all the insurers not to accept any business from GTFS and its allied bodies. Subsequently, NIC informed GMSC (December 2004) about its decision to not accept any business from them.

The Management while admitting the above facts, stated (September 2005) that in view of IRDA circular (July 2005) it had become necessary for such clubs that took group master policy to convey to its members information on actual premium paid to the insured. NIC further stated that before issue of any long term policy, its terms and conditions, pricing, handling of claims etc would be reviewed at their Head Office.

Thus, by accepting business from GTFS/GMSC on terms and conditions that were detrimental to their interests, NIA and NIC incurred loss of Rs.21.57 crore and Rs.5.59 crore respectively by the end of 2004-05 and these would increase in future.

The matter was reported to the Ministry in December 2005; its reply was awaited.

The New India Assurance Company Limited

11.4.1 Loss due to application of incorrect tariff

The Company suffered a loss of Rs.1.41 crore owing to incorrect rating of civil works contract under 'Erection All risk Insurance' tariff instead of 'Contractors All Risk Insurance' tariff.

According to All India Tariff on Contractors All Risk Insurance (CAR), the CAR tariff should be applied to all risks situated in India, where the value of civil works involved is more than 50 *per cent* of the total contract value. In all other contracts or projects, the risk has to be covered under 'Erection All Risk Insurance' (EAR) tariff.

M/s. Jai Prakash Industries Limited, New Delhi, a contractor of National Hydro Power Corporation Limited, Faridabad, proposed to obtain an insurance coverage for the execution of civil works involved in the construction of dam works and of power house works of Teesta Hydro Electric Power Project at Sikkim. The total contract value of Rs.395 crore for dam and allied works and Rs.207 crore for civil work of powerhouse was indicated as the sum insured in the proposal.

In response to the proposal, Silguri Divisional Office (DO) of the Company quoted (September 2001) the premium provisionally at 12.895 per Mille for the dam work under CAR tariff and at 7.396 per Mille for the Power House work under EAR tariff on the plea that the civil contract value of Rs.207 crore for construction of power house was less than 50 *per cent* of its total project cost of Rs.700 crore. Simultaneously, the RO sought approval from its Head Office (HO) for the rates adopted in the quotations.

The HO advised (September 2001) the Kolkotta RO to underwrite the insurance business on provisional basis provided the insured was agreeable to pay the premium as and when decided by Tariff Advisory Committee (TAC). The Head Office also called for details of "Allied Works" in the absence of which, rates quoted under CAR tariff for the dam work could not be confirmed.

However, Siliguri DO confirmed (October 2001) the rates quoted earlier in September 2001, as the proponent insured did not accept provisional rating subject to approval by TAC but insisted on the firm rates. The DO further allowed the proponent insured to pay the premium amount of Rs.5.56 crore and Rs.1.67 crore respectively. Accordingly, the proponent insured placed (November 2001) the insurance business with the Company subject to a coinsurance arrangement to the extent of 40 *per cent* with M/s. Royal Sundaram and the Company issued the policies for the period from 9 November 2001 to 8 November 2006.

In response to the reference made (October 2001) by the HO, TAC advised (22 November 2001) the Company to rate the power house work only under CAR tariff and not under EAR tariff as advised earlier on 8 November 2001, since the proposal for power house was only in respect of civil works involved therein. In regard to the dam work, which involved making of tunnels above the sea level, TAC decided (March 2004) to rate the proposal under 'Tunnels – Others' of CAR tariff instead of under the sub head "bridges on rivers, dams etc.", adopted by the Company.

Accordingly, the HO advised (March 2004) the Siliguri DO to recalculate the correct premium for dam work contract and to collect the differential premium from the insured. Further, in respect of the policy issued for the power house contract, the HO directed the DO to convert the same from EAR policy to CAR policy by recalculating the correct premium and by recovering the differential premium from the insured. Consequently, the Siliguri DO worked out the differential premium for the dam work and power house work at Rs.60.61 lakh and Rs.1.74 crore respectively and raised the demand (April 2004) from the insured. The insured, however, refused (May 2004) to make the payment on the ground that insurance rates were quoted by the Company on firm basis and hence any decision in the rating advised by the TAC at a later date would not render them liable.

Thus, disregard of HO directives and incorrect interpretation of tariff put the Company to a loss of premium of Rs.1.41 crore without reckoning Rs.0.94 crore being the share of coinsurers.

The Management in reply to the Audit query admitted (June 2005) the short collection of premium and agreed to recover the same from the claims made by the insured.

The matter was reported to the Management/Ministry in August 2005; their replies were awaited (November 2005).

11.4.2 Loss of premium

The Company suffered a loss of premium of Rs.1.25 crore due to application of incorrect tariff rates meant for laying of water pipeline instead of oil/liquid petroleum pipelines tariff rates to the pipelines erected for transportation of liquid petroleum products.

The general regulations of All India Tariff on the "Erection All Risks (EARs) Insurance" stipulate that the risk insurance for the implementation of any Engineering Project, irrespective of whether taken up departmentally or through contractors or sub contractors, should be covered under the EARs Insurance Policy with or without marine or/and storage risks. The EARs Insurance Engineering tariff, envisaged that the projects for "laying of water pipelines" are to be rated as per risk code 110603 and the projects for "oil/liquid chemical/liquid petroleum product pipelines" are to be rated as per risk code 140308.

Hindustan Petroleum Corporation Limited (HPCL) approached (April 2000) the Divisional Office (DO) of the Company to take an insurance cover for its project for "laying of multi petroleum product pipelines from Mangalore to Bangalore" to be implemented by its joint venture unit, M/s. Petronet MMB Limited. A Storage-cum-Erection All Risks Insurance Policy for an aggregate sum insured of Rs.413.97 crore was issued covering the period from 23 June 2000 to 22 July 2002.

The insurance premium of Rs.1.52 crore was, however, calculated at a comprehensive rate of Rs.3.6775 per Mille based on the rates prescribed for "laying of water pipelines" (code 110603) on the plea that the testing of pipeline was restricted to hydro testing i.e. testing with water instead of applying the comprehensive rate of Rs.6.71 per Mille meant for transportation of "petroleum products pipelines"(code 140308). The Tariff Advisory

Committee confirmed that different rates had been provided in the tariff for pipelines depending on the end use i.e. materials to be carried.

In view of the fact that pipelines were meant for transportation of petroleum products, the premium should have been calculated at a comprehensive rate of Rs.6.71 per Mille applicable to the rates prescribed for "Liquid Petroleum Product Pipeline" under the risk code 140308. Accordingly, the premium amount chargeable worked out to Rs.2.77 crore. As against this the Company had actually charged an amount of Rs.1.52 crore only from the insured. Thus, the incorrect application of tariff by the Company resulted in loss of premium by Rs.1.25 crore.

The matter was reported to the Management/the Ministry in September 2005; their replies were awaited (November 2005).

11.4.3 Avoidable payment of rent

Failure of the Company to execute the tenancy agreement and to accept the conditional vacation offered by the tenant resulted in avoidable expenditure of Rs.1.15 crore towards payment of rent on office accommodations hired by it in the same vicinity.

New India Assurance Company Limited (Company), without executing any tenancy agreement, had let out (1981) an area of 4,673.54 square feet in its Head Office building at Mumbai to M/s. Air India Limited (tenant) at a monthly rent of Rs.7,084. The Company demanded (May 1999) vacant possession of the premises as there was shortage of space to accommodate its own staff due to expansion of business. Subsequently, in December 1999 the Company issued the first notice of termination of tenancy and in February 2001 another notice, demanding a compensation of Rs.9.45 lakh per month from April 2001 onwards in the event of the tenant's failure to handover possession on or before the end of March 2001.

After much persuasion the tenant agreed (October 2001) to hand over the premises after removing its movable property. In regard to the furniture and fixtures that could not be removed from the premises, the tenant requested the Company (December 2001) to pay compensation of Rs. six lakh. The Company, however, did not agree to the payment of compensation as the furniture and fixtures were of no use to it but insisted on vacation of the premises.

The dispute over payment of compensation for left over furniture and fixtures remained unresolved till October 2005 with the result that the tenant neither handed over the possession of the premises nor paid the enhanced rent of Rs.9.45 lakh per month demanded by the Company. Even the agreed rent amount of Rs.7,084 per month was paid only upto October 2001 on the plea that they vacated the premises by shifting their moveable assets other than the fixtures in dispute.

In view of the deadlock, the Company issued (June 2002) a legal notice to the tenant demanding payment of Rs.1.51 crore towards arrears of enhanced rent and for surrender of premises. In the absence of a reply to the legal notice, the Company filed (December 2002) a case with the Estate Officer, the designated authority under the Public Premises

(Eviction of Unauthorised Occupants) Act, 1971 (PP Act), for vacation of the premises and for recovery of damages at Rs.9.45 lakh per month from February 2001 together with interest at 21 *per cent* per annum. The final decision of the Estate officer in the case was awaited (October 2005).

In the meantime the Company continued to hire office space of 12,762 square feet at an average rate of Rs.57.25 per square feet per month in the same vicinity, resulting in avoidable payment of rent of Rs.1.15 crore for the period April 2002 to October 2005.

In reply, the Management stated (August 2005) that since the Company was in dire need of the premises for their HO due to expansion of business, they issued notice (May 2001) to the tenant to vacate the premises. As the tenant was not willing to budge from its stand, the Company, after taking approval from the Ministry, served notice in June 2002 followed by a suit under the PP Act. The Ministry endorsed (September 2005) the views of the Management.

The above contention of the Management/Ministry is not tenable as the failure on the part of the Company to let out its premises without any tenancy agreement initially and the decision not to pay a meagre compensation of Rs. six lakh towards the left over furniture and fixture offered by the tenant for the vacant possession of the premises subsequently, resulted in avoidable payment of rent amounting to Rs.1.15 crore

11.4.4 Loss due to violation of tariff

The Company suffered loss of Rs.70.86 lakh due to non-observance of tariff provisions.

All India Fire Tariff (fire tariff) prescribes rates chargeable depending on the location of storage of risks (Section VI) and the procedure to be followed (Section VIII) for covering the additions, alteration, etc. to the properties covered under the fire policy. It was observed in Audit that New India Assurance Company Limited (Company) erroneously adopted the wrong rates/did not follow the prescribed procedure and suffered loss of revenue in two cases given below.

CASE - A

A Bangalore based Divisional Office of the Company issued (April 2002) fire policy to M/s. IBM India Limited, Bangalore covering the stocks of computers, spares, consumables, etc. for the period 2002-03. The sum insured was Rs.70 crore. The Company collected premium at the rates of Rs.2.50 per Mille for the storage risk for goods stored outside the compound under Section VI of fire tariff. The policy was renewed (May 2003) for 2003-04 at the same rate.

Scrutiny revealed that the stocks were kept at the godowns of M/s. Bhandari Southern Carriers (P) Limited, Pondicherry and M/s. AFL Logistics, Bangalore, both of whom were transporting the goods to various destinations. As such, storage risk had to be classified under 'Transporter's godown and godowns of clearing and forwarding agents' for which the applicable rate of premium as per All India Fire Tariff was Rs.5.50 per Mille. Due to non-adoption of this rate, the Company lost premium of Rs.41.90 lakh during the years 2002-03 and 2003-04.

The Management stated (April 2005) that the stocks of the insured only were stored in the godowns of transport contractors and the godowns were for the exclusive use of the insured and as such the applied rate was in order.

The Management reply is not tenable as according to the fire tariff provisions, stocks stored in the transporter's godown had to be rated at Rs.5.50 per Mille and there was no provision for adoption of lower rate for exclusive usage of transporter's godown by the insured.

CASE - B

Ernakulam Divisional Office of the Company issued fire policies covering Plant and Machinery of M/s. Hindustan Organic Chemicals Limited (Insured) for the years 1998-99 to 2003-04.

The fire tariff provides for coverage to additions to the insured property against payment of advance premium at the time of inception of the policy. The fire tariff stipulates set off of the actual premium for such additions against the advance premium and refund of the balance to the insured, provided the insured declared the value of additions within 30 days of the expiry of the policy.

It was observed that in respect of policies for the years 1998-99 to 2000-01, 2002-03 and 2003-04 there was delay beyond the specified period ranging from 29 days to three and a half years in the declaration of value of additions after expiry of the policies. As the advance premium collected was higher compared to declared value of such additions, an amount of Rs.28.96 lakh was refunded to the insured in respect of these years. As per fire tariff, the insured was not eligible for the refund for declaration beyond the specified period of 30 days, after the expiry of the policy periods.

The Management stated (April 2005) that there was delay in finalisation of accounts by the insured during the above period and accordingly declaration of values for the additions was also delayed.

The reply is not tenable as the declarations for the additions were not made within the stipulated period according to the tariff conditions and therefore the refund of premium of Rs.28.96 lakh made was in violation of tariff.

Thus, violation of tariff provisions resulted in loss of revenue of Rs.70.86 lakh.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

11.4.5 Settlement of claim in excess

Failure on the part of the Company to settle a claim on non-standard basis due to a breach of warranty that was material to the loss resulted in undue benefit of Rs.61.59 lakh to the insured.

In accordance with the general conditions of Standard Fire and Special Perils (SFSP) policy, in the event of misrepresentation or wrong description or non-disclosure of any

material particulars, the policy shall become voidable. The guidelines for settlement of claims issued by the Company, *inter alia*, envisage that if the breach of a warranty is material to the loss, the payment of claim may be considered upto a maximum of 75 percent of the assessed loss.

The Insured, M/s. Sharon Bio-Medicine Limited approached (September 2000) the Belapur Divisional Office (DO) of the Company for an insurance cover for its pharmaceuticals and chemical plant at Taloja. Even though basic solvents like acetone and methanol with flash point below 32 degree centigrade were being used, the insured had not disclosed the fact in clause 15 of the proposal form, which required disclosure about stocks like oils, ether, industrial solvent and other inflammable liquids with a flash point below 32 degree centigrade stored in the plant.

The Regional Engineer of the Company, in his risk inspection report (October 2000), declared that chemicals with a flash point below 32 degree centigrade were not used by the insured and assessed the rating at 2.25 per Mille. Accordingly, the SFSP policy for a sum insured of Rs. seven crore was issued for the period September 2000 to September 2001 incorporating therein the warranty clause six regarding non-use or non-stocking of materials having flash point below 32 degree centigrade in the premises. The policy was renewed for the subsequent year on the same terms and conditions.

A fire occurred in the insured premises in February 2002. The surveyor in his final survey report (September 2002), observed that the fire, which started in the stock in process due to electrical short circuit, spread very fast due to the presence of solvents and chemicals having flash point below 32 degree centigrade. While assessing the loss at Rs.2.49 crore on re-instatement value basis the surveyor reported that the insured breached warranty number six and hence requested the Company to decide suitable adjustment of the loss assessed in lieu of breach of warranty.

Despite the surveyor's report highlighting the breach of warranty, which was material to the loss, the Company decided (January 2003) to collect additional premium of Rs.0.96 lakh (Rs. 0.53 lakh towards rectification of policy for covering the stocks having a flash point below 32 degree centigrade and Rs.0.43 lakh towards reinstatement premium) and settled the claim at Rs.2.48 crore after making minor adjustments towards under-insurance not considered by the surveyor.

However, the claim should have been settled on non-standard basis in line with the claim settlement guidelines since, *prima-facie*, the insured failed to disclose the fact in the proposal form which was the basis for the issuance of the policy. Thus, the decision to settle the claim on standard basis resulted in an undue benefit to the insured by Rs.61.59 lakh after reckoning the differential premium.

In reply to Audit query statement, the Management stated (October 2004 and April 2005), that the breach of warranty as to the usage of stocks with flash point below 32 degree centigrade was not considered as percentage of the value of such stocks to the value of total stocks was only 0.69 *per cent* and according to section VI of the All India Fire Tariff the presence of hazardous goods not exceeding five *per cent* of the total value of the stocks could be ignored. Further, the relevant question number 15 in the proposal

form did not elicit information regarding the flash point of the materials in use in the manufacturing process.

The contention of the Management is not tenable in view of the following: -

(i) In determining the percentage of hazardous stock to total stock, the Management had not considered the value of stock-in-process. As per surveyor's report, the value of stock with flash point below 32 degree centigrade worked out to Rs.0.77 crore out of the total stock of Rs.2.45 crore. Accordingly, the percentage of hazardous stock to total stock worked out to 31.43 *per cent* and not 0.69 *per cent* as claimed by the Company; and

(ii) The relevant question number 15 in the proposal form was overridden by the inclusion of warranty clause six in the policy terms and conditions specifying the non-use or non-storage of stocks having flash point below 32 degree centigrade, which was binding on the insured.

Thus, the failure of the Company to consider the breach of warranty as material to loss and to make the claim payment on non-standard basis resulted in extension of undue benefit of Rs.61.59 lakh to the insured.

The matter was reported to the Management/Ministry in August 2005; their replies were awaited (November 2005).

The New India Assurance Company Limited and The Oriental Insurance Company Limited

11.5.1 Loss of premium due to application of incorrect rate

The New India Assurance Company Limited and The Oriental Insurance Company Limited lost premium of Rs.12.26 crore on the insurance of the compressors and terminals of GAIL (India) Limited during April 2003 to March 2005.

The New India Assurance Company Limited issued a Standard Fire and Special Perils Policy with a sum insured of Rs.2,299.41 crore to M/s GAIL (India) Limited covering their compressor stations and terminals along Hajira Bijaipur Jagdishpur/Gas Rehabilitation and Expansion Project (HBJ/GREP) pipelines for the period April 2003 to March 2004. The Company charged basic fire premium at the rate of Rs.1.20 per Mille instead of Rs.4.50 per Mille chargeable as per the instructions of Tariff Advisory Committee (TAC) (December 2001) resulting in loss of Rs.6.13 crore.

The Oriental Insurance Company Limited also insured these Compressor Stations and Terminals of GAIL (India) Limited for the period April 2004 to March 2005 charging the premium at the rate of Rs.1.25 per Mille instead of Rs.4.50 per Mille chargeable as per the above instructions of TAC resulting in loss of Rs.6.09 crore.

The Oriental Insurance Company Limited also allowed claims experience discount on terminals where the sum insured was less than Rs.50 crore in violation of Section I - General Rules and Regulation of All India Fire Tariff, under which such discount was

allowed only where the risks (on buildings and contents of all blocks in one compound of one complex in one location) had sum insured above Rs.50 crore. Thus, due to inadmissible claim experience discount, the Oriental Insurance Company Limited suffered an additional loss of premium of Rs.3.57 lakh.

The New India Assurance Company Limited in their reply (May 2004) stated that:

(i) The underwriting office rated the 'Compressor Stations' on the pipelines at Rs.1.20 per Mille on the basis of TAC letter of July 1999 as it had not yet been withdrawn by TAC.

(ii) TAC instructions of December 2001 were for rating of 'stand alone compressor stations' and not for compressors 'along with the pipelines'.

The Ministry endorsed (July 2004) the reply of The New India Assurance Company Limited.

The Oriental Insurance Company Limited also gave a similar reply (August 2005) stating that

(i) TAC instructions of December 2001 were applicable to independent compressor houses located outside the industrial compounds e.g. in case of CNG fuel filling stations. The subject matter of insurance in this case was pipeline and linepack had also been insured. The risk had accordingly been rated as per tariff item pipeline (others) Risk /Rate Code 12/04 under Section V on single risk single rate concept.

(ii) Claim experience discount had been given on the basis of data furnished by previous insurance companies at the time of renewal of this policy. No major loss seemed to have been reported in the installation of pipelines.

The replies of both the Companies are not tenable because:

(i) TAC confirmed in November 2004 that the said compressor stations/terminals along with HBJ pipeline of GAIL (India) Limited were rateable as per their instructions of December 2001 depending on the type of material carried through pipeline.

(ii) TAC also clarified (September 2004) that their instructions of July 1999 were superseded by the new Tariff effective from May 2000.

(iii) The policy covered compressor stations and terminals on HBJ/GREP pipelines and not the 'pipelines'. This was also confirmed by The New India Assurance Company Limited and was endorsed by the Ministry. The linepack covers the contents and not the pipelines.

(iv) The Oriental Insurance Company Limited itself renewed the above policy for the period April 2005 to March 2006 by applying the basic rate of Rs.4.50 per Mille on the Compressor Stations as per TAC instructions of December 2001.

(v) Even if there were no claims under the policy in the earlier periods, the claim experience discount was not admissible where the sum insured (on buildings and contents of all blocks in one compound of one complex in one location) was less than Rs.50.00 crore.

Thus, due to application of incorrect tariff and allowing inadmissible discount the Companies suffered a loss of premium of Rs.12.26 crore.

The Oriental Insurance Company Limited

11.6.1 Short collection of premium due to irregular grant of group discount

The Company issued a Group Mediclaim Policy to the employees of M/s. Larsen & Toubro Limited allowing excess discount, which resulted in loss of premium of Rs.6.62 crore.

The guidelines issued (October 1999) by M/s. Oriental Insurance Company Limited (Company) on issues relating to group policies of Personal Accident, Mediclaim, Janata Personal Accident etc. envisaged group discount on the basis of actual number of persons in the group at the time of granting cover.

A Chennai based Divisional Office (DO) of the Company issued group Mediclaim policies to M/s. Larsen & Toubro Limited covering its employees and their family members for the period from February 2000 to January 2001 and renewed the same on yearly basis till 2003-04.

Scrutiny revealed that the DO erroneously allowed group discount at 40 *per cent* as against 10 *per cent* for group size in the range of 6,000 to 7,000 persons. The irregular discount allowed was to the extent of Rs.6.62 crore during the period February 2000 to December 2004.

The Management stated (May 2005) that 40 *per cent* group discount was allowed on the Mediclaim policy as M/s. Larsen & Toubro Limited was having a diversified insurance business relationship with the Company and had placed with it highly profitable business of projects and fire insurance. The Management further stated that such an approach was essential in the competitive environment.

The reply is not tenable, as the higher discount allowed was not in line with the guidelines issued by the Company.

Thus, grant of irregular discount resulted in loss of premium to the extent of Rs.6.62 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

11.6.2 Short collection of premium

The Company suffered loss of revenue of Rs.1.66 crore due to allowing inadmissible discount and adopting erroneous rate.

As per All India Fire Tariff (fire tariff) claim experience discount shall be allowed only for risks having sum insured exceeding Rs.50.00 crore in one location. The fire tariff prescribes a rate of Rs.4.50 per Mille for Liquified Petroleum Gas (LPG) Bottling Plants.

A Chennai based Divisional Office (DO) of Oriental Insurance Company Limited (Company) had issued fire policies to Indian Oil Corporation Limited covering individual LPG Bottling Plants in the Southern Region. A test check of three annual policies covering the period August 2001 to July 2004 revealed that the DO erroneously allowed claim experience discount to locations having sum insured of less than Rs.50.00 crore and also rated the LPG bottling plants at lower rates than the one prescribed under the tariff. This resulted in under recovery of premium of Rs.1.66 crore as below:

(Rs. in crore)

Year	Inadmissible claims discount allowed	Erroneous rate adopted (for LPG Bottling Plant)
2001-02	0.26	--
2002-03	0.40	0.04
2003-04	0.15	0.81
Total	**0.81**	**0.85**

The Management stated (August 2005) that as per tariff provision "no claim experience discount" can be granted if the sum insured in one location was more than Rs.50.00 crore because nowhere in the fire tariff provision it was mentioned that the sum insured had to be above Rs.50.00 crore in all the locations. The Company also stated that the rating at Rs.1.75 per Mille was being followed by all the insurance companies in respect of marketing division products of the insured as per TAC circular of September 1989 which had not been withdrawn even after the revision of the fire tariff as well as Petrochemical tariff in the year 2001 and 2002.

The reply is not tenable as the fire tariff allows claim experience discount of upto 15 *per cent* only for risks having a sum insured of more than Rs.50.00 crore in each individual location. Hence, locations where the sum insured was less than Rs.50.00 crore the claim experience discount should not have been allowed. Also the policy for stock of LPG products stored in Bottling Plants was issued under Fire Tariff and not under Petrochemical Tariff and the bottling plants of LPG were specifically excluded from the scope of Petrochemicals Tariff with effect from 31 March 2001. Hence the rate at Rs.4.50 per Mille prescribed under the fire tariff should have been applied.

Thus, the inadmissible discounts and the application of erroneous rate resulted in short collection of premium of Rs.1.66 crore.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

11.6.3 Loss of premium due to not adhering to the tariff terms and rates

The Company failed to apply the rates prescribed in tariff for pipelines meant for transportation of liquid petroleum products, resulting in loss of premium of Rs.61.00 lakh.

The general regulations of All India Tariff on the "Erection All Risks (EARs) Insurance" stipulate that the risk insurance for the implementation of any Engineering Project, irrespective of whether taken up departmentally or through contractors or sub contractors, should be covered under the EARs Insurance Policy with or without marine or/and storage risks. The EARs Insurance Engineering tariff, envisages that the projects for "laying of water pipelines" are to be rated as per risk code 110603 and the projects for "oil/liquid chemical/liquid petroleum product pipelines" are to be rated as per risk code 140308.

Hindustan Petroleum Corporation Limited (HPCL) approached (April 2000) Mumbai city Divisional Office (DO) number -21, of the Company to take an insurance coverage for its project for laying of multi petroleum product pipeline from Vijayawada to Secunderabad. A Marine-cum-Erection All Risks Insurance Policy for an aggregate insured sum of Rs.266.74 crore was issued covering the period July 2000 to September 2002.

The insurance premium of Rs.1.66 crore was, *inter alia*, calculated applying the tariff rates of 7.390 per Mille (meant for water pipelines) and 3.440 per Mille for terminals. However, as the pipelines were meant for transporting petroleum products, the premium at the rate of 8.4225 per Mille based on tariff rates meant for oil/liquid petroleum products covered under risk code 140308 should have been charged. Accordingly, the premium amount chargeable worked out to Rs.2.27 crore. Thus, incorrect application of tariff resulted in undercharge of premium by Rs.61.00 lakh.

In reply to the factual statement the Mumbai city DO number 21 stated (March 2005) that it offered two alternatives to the insured (i) premium with coverage upto hydro testing and (ii) premium with coverage upto product testing. As the insured had opted for alternative one, the Company construed the risk similar to water pipeline and, therefore, charged the rates meant for water pipelines.

The above contention of the Management is not tenable, since the tariff is prescribed on the basis of the ultimate usage of the pipeline as the criteria for rating and not the method of testing. The Tariff Advisory Committee also confirmed that different rates have been provided in the tariff for pipelines depending on the end use i.e. materials to be carried. Thus, interpretation of the Company justifying application of water pipeline tariff rates to the liquid petroleum products pipelines was not correct.

The matter was reported to the Management/Ministry in September 2005; their replies were awaited (November 2005).

11.6.4 Irregular settlement of claim

A claim for damage to a locomotive was settled under a policy, which was not in existence at the time of occurrence of the accident resulting in loss of Rs.51.00 lakh.

A Chennai based Divisional Office of Oriental Insurance Company Limited (Company) covered the properties of M/s. Chettinad Cement Corporation Limited, Chennai (Insured) under Industrial All Risk (IAR) policy for the period from April 1999 to March 2000. The properties covered included three meter gauge locomotives (locomotives). One of the covered locomotives met with an accident in June 1999 and the Insured preferred a claim (June 2000) for Rs.1.54 crore.

While processing the claim, it was noticed by the Company that the IAR policy specifically excluded railway locomotives. Therefore, the Company deleted (April 2001) the locomotives from the IAR policy and issued a fresh Special Contingency Policy (SCP) covering the three locomotives retrospectively from April 1999 and recovered the incremental premium (Rs.0.95 lakh). After issuing the policy post event, the Company settled the claim at Rs.51.00 lakh (March 2001).

The Management/Ministry stated (July 2004/August 2004) that the Insured had been taking SCP since 1986. With the introduction of IAR, which carried lower rates all the properties of the Insured were brought under IAR policy from April 1999. It further stated that after the loss was reported it came to notice that locomotives were specifically excluded under the IAR policy. Considering that the Company had issued the policy covering *inter alia* locomotives it would have been improper to disown the liability for the error committed by the underwriting office and thus, the Company had no alternative but to change the coverage of the affected items from IAR to Special Contingency Policy and settle the claim.

The reply is not tenable as the locomotives were not covered under IAR policy because of exclusion clause and SCP was not in existence at the time the accident occurred. No responsibility on the erring official was fixed even though the Company had directed (September 2000) its regional office to do so. Therefore, settlement of the claim by issuing SCP post event was not in order as retrospective coverage of the asset was irregular and resulted in a loss of Rs.51.00 lakh.

United India Insurance Company Limited

11.7.1 Loss due to issue of irregular policies

Due to providing Tailor Made Group Mediclaim Policies in violation of its own guidelines the Company suffered a loss of Rs.7.05 crore.

A Hyderabad based Divisional Office of United India Insurance Company Limited (Company) had been issuing Tailor Made Mediclaim Policy covering the employees of Dr. Reddy's Laboratories Limited (insured) since 2000 – 2001. The premium charged and the claims paid were as below:

(Rs. in crore)

Year	Premium charged	Claims paid
2000 – 2001	0.52	1.15
2001 – 2002	1.40	2.22
2002 – 2003	1.40	4.08
2003 – 2004	1.58	4.50
Total	**4.90**	**11.95**

According to the Company's circular (October 1999) all Tailor Made Policies whether existing or new were to be referred to General Manager (Technical) of the Company for consideration and written approval without which such policies /schemes could not continue or be issued even provisionally. The above policy was issued/renewed without the express approval of the General Manager (Technical), rendering the underwriting irregular. The payment of claims against this policy was, thus, irregular and resulted in an avoidable loss of Rs.7.05 crore being the excess of the claims paid over the premium received.

The Management accepted the lapse by stating (May 2005) that the Head Office did not approve the proposal due to oversight and the policy was discontinued when overall portfolio of the client became non-profitable. It was, however, observed in Audit that the Company continued to renew policies despite the fact that the overall portfolio of the insured was generating losses through the years 2000-2001 to 2003-04.

Thus, underwriting of Tailor Made Group Mediclaim policy in violation of its own guidelines resulted in an avoidable loss of Rs.7.05 crore.

The matter was reported to the Ministry in April 2005; its reply was awaited (November 2005).

11.7.2 Loss due to issue of irregular policies

The Company issued and renewed tailor-made group mediclaim policies to cover the existing and retired employees of an Insured in violation of its guidelines, which resulted in a loss of Rs.5.53 crore.

The exclusion clause of tailor-made group mediclaim policy (policy) of M/s. United India Insurance Company Limited (Company) includes coverage to pre-existing diseases when the cover incepts for the first time. Further, the Company's circular of December 2001 stipulates inclusion of pre-existing diseases in the policy from the third year of continuous insurance with it after loading the premium by 25 *per cent*.

A Bangalore based Divisional Office of the Company issued a policy to Bharat Electronics Limited (Insured) to cover the existing employees and their families from September 2002 to September 2003. Though it was the year of inception of the policy, the cover was extended to pre-existing diseases. Thereafter, the policy was renewed from time to time till March 2006 with the same cover. It was observed in Audit that extending cover to pre-existing diseases in the policy for the year 2002-03 (year of inception) and its subsequent renewals were in violation of the instructions of December 2001. Though

claim ratio of the previous years at the time of renewal of the policies for 2003-04 and 2004-05 were 299 *per cent* and 263 *per cent* respectively, the policies were renewed without obtaining approval from Head Office in terms of circular of December 2001. The Company paid claims of Rs.8.30 crore against the premium of Rs.3.66 crore collected during September 2002 to March 2005.

The Divisional Office had also been issuing the policy to the Insured on annual basis to cover its retired employees and their spouses since October 1997. Audit scrutiny revealed that the Divisional Office renewed (October 2002) the policy for the period from October 2002 to October 2003 without prior approval from the Head Office despite an incurred claim ratio of 141 *per cent* during the three preceding policy years excluding the immediately preceding year. This was contrary to guidelines issued by the Company and therefore, renewal of the policy was irregular. Besides, the Divisional Office while renewing (October 2003) the policy for the period from October 2003 to September 2004, granted cover for pre-existing diseases without charging additional premium, without the approval of the Head Office and in violation of the circular of December 2001. The Company settled claims of Rs.3.21 crore against the premium of Rs.2.32 crore during the period from October 2002 to September 2004.

Regarding policy for existing employees, the Management stated (May 2005) that the coverage of pre-existing disease could be allowed without any loading if the policy had been in existence for a period of three years or more. Further, it also stated that the policies were renewed with the verbal approval of the General Manager at Head Office who was empowered by the Board of Directors to deviate from the guidelines. The Ministry stated (October 2005) that the Company had to view the overall profitability of the Insured while computing the renewal premium and it was not advisable to load the premium on every policy to make it profitable. Regarding policies to the retired employees the Management stated (May 2005) that there was no need to load the premium for pre-existing diseases in respect of over three years continuous policies and renewals of policies was done with verbal approval. The Ministry stated (November 2005) that standard guidelines were not applicable to clients like the insured and endorsed the views of the Management.

The reply is not tenable as there was no documentary evidence to show that the verbal approval was obtained and at the time of underwriting the policies (September 2002) General Manager at Head Quarters was not empowered /authorised to deviate from the guidelines. Further, pre-existing diseases were included in the policy for the first year as against third year without requisite approval and in case of retired employees without collection of additional premium in violation of the Company's guidelines. The guidelines were applicable to all tailor made group mediclaim policies without exception as to the size of the group or the profitability of the entire portfolio of the insured.

Thus, issue and renewal of tailor made group mediclaim policies in violation of the Company's guidelines to the existing and retired employees of the Insured resulted in a loss of Rs.5.53 crore.

11.7.3 Loss due to under charging of premium

Failure of the Company to charge appropriate group mediclaim premium led to under recovery of premium amounting to Rs.3.09 crore.

United India Insurance Company Limited (Company) issued tailor made mediclaim policies to M/s. Motor Industries Company Limited (insured) for the period 1998 to 2004 covering their employees and families.

The Company's circular (September 1998) stipulates that standard mediclaim policy's terms and condition shall be followed in the Tailor Made Group Mediclaim Policy for corporate clients subject to deviations permitted therein. The Standard Group Mediclaim Policy stipulates loading of premium at the time of renewal for adverse claim ratio for the preceding three completed years excluding the year immediately preceding the year of renewal. The guidelines did not permit modifications to stipulation relating to loading for adverse claims experience of earlier policies. The loading criteria specified in the standard mediclaim policy, therefore, were applicable to this policy. As the claim ratio for the years 2002 to 2004 worked out to 183 *per cent*, 179 *per cent* and 98 *per cent*, the Company should have loaded the premium by 150 *per cent* for the policies issued during the years 2002 and 2003 and by 25 *per cent* for the year 2004. This was not done which resulted in under charging of premium by Rs.3.09 crore.

The Management stated (May 2005) that it was not possible to load the premium under non-tariff policies like mediclaim since overall portfolio of the insured was profitable and that the Company had been able to retain the client with great difficulty against stiff competition. The Management further added (August 2005) that in view of overall profitability it was not justifiable to follow the general guidelines and load the premium in individual policies based on the claim experience of that particular policy. The Ministry endorsed (October 2005) the views of the Management.

The reply is not tenable as the policies were not in line with the Company's own guidelines, which stipulated that terms and conditions of the standard group mediclaim policy should be applied and hence the premium should have been loaded accordingly.

Thus, failure to load the premium in accordance with guidelines resulted in loss of premium to the tune of Rs.3.09 crore.

11.7.4 Loss of revenue due to under-charge of premium

The Company suffered a loss of Rs.2.91 crore due to non-incorporation of premium adjustment clause in the agreement entered with Railways.

United India Insurance Company Limited (Company) entered into an agreement (July 1994 renewed in July 2003) with Indian Railways to insure the victims of accidents and untoward incidents under Section 123, 124 and 124A of Railways Act 1989. Accordingly, a Delhi based Divisional Office of the Company issued an insurance policy to Railways every year from August 1994.

The policy covered all passengers who were holding valid tickets/Railway passes, platform tickets and Railway men on duty. Thus, the liability of the Company was for the

actual number of passengers who travelled during the year and the premium received in the beginning of the year was required to be adjusted (based on the actual number of passengers) after the end of the year as per the normal practice intimated by the Company. The Company, however, did not have any premium adjustment clause to this effect in the agreement with the Railways and in the policy issued to them and therefore, could not succeed in making the Railways pay the differential premium of Rs.9.36 crore for the period August 1994 to July 2004. Though the Company had incorporated the clause in the policies issued to Railways for the period from August 2003 onwards, it did not incorporate this clause in the renewed agreement with the Railways (July 2003). The Railways, did not pay the differential amount even for periods subsequent to August 2003 in the absence of premium adjustment clause in the agreement.

Considering the fact that the policy was covered by the Company under re-insurance ranging from 30 *per cent* to 84 *per cent* (excluding General Insurance Corporation of India and inter group), the loss to the Company/group during the period August 1994 to July 2004 was Rs.2.91 crore.

The Management stated (June 2005) that the policy was re-insurance driven. As the re-insurers did not ask for premium adjustment clause, the Company was not expected to change the terms and conditions of the policy. Noting the Audit observation, re-insurers had been asked to incorporate the adjustment clause in future.

The reply is not acceptable as the Company inserted this clause in the policy issued to Railways in August 2003 without the approval of re-insurers. In view of the normal practice of adjusting the premium on the basis of actual number of passengers in such cases, it was in the Company's own interests to incorporate this clause in the agreement as well as policy issued to Railways since 1994.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

11.7.5 Loss due to belated submission of reinsurance claims

The Company failed to prefer reinsurance claims within the prescribed time under a scheme of settlement, which resulted in loss of Rs.49.00 lakh and non-recovery of Rs.62.00 lakh from a broker.

Reinsurance is an arrangement whereby an insurance company apportions a part of the risk underwritten to other insurance companies so that the loss, if any, could be recovered to the extent of reinsurance effected. United India Insurance Company Limited (Company) had reinsurance arrangement with both Indian and foreign reinsurers. M/s. Arig Insurance Company Limited, United Kingdom (Reinsurer) was one such reinsurer.

The Company was aware (June 2003) that the financial position of the Reinsurer was deteriorating and was advised by M/s. Castlewood (EU) Limited (Scheme Manager) to act swiftly in formulating their commutation proposal but did not initiate any action on this. Subsequently, the Scheme Manager informed (October 2003) the Company that a scheme arrangement for the creditors of the Reinsurer had been finalised whereby the Company (scheme creditor) had to submit information in respect of the claims against the

Reinsurer within 90 days from the effective date of the scheme viz. 30 September 2003. The deadline for submission of the claim in the prescribed format was 30 December 2003.

The Company preferred a claim for US$ 0.79 million on 24 December 2003 at the fag end of the deadline fixed for submission of claims. Thereafter, in July 2004, the Company preferred another claim for US$ 0.32 million, which had been omitted in the claim form. The Scheme Manager refused (July 2004) to include the claims. In September 2004, the Scheme Manager confirmed that no further payments would be made to scheme creditors by the scheme company in respect of scheme liabilities and notified the termination of the scheme on 23 September 2004. The Company received (September 2004) US$ 0.79 million for the claim submitted within the due date.

The Management stated (July 2005/September 2005) that:

(i) The Scheme Manager informed them during the third week of December 2003 about submission of the claim on or before 31 December 2003.

(ii) The commutation proposal received from the Reinsurer in June 2003 could not be processed since the scheme of arrangement was not provided and no guidelines/parameters were formulated to deal with such proposals.

(iii) Out of the claim of US$ 0.32 million made subsequent to the deadline an amount of US$ 0.11 million (Rs.49.00 lakh) remained recoverable from the Reinsurer and US$ 0.13 million (Rs.62.00 lakh) from its broker. The Company further stated that dues from the broker came to light only in June 2004 when the Company collected the details of amount outstanding from its broker for finalisation of accounts.

The Ministry endorsed (September 2005) the views of the Management.

The reply of the Management is not tenable as they had received communication about lodging of claims from the Reinsurer in October 2003 itself. The Company did not take necessary action for getting complete details of the scheme in time. Also in June 2003 itself the Scheme Manager had informed about the financial deterioration of the Reinsurer. In spite of it the Company failed to expedite procedures to lodge a comprehensive claim. Further non-maintenance of records relating to reinsurers also indicated system failure/ lack of internal controls as the Company solely depended on the brokers' records.

Thus, due to failure to initiate action at the opportune time and submit a comprehensive claim, the Company suffered a loss of Rs.49.00 lakh and could not recover Rs.62.00 lakh from the broker since 2002-03.

CHAPTER XII: DEPARTMENT OF HEAVY INDUSTRIES

Andrew Yule & Company Limited

12.1.1 Loss due to non-execution of work

Consequent upon acceptance of job without assessment of its financial capability and diversion of mobilisation advance for repayment of bank loan, the Company could not execute the work as per milestone. As a result the contract was terminated and the Company suffered a loss of Rs.85.34 lakh.

Andrew Yule & Company Limited (Company) entered into an agreement (February 2001) with Chennai Metropolitan Water Supply and Sewerage Board (CMWSSB) for execution of a work relating to the expansion of capacity of interceptors and pumping station in Thomas Road, Chennai and construction of new pumping station at South Boag Road, Chennai at a total value of Rs.11.02 crore. The work order and notice to proceed with the work were issued in December 2000 and February 2001 respectively. The main terms of the contract, *inter alia*, provided

(i) The work should be completed within 30 months.

(ii) The Company would pay liquidated damage at a prescribed rate for delay in attaining the scheduled completion date for the whole of the work or the milestone as stated in the contract, subject to a maximum of 10 *per cent* of the final contract price.

(iii) The Company would furnish bank guarantees (BG) of Rs.44.10 lakh for performance and Rs.1.10 crore against the receipt of interest bearing mobilisation advance of equivalent amount.

(iv) In case of failure to achieve two successive milestones, which constituted a fundamental breach of contract, the CMWSSB could terminate the contract and consequently 20 *per cent* of the value of the unfinished work would be recovered from the Company.

(v) The contractor was to use the advance payment only to pay for equipment, plant and mobilisation expenses required specifically for execution of the works and demonstrate that the advance payment had been used in this way by supplying copies of invoices or other documents to the Engineer.

The Company received mobilisation advance of Rs.1.10 crore in March 2001 and furnished the two BGs of Rs.44.10 lakh (February 2001) and Rs.1.10 crore (March 2001) for performance and advance payment respectively.

The Company diverted (March 2001) the mobilisation advance towards repayment of working capital loan. Against the committed value of work of Rs.2.58 crore to be done by December 2001, the Company actually executed work of Rs.5.92 lakh. It could not execute the work as per schedule and failed to achieve two successive milestones. Consequently, the work was terminated in May 2002. However, the termination was revoked (June 2002) on commitment to execute the work as per schedule and to furnish additional BG of Rs.60.00 lakh towards security and interest on mobilisation advance. The Company, however, again failed to complete the job as per commitment as well as to furnish additional BG. The work was finally terminated (October 2002) and both the BGs of Rs.1.10 crore and Rs.44.10 lakh were encashed (December 2002) by CMWSSB. The Company's appeal to stop the encashment of BGs was rejected (December 2002) by the Court and CMWSSB was directed by the Court to deposit the amount of BGs in an interest bearing fixed deposit. The CMWSSB also preferred a claim of Rs.2.99 crore towards interest on mobilisation advance, cost of unfinished work, liquidated damages etc., after adjusting the BG of Rs. 44.10 lakh. The Company opted for arbitration.

The Management while accepting (April 2005) the facts of non- execution of work due to financial weakness further stated that the termination of the contract was wrong and the matter was under arbitration. The contention of the Management is not acceptable as termination took place due to fundamental breach of contract as per agreement and consecutive failure to execute the work as assured. Further, the appointment of Arbitrators was yet to be finalised (April 2005).

Thus, due to acceptance of contract without assessment of financial capability to execute the work, subsequent diversion of mobilisation advance for repayment of bank loan and consequent non-execution of work, the Company had to suffer a loss of Rs. 85.34 lakh[♣] and is facing a claim of Rs.2.99 crore.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

Bharat Heavy Electricals Limited

12.2.1 Loss of Rs.12.40 crore due to delay in supply

The Company suffered a loss of Rs.12.40 crore on account of payment of liquidated damages and penal interest because of delay in supply of equipment and spares, caused due to incorrect assessment of shop floor needs.

Bharat Heavy Electricals Limited (Company) received (May 1990) orders from M/s. Tamil Nadu Electricity Board (TNEB) for the supply and erection of steam turbine generator and turbo generator along with supply of spares for North Chennai Thermal Power Project (unit III) of 210 MW at a total price of Rs.113.27 crore. The equipment were to be delivered by the Company to suit the commissioning of unit III by November 1993. In case of delays, the Company was liable to pay liquidated damages (LD) of 10

[♣] *Rs.44.10 lakh value of bank guarantee encashed plus Rs.8.55 lakh value of work not accepted by CMWSSB plus Rs.25.69 lakh expenses on maintenance of letter of credit plus Rs.13.21 lakh liability toward contractor minus Rs.6.21 lakh value of work accepted by the CMWSSB*

per cent of the contract price as well as interest at the rate of 18 *per cent* on the unadjusted portion of advance beyond the stipulated delivery schedule.

For execution of the contract, the Company allocated various works among its units[♣]. The major works to the extent of Rs.51.95 crore and Rs.33.19 crore were to be executed by Trichy and Hardwar units[♦] respectively.

It was observed in Audit that there were substantial delays on the part of the Company to supply the equipment and spares. While Trichy unit could complete the supply of the spares only in June 2000, i.e. with delay of more than six years, Hardwar unit completed the supply of the equipment in March 1995 and of spares by September 1997, but replenished the shortages till the year 2001, i.e. with a delay of more than four years from the date of commissioning of the unit. The main reasons for delays were identified as manufacturing problems in shop floor, such as bunching of various orders.

As a result, unit-III could be commissioned in November 1996 after a period of more than three years from the scheduled date of commissioning. Accordingly, TNEB deducted a sum of Rs.10.89 crore progressively (from March 1992 to December 1999) on account of LD and recovered Rs.1.15 crore, being the interest on the unadjusted portion of advance against the delayed supplies, besides recovering an amount of Rs.36.00 lakh on account of short closed items of spares, as the Company could not supply some of the spares.

As the reasons for delay were mainly attributed to the Company and there was no scope for legal action for recovery of the amount of Rs.12.40 crore, the Company wrote off (April 2004) the amount from its books of accounts for the year 2003-04.

The Management/Ministry contended (July/September 2005) that various factors such as delay on the part of TNEB in providing infrastructure facilities, constraints of funds faced by TNEB and foreign exchange crisis contributed to the delay in manufacturing of the equipment. They added that new measures had been taken to correctly assess the requirements at the shop floor and improve delivery.

The reply is not tenable, as while writing-off the amount from the books of accounts, the Company identified the manufacturing problems in the shop floor as the main reason for delay. Further, the fact that the units were advised to carefully assess the shop floor needs while bidding in future, indicated that the Company could not correctly assess the shop floor needs in this case.

Thus, the Company incurred a loss of Rs.12.40 crore in execution of this contract mainly due to incorrect assessment of shop floor needs.

[♣] *Hardwar, Hyderabad, Bangalore, Trichy, Bhopal and Jhansi*

[♦] *after deletion of short closed spares*

12.2.2 Loss due to delay in completion of work

Though the Company had obtained a contract below cost, it did not take advance manufacturing action and could not adhere to the delivery schedule and thus incurred a loss of Rs.1.32 crore on account of liquidated damages imposed by the Customer. Overall, the Company incurred loss of Rs.7.66 crore in the execution of the contract.

In response to a tender issued by M/s. Bannari Amman Sugars Limited (Customer) for its plant at Sathyamangalam, Bharat Heavy Electricals Limited (Company) submitted (October 2000) its bid for supply, erection and commissioning of one 20 MW turbine generator (TG) set and one 120 tonne per hour high pressure boiler. After opening of bids, all the bidders were called (November 2000) for negotiations, during which the Customer informed the Company that for the same scope of TG set the other two bidders had quoted lower price and asked the Company to match the lowest price. In order to prevent the entry of foreign firms in the sugar industry and to have additional load on the shop floor, the Company decided to accept the order at below cost. The order for the boiler was also quoted and accepted at below cost due to stiff competition in the market in this segment.

The Customer placed the letter of intent (LOI) in November 2000 at a total price of Rs.26.31 crore (excluding taxes and duties). Against the contractual commissioning date of 14 May 2002, the Company could commission the project on 26 August 2002 at a cost of Rs.32.65 crore with delay of more than three months and a cost overrun of Rs.6.34 crore.

The main reasons for delay were delay in receipt of casing from its Hardwar unit, delay in removing the defects in casing and delay in finalising equipment and composite piping layout. In view of the delay in the commissioning, the Customer levied liquidated damages (LD) and withheld (August 2002) an amount of Rs.1.32 crore. The Company's request for waiver of LD was turned down by the Customer (October 2003). It was observed that though the Company had obtained the contract below cost, it did not take timely action to place internal order for the casing in an effort to adhere to the delivery schedule.

While accepting that there had been cost overrun and overall loss, the Management stated (April/October 2005) that every steam turbine for sugar segment was a tailor made item and it took some time to sort out problems in the drawings which were to be finalised at the detailed engineering stage. They added that there was a net contribution of Rs.69.27 lakh after taking into account all variable cost and LD and actions had been taken for design standardisation and automation to avoid recurrence of such problems in future. It was also stated that efforts were being made to get LD waived.

The reply is not tenable as during the process of according ex-post facto approval, the Management laid (February 2002) emphasis on compressing the delivery time in such a way that no LD was imposed. Even then, no advance manufacturing action (such as advance procurement of materials, finalisation of design, etc.) for the project was taken in an effort to compress delivery time. Further, the Management considered all factory and administrative overheads as fixed cost in working out the contribution, which was not

appropriate, since a part of these overheads happened to be variable in nature as per the estimates prepared by the Management for obtaining the contract. It was also observed that the actual loss incurred by the Company exceeded the loss estimated at the time of obtaining the contract. As regards waiver of LD, the Customer had not released the amount of Rs.1.32 crore towards LD for more than three years (September 2005).

Thus, had the Company taken advance manufacturing action, it could, at least, have avoided loss to the extent of Rs.1.32 crore on account of LD. Overall, the Company incurred loss of Rs.7.66 crore in the execution of the contract.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

12.2.3 Avoidable payment of interest of Rs.6.14 crore due to short payment of advance tax

The Company's failure to assess the advance tax liability resulted in avoidable payment of interest of Rs 6.14 crore.

As per the Income Tax Act (IT Act), advance tax as calculated on the current income is payable in four instalments falling on or before 15 June, 15 September, 15 December and 15 March of each financial year. In case the assessee did not pay advance tax or underestimated the instalment of advance tax, interest at the rate of one *per cent* per month (1.25 *per cent* prior to 7 September 2003) was payable under section 234C of the IT Act. However, no interest is payable if the amount of advance tax paid is not less than 12 *per cent* and 36 *per cent* of the tax due in the first and second instalments respectively.

A review of the income tax returns filed by Bharat Heavy Electricals Limited (Company) revealed that there was shortfall in payment of advance tax ranging between Rs.11.58 crore and Rs.49.92 crore during the assessment years (AY) 2003-04 and 2004-05. It was observed that underestimation of advance tax was due to improper estimation of some items of income and expenditure. As a result, the Company had to pay an amount of Rs.6.14 crore as interest under section 234C on short-payment of advance tax for AY 2003-04 and 2004-05.

While accepting (May 2005) the Audit observation for future, the Management stated (October 2005) that taxable income for AY 2003-04 increased due to (i) increase in the amount of the provisions (net) as compared to estimates, (ii) increase in disallowances and (iii) reduction in the amount of deductions assumed under section 80 HHB. The increase in the taxable income for AY 2004-05 was attributed to (i) increase in the order booking and turnover over the anticipated levels, (ii) increase in provisions (net) and (iii) unbudgeted payout under voluntary retirement scheme (VRS).

The reply is not tenable on account of the following:

(i) Underestimating the provisions had no implication as taxable income was calculated without considering the provisions.

(ii) Main component of the disallowances was the leave encashment. Though the expenditure on leave encashment was allowed as deduction on actual payment basis from AY 2002-03 instead of on actuarial basis, the Company did not consider the same in working out the tax liability.

(iii) The deduction under section 80 HHC should have been considered separately under sections 80 HHB and 80 HHC because of different methods of calculation.

(iv) Although the Company was anticipating high level of orders during AY 2004-05, it did not fix the turnover target accordingly.

(v) VRS scheme was introduced by the Company in May 2003 and therefore the estimated amount of VRS payment could have been considered while calculating the advance tax in June and September 2003.

As such, while assessing the advance tax liability, suitable provision for variation in estimates was needed, besides paying sufficient tax during initial instalments to avoid payment of interest.

Thus, the Company's failure to assess the advance tax liability correctly resulted in avoidable payment of interest of Rs.6.14 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

12.2.4 Violation of environmental norms

Due to delay of more than five years in commissioning of Air Pollution Control System, the Company continued to ignore the health and safety of local surroundings in violation of environmental norms. Besides, an amount of Rs.2.57 crore remained blocked for more than two years.

The Central Foundry Forge Plant (CFFP), Hardwar, a metallurgical unit of Bharat Heavy Electricals Limited (Company), is engaged in the production of plain carbon and alloy steel castings and forging of various shapes and sizes. CFFP has three Electric Arc Furnaces and it is obligatory in terms of Environmental (Protection) Rules, 1986 and Air Pollution Act, 1981 to install an Air Pollution Control System (APCS) to reduce the air pollution to an acceptable level.

The Uttar Pradesh Pollution Control Board (UPPCB) had been raising the issue of air pollution with the Company since 1996. During a meeting with UPPCB in March 1998, the Company committed that order for APCS would be placed by June 1998 and APCS commissioned by December 1999. However, only in June 1999, the Company placed the order on its unit, Boiler Auxiliaries Plant (BAP), Ranipet, for design, engineering, manufacture, supply and commissioning of Fume Extraction and Dust Collection System (i.e. APCS) for Rs.3.25 crore. The delivery was to be completed by 15 February 2000 and the system commissioned by 15 May 2000.

It was observed in Audit that though CFFP had awarded the order in June 1999, it finalised the capital investment proposal for Fume Extraction and Dust Collection System

(Rs.5.97 crore) in May 2000. The proposal was, however, approved by the Board of Directors in January 2003 due to inordinate time taken by the Company on unsuccessful efforts to reduce the cost and studies conducted for energy savings. In the mean while, BAP had supplied material worth Rs.2.57 crore between March 2000 and September 2000. Even after completion of the civil work in October 2003, APCS could be commissioned in June 2005 only, with a delay of more than five years from the commissioning schedule of December 1999, at a total cost of Rs.5.54 crore. As a result, the Company continued to ignore the health and safety of local surroundings for more than five years and violated environmental norms. Besides, the amount of Rs.2.57 crore incurred on materials remained blocked for 27 months from October 2000 to December 2002.

The Management stated (February/October 2005) that the time taken for approval was necessary due to criticality of the system and the quantum of investment involved and due to the efforts made to reduce the cost of the project and studies conducted for energy savings. Delay in erection was attributed to non-deployment of adequate manpower by the sub-contractors, as also delays in a few critical supplies of material.

The reply is not tenable as no urgency was shown by the Company to install the pollution control equipment. Though the Company gave commitment to UPPCB to commission APCS by December 1999, an inordinate time of more than 41 months was taken in finalising and approving the capital investment proposal and an ISO 14001 certified Company ran its arc furnaces till June 2005 without meeting legal requirements.

Thus, due to delay of more than five years in commissioning of APCS mainly due to belated approval of the proposal, the Company continued to ignore the health and safety of local surroundings and violated environmental norms Besides, an amount of Rs.2.57 crore remained blocked for more than two years.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

12.2.5 Loss due to unrealistic estimates

Instead of achieving the anticipated profit of Rs.2.40 crore, the Company suffered a loss of Rs.2.38 crore in the production of motors mainly due to under-estimation of manhours required for completion of work.

M/s. Kirloskar Brothers Limited (KBL) placed (April 2000) an order on Bharat Heavy Electricals Limited (Company) for supply of 10 pump motors at a total sale price of Rs.7.04 crore at the rate of Rs.67.50 lakh per motor, along with spares of Rs.28.48 lakh. The delivery was to be completed by February 2002. Internal order for production of the motors was given (May 2000) to Heavy Electricals Equipment Plant (HEEP), Hardwar, which completed the supply in September 2002.

The Company had estimated the cost as Rs.4.35 crore with an anticipated profit of Rs.2.40 crore on manufacturing of these motors. However, a review of cost sheet of the motors revealed that the Company manufactured and supplied the motors by incurring

expenditure of Rs.9.13 crore, against the sale price of Rs.6.75 crore. The increase in cost of production was attributable to the following reasons:

(i) The Company took excessive manhours (55,771) for completion of the order. The manhours were higher by 24,914 (80.74 *per cent*) as compared to the estimated 30,857 manhours (after considering efficiency factor). This resulted in abnormal increase in manufacturing overhead and direct labour charges.

(ii) Actual consumption of direct material increased to Rs.3.21 crore against the estimated cost of Rs.2.58 crore.

(iii) Due to increase in the manufacturing cost, commercial and administrative overheads also increased by more than 180 *per cent*.

It was observed that there was under-estimation of manhours required for completion of the work as well as excess consumption of materials. Resultantly, the Company suffered a loss of Rs.2.38 crore, against the estimated profit of Rs.2.40 crore.

The Management stated (May 2004 and August 2005) that:

(i) These motors were the first of its type and because of design complexity, it took more time to establish the motors at shop floor.

(ii) Labour rates increased by 50 *per cent*, causing excessive labour and overhead charges due to wage revision.

(iii) The Company recovered direct and variable cost as well as part of overheads and there was no direct loss.

The reply is not tenable on account of the following:

(i) During the execution stage, the Company re-worked the required manhours to 46,441 against the estimated figure of 30,857. The vast variation between the initial and revised estimates indicated that the initial estimates, which formed the basis for quoting the rates, were unrealistic. Even then, the Company could not complete the work within the revised estimated manhours and utilised 55,771 manhours.

(ii) Actual increase in labour rate was 28 *per cent* only till the scheduled date of supply (by which seven motors had already been delivered).

(iii) As per the cost data provided by the Management, the Company incurred manufacturing cost of Rs.7.96 crore after taking into account all direct cost and manufacturing overheads, against the sale price of Rs.6.75 crore. Accordingly, it could not recover even the manufacturing expenditure.

Thus, the Company could not achieve the anticipated profit of Rs.2.40 crore and instead suffered a loss of Rs.2.38 crore in the production of motors due to under-estimation of manhours and excess consumption of materials.

The matter was reported to the Ministry in April 2005; its reply was awaited (November 2005).

12.2.6 Avoidable expenditure of Rs.1.75 crore towards interest for delayed payment of differential customs duty

Despite instructions of Corporate Office for payment of differential customs duty, the unit delayed its payment, which resulted in levy of interest by the Customs and consequent avoidable expenditure of Rs.1.75 crore.

The Company entered into (March 1999) two separate contracts with M/s. Sujana Power Limited (Customer) for supply of four Gas Turbine Generators and two Steam Turbine Generators along-with associated equipment at a total price of Rs.125.23 crore plus US$ 23.77 million (equivalent to Rs.101.66 crore). With regard to commencement of work, clause 3.2.5 of the contract provided that if a notice to proceed (NTP) was not issued by 31 December 1999, either party would have the right, in its sole discretion, to terminate the contract in which case neither party would incur any liability of any kind to the other party in relation thereto. As a part of advance manufacturing action, the Heavy Power Equipment Plant, Hyderabad (unit) imported material valuing Rs.36.42 crore between January 1999 and August 1999 without issuance of NTP[•]. As the project had been classified under Project Import category by Customs at the request of the Company, the imported material was cleared on payment of concessional customs duty of Rs.8.16 crore on provisional basis. The Customer did not issue the NTP by the stipulated date and terminated the contract.

In view of the termination of the contract, the Corporate Office advised (June 2001) the unit to immediately pay the differential duty and take necessary steps for the alternative use/disposal of the material. While the unit diverted (September 2001/March 2002) the material to the other projects and also informed (June 2003) the Customs Department, it did not immediately pay the differential duty on that material. It paid the same in three instalments: Rs.7.55 crore in June 2003, Rs.3.89 crore in March 2004 and Rs.1.65 lakh in July 2004.

On account of the delay in payment of duty the Customs Department demanded (October 2004) payment of interest at the rate of 15 *per cent* towards delayed payment of differential duty. The unit accordingly paid (December 2004 and January 2005) an amount of Rs.6.68 crore.

It was observed in Audit that the unit could have saved Rs.1.75 crore[♣] had it paid the differential duty in June 2001 itself in keeping with the advice of the Corporate Office.

The Management in its reply (July 2005) accepted that the Corporate office did advise for payment of differential duty in the month of June 2001, however, the same was not acted

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[•] *The lapses of the Management on this account were reported vide para 13.2.2 of the Audit Report No. 3 of 2003, Union Government (Commercial) of the Comptroller and Auditor General of India.*

[♣] *Difference between the amount of interest paid to Customs and amount of interest incurred on cash credit or earned on short term deposits*

upon immediately as the goods imported under project imports were assessed provisionally and hence no interest was payable till the finalisation of the assessment as per Section 18 of the Customs Act, 1962 and the Customs Department had not issued any directives to the Company for finalisation of the provisional assessment in this case. It added that the unit made a profit of Rs.51 Crore in the projects for which it had diverted the materials after taking into account the payment of differential duty and interest thereon.

The reply of the Management is not tenable because the benefit of concessional custom duty was no longer available after termination of the contract in December 1999 on account of which the Corporate Office had categorically directed the unit in June 2001 to pay the differential duty without any delay. Thus, there was no justification in delaying the payment of the same for more than two years. The argument that the unit earned profit of Rs.51 crore on other projects is also not relevant as the point still remains that the Company could have saved Rs.1.75 crore on payment of interest and the profit would have been that much higher.

Thus, the failure of the unit to pay the differential duty even after the decision of its Corporate Office resulted in avoidable expenditure of Rs.1.75 crore.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

12.2.7 Loss due to faulty preparation of estimates and delay in execution of the contract

Due to failure to estimate the workable cost and adhere to the completion schedule, the Company incurred a loss of Rs.96.86 lakh in the execution of a contract.

The Oil and Natural Gas Corporation Limited (Customer) entered into (June 2000) an agreement with Bharat Heavy Electricals Limited (Company) for revamping of chemical injection system at WIN♣ and ICW off-shore platforms on turnkey basis at a lumpsum price of Rs.4.56 crore (inclusive of all taxes and duties). The work was to be completed by December 2001, failing which liquidated damages (LD) to an extent of 10 *per cent* of the contract price was leviable by the Customer.

The Company completed the work in March 2003 at an actual expenditure of Rs.4.90 crore with a delay of more than 14 months. An analysis of the cost data revealed that while preparing original estimates, the Company had not considered various vital elements, such as GRE pipes and fittings (additional), experts' visit, motor and accessories, valves SS, rota meter, etc., having an overall impact of Rs.2.11 crore♣ on the estimated cost, indicating that the estimates, which formed the basis for quoting the bids, were not prepared with due care. Further, the Company had to pay LD of Rs. 45.62 lakh

♣ *Water Intake North*

♣ ***GRE pipes and Fittings (additional) Rs.56.69 lakh, charges towards experts visit (Rs. 24.24 lakh), Motor & Accessories (Rs.15.40 lakh), Valves SS (Rs.15.99 lakh), Rota meter (Rs.15.63 lakh) CEIL pump inspection (Rs.16.63 lakh), third party inspection (Rs.10.19 lakh) and other items (Rs.56.44 lakh)***

for delay which was attributable to delay at design and engineering stage as well as in finalisation of suitable vendors for supply of necessary equipment.

Further, the Company could not bill and receive a sum of Rs.94.61 lakh for more than 30 months, because certain deficiencies, as noticed by the Customer during the commissioning, were still to be rectified (September 2005). Resultantly, it suffered loss of interest amounting to Rs.17.24 lakh on the un-billed amount upto September 2005, which would increase further till the matter is resolved.

Thus, the Company not only failed in estimating the workable cost, it could not also adhere to the completion schedule, due to which it suffered a loss of Rs.96.86 lakh (Rs.34.00 lakh plus Rs.45.62 lakh plus Rs.17.24 lakh).

Though the Company lodged (August 2003) a claim of Rs.88.32 lakh with the Customer on account of subsequent changes in specifications and increase in scope of work and requested for waiver of LD, the same had not been accepted by the Customer for more than two years (September 2005).

While accepting that there were errors in the estimates, the Ministry stated (October 2005) that it was the first order of its type and the Company did not have any previous experience. They added that the matter was being pursued with the Customer to accept the claim.

The reply is not tenable because while accepting such an order for the first time, greater care was needed in finalising the design and estimating the cost, particularly when the contract was accepted on lumpsum price basis and the agreement required the Company to carry out any upward revision and additions of quantities/specifications without any time and cost effect to the Customer. As regards the claims lodged by the Company, the Customer had not accepted the same for more than two years (September 2005).

Thus, the Company suffered a loss of Rs.96.86 lakh due to faulty preparation of estimates and delay in execution of the contract.

12.2.8 Loss of Rs.95.46 lakh in the execution of a work

The Company undertook renovation and modernisation of a thermal station without undertaking any detailed study before agreeing on the scope of work and guaranteed performance of the same, which resulted in an additional expenditure of Rs.64.07 lakh and liquidated damages of Rs.31.39 lakh.

The Company obtained (July 1998) an order for Renovation and Modernisation (Rand M) of the third and fourth Units (110 MW each) of Ennore Thermal Station under refurbishment scheme of Tamil Nadu Electricity Board (TNEB). Power Sector Southern Region (PSSR) of the Company was entrusted (Internal Order August 1998) with dismantling, erecting, commissioning, testing and conducting performance guarantee test as a package work for Rs.15.26 crore. The scope of work and the scheme reports for the refurbishment were identified and formulated by TNEB on the basis of Performance Evaluation Reports with a view to achieve a Plant Load Factor (PLF) of 80 *per cent*. The

fourth and third units were to be erected and commissioned by June 2000 and October 2000 respectively.

After refurbishment, the fourth unit was commissioned and synchronised in November 2000. However, the unit had to be shut down (May 2001) due to various technical snags and its inability to take full load of 110 MW. The third unit was commissioned and synchronised (March 2001) but it also faced similar problems. In the process, PSSR incurred an additional expenditure of Rs.64.07 lakh towards modifications in the third unit. Although no modification work was taken up on the fourth unit till August 2005, an expenditure of Rs.24.10 lakh was estimated (July 2002) by PSSR for modification work on this unit also. On account of the delay, TNEB levied (September 2001) liquidated damages of Rs.1.16 crore against which PSSR had made a provision for Rs.31.39 lakh in the accounts of 2004-05. Further, due to its inability to run the plant at full load continuously, PSSR was yet to realise Rs.4.28 crore from TNEB.

It was observed in Audit that as per the guidelines of Central Electricity Authority (CEA), the thermal power units, which had completed 25 years of life or run one lakh operating hours, whichever was earlier, needed to undergo comprehensive Residual Life Assessment (RLA) studies before starting any R and M work. It was, thus, imperative that the scope of work was decided based on a comprehensive RLA study before the Company made any commitment about performance guarantees.

The Management replied (August 2005) that guidelines of CEA regarding RLA studies were issued only in June 2000 and the tender specification for the contract was issued by TNEB in 1997.

The reply is not tenable as the Company was aware of the importance of RLA studies as it had conducted the same in the year 1995 for both boiler and turbine portion of a power plant of Andhra Pradesh Electricity Board. Moreover, the Company being a major manufacturer of power equipment with many years of experience in the sector, should have been aware that guaranteeing performance parameters in a limited R and M job of the power plant whose economic design life was over, without ascertaining the condition of the plant through detailed RLA studies, was fraught with risk.

As the Company undertook R and M work without detailed RLA studies and guaranteed performance parameters, it had to carry out additional works and modifications at an expenditure of Rs.64.07 lakh till August 2005. Besides, delay in proving performance parameters resulted in liquidated damages of Rs.31.39 lakh and non-realisation of Rs.4.28 crore.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

12.2.9 Inordinate delay in writing off bad debts and resultant delay in availing deduction of corporate tax led to avoidable loss of interest of Rs.47.05 lakh

Even after rejection of various claims by the Director General of Foreign Trade in the year 1998, the Company took four years and nine months to write off the same from the accounts and suffered a loss of interest of Rs.47.05 lakh.

The Heavy Power Equipment Plant (unit) of the Company registered claims amounting to Rs.4.50 crore during 1989-90 with Joint Director General of Foreign Trade (JDGFT), Hyderabad for reimbursement of cash compensatory support, duty draw back and central excise duty rebate on the supplies made to the deemed export projects as per the EXIM Policy prevailing at that time. The unit recognised these claims as income in its accounts of that year. As the amount was not forthcoming, it made a provision of Rs.4.19 crore in 1992-93 and Rs.30.64 lakh in 1995-96 for doubtful debts. In May 1998, Director General of Foreign Trade finally rejected the claims.

Under the provisions of Section 36(1) (vii) (b) of the Income-Tax Act 1961, amount of any debt or part thereof is allowed as deduction if it is written off as irrecoverable in the accounts of the assessee in the previous year. The Company could have availed a deduction of Rs.4.50 crore from its business income, had it written off the amount in 1998-99 itself when the final decision of the DGFT was received and saved Rs.1.57 crore (at the rate of 35 *per cent*) towards income tax for the assessment year 1999-2000. Instead, it wrote off the same in 2003-04 i.e. after a delay of four years and nine months for claiming the income-tax deduction, while during this period it borrowed money from the market.

The inordinate delay in writing off a clear bad debt and availing related income tax benefit resulted in an avoidable interest payment of Rs.47.05 lakh on borrowed funds during the period 1998-99 to 2002-03.

The Management stated (April 2005) that the unit could not take decision and obtain approval of the competent authority for the write off proposal within time due to the *en masse* changes in administrative set up at various levels consequent to the introduction of Voluntary Retirement Scheme (VRS) in the Company.

The reply of the Management that *en masse* retirements caused the delay is not correct as the unit did put up proposals for writing off various other cases at the end of each annual accounts during the same period and these were approved by the competent authority.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

Bridge and Roof Company (India) Limited

12.3.1 Loss in execution of a job

The Company accepted a job without a realistic assessment of the work involved and failed to execute it in time, resulting in time and cost overruns leading to a loss of Rs.2.04 crore.

Bridge and Roof Company (India) Limited (Company) quoted (January 2000) Rs.12.59 crore for construction of retail/ jubilee outlets at seven different locations in response to a tender floated by Indian Oil Corporation Limited (IOCL). The Company accepted the job (February 2000) at a negotiated price of Rs.11.51 crore which was lower than even the lowest bidder's price by Rs.20.00 lakh. The work order was received by the Company in March 2000. The main terms and conditions of the contract *inter alia* provided that the

work was to be completed within 12 weeks from the date of handing over of site failing which the contractor would be liable to pay compensation for delay at the rate of one *per cent* per week subject to a maximum of 10 *per cent*. It also stipulated that the quantity as mentioned in the contract was not the final quantity and only indicative. The actual quantities had to be worked out by the tenderer based on the final design and approval. Quantities could increase for which no additional amount was payable.

Though the scheduled completion time was extended to November 2000 (six locations) and January 2001 (one location), the Company could complete the job with delays ranging from five to seven weeks on four locations.

It was observed in Audit that the Company incurred an expenditure of Rs.12.58 crore in executing the job against an estimated expenditure of Rs.10.07 crore. The final value of the work executed was determined as Rs.10.95 crore after adjusting towards the value of the extra work done by the Company and deduction for non/less execution of work items in the contracted price of Rs.11.51 crore. Thus, the Company suffered a loss of Rs.1.63 crore on the execution of the job (Rs.12.58 crore less Rs.10.95 crore) against an estimated site contribution of Rs.1.44 crore. In addition IOCL levied Rs 41.00 lakh as liquidating damages raising the loss to Rs.2.04 crore. Out of Rs.10.95 crore that was due, the Company received Rs.10.46 crore till March 2005 and another sum of Rs. six lakh was expected to be received.

While accepting the loss on the project, the Ministry explained (February 2005) that the main reason for cost overrun was that the quantity of estimate done by the Company inhouse at the time of tendering turned out to be on the lower side as compared to the quantity of estimate done by the Consulting Engineer after award of contract. The time overrun was attributed to inexperience and lack of coordination with the customer. Further, it was stated that this was a new type of job in which the Company had ventured for the first time for opening up new areas of business.

The contention of the Ministry is not acceptable as the Company has been engaged in the construction business for a long time and more than 75 *per cent* of the work involved in the job was of civil nature. The Company has also not derived any other benefit from the experience, as it has not been able to get similar orders from other companies.

Thus, the Company suffered a loss of Rs.1.63 crore due to preparation of unrealistic estimates and Rs.41.00 lakh due to delay in completion of job despite extension in execution period.

National Instruments Limited

12.4.1 Wasteful investment on a rehabilitation scheme

Improper formulation and implementation of a rehabilitation scheme resulted in failure of the scheme with consequent wasteful investment of Rs.2.41 crore.

National Instruments Limited (Company) was referred to Board for Industrial and Financial Reconstruction (BIFR) in 1992. A rehabilitation scheme of Rs.34.31 crore, which consisted of modernisation, renewals and diversification of plant and machinery,

payment to pressing creditors, provision for working capital and cost of Voluntary Retirement Scheme (VRS), was sanctioned in November 1999 by BIFR. Out of this Rs.4.23 crore was for modernisation and diversification, Rs.11.87 crore for working capital and Rs.18.21 crore for meeting cost under VRS.

The sources of finance to meet the total cost were (i) Rs.2.63 crore as contribution from Government of India to partially meet the cost of modernisation and diversification (ii) Rs.13.47 crore to be arranged by the Company from the sale of surplus land to meet the remaining cost of modernisation and diversification and the balance to meet the requirement for working capital (iii) and Rs.18.21 crore to be released as VRS fund by Government of India. With the above funding pattern the Company had projected that it would achieve sales ranging from Rs.11.57 crore in the first year to Rs.23.96 crore in the seventh year.

While the Government of India released (March 2000) Rs. two crore out of its share of Rs.2.63 crore immediately on approval of the Scheme, the Company failed to fulfil its commitment of arranging fund from the sale of land and sold only one plot for Rs.4.68 crore. Its sale proceeds were utilised by the Company to meet a part of their pressing liabilities and normal retirement dues of the employees. The Company also went ahead and incurred an expenditure of Rs.2.41 crore till March 2001 towards modernisation, repair and renewal programme. No further expenditure was committed nor any investment made beyond 2000-01. The BIFR concluded (September 2002) that the Company was not likely to become viable on long term basis and recommended winding up of the Company.

It was observed in Audit that the formulation and implementation of the rehabilitation package was faulty because of the following:

(i) The Company had projected unrealistic targets of sale of Rs.11.57 crore to Rs.23.96 crore where the actual sale of the Company in 1999-2000 and 2000-2001 was only Rs.2.94 crore and Rs.5.34 crore respectively. The unrealistic projection was borne out by the poor performance of the Company for the first two years after the rehabilitation package came into effect. The Company in the years 2001-02 and 2002-03 achieved sales of Rs.6.36 crore and Rs.6.23 crore but also registered an increasing loss.

(ii) As against the planned capital investment of Rs.4.23 crore in modernisation and diversification, the Company invested only Rs.2.41 crore and was operating with negative working capital during these years as it failed to arrange for working capital required through sale of surplus land as envisaged in the rehabilitation scheme.

(iii) The original proposal for modernisation included, *inter alia,* replacement of the existing CNC milling machine for increasing productivity. However, the company chose to procure one vacuum coating machine for Rs.30.27 lakh, which was not a part of the original scheme and was since lying idle. Further the Company procured a CNC Lathe machine for Rs.21.04 lakh which was also lying idle.

The Management explained (June 2003) that the vacuum coating machine was purchased in anticipation of a defence order, which had not materialised (August 2005) and that under the VRS, most of the skilled workers who were to operate the machines left the Company. Thus, due to the absence of any order and non-availability of working capital and skilled workers, neither of the machines could be utilised. The Management's plea regarding most of the skilled workers opting for VRS was not tenable as against 424 employees envisaged as opting for VRS, actually 748 employees were relieved under VRS between 1998-1999 and 2003-2004 indicating poor resource planning. As the Company could not be revived as per the rehabilitation scheme, the entire capital expenditure of Rs.2.41 crore was wasteful.

While accepting the fact of the failure of Rehabilitation Scheme, the Ministry stated (December 2004) that the major reason for failure was acute shortage of working capital. The Ministry's views are not acceptable as the revival scheme itself was unrealistic as there was no firm tie up for the disposal of land which was to be the major source of fund for the working capital of the Company. The Government on its part, had approved the Rehabilitation Scheme and released fund hastily without adequate assessment of the viability of the Company after the proposed modernisation vis-à-vis status of funding arrangement and order book position nor had it carried out proper monitoring of the progress of the Modernisation Scheme as was necessary.

Praga Tools Limited

12.5.1 Non-adoption of market rate while selling land resulted in loss of Rs.52.11 lakh

The Company did not consider the market value while selling the land to another Company which resulted in a loss of Rs.52.11 lakh.

Praga Tools Limited (Company), which was declared sick by the Board for Industrial and Financial Reconstruction (BIFR) in May 1999 got the approval of BIFR (February 2001) to sell its 67,760 square yard of land in Kavadiguda, Secundarabad after fixing a reserve price based on the market valuation report.

In December 2001, the Company obtained approval of its Administrative Ministry for selling 9,680 square yards of land, at the rate of Rs.10,000 per square yard to Canara Bank, which however did not materialise. The Company then agreed (October 2002) to sell 19,360 square yard of land to the Central Public Works Department (CPWD) at the rate of Rs.9,000 per square yard, being the rate fixed by the Registration and Stamps Department of the State Government (Registrar) at the time of start of negotiations (May 2001) with the CPWD. The CPWD acquired 10,203 square yard at the above rate and the sale deed was executed (June 2004).

The Company offered (July 2002) another 5,211 square yards of land to NTPC Limited (NTPC) at the rate of Rs.10,000 per square yard i.e. at the rate approved by the Administrative Ministry for sale to Canara Bank. The NTPC also accepted the offer and sale deed was executed (June 2003).

It was observed that while selling the land to the CPWD, the Company accepted the market rate on the date of start of negotiation (as fixed by the Registrar) as the

benchmark. However, the same was not done in the case of sale of land to the NTPC. As per the Registrar, the rate of the land, when negotiations with the NTPC started, was Rs.11,000 per sq. yard while the land was sold to the NTPC at the rate of Rs.10,000 per square yard. The reasons for selling land at lower than market rate were also not on record. The above sale to the NTPC resulted in a loss of Rs.52.11 lakh to the Company.

The Ministry stated (September 2005) that the Company was negotiating the sale of the said land to NTPC since July 2002 and the rate of Rs.10,000 per square yard was taken as benchmark because the same was approved by the Government for sale of land to Canara Bank. It further stated that the enhanced circle rate of Rs.11,000 per square yard was noticed only after the deal with the NTPC was over.

The reply is not tenable, as the BIFR had directed the sale of land using prevailing market rates as the benchmark. Further, there was no logic in adopting Rs.10,000 per square yard approved by the Administrative Ministry in December 2001 as a bench mark for the sale initiated in July 2002 without considering the prevailing market rate. It was imperative on the part of the Company to obtain the market rate of land from time to time from the registrar.

Thus, non-consideration of prevailing market rate while selling the land to the NTPC resulted in loss of Rs.52.11 lakh.

CHAPTER XIII: MINISTRY OF NON-CONVENTIONAL ENERGY SOURCES

Indian Renewable Energy Development Agency Limited

13.1.1 Loss due to delay in hedging interest on foreign currency loan

The Company delayed hedging of its interest liability under a foreign currency loan from December 2002 to January 2005 resulting in avoidable payment of interest of Rs.3.18 crore.

Indian Renewable Energy Development Agency Limited (Company) entered into (July 1999) an agreement with Kreditanstalt fur Wiederaufbau, Germany (KfW) for raising a term loan of Duetsche Marks (DM) 120 million equivalent to Euros 61.355 million• (Rs.327.94 crore). The loan assistance consisted of two portions viz., portion I (soft loan) amounting to DM 70 million carrying an interest rate of 0.75 *per cent* per annum and portion II (market loan) amounting to DM 50 million carrying an interest rate of 6.56 *per cent* per annum. The loan was released by KfW in tranches between October 2000 and March 2004.

In order to manage the foreign exchange risk on KfW line of credit, the Company after inviting offers from five banks for management of foreign exchange risk, entered into another agreement (March 2000) with Canara Bank under which it placed the proceeds of Euro loan from KfW as a deposit with Canara Bank and availed an equivalent Rupee loan from Canara Bank against the Euro deposit. The Euro deposit with Canara Bank was to be used to meet the repayment of KfW loan and the interest earned on this deposit was to be used for paying interest on the KfW loan.

Under the above loan arrangements the interest earned on the Euro deposit with Canara Bank was at floating Euribor♠, while the payment of interest for KfW loan was fixed at 3.17 *per cent* per annum (weighted average of portion I-Euros 35.79 million at 0.75 *per cent* and portion II-Euros 25.56 million at 6.56 *per cent*). The interest rates received by the Company from Canara Bank on Euro deposit showed a continuous declining trend from 4.79 *per cent* per annum (for half year ended June 2001) to 2.07 *per cent* per annum (for half year ended December 2003) except for a marginal increase from 3.25 *per cent* to 3.51 *per cent* during the half year ended December 2002. Though the interest earned on the Euro Deposit with Canara Bank was more than the interest paid on the KfW loan upto December 2002, due to the declining interest rates it became less than the interest paid on KfW loan thereafter.

In order to protect itself against the adverse movement of interest rates, the Company belatedly finalised the Interest Rate Swap agreement with Standard Chartered Bank in

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• *1Euro =DM 1.95583 (fixed by European Union) and 1 Euro =Rs.53.45*

♠ *Euribor =Euro Interbank Offered Rate*

January 2005. Under the agreement the Company had to pay floating Euribor to the Standard Chartered Bank against which it was to receive an interest of 2.9625 *per cent* per annum every six months. However, by the time the Company finalised the swap with Standard Chartered Bank it had already incurred a loss of Rs.3.18 crore upto December 2004 on account of difference in the interest paid to KfW and the interest earned on Euro deposit with Canara Bank.

The Management while accepting that there was a net outflow of Rs.3.18 crore stated (April 2005) that :

(i) The interest on Euro deposit started falling from June 2001 but it increased during half year ended December 2002. Accordingly, movements of interest rates for next one year were watched with the expectation of improvement in the rates and on its failure to do so, they explored hedging the risk which was finalised in January 2005.

(ii) There was a net inflow of Rs.57.08 crore if the onward lending of Rupee loan by the Company to renewable energy projects is considered.

The reply of the Management is not tenable because

(i) In a dynamic environment with declining trend in interest rates it was not a prudent financial decision to wait for two years (December 2002 to December 2004) to hedge the interest.

(ii) Though the Company reported a net inflow of Rs.57.08 crore, timely hedging would have increased the inflow by Rs.3.18 crore.

Thus, delay in employing a hedging instrument against falling interest rates resulted in avoidable loss of Rs.3.18 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

CHAPTER XIV: MINISTRY OF PETROLEUM AND NATURAL GAS

Balmer Lawrie & Company Limited

14.1.1 Injudicious payment of Rs.15.07 crore towards undue benefits

The Company contributed Rs.15.07 crore to a superannuation fund required to be maintained solely by its officers and in which the Company did not have any legal or contractual obligation to contribute, resulting in extension of undue benefit to a group of employees.

Balmer Lawrie & Company Limited (Company) introduced (January 1988) a superannuation benefit fund scheme for its officers' cadre. The fund scheme envisaged that the funds towards operation of the scheme would be contributed by the officers by way of monthly contribution varying from two to five *per cent* as well as through surrender of certain existing facilities extended by the Company. It was also envisaged that there would be no additional cost to the Company except for a token annual contribution of Rs. one hundred per annum. No actuarial valuation of the liability was undertaken at the time of creation of the fund and past service liability of the officers was not funded. The Board of Directors of the Company was satisfied of the viability of the scheme and a trust deed was executed introducing the scheme from first January 1988.

An actuarial valuation made in June 2000 indicated that as on March 2000 the fund would be insolvent as there would be a deficit of Rs.3.30 crore which was more that 50 *per cent* of the assets of the fund. However, no action was taken on the recommendation (June 2000) of the actuary for increase in contribution for making the fund viable. Even the increase of five *per cent* in variable contribution every second year by the beneficiaries as envisaged at the time of formation of the fund had not taken place. The deficit increased to Rs.15.07 crore as of March 2002 as shown in the actuarial valuation report of May 2002. In order to make good the deficit, the trustees of the fund approached the Company (October 2002) to increase its annual contribution from Rs. one hundred to Rs.1,50,00,000. No increase in the contribution from the members was proposed. They also requested the company to pay Rs.15.07 crore as advance to be adjusted against such future contributions. Despite no legal or contractual liability the Company decided (November 2002) to make good the deficiency of Rs.15.07 crore by itself, as suggested by the trustees, even though there was no increase in the contribution from the members. The amount was finally paid in December 2003 as an advance contribution to the fund to be adjusted against the profit of the Company in subsequent years.

The rules of the fund were subsequently amended and it was converted to a 'defined contribution scheme' and its management was transferred to the Life Insurance Corporation of India in January 2004.

Audit observed that the contribution made by the Company without any legal liability was an undue benefit extended to the officers of the Company. By doing this, it departed

from the practice followed by other Oil Companies where the funds were being managed by the trustees.

The Management stated (May 2005) that (i) they were aware of the fact that there might be deficiency in the long-term viability of the fund. (ii) the service manual of the Company also provided for granting superannuation benefits based on the defined benefit scheme. Due to rightsizing of manpower, the contribution to the fund got substantially reduced and also higher outflow from the fund took place since contribution to the officers not completing the qualifying years of service had to be refunded and the Company had to make up the deficit to fulfil its obligation to honour the terms of agreement as well as to discharge its responsibility as settler of trust. (iii) the decision was taken based on commercial expediency for running the Company efficiently by retaining its human talent and (iv) the decision had addressed the anxiety of the officers when the Company was under active consideration of disinvestment by the Government.

The Management's contention is not tenable in view of the fact that (i) the Company was not answerable for the financial liability of a fund that was managed independently by a trust and was not liable for paying pension to its officers as the fund was contributory and self-generated by the beneficiaries. (ii) the fund was deficit since inception and the rightsizing of manpower was not the main factor. (iii) the disinvestment process had no relation with the fund because it was independently managed. (iv) the decision was not related with commercial expediency for efficient running of the Company as it was confined to the officers' cadre alone and was not extended to the entire workforce.

The Ministry while admitting that the decision was not correct from a legal point, stated (September 2005) that membership of the superannuation fund was compulsory for all the officers who joined the Company after the fund was launched in January 1987. It was also provided for in the Manual of the Service Terms and Conditions that the members would be eligible for certain superannuation benefits. Therefore it was evident that there was certain tacit understanding of underwriting of the fund by the Company and it may not be prudent to take a purely technical and legalistic view.

The Ministry's contention is not tenable in view of the fact that employees of the Company are governed by the Contributory Provident Fund Rules. Compulsory membership of the fund by the new officers joining after January 1987 does not imply that the Company was liable for paying pension to its officers, as the fund was contributory and was self-generated by the beneficiaries.

Thus, the Company extended undue benefits of Rs.15.07 crore to its officers in the form of contribution towards an actuarially unviable superannuation fund which was required to be maintained solely by its officers and in which the Company did not have any legal or contractual obligation to contribute.

Bharat Petroleum Corporation Limited

14.2.1 Blockade of funds caused by management failure to modify the software

Failure to implement the orders issued by the excise authorities in time due to inability to manage the software led to blockade of Company's fund of Rs.7.67 crore and unnecessary litigation.

The New Jalpaiguri Tap-Off Point (NJP-TOP) of Bharat Petroleum Corporation Limited (Company) receives petroleum products of North East (NE) Refineries through pipeline transfer from Siliguri Terminal of Indian Oil Corporation Limited (IOCL). While Motor Spirit (MS) and High Speed Diesel (HSD) were transferred on 'Bonded' basis under the Central Excise Act/Rules, other products were transferred to NJP-TOP after payment of excise duty. The bonded products were cleared on subsequent payment of duty. The Government of India issued a notification in March 2002 permitting removal of petroleum products drawn from NE refineries by paying excise duty at 50 *per cent* of normal rates. The price of the products to end-consumers was to remain unchanged irrespective of source refinery and the excise benefit so arising was to be passed on to NE refineries. The differential duty of 50 *per cent* in respect of NE products was adjusted by the marketing companies in the assessable value, by calculating the concessional excise duty using a suitable formula.

Despite the notification, NJP-TOP continued to generate invoices showing excise duty payable at normal rates and as a consequence the Company paid excise duty in full upto September 2002 when it noticed that 100 *per cent* excise duty was being paid in respect of products received from NE refineries. The Company then immediately started depositing only 50 *per cent* of the excise duty from the second fortnight of September 2002, but failed to generate invoice with necessary modification due to its inability to make necessary adjustment in its ERP[♠] package. As no change could be effected in the invoicing pattern, the invoices generated by the package continued to show excise duty charged at normal rates from September 2002 to December 2002 when actually only 50 *per cent* of the collected duty was deposited with the excise authority. As the problem of changing the invoicing system in the ERP package persisted, the Company after it cleared all the bonded products by December 2002 started drawing only duty paid products from IOCL's terminal. The Company subsequently lodged (April 2003) a claim with the excise authorities towards refund of 50 *per cent* excise duty amounting to Rs.7.25 crore for the period from April 2002 to September 2002. The claim of the Company was rejected by the Excise Department (March 2004) which also issued a Show Cause cum Demand Notice for Rs.2.46 crore towards payment of differential duty for the period from September 2002 to December 2002. The Company did not pay this amount and filed the appeal against the order before the Custom, Excise and Service Tax Appellate Tribunal in March 2005, which was pending (October 2005).

The Management stated (August 2004) that applicability and availability of this concession to a non-refinery bonded location like Siliguri (NJP) was announced by the Government much later i.e., June 2002 and due to the billing system and peculiar nature

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[♠] *Enterprise Resource Planning*

of the transaction, duty paid on old basis came to light at a later stage and that ERP system was a highly integrated and standardised system and making the change in the fundamental rule of applying excise duty rates was a major development which had a cost and time implication.

The Management's contention is not tenable because although the clarifications for extending the duty benefit to bonded location were issued in June 2002, the Company continued to pay 100 *per cent* excise duty till September 2002 resulting in overpayment of excise duty and thereafter also failed to make necessary modification in ERP package or introduce an alternate mechanism to issue invoice at revised assessable value and ED payable resulting in blockage of Rs.7.67 crore.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

14.2.2 Non-recovery of dues

Supply of lubricant to a new customer without financial security and continuation of the supply even after dishonour of cheques led to non-recovery of dues of Rs.69.53 lakh.

The Lubricant Strategic Business Unit (SBU) of BPCL supplied lubricant on 30 days credit (August 1998 to December 1998) to a new customer M/s. Leela Petroleum. The credit was granted without entering into a formal agreement, without obtaining financial security/guarantee and without assessing the credit worthiness of the customer.

Cheques against the initial supplies made between 4 August and 25 August 1998 were honoured. Thereafter, 10 cheques dated 30 September 1998 valued at Rs.21.19 lakh were dishonoured as intimated by the bank on 2 October 1998. Despite receiving the dishonour advice, SBU continued the supply upto 19 November 1998 on cheque payment basis. On receipt of another intimation of dishonour of 13 cheques for supplies made in September 1998, the supply to M/s. Leela Petroleum was stopped on 20 November 1998. The party approached (November 1998) SBU for supply of lubes to two of its sister concerns. Supplies to the sister concerns were also made on cheque payment basis from 26 November 1998 and the supply was stopped from 30 December 1998 as cheques received from the sister concerns (Rs.8.43 lakh) were also dishonoured on 29 December 1998.

Two summary suits filed (August 2001) against M/s. Leela Petroleum and its sister concerns for recovery of Rs.69.53 lakh were decided (January/July 2003) in favour of BPCL. The Court also decreed for payment of interest at the rate of eight *per cent* per annum from the date of filing of the suits. However, the dues could not be recovered till date (July 2005).

The Management stated (June 2005) that credit was granted to the party based on commercial opinion and likely business potential and the supplies continued after the dishonour of cheques in the hope of recovering past dues by supporting the party. The Management further stated that a private detective agency, appointed in March 2005 for identifying the properties of the parties, submitted its report and the same was being

examined by its legal department. Disciplinary action was also initiated against the erring officer and a warning letter was issued, as there was no *mala-fide* intention on his part.

The Management's contention is not acceptable as the supply on credit basis to a new customer without securing the Company's financial interests was not a prudent commercial decision and continuation of the supply even after the dishonour of cheques led to unwarranted accumulation of dues which made the recovery of dues even more difficult. Further, though the Court's decree came in January/July 2003, BPCL did not take emergent effective action for recovery of the dues. It was only in March 2005, after a period of about two years, that a private detective agency was engaged to gather information about the property of the defaulting party and the chances of recovery of dues became bleak.

Thus, lack of commercial prudence in supply of lubricant and subsequent ineffective recovery efforts after the Court's decree led to non-realisation of dues of Rs.69.53 lakh and interest thereon.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

14.2.3 Loss due to weak monitoring and failure to take timely action

Lax monitoring of the operations of a depot and failure to take timely action against the financial irregularities of the operator rendered an amount of Rs.57.39 lakh unrecoverable.

The Company entered into an agreement (April 1994) with M/s. Ghasi Ram Panna Lal, (operator) for the operation of its Commission Operated Depot at Gurgaon (COD). The COD was meant to take supplies of petroleum products of the Company for further sales to the retail outlets in Gurgaon and Faridabad.

The operator was required to submit indents, invoices and stock transfer notes for the disposal of the Company's products everyday. The operator was also required to make bank deposit slips, tally the receipts with the invoices raised and lodge the bank deposit slips along with the payment instruments in the bank daily. From February 1998 the operator started committing financial irregularities and passed extraneous credits by including the same instrument number twice or fictitious credit in the bank deposit slips intimated to the Company. Over a period of two and a half years 37 such irregularities were committed by the operator which remained unnoticed by the Company till January/February 2000 after which they deputed (May 2000) two clerical staff to oversee the activities of COD. Further analysis of transactions by the Management established (in the beginning of 2001) that the operator had committed irregularities.

The Company closed the operations at COD in March 2002 after opening of their own supply location in Rewari and belatedly took up the matter with the operator (August 2002 and September 2003) for reconciliation and recovery of the accounts. However, the operator denied (October 2003) having committed any irregularity stating that the COD operated under the direct supervision and control of the Company staff. Due to financial irregularities an amount of Rs.57.39 lakh remained unrecovered from the operator/retail

outlets (June 2005). The Management did not initiate legal action against the operator and the case had become time barred. The Company was planning (June 2005) to file a criminal case against the operator in the court but the same had also not been filed. (September 2005).

While accepting the facts, the Management stated (June/September 2005) that:

(i) fictitious instruments were entered by the operator in the bank deposit slips which gave the false impression that the collections were correctly done and the credits were getting delayed by the bank.

(ii) Finance exercises control of locations through bank reconciliation and whenever any outstanding is observed, the same is taken up with COD/Territory for resolution.

(iii) Till the time the operator's response through his legal counsel was received (October 2003) the Company was hopeful to resolve the issue through dialogue because of their long association with the operator.

(iv) Legal action was not taken in order to resolve the issue amicably. An FIR had been submitted by post (July 2005) to the police and a reminder was also sent to register the FIR.

The reply of the Management is not tenable because

(i) Delay of over two and a half years in detection of the irregularities indicated ineffective monitoring of the operations of COD by the Management. As per terms of the agreement the operator was required to send remittances daily. The Management ignored the unreconciled entries in the customers' accounts for unreasonably long periods, considering them bank delays.

(ii) Submission of fictitious credits in bank deposit slips by the operator highlighted loopholes in the system of evaluation through bank reconciliation process.

(iii) Once the Management established the fraudulent irregularities committed by the operator in 2001 there was no point waiting for resolution through a dialogue. Despite various irregularities/fraud by the operator not even an FIR could be got registered by the Company so far (September 2005).

Thus, laxity on the part of the Management in monitoring the operations of COD on regular basis and failure to take timely action rendered the amount of Rs.57.39 lakh unrecoverable.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

Engineers India Limited

14.3.1 Loss due to execution of sub-standard work

Deficiency in design coupled with execution of sub-standard work resulted in loss of Rs. one crore.

Indian Oil Corporation Limited (IOCL) awarded (January 1994) to Engineers India Limited (Company) a contract for providing consultancy services for construction of Marketing Terminal at Panipat for Rs.7.95 crore. The work was to be completed by August 1996. The scope of work included construction of terminal with all allied facilities such as receipt, storage and despatch of petroleum products and construction of tank lorry filling (TLF) area with flexible pavements (inner roads). As per the agreement, the Company had to guarantee that the services were provided free from defects. In the event of faulty engineering, it had to carry out corrective studies without any additional cost to IOCL and had to make good the loss for any failure in the structure/system/facility due to error or omission in the technical studies performed by the Company. In addition, the Company was to provide guarantee by obtaining a Professional Liability Insurance (PLI) for Rs. one crore for a period of 12 months from the date of commissioning of the terminal or 18 months from the date of mechanical completion whichever was earlier. Accordingly, the Company obtained (January 1998) a PLI for Rs. one crore for a period of 18 months from National Insurance Company Limited (NICL). The work was completed in June 1998.

After completion of the project, IOCL intimated the Company (July 1998) that there were defects in the internal roads of the marketing terminal and insisted on remedial action by the Company. Subsequently, the Company appointed (December 1998) Central Road Research Institute (CRRI), New Delhi to study the problems relating to the internal roads and suggest remedial action. CRRI reported (March 1999) that there was design deficiency in pavement thickness (290-320 mm against the requirement of 450-540 mm), inadequate drainage facility and improper levels of finished roads, which led to the damage of the roads. IOCL held the Company responsible for sub-standard execution of work and recovered (March 2003) Rs. one crore as damages.

Meanwhile, the Company lodged a claim with NICL (June 1999) for Rs. one crore under PLI. The claim was, however, rejected (January 2003) by NICL on the grounds that the loss was due to neglect, error or omission prior to the retroactive date of policy and due to non-compliance with technical standards commonly observed in professional practice. Thus, due to execution of sub-standard work coupled with deficiency in design, the Company had to suffer a loss of Rs. one crore.

The Ministry stated (November 2005) that the design was in accordance with the Company's standard and matched the recommendations of Indian Road Congress and the failure of the flexible pavement was observed only in a small pocket of the entire road network, which might be due to some localised problems.

The reply of the Ministry is not tenable as the Company's consultant CRRI found (March 1999) that the designed thickness of the road was not sufficient considering the type of heavy vehicles which used the road and the volume of traffic. The condition of the roads

deteriorated not only in small portion of road in TLF area but also in approach road connecting the bitumen loading shed. The Company had also concluded after examination (November 1999) that there was lacuna in recommendation of proper design by their technical department and the road thickness was not provided as per design during construction. The above facts indicate that deficiency in design coupled with execution of sub-standard work resulted in loss of Rs. one crore.

GAIL (India) Limited

14.4.1 Loss due to tampering of meters by consumers

Agra unit of GAIL (India) Limited sold Natural Gas as well as Re-gasified Liquid Natural Gas to various consumers in Agra and Firozabad. Due to tampering of Meter skids by consumers, gas valuing Rs.10.10 crore was not billed.

GAIL (India) Limited (Company) was selling Natural Gas transported through its Gas Rehabilitation and Expansion Project pipeline to various consumers in Agra and Firozabad under Administered Price Mechanism (APM). During the period January 2004 to February 2005, the Company received 40.62 crore Standard Cubic Meters (SCM) of gas at its Agra Unit but the quantity billed to customers was 38.96 crore SCM only, leaving an unaccounted/unbilled quantity of 1.66 crore SCM gas valuing Rs.13.20 crore.

The shortfall in the quantity of gas billed to the consumers *vis-a-vis* gas received by the Company at Firozabad City Gas Station increased after December 2003. The shortfall increased from 0.90 *per cent* in December 2003 to 2.15 *per cent* in January 2004, 2.29 *per cent* in February 2004 and 2.72 *per cent* in March 2004. Only when the shortfall reached 8.22 *per cent* in September 2004, the Company conducted detailed inspections (September/October 2004) and checking of meters in the consumers' premises and found that 11 consumers had tampered with the meters installed in their premises, resulting in under-billing of gas. The period of tampering in these cases ranged from 72 days to 290 days. The Company raised (June 2005) demand notes for Rs.36.53 crore (including penalty) against these 11 customers but the recovery was awaited (September 2005).

It was observed in Audit that after five cases of tampering in 2001, the Company initiated measures to strengthen its internal controls but the steps taken proved inadequate as the number of cases increased to 11 during 2004 and the tampering continued even upto 290 days.

The Management stated (April 2005/June 2005) that:

(i) From March 2004, the Company started supplying Re-gasified Liquid Natural Gas (RLNG) through the same pipeline along with the APM natural gas. Billing for the gas drawn by customers beyond their contracted quantity was charged at RLNG rates which were almost double the APM rates. Due to implementation of billing at RLNG rates some of the customers in Firozabad started tampering with the meters to avoid the payments at higher rates.

(ii) Various steps like inspection and detailed checking of meters, providing tamper proof locks, sealing the skids, surprise checks at consumers' terminals at odd

hours were taken in the later part of 2004-05 to prevent theft of gas by tampering with the gas meters.

(iii) Indraprastha Gas Limited and Mahanagar Gas Limited (Joint Ventures promoted by the Company) were in the business of city gas distribution and there was one *per cent* acceptable loss in these companies also.

(iv) In 2001 customers tampered by bypassing the meters and changing the pressure settings of the meters but tampering in 2004 was more sophisticated when the customers tampered with the meter assemblies and gears. Also the number of customers increased to 270 in 2004 from 97 in 2001 which made control by frequent visits difficult.

The reply of the Management is not acceptable because:

(i) After tampering of meters was noticed in 2001, the technical audit of the Company had recommended (August 2001), terminal visits by Company's representatives at least once a week and surprise checks in odd hours and holidays. The steps taken by the Company in the later part of 2004-05 were, therefore, required to be taken from August 2001 onwards and should have been intensified immediately after noticing increase in the shortfall after December 2003.

(ii) Tampering ranging from 72 to 290 days and repeated tampering of meters (two to five times) indicated deficiencies in the monitoring and control mechanism.

(iii) The loss on account of unaccounted gas during 2004-05 (upto February 2005) ranged from 1.72 *per cent* (July 2004) to 8.22 *per cent* (September 2004). Even after considering one *per cent* acceptable business loss, the value of the unbilled gas was Rs.10.10 crore.

Thus, failure of the Company to put adequate control mechanism in place to arrest tampering of meters resulted in a loss of Rs.10.10 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

14.4.2 Loss of revenue due to lack of coordination in laying and use of pipeline

The Company did not co-ordinate with ONGC and the Government of Tripura for laying and use of its Konaban-Rokhia pipeline resulting in a loss of revenue of Rs.9.12 crore during April 1998 to February 2002.

GAIL (India) Limited (Company), the Government of Tripura and Oil and Natural Gas Corporation Limited (ONGC) decided (December 1994) that requirements of 0.20 MMSCMD[♣] gas for two units (V and VI) of Tripura State Electricity Department at Rokhia, Tripura (TSED) would be met from Konaban GGS[♠] of ONGC which was about

[♣] *Million Metric Standard Cubic Meters per Day*

[♠] *Group Gathering Station*

15 Kms from Rokhia. The gas was to be made available by ONGC at their Konaban GGS and the Company was to create gas supply facilities by laying a pipeline from Konaban GGS to Rokhia. Gas sale agreement for supply of 0.19 MMSCMD gas for these units was signed by the Company with TSED (August 1996) effective from 1 April 1997.

The Company, however, could not complete the pipeline by April 1997 due to delays in its tendering process. The supply of additional gas was, therefore, met from Rokhia field of ONGC from September 1997. The pipeline was finally completed in March 1998 at a cost of Rs.8.33 crore but the Company could not start gas supply through it, as Konaban GGS of ONGC was not ready until March 1999. Even after commissioning of Konaban GGS, ONGC continued to supply additional gas to TSED from Rokhia as TSED was reluctant to take gas from Konaban pipeline of the Company as their entire requirement was fulfilled from Rokhia. Despite all gas facilities being ready by March 1999 and TSED having a subsisting contract to purchase gas from the Company, the Company could not impress upon them to receive gas through the pipeline which was laid to meet their requirements.

The gas supply could finally commence from July 2002 but was discontinued because supply of gas through the pipeline resulted in pressure drop at another power plant. TSED again started taking gas from Rokhia but had been paying transportation charges from April 2002 irrespective of the drawal of gas. The transportation charges aggregating to Rs.9.12 crore for the period April 1998 to February/March 2002, however, remained unrecovered and had to be waived by the Company.

The Management stated (February 2004/September 2005) that :

(i) The Company could not commence supply of gas through Konaban-Rokhia Pipeline due to uncertainties of gas supply from Konaban GGS of ONGC.

(ii) The Company took up the issue with ONGC who were ready to supply gas through the pipeline after March 1999 but TSED insisted on getting supplies from Rokhia.

(iii) Entire outstanding from TSED had been settled (April 2005) through one time settlement and there were no dues from them.

The Ministry stated (October 2005) that the Company had been pursuing with ONGC as well as TSED and the efforts had resulted in TSED making payment of transportation charges from April 2002 onwards.

The reply is not tenable because :-

(i) The Company could not effectively co-ordinate with ONGC to ensure that their Konaban GGS was ready in time to avoid idling of its pipeline.

(ii) Under the terms of the contract TSED had bound itself to buy minimum guaranteed off take of gas. Therefore, after readiness of all gas supply facilities in March 1999, the Company should have impressed upon TSED to purchase gas through pipeline which was laid to meet their requirements.

(iii) The amount recovered through one time settlement did not include the transportation charges of Rs.9.12 crore for the period April 1998 to March 2002 which were waived off resulting in a loss to the Company.

Thus, the Company suffered a loss of Rs.9.12 crore due to lack of coordination in laying and use of its pipeline.

14.4.3 Loss due to lack of planning and commercial appreciation in investment of surplus funds

Due to lack of planning and commercial appreciation in investment of surplus funds, the Gas Pool lost an interest of Rs.6.72 crore during March 1999 to March 2005.

As per the directions of the Ministry (December 1991, September 1997 and March 1999), GAIL (India) Limited (Company) was required to maintain Gas Pool Account on behalf of Government of India and invest the surplus funds therein in terms of guidelines of Department of Public Enterprises (DPE). For investment of surplus funds by the Public Sector Enterprises, the guidelines of DPE (December 1994) *inter alia* advised Public Sector Enterprises to observe proper commercial appreciation before any investment decision was taken and laid down the broad principles for the kind of instruments in which investments could be made.

It was observed that even after meeting directions of the Ministry for transfer of funds from Gas Pool, surplus funds ranging from Rs.113.99 crore to Rs.956.64 crore remained in the Gas Pool Account during March 1999 to March 2005. The Company /Ministry did not finalise an investment policy for the investment of surplus funds of Gas Pool and invested these funds in short term deposits ranging from 46 to 69 days in Bank of Baroda Bhikaiji Cama Place, New Delhi, without any commercial appreciation of rates being offered by other banks for similar deposits. A test check disclosed that on short-term deposits (15 to 89 days) of the Company's own surplus funds, the Company earned a higher rate of interest ranging from 0.25 *per cent* to 2.40 *per cent* per annum during August 1999 to February 2005 as compared to the short term deposits from surplus funds from the Gas pool Account. Even if a minimum rate difference of 0.25 *per cent* per annum was considered, the Gas Pool lost interest amounting to Rs.6.72 crore during the period from March 1999 to March 2005 on short term deposits due to lack of commercial appreciation of the rates by the Company.

Further, as the surplus funds were available over the period of six years, these could be invested on long-term basis to earn higher rates of interest by an appropriate investment policy and funds planning.

The Ministry while agreeing to improve the efficacy of the Management of the Gas Pool Account stated (September 2005) that

(i) the claims against the Gas Pool were submitted by various claimants from time to time and were disbursed after due examination. The funds were being invested for short duration as there was no fixed periodicity in submission and settlement of claims.

(ii) Gas Pool funds were invested / re-invested in Bank of Baroda where the account was maintained to avoid the cumbersome procedure of calling for quotations for interest rates from various banks for dealing with Government funds, which involved certain amount of risk.

The reply is not tenable because

(i) absence of appropriate periodicity for submission and settlement of claims indicated deficiencies in proper planning and assessment of surplus funds to avail of better returns.

(ii) calling quotation was not a cumbersome process as the Company was already following this process for investment of its own surplus funds.

Thus, due to lack of appropriate planning and commercial prudence by the Company in investment of surplus funds from the Gas Pool Account, there was a loss of interest of Rs.6.72 crore during March 1999 to March 2005 to the Gas Pool Account which would have accrued to the Government.

14.4.4 Blockage of funds on land and payment of extension charges

GAIL (India) Limited purchased land at NOIDA but did not fruitfully utilise it resulting in blockage of funds amounting to Rs.1.36 crore and payment of extension charges of Rs.1.14 crore for delayed construction.

The Company took two plots of land measuring 8,000 square meters each on 90 years' lease from New Okhla Industrial Development Authority (NOIDA), at a cost of Rs.2.72 crore for construction of its office complex. The plots in Sector I NOIDA (Uttar Pradesh) were allotted to the Company in February 1986 and the Company took their possession in March 1986.

As per terms of the lease deed, the Company was required to complete construction within five years from the date of allotment or four years from the date of possession, whichever was later and was thereafter liable to pay extension charges at the rate of four *per cent* per annum of the cost of land i.e. Rs.10.88 lakh per annum. Instead of constructing the building on these plots, the Company purchased (January 1989), another plot of land in Delhi (Bhikaiji Cama Place) from Delhi Development Authority (DDA) at a cost of Rs.16.94 crore for the same purpose. The building on the plot in Delhi was constructed at a cost of Rs.9.09 crore and was occupied by the Company in October 1990.

Subsequently, the Company partly constructed (6,000 square meters as against the minimum requirement of 12,000 square meters under the NOIDA bye-laws) an office complex (December 1999) on the NOIDA plot.

Due to delay in construction on the plot followed by construction on area less than the minimum required area, the Company had to pay Rs.1.14 crore as extension charges from 1991-92 to 2000-01. However, on requests of the Company (April/August 2001) NOIDA agreed to waive the extension charges from 2001 to 2012. Surrender of plots was not

possible as the Ministry stated (September 2005) that in that case two other plots allotted by NOIDA for the Company's Training institute and residential colony were also required to be surrendered. Such condition by NOIDA had not been successfully challenged by the Company. Thus, the Company could effectively use only one half of the plots (6,000 square meters out of 12,000 square meters) and the other half costing Rs.1.36 crore remained unutilised.

The Management/Ministry stated (May 2005/September 2005) that:

(i) Land was not allotted by DDA so the Company had no alternative but to approach adjoining authority NOIDA for allotment of land. Nevertheless the Company always considered it prudent to have its corporate office at Delhi. Purchase of building for Corporate Office at New Delhi instead of NOIDA was due to various functional problems of operating from NOIDA.

(ii) Land was retained for its various expansion activities in future.

(iii) To save recurring penalty an undertaking was given (August 2001) to NOIDA not to undertake construction upto 2012.

The reply is not tenable because

(i) Functional problems for Corporate Office at NOIDA were required to be foreseen before purchase of the land. It was not obligatory for the Company to purchase an unsuitable piece of land.

(ii) If the Company had always considered it prudent to have its Corporate Office at Delhi, it could have waited for an appropriate opportunity to purchase land in Delhi instead of blocking funds in NOIDA. The Company ultimately got the desired land in Delhi within three years of the purchase of the land at NOIDA.

(iii) The land cannot be used until 2012 and the funds have, accordingly, been blocked.

Thus, purchase of land without its fruitful use resulted in blockage of funds amounting to Rs.1.36 crore and payment of extension charges of Rs.1.14 crore.

14.4.5 Wasteful expenditure on construction of terminal facilities

The Company accepted units of Unit Trust of India instead of bank guarantee as security and constructed its terminal for supply of gas without waiting for the corresponding progress by the buyer's plant resulting in blockage of Rs.1.15 crore.

GAIL (India) Limited (Company) entered into a contract (February 1991) with Usha Rectifier Corporation India Limited (buyer) for supply of gas to their gas based sponge iron plant at Jagdishpur (UP), to be constructed by December 1994.

The buyer deposited Rs.2.04 crore and 46.55 lakh units (reduced to 36.2 lakh units due to release of units by the Company in March 1994 and May 1994) of the Unit Trust of India

(Unit Scheme 1964) with a face value of Rs.10 each as security in February 1991. The Company accepted the units of the UTI in deviation of its usual practice of accepting bank guarantees as security.

The contract identified four key activities of the sponge iron plant that the buyer had to complete between June 1991 and December 1994 and provided that for delay of more than three months in any key activity, the Company had the right to recover 25 *per cent* of the units of the UTI submitted by the buyer as security. In case of non-drawal of gas within the stipulated period of six months after the scheduled date of commencement of supply (December 1994) the UTI bonds/units and deposit were to be forfeited.

In January 1994 (when three out of four key activities were required to be completed) the Ministry of Steel informed the Ministry of Petroleum and Natural Gas that the buyer had revised the project parameters and the project was to be implemented in the name of M/s. Malvika Steel Limited (MSL), (a subsidiary of the buyer), with scheduled date of completion as December 1996 as against December 1994. Based on the revised requirements, the Ministry of Petroleum and Natural Gas reduced the buyer's gas allocation (May 1994) from 0.80 MMSCMD[♣] to 0.36 MMSCMD (further reduced to 0.35 MMSCMD in May 1995) and also advised that the allocation in the name of MSL would be treated as fresh allocation. The buyer neither signed the amendment contract with the Company nor implemented the project as per the original contract entered into in February 1991. Despite non-implementation of the project the Company commenced construction (1995) of the terminal/pipelines at buyer's end for supply of gas to them and completed them in 1997 at a cost of Rs.5.48 crore.

The buyer/ MSL did not purchase the gas from the Company, as their project was not complete. The Company forfeited the security (2003-04) of Rs.2.04 crore and salvaged the material (March 2004) worth Rs.2.29 crore after dismantling its terminal at the buyer's end. The units of the UTI could not be transferred/encashed because they were only accompanied by duly signed blank transfer deeds and the UTI informed (April 2003) that a resolution by the Board of Directors of the buyer was also required to transfer the units. The Company had neither made a formal enquiry from the UTI about this requirement before accepting the units as security nor did it get them hypothecated in its favour as per the terms of the contract with the buyer.

The Management stated (June 2003 and April 2004) that though the expenditure on construction of terminal facilities had become wasteful, the interest of the Company was well protected and no loss on this account would be suffered by the Company as the present value of the security deposit and US-64[♦] units including interest on security deposit amounted to Rs.7.63 crore which was sufficient to recover the loss.

The reply of the Management is not tenable because the Company could make good the loss only to the extent of Rs.4.33 crore by forfeiting the security and salvaging the material. The balance wasteful expenditure of Rs.1.15 crore (Rs.5.48 crore less the amount of security forfeited/material reused Rs.4.33 crore) could not be made good as the UTI units could not be encashed (October 2005) despite efforts by the Company since

[♣] ***Million Metric Standard Cubic Meters per Day***

[♦] ***Unit Scheme 64***

April 2003. Though the Company had earned interest on the security deposit of Rs.2.04 crore, it had simultaneously lost interest on the blocked funds of Rs.5.48 crore.

Thus acceptance of units of the UTI instead of bank guarantee as security and commencement of construction without waiting for the corresponding progress by the buyer's plant as per contract resulted in blockage of Rs.1.15 crore.

The matter was reported to the Ministry in May 2004; its reply was awaited (November 2005).

Hindustan Petroleum Corporation Limited

14.5.1 Extra expenditure on transportation due to resiting of LPG plant

Due to shifting of bottling plant away from its refinery, HPCL incurred an extra expenditure of Rs.70.60 crore between 2000-01 and 2004-05 on transportation of bulk Liquified Petroleum Gas from Mumbai to bottling plant at Usar and its re-transportation to Mumbai for sale to consumers.

Hindustan Petroleum Corporation Limited (HPCL) had two Liquified Petroleum Gas (LPG) bottling plants at Mahul, Mumbai viz., Mahul Bottling Dispatch Unit (Mahul BDU) and Hindustan Petroleum Fuel Refinery (HPFR) plant, with an annual production capacity of 25 thousand metric tonne per annum (TMTPA) and 65 TMTPA respectively. These plants catered to LPG demand of consumers mainly in Greater Mumbai district, besides Thane and Raigad districts. The bulk LPG demand of these two plants was being met from Mumbai Refinery of HPCL.

In early nineties, a proposal was mooted to resite Mahul BDU for safety reasons. The Management selected Usar location (in Raigad District) on the basis of its cheapest land cost and availability of assured supply of bulk LPG from the adjacent plant of GAIL. It was envisaged that the consumers' demand of LPG in Thane and Raigad Districts would be met by this plant. Apprehensions were expressed (October 1995) about operational constraints, as the shifting of bottling plant would entail long lead for distribution of cylinders and there was possibility of LPG availability ex Usar being lower than originally planned but these were ignored in the final analysis and the BDU plant was resited in August 1998 to Usar. Its capacity was simultaneously enhanced to 44 TMTPA.

In December 1998, HPCL decided to shift the second plant (HPFR) also for safety reasons and in April 2000, it was resited at Usar with an augmented capacity of 88 TMTPA. However, the supply received from GAIL was not adequate to meet the increased requirement. As a result, HPCL had to transport bulk LPG from its Mahul Refinery/Terminal to Usar and transport back the bottled cylinders to different places at Mumbai and, in the process, incurred incremental expense on transportation of LPG besides additional payment of octroi to Mumbai Municipal Corporation.

The Management stated (May 2004) that:

(i) The price built up of packed LPG under the subsidy scheme upto 2002-03 took care of freight/octroi element and under recoveries towards transportation from 2003-04 would be only around Rs.4.74 crore per annum;

(ii) HPCL expected uninterrupted supply from GAIL as it had indicated its production capacity at 137 TMTPA, but GAIL failed to produce LPG to its rated capacity and

(iii) HPCL was now revamping Mahul BDU with a bottling capacity of 80 TMTPA to check the extra expenditure of transportation/octroi.

The Management's reply is not tenable due to the following:

(i) Since Oil Coordination Committee was reimbursing the cost of transportation through the Oil Pool Account, HPCL ignored the inherent unviability of the proposal of transporting LPG in bulk away from Mumbai and bringing the LPG cylinders back to Mumbai for sale. This led to extra burden on the Government/consumers.

(ii) Though the availability of LPG at Usar was felt insufficient at the time of resiting BDU plant, no prior assurance was obtained from GAIL with regard to supply of bulk LPG. Even if adequate supply was available from GAIL at Usar, the extra expenditure on transportation of LPG cylinders to Mumbai and octroi payment to Mumbai Municipal Corporation had to be incurred due to the disadvantage of Usar location.

(iii) The revamping of the Mahul BDU plant after five years reinforces the fact that the decision of resitement of the HPFR bottling plant to Usar was injudicious. It was observed in Audit that an in-house Committee set up (March 1998) to review resitement of HPFR plant had recommended closure of HPFR plant by March 2000 after re-building of Mahul BDU plant in Mumbai with modern technology to meet the Mumbai demand. This would have taken care of the requisite safety aspects besides saving substantially on the cost of transportation/octroi. However, the proposal was shelved (September 1998) without assigning any reason.

The Ministry stated (November 2005) that a new plant at Mahul BDU was feasible due to subsequent change in safety requirement in February 2001 and acquisition of 2.15 acres of adjacent land (against existing land: 11.60 acres) in January 2004 to meet the safety distances. However, this contention fails to justify the shelving of the Committee's recommendation in September 1998 without assigning any reason.

The Management while deciding (April 2003) the revamping of Mahul BDU at Mumbai with a capacity of 80 TMTPA had envisaged an annual saving Rs.14.12 crore on the transportation and octroi. Thus, the total avoidable expenditure, due to injudicious decision of resiting the HPFR plant to Usar, amounted to Rs.70.60 crore for the five years ended March 2005.

14.5.2 Avoidable payment on safe keeping arrangement

The Company incurred avoidable expenditure of Rs.2.56 crore on safekeeping arrangement of products due to significant delays in completing the repairs of decommissioned tanks.

Paradeep Terminal of Hindustan Petroleum Corporation Limited (Company) was commissioned in April 1994. The terminal had four High Speed Diesel (HSD) and two Motor Spirit (MS) storage tanks with a total capacity of 47,000 Kiloliter (KL) for lighterage of ocean tankers before onward movement to Haldia. In the absence of MS handling facilities at Paradeep, MS tanks were being used in Superior Kerosene Oil (SKO) service.

In December 1999, the Company identified major repairing jobs in respect of two tanks having capacity of 11,500 KL each. A proposal was initiated (February 2000) for revamping the tanks with the target of completion by five months from the date of appropriation of fund. Rs.23.50 lakh was sanctioned (June 2001) for this by the Company, with target completion time by March 2002. Meanwhile, teams from Oil Industry Safety Directorate (October 2001) and Company's headquarters (August 2002) inspected the tanks and found severe corrosion in all the tanks. They recommended action for arresting corrosion and improved maintenance and repair work. The Company, therefore, decided to decommission and revamp the tanks in phases to avoid disruption of work in the terminal.

During Audit scrutiny it was observed that though the two tanks were decommissioned in September 2002 and October 2001 respectively, the purchase order for revamping both was issued in April 2004 and repair work completed in March 2005 and May 2005.

As is evident from above, there were considerable delays in taking up the repair work even after decommissioning which affected the storage capacity of the terminal. In order to handle the coastal inputs, the Company availed of additional safe keeping arrangements from other Oil Marketing Companies at Paradeep at an expenditure of Rs.2.56 crore during April 2002 to March 2005.

The Management could not cite any reason for the long delay in revamping the storage tanks. They stated (June 2005) that safekeeping arrangement had to be made due to fluctuations in input of the terminal.

Thus, due to significant delays in taking up the repairs and reduced effective available storage capacity, the Company had to hire additional storage capacity from other Oil Marketing Company for safekeeping arrangement of products and incurred an avoidable expenditure of Rs.2.56 crore.

The matter was reported to the Ministry in June 2005 its reply was awaited (November 2005).

14.5.3 Avoidable payment of lease rent

Excessive time was taken in firming up a decision for dismantling and disposal of the virtual jetty at Kandla Port. Further delay in award of the contract during 2003 and 2004 for the dismantling and disposal of the jetty resulted in an avoidable expenditure of Rs.1.46 crore towards lease rent of the jetty space.

As per directives of Oil Coordination Committee (OCC), HPCL constructed and commissioned a virtual jetty at Kandla Port in June 1996 at a capital cost of Rs.19.38 crore. In terms of the draft Memorandum of Understanding with Kandla Port Trust (KPT) it was required to pay annual lease rent of Rs. one crore with an escalation of five *per cent* annually. The jetty was operative upto September 1999 and was thereafter discontinued due to commissioning of Vadinagar Kandla submarine pipeline. OCC stated in April 2000 that it did not foresee any need to handle oil products at HPCL's jetty. In June 2000, HPCL requested KPT to take over the jetty but KPT did not agree (August 2000) as it found that the jetty operation was commercially unviable and suggested that HPCL could explore the possibility of identifying any party interested in taking over the jetty on conditions as may be agreed upon by HPCL, KPT and the third party.

In January 2001, an earthquake damaged the jetty and HPCL appointed a consultant to assess the extent of damage and viability of repairs/restoration *vis-a-vis* dismantling of the same. The consultant submitted its report in December 2001 and estimated the cost for restoration of facility as Rs.19.75 crore and for dismantling as Rs.11.13 crore. In the interim HPCL did not pay the lease rentals for 2000-01 and 2001-02 to KPT. On demand by KPT in August 2002 for payment of lease rent arrears, HPCL initiated a proposal (October 2002) both for the payment of arrears and for floating of tenders for disposal of the jetty on 'as is where is basis', which was approved by the appropriate authority in January 2003. The open tenders were floated in April 2003 for taking over the equipment/facilities with two options, one for operation of the jetty after entering into lease with KPT and the other for dismantling of the jetty. Two offers were received, one for each of the two options. While the offer for operation of the jetty was technically rejected as KPT did not agree (September 2003) for sub leasing of the jetty to a third party, the bidder for dismantling option was requested to extend the validity period (expiry October 2003). The short listed party changed its terms and price while extending the validity period due to which HPCL decided (January 2004) to invite the tenders again. HPCL reinvited the tenders in February 2004 for taking over the assets and dismantling of the jetty. The contract was awarded in October 2004 to the lowest bidder at Rs.56.31 lakh to be paid by HPCL.

It was observed in Audit that HPCL took excessive time in firming up a decision for dismantling and disposal of the jetty, even after the receipt of the consultant's report in December 2001. Further, if the contract for dismantling was awarded by October 2003, before expiry of the validity period of the original bid, the lease rental for one year amounting to Rs.1.46 crore could have been avoided.

The Management stated (May 2005) that during the period January 2002 to September 2004 it was exploring the feasibility of handing over the jetty to interested buyers who could operate the same after restoration of facilities and entering into a lease agreement

with KPT. However, the Management admitted that the time taken from September 2003 to October 2004 in awarding the contract could be marginally reduced. The Ministry endorsed (October 2005) the views of the Management.

The Management's reply is not tenable because both OCC and KPT had indicated in April/August 2000 that the operation of virtual jetty would not be commercially viable in the changed scenario and Management's efforts of exploring the possibility of handing over the jetty to a third party did not yield any results in the year 2000. The consultant's cost estimate of Rs.19.75 crore in restoration of facilities further indicated that all the efforts for operation of the jetty would be rendered futile.

Thus, the delay in taking a firm decision on dismantling and disposal of the jetty and the further delay in award of the contract resulted in avoidable payment of lease rent amounting to Rs.1.46 crore.

Indian Oil Corporation Limited

14.6.1 Idle investment in Sulphur Recovery Unit

The Company installed Sulphur Recovery plant with unrealistic capacity and assumed higher sulphur content in HSD feed stock. As a result the unit remained idle for two and a half years due to insufficient feed with a lower sulphur content and an investment of Rs.13.05 crore remained fruitless apart from loss of interest of Rs.1.63 crore.

With a view to meet the improved specification of 48 cetane* of High Speed Diesel Oil (HSD) and to bring about overall reduction in emission of sulphuric gases, India Oil Corporation Limited (Company) approved (February 1999) a proposal for installation of Hydrotreatment facilities at Guwahati Refinery (GR) at an estimated cost of Rs.497.00 crore. The Hydrotreatment facilities consisted *inter alia* of Sulphur Recovery Unit (SRU) and Delayed Coking Unit (DCU). The design capacity of SRU was based on the assumption of an hourly Hydrogen Sulphide (H_2S) feed of 230.70 Kg per hour and design sulphur content of 0.24 weight percentage (wt *per cent*) in HSD feed stock.

The SRU was commissioned in December 2002 along with Amine Regeneration Unit (ARU) and Sour Water Stripper (SWS) at a cost of Rs.141.06 crore of which the plant and machinery cost of SRU was Rs.13.05 crore. The Company had to suspend the operation of SRU after four days of operation due to insufficient feed and could produce only three MT of sulphur during this period as against the capacity of five MT per day. Thereafter, the SRU was idle. The available H_2S feed was 88-110 kg/hrs against the designed requirement of 230.70 kg per hour even at 80 *per cent* capacity utilisation of refinery, which was inadequate for SRU operation. Moreover, the actual sulphur content in HSD feed stock was lower than the design content even though there was no change in source and nature of crude processed at GR. Due to non-operation of SRU, H_2S was

* ***A rating on a scale used to indicate the tendency of a fuel for diesel engines to cause knock, it is also the percentage by volume of cetane in the mixture that has the same performance as the fuel being tested.***

being burnt in the acid flare without recovery of sulphur. However, the GR was meeting the desired sulphur emission norms.

The SRU continued under idle condition and the Company was incurring recurring expenditure of Rs.65.00 lakh per annum towards interest on the loan taken for the investment made in SRU (March 2005).

The Management stated (June 2005) that sulphur level in Assam crude at that time was much lower than earlier level, which in turn resulted in lower than designed feed for SRU required for its start up and operation. The Management also stated that the Company would be able to operate the SRU at 45 *per cent* to 50 *per cent* capacity with availability of HSD from Bongaigaon Refinery and Petrochemicals Limited (BRPL) on sustained basis.

The Management's contention is not tenable as sulphur level in Assam crude remained almost constant over the last 20 years and ranged between 0.16 *per cent* wt to 0.23 *per cent* wt. Designing of SRU on the basis of high sulphur level without considering the past average indicated lack of proper recognition of risk of variance from a critical factor while designing the SRU. Also, BRPL had already taken up Diesel Hydro Treatment project for processing of its HSD and thus, availability of BRPL HSD to GR on a sustained basis in future was doubtful.

Thus, due to installation of a plant without making realistic assessment of the parameters of a critical input and subsequent non-reduction of capacity of the plant, the Sulphur Recovery Unit remained idle for two and a half years and an investment of Rs.13.05 crore remained unfruitful, on which interest of Rs.1.63 crore♥ had already been paid.

14.6.2 Non-recovery of dues

IOCL could not recover an amount of Rs.13.69 crore from Dabhol Power Company due to (i) absence of system for timely flow of documents between its various departments and consequent inordinate delay in raising final bills and (ii) non-collection of 'C' forms in advance as per agreement with the customer.

Indian Oil Corporation Limited (IOCL) supplied High Speed Diesel (HSD) from September 1999 to April 2001 and Naphtha from January 2001 to May 2001 to Dabhol Power Company (DPC). As per the agreement entered into with DPC for supply of HSD, IOCL had to raise provisional bills towards cost of HSD within two days of the supply. On receipt of the final bills towards insurance, demurrage, surveyors charge, port dues and actual freight, DPC was required to pay for the final bills within two working days of receipt. In the event of failure, IOCL was entitled to recover interest. The agreement also provided for obtaining 'C' forms in advance from DPC for charging concessional rate of central sales tax. As regards Naphtha, no formal agreement was signed but a term sheet existed. As per the term sheet, IOCL was required to raise an invoice within 10 days of supply, for which DPC was to make payment within thirty days.

♥ *Rs. 13.02 crore at the rate of five per cent = 0.65 crore per annum x 2.5 years= Rs.1.63 crore*

IOCL raised the provisional bills for supply of HSD and Naphtha and also received payment regularly. However, there was inordinate delay in raising the final bills, as there was no proper coordination amongst its Maharashtra State Office (MSO) and Head Office, Supply Points and Western Regional Office, which were responsible for furnishing supporting documents/information to MSO for raising the final bills. In May 2001, Maharashtra State Electricity Board (MSEB), which had a contract with DPC for purchase of power, scrapped the Power Purchase Agreement and DPC's plant was shut down in June 2001. IOCL raised the final bills in June 2001 for Rs.1.82 crore and Rs.70.00 lakh for supply of HSD and Naphtha respectively. In July 2001, IOCL raised further debit notes for Rs.1.05 crore towards differential excise duty and sales tax thereon relating to supply of HSD. Further, an amount of Rs.4.98 crore and Rs.4.52 crore in respect of supply of HSD and Naphtha respectively were due from DPC on account of differential sales tax due to non-collection of 'C' forms in advance during the year 2001-02.

As pursuance with DPC did not elicit any response, IOCL invoked the arbitration clause and an *ex-parte* award was given in favour of IOCL in July 2003. DPC was directed to pay a sum of Rs.8.47 crore, which included the amount of final bills, debit notes and interest in respect of HSD supply. IOCL could not execute the award as DPC plant was shut down since May 2001 and all its assets were in the custody of the Court Receiver. Chances of recovery of the dues from DPC were bleak because it was heavily indebted to the financial institutions that held lien on all its immovable assets.

Since no formal agreement was signed with DPC for supply of Naphtha, IOCL could not proceed for arbitration and instead filed summary suit against DPC for recovery of dues. Summons issued by the Hon'ble High Court in pursuance thereof, could not be delivered as the offices of DPC were closed. The summons were lodged with the Sheriff of Bombay for deliverance at a later date.

The Management stated (August 2005) that the final bills in respect of other charges could not be raised in time due to involvement of several external agencies and collection of supporting documents for the actual charges from them. Further, the circumstances leading to non-collection of 'C' forms for 2001-02 were beyond control as DPC went for closure abruptly.

The Management's contention is not tenable as there was no proper structural system for flow of documents/information among the various departments of IOCL, which contributed to the delay of more than one year in raising the final bills.

Thus, inordinate delay and lapses in raising the final bills/debit notes and non-collection of 'C' forms in advance from DPC resulted in non-recovery of dues aggregating to Rs.13.69 crore (Rs.8.47 crore towards HSD and Rs.5.22 crore towards Naphtha).

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

14.6.3 Wasteful expenditure on creation of Bitumen Handling Facilities

The Company's failure to ensure the availability of bitumen in bulk quantity either locally or through imports before embarking upon the project for creation of bitumen handling facilities led to wasteful expenditure of Rs.3.94 crore.

Indian Oil Corporation Limited, Southern Region (Company) placed (May 2000) consultancy order on M/s. MECON Limited, Bangalore on total responsibility basis for providing storage facilities for bulk quantity of bitumen at Mangalore and Wellington Island by converting the existing tanks being used for storing furnace oil and light diesel oil. The modified storage facilities were meant for retaining /increasing market share for bitumen and proposals in the matter were mooted in June 1999. The cost estimates for these works at Mangalore Terminal and Wellington Island were Rs.2.59 crore and Rs.1.43 crore respectively. The scheduled completion date was October 2000 for Mangalore and September 2000 for Wellington Island.

Scrutiny in Audit revealed that the Company had not obtained firm commitment from any manufacturer /supplier about the availability/feasibility of moving bitumen in bulk quantity to Mangalore and Wellington Island at the proposal stage itself. After incurring an expenditure of Rs.2.24 crore at Mangalore Terminal and Rs.1.70 crore at Wellington Island, the Company decided (February 2002) to foreclose the work/project due to non-availability of bitumen in bulk quantity either from imports or from local sources like Haldia Refinery.

The Management stated (October 2004) that the tanks were converted to store furnace oil and subsequently low viscosity furnace oil (LVFO) and other pipelines /materials were used for alternate purpose like maintenance and repair.

The reply is not tenable as the heating facilities, pipeline and insulation created for moving bitumen were not required for carrying /pumping furnace oil/LVFO etc. Further, these tanks were already in existence and were being used for storing furnace oil/light diesel oil and the Company after discontinuing with the project merely reverted back to using them for the same purpose. Hence, the customised facilities created for storing and transporting bitumen could not be used for the intended purpose.

Thus, the Company's failure to contract regular supply of bitumen before embarking upon the project led to its foreclosure resulting in wasteful expenditure of Rs.3.94 crore.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

14.6.4 Non-recovery of dues from customer

Allowing unsecured credit to a customer, beyond approved terms, resulted in seriously jeopardising the recovery of sale proceeds amounting to Rs.1.97 crore.

M/s. Ispat Alloys Limited (IAL) was a customer of Indian Oil Corporation Limited (Company) requiring Furnace Oil (FO) for their captive power generator plant at Orissa. In July 1999, after extensive negotiation with IAL, the Company decided to enter into a

long-term agreement with the latter for five years for 100 *per cent* supply of FO on the following terms

(i) Delivered supply to the customer plant

(ii) Thirty days clear credit

(iii) Discount of Rs.340 per per KL to the general trade price

The approval to the above proposal categorically stated that 30 days' credit would be provided only against unconditional Letter of Credit (LC) to be opened before commencement of supplies. However, the Company did not sign any formal agreement on this issue with IAL.

Despite IAL's track record of delayed payment and pending signing of the agreement, the Company started (June 1999) supplying the product on liberal credit. IAL did not open LCs prior to commencement of supplies and in most of the cases released payments only after 45 days. Consequently, outstandings started mounting and stood at Rs.5.16 crore in August 1999. Though IAL agreed in September 1999 to clear the dues in a staggered manner and to open advance LC or Bank Guarantee for supplies from October 1999, it did not honour these commitments. Inspite of huge outstanding, the Company continued to supply FO during September 1999 to December 1999 on credit and also allowed discount instead of charging interest on outstanding dues. The outstanding dues as on December 1999 stood at Rs.4.81 crore. IAL stopped taking supplies of FO from January 2000.

The Company collected Rs.2.20 crore between January 2000 and February 2001 leaving an outstanding balance of Rs.2.61 crore. However, IAL accepted outstanding dues of only Rs.2.17 crore. The Company filed winding up petition at High Court of Orissa, Cuttack against IAL under Companies Act, 1956 in July 2001 as a last resort for recovery of dues of Rs.2.61 crore. Following the Court's intervention, the Company, was able to recover Rs.64.00 lakh till November 2003. Meanwhile, IAL filed (May 2003) a case before BIFR for declaring itself as sick industry. Consequently, the Company could not take any further action for recovery of the dues.

The Management while admitting the facts stated (July 2005) that it was a conscious decision to release FO to the customer against 30 days' credit along with discount pending opening of letter of credit in the overall interest of the Corporation, as there was already a threat of losing substantial volume of business. The Management further stated that efforts were on to recover the dues.

The contention of the Management is not acceptable as the supply of FO to IAL on the above terms was in violation of the Company's considered decision to extend credit only against unconditional LC as a part of its long-term business strategy. The Company's action indicates failure to take necessary financial safeguards in dealing with a customer especially when the Management was aware that the customer was already defaulting in paying the outstanding amounts due. In view of IAL's application before BIFR, possibility of recovery of the Company's dues is remote.

In attempting to derive short-term advantage, the Company failed to safeguard its interest and took a normally unacceptable risk in supplying FO to IAL, which ultimately resulted in non-recovery of dues amounting to Rs.1.97 crore since December 1999 with consequent loss of interest.

The matter was reported to the Ministry in August 2005; its reply was awaited (November 2005).

14.6.5 Idling of assets due to irregular construction

Indian Oil Corporation Limited constructed a housing colony for its employees at Varanasi without obtaining approval of the local authority and without ascertaining basic amenities, leading to idling of assets valuing Rs.1.54 crore.

The Company decided (November 1996) to construct a housing colony for its officers and workmen working in the LPG[*] Bottling Plant and for other field offices at Varanasi. Without getting the layout plan approved by the Varanasi Development Authority (VDA), the Company awarded (January 1998) construction work to M/s. APCO Private Limited.

After the start of work, the Company received notices (September 1998) from VDA to stop the construction as it was unauthorised. In response to the notices, the Company deposited (October 1998) requisite fee for approval of layout plan but its request was rejected by VDA (January 2000). The Company also did not obtain permission for conversion of land use from agriculture to residential from VDA before commencing construction.

Despite notices from VDA, the Company continued the construction activities and completed 16 flats (June 2000) at a total cost of Rs.1.41 crore. The Company thereafter deposited (December 2000) Rs.9.96 lakh under self-assessment scheme of VDA as conversion charges for using the agricultural land for residential use and Rs.2.61 lakh for electricity connection (February 2001).

The flats were lying vacant (July 2005) as the employees resisted occupation of the flats mainly due to distance from the city and non-availability of other basic amenities like medical/education facilities. Efforts of the Company to lease out the property were also not successful. The Company could not dispose of the property pending its regularisation by VDA.

The Management stated (December 2004/July 2005) that

(i) Submission of layout plans to VDA was not envisaged as the land for the LPG plant was acquired 16 Kms away from the city;

(ii) With the setting up of LPG plant great development was expected in the area;

[*] *Liquified Petroleum Gas*

(iii) The decision to construct the flats was based on the need and willingness of the employees at that point of time. The situation changed drastically since last four years due to liberalised self-lease facility for workmen.

The Ministry endorsed (August 2005) the above reply of the Management.

The reply is not tenable because:

(i) It was essential for the Company to ensure necessary conversion of land use and approvals of the regulatory authorities before commencing construction. The Company proceeded with the construction work even after objection from VDA in September 1998.

(ii) The LPG plant was commissioned in 1991. Before commencing construction in 1998, there was enough time for the Company to assess development in the area.

(iii) The Company was aware of the liberalised self lease scheme at the time of taking decision for construction. The possible impact of such scheme on the occupancy of flats should have been assessed before commencement of construction.

Thus, the decision to construct the housing complex in a remote area, without obtaining the approval of VDA or assessing the requirement of employees resulted in idling of assets of Rs.1.54 crore (Rs.1.41 crore on construction cost, Rs.9.96 lakh as conversion charges and Rs.2.61 lakh for electricity connection).

14.6.6 Loss due to inadequate security

The Company continued supply of lubricants on credit without security to a suspended retail outlet resulting in non-realisation of sale proceeds, interest and penalty thereto amounting to Rs.1.44 crore.

The Company entered into (December 1998) a dealership agreement with M/s. AAUI (dealer) to operate its retail outlet at New Delhi. As per terms of the agreement and credit policy the Company supplied Motor Spirit and High Speed Diesel against cheques and lubricants at 30 days' interest free credit against post-dated cheques to the dealer.

The retail outlet had to be closed for resitement (August 1999) under the orders of the Hon'ble Supreme Court. The resitement could not materialise and the Company suspended the supplies of Motor Spirit and High Speed Diesel to the dealer from September 1999. It however, continued to supply lubricants on 30 days' credit against post-dated cheques and at discounted rate. The supplies of lubricants from September 1999 were made ex-depot instead of supplying at the designated premises. No security was also obtained for this. The payment for supplies upto 24 November 1999 was received from the dealer but supplies aggregating to Rs.95.76 lakh (sales value Rs.91.65 lakh plus discount allowed Rs.4.11 lakh) made during 25 November 1999 to 28 December 1999 remained unpaid due to dishonour of the dealer's post-dated cheques on presentation.

The Company initiated criminal proceedings under the Negotiable Instruments Act (February and March 2000) for dishonoured cheques but referred the case to arbitration

after two years (February 2002). The arbitration as well as cases under Negotiable Instruments Act were pending (July 2005). Meanwhile the dealer paid Rs.10.00 lakh (March 2000) and the balance amount was considered doubtful and provided for by the Company in its accounts (March 2002).

The Management in its reply (November 2004/ August 2005) stated that:

(i) The suspension of operation of retail outlet was due to its resitement as per directives of the Court. Since dealer was doing very well in lube sales particularly in bazaar trade, they continued to supply lubricants to the dealer even after closure of retail outlet in their commercial interests.

(ii) As AAUI continued to remain a dealer despite temporary suspension of operation at the old premises, no need was felt to review their dealership status and other benefits.

(iii) The supplies of the lubricants to the dealer continued to be based on the approved 30 days' credit against post-dated cheques as per policy, which did not provide for obtaining any security from the dealer.

The reply of the Management is not tenable as

(i) The supply was continued even after closure of the retail outlet on credit on ex-depot basis which was not envisaged in the agreement. Ex-depot sales in the absence of an alternative approved storage/ retail outlet deprived the Company of its right to take the possession of its products from the dealer even when post dated cheques were dishonoured.

(ii) The suspension of operation of retail outlet being a new development, adequate securities should have been obtained from the dealer to safeguard the interests of the Company.

(iii) The credit policy was deficient as it did not provide for adequate safeguards in such cases.

Thus, continuance of supplies even after closure of operations of the retail outlet and extension of credit in the absence of security resulted in non-realisation of Rs.1.44 crore (Principal amount: Rs. 81.65 lakhs, discount allowed: Rs.4.11 lakh, interest: Rs.56.00 lakh and penalty: Rs. two lakh) from the dealer.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

14.6.7 Avoidable expenditure due to delay in closing a depot

Due to delay in closure of Gorakhpur depot, the Company incurred an avoidable expenditure of Rs.66.75 lakh during May 2002 to March 2004.

The Company commissioned a depot at Baitalpur (December 1994) as a relief depot for its Gorakhpur depot. The supplies to different regions that were being met through

Gorakhpur Depot were shifted in a phased manner from December 1994 to June 2001 to the Baitalpur depot. Due to commissioning of Baitalpur depot, the Company noticed (May 2001) that wasteful expenditure was being incurred at Gorakhpur depot and decided (June 2001) to close it by 15 June 2001 and surrender the land to Railways. It was also decided that all work at Gorakhpur Depot should be completed so that there would be no further outgo.

Though the Company closed white oil operations of the Gorakhpur Depot in June 2001, it continued its lube operations which were finally closed in April 2002. The Company then entrusted the job of disposal of assets to MSTC Limited in November 2002 and tenders for disposal to M/s. Said Steel Traders, Kanpur were finalised by October 2003. The disposal work was completed only in March 2004 when the land was handed over to the Railways.

Thus, despite a decision to close the depot by June 2001 and final cessation of all activities of the Depot by April 2002, the Company completed the closure activities only by March 2004 and incurred an avoidable expenditure of Rs.66.75 lakh on account of lease rent and security during May 2002 to March 2004.

The Management stated (October 2004/September 2005) that:

(i) Lube operations had to be continued at Gorakhpur depot till registration of Baitalpur depot with Central Excise Department for MODVAT facility which was obtained in December 2001.

(ii) Gorakhpur depot land could be surrendered to Railways in March 2004 after all the assets were fully disposed of by February 2004.

The reply is not acceptable because:

(i) Even after obtaining the registration for MODVAT in December 2001, the Company took more than two years to close the depot and surrender the land.

(ii) Despite closure of all operations in April 2002 and knowing that wasteful expenditure was being incurred at Gorakhpur depot, dismantling of assets and handing over of land was delayed due to slow processing of activities of routine nature like entrustment of job to MSTC Limited and finalisation of tenders. The Company had taken more than two and a half years in dismantling/disposal of assets and in surrendering (March 2004) the land to Railways.

Thus, due to delay in closure of Gorakhpur depot, the Company incurred an avoidable expenditure of Rs.66.75 lakh during May 2002 to March 2004.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

Oil and Natural Gas Corporation Limited

14.7.1 Loss due to improper contract Management

ONGC incurred an avoidable expenditure of Rs.42.77 crore due to delay in award of contract for logging services and subsequent injudicious termination of the contract, which led to payment for the services at higher rates and idling of its rigs.

ONGC had contracts with two firms for logging services in its offshore field; the contracts were to expire in December 1999. As per ONGC's prescribed time schedule for finalisation of contracts, ONGC should have invited the tenders by June 1999♣. However, in June 1999, a Committee was appointed by ONGC to firm up specifications and bids evaluation methodology. The Committee finalised its recommendations after almost one year, based on which Bid Evaluation Criteria (BEC) was determined in July 2000. Tenders were invited in August 2000 and the contract awarded in March 2001. Meanwhile, due to delay in finalisation of the new contracts, ONGC extended the existing contracts on the same terms upto May 2001.

A comparison of the rates quoted by the bidders, with the rates at which the original contract was awarded, showed that there was an overall decrease in prices by 16.5 *per cent* in Segment-I♦, 14.90 *per cent* in Segment-II and 38 *per cent* in Segment-III B. The cost reduction on account of the decrease in rates, for the tendered volume of work, worked out to Rs.3.47 crore per month. The cost saving foregone from October 2000 (date of opening of bids) to May 2001 (expiry of extended contract period) worked out to Rs.12 crore approximately (at 14.90 *per cent* on actual outgo).

The Management stated (July 2004) that the pre-tender conference, bidders' conference and subsequent technical committee recommendations took some time and this process resulted in competition generation and the savings in contractual outgo because of lower prices compared to earlier prices across all segments. The reply is not tenable since the Company could still have reaped these advantages if it had firmed up its requirements and specifications in advance and invited the tenders well in time, considering the lead time required.

The contract was awarded in March 2001 for providing logging services, including supply of logging equipment/tools for rigs engaged in drilling/work over activities, in 16 units to M/s. Halliburton Offshore Services Inc. (HOSI) and in 12 units to M/s. Schlumberger Asia Services Limited (SASL). The services to be provided by HOSI included supply of a new tool in Segment-I called 'Reservoir Monitoring Tool (RMT)' which was to be imported from USA. However, USA had meanwhile imposed sanctions against India and placed restrictions on export to India of dual use technology/equipment like nuclear sensing tools. RMT was at par with ONGC's specification code NIGS♥ and

♣ *Providing 120 days for tender finalisation plus mobilisation time*

♦ *Logging services generally fall under four segments relating to development drilling (Segment-I), exploratory and side tracking drilling (Segment-II), on line logging (Segment-III) and slick line operation (Segment-IV). Each segment requires a specific set of tools.*

♥ *Nuclear Induced Gamma Ray Spectroscope Tool*

could not have been imported from USA, but this fact was not highlighted by ONGC during pre bid conference and the tender finalisation process.

HOSI, having failed to mobilise RMT, proposed another equivalent tool, but ONGC did not agree and cancelled the contract (October 2001) with HOSI under Segment-I and awarded this work on the same rates to SASL. HOSI withdrew from the contract (December 2001) also under Segment-II and III B, as working in these Segments was not financially viable to it without working in Segment-I. ONGC had to award the contract (February 2002) for these units also to SASL at a price higher by about 28 *per cent* than those quoted by HOSI, as SASL did not agree to HOSI's rates. With a view to save on costs, ONGC cut down on the total number of tools while awarding this contract to SASL. However, the shortage of these tools led to idling of some of the rigs and impacted adversely the logging and drilling operations.

Due to offloading of work to SASL at higher rates, ONGC had to bear an extra avoidable expenditure of Rs.20.37 crore on actual outgo. The loss on account of idling of rigs worked out to Rs.10.40 crore during the period from December 2001 to March 2004, based on prevailing hire charges of the rigs.

The Management stated (July 2004/June 2005) that there was no reason to believe that HOSI would not be able to provide RMT and the alternate tool offered by HOSI was not a substitute of RMT. The Management also contented that had they allowed HOSI to operate without the essential tools/services, it would have resulted in vitiation of the tendering process. The Ministry endorsed (June 2005) the views of the Management.

The Management reply is not tenable because before the award of the contract ONGC should have assured itself of the availability of RMT or equivalent tool keeping in view the USA sanctions. Further, the criticality of RMT for the contract work was debatable as was evident from the submission of the technical personnel that frequency of use of the tool was very low and foregoing of this service would not have any major impact on the development and work over activities. The technical personnel also found the alternative tool offered by HOSI viz. 'Thermal Multigate Décor Log (TMDL)' to be acceptable. ONGC did not also consider using the equivalent service 'Reservoir Saturation Testing tool (RST)' available with SASL as and when required. An Out Expert Committee (OEC), to whom the disputes between ONGC and HOSI were referred for settlement, rejected the claims of ONGC and observed in its final report (September 2004) that 'ONGC has not shown requisite prudence and sound commercial judgment in cancellation of the contract for Segment-I with HOSI'. OEC also observed that failure to procure RMT should not have been viewed so seriously, as ONGC knew by October 2001 that sanctions had been lifted by USA and procurement of RMT by HOSI would not get delayed.

Thus, the injudicious termination of the contract with HOSI for Segment-I led to an extra avoidable expenditure of Rs.20.37 crore (on actual outgo) and the loss of Rs.10.40 crore on account of idling of rigs. Besides this, due to delay in award of the contract, ONGC lost the possible cost saving of Rs.12 crore on account of reduced rates.

14.7.2 Loss due to delay in applying for wheeling of power

ONGC suffered loss of Rs.19.61 crore between October 2001 and October 2002 due to delay of 13 months in submission of application to Gujarat Electricity Board for wheeling of surplus power from its Hazira plant to Mehsana unit.

Gujarat Electricity Board (GEB) declared its captive power policy in December 1998, which was effective from 9 November 1998, allowing wheeling of surplus power from Captive Power Plant (CPP) of an industrial company to other industrial units within the same company or to any industrial unit of its group company.

Hazira Plant of ONGC had installed capacity of 57.6 MW of power generation (3 x 19.2 MW) against the total operational power requirement ranging from 30 MW to 35 MW. The competent authority had approved (January 2000) a proposal for wheeling of power to Mehsana Asset (another unit of ONGC) as it was considered more beneficial than selling its surplus power to GEB. The Asset confirmed in December 1999 itself that its Enhanced Oil Recovery (EOR) Plant at Santhal Phase II would be operational by June 2000 and would require 10 MVA power initially, which might go upto 50 MVA in 2004.

Application, seeking permission for wheeling of 15.7 MVA surplus power to Mehsana, was submitted to GEB only in February 2001 i.e. after 13 months of approval of the proposal for wheeling. ONGC was well aware of all the requisite documentations required for the same as early as in January 1999 as was advised by GEB itself to the Hazira Project of ONGC. GEB accorded the permission for wheeling of power in June 2002 and, after making arrangements with GEB for the meter readings, the actual wheeling of power to Santhal Main at Mehsana commenced from November 2002. Thus, it took 21 months from the date of application to the wheeling of power. If the application had been submitted to GEB in January 2000 on approval of the competent authority the wheeling of power could have commenced from October 2001, based on the actual time of 21 months taken in wheeling of the power.

The delay in submission of the application to GEB for permission to wheel the power, despite adequate time available for preparation of the documentation after intimation by GEB in January 1999, resulted in loss of Rs.19.61 crore during the period October 2001 to October 2002. The loss was on account of difference between high cost of power purchased by Mehsana Asset (Santhal Phase-II) from GEB and the revenue earned by the Hazira Plant from sale of equivalent units of its surplus power to GEB, during the period from October 2001 to October 2002.

The Management stated (May 2005) that Hazira Plant had faced numerous black out situations due to problems in GEB gird prior to 2000. ONGC opted for complete revamp of 66 KV protection systems and included grid islanding scheme with the state of the art numerical control relays, which enabled automatic isolation of their system from that of GEB in case of grid faults. Establishing reliability of system and removal of apprehension of 'process upsets' was essential to ensure and establish that it did not affect the plant operation. The exercise of confidence building and the coordination and documentation, required from multiple sources, took time. The Ministry endorsed (July 2005) the views of the Management.

The Management's reply is not tenable in view of the following:

(i) To remove the problems in GEB grid, Hazira project had already commissioned the islanding system for safe inter-connection with GEB grid on continuous basis in December 1999. The GEB grid was synchronised with Hazira Gas Processing Complex on 8 March 2000 upto 7 April 2000 on trial basis and no problem was faced by the project due to the installation of the state of the art protection system.

(ii) ONGC was aware of all the documentations required for the application to GEB for grant of wheeling power, two years prior to applying for the same. Despite the significant benefit that would arise from the wheeling of power, ONGC did not complete the application and documentation in advance and did not apply for the permission immediately after approval of the competent authority.

Thus, the inordinate delay of 13 months in submitting the requisite application/documents to GEB and the resultant loss of Rs.19.61 crore was avoidable.

14.7.3 Loss due to avoidable flaring of gas

ONGC's failure in arrangement of gas compression facility at the Group Gathering Station-II at Ankleshwar, resulted in avoidable flaring of gas valued at Rs.10.65 crore during the period from April 2000 to April 2003.

ONGC awarded a two year contract in April 1997 for hiring of compressors to be installed in four Group Gathering Stations (GGS) to achieve zero flaring of low pressure gas in Ankleshwar project. The Company did not include in the scope of the contract the requirement of GGS-II, on the ground that no gas was being flared. The contract was valid upto April 1999 and extended from time to time till September 2003 due to delay in finalisation of a new contract. Actual flaring of gas in GGS-II started in May 1998, which went upto 58,000 cubic meter per day in January 1999 and ranged between 50,000 and 64,000 cubic meter per day during the period from February 1999 to June 2000. The Management, instead of arranging compressor facility at GGS-II in April 1999 (after considering three months time from January 1999 for observation) when gas flaring reached 58,000 cubic meter per day, initiated the action for correction only in July 2000 when fresh tenders were invited for hiring a new set of compressors at all GGSs including GGS-II.

The new contract was awarded in August 2001 and the hired compressors at GGS-II were installed and commissioned by March 2002. However, due to delay in mobilising and commissioning of compressors at other GGSs, the entire contract was terminated by ONGC in May 2002. While the flaring of gas at other GGSs continued to be controlled through the compressors installed under the previous contract and internal arrangements by the Management, no alternate arrangement of compressors was available at GGS-II. Hence, the termination of the new contract led to the further flaring of gas at GGS-II from May 2002 to May 2003 when a new contract was entered into for all GGSs (including GGS-II).

It was observed in Audit that an option was available under clause 4.6 (A) (b) of the contract which provided for termination of the contract partially but was not made use of

by ONGC. Had this option been utilised and the contract terminated partially by retaining it for GGS-II, the flaring of gas could have been avoided. The delays and the avoidable termination led to flaring of gas during the period from April 2000 and April 2003 valued at Rs.10.65 crore.

The Management stated (August 2004) that the contract was terminated due to delay by the contractor in commissioning of the compressors at other GGSs. The Management further stated that they installed two alternative compressors at GGS-II in October 2002 to minimise the gas flaring.

Reply of the Management is not tenable as with the two alternate compressors arranged in October 2002, the gas flaring at GGS-II could be curtailed only marginally. As against 18.73 lakh cubic meters of gas compressed at GGS-II during October 2002 to May 2003, gas to the extent of 92.81 lakh cubic meters had to be flared. Despite the absence of adequate alternate arrangement of compressors, ONGC did not utilise the option of partial termination of the contract.

Thus, the failure of ONGC in arranging adequate compression facility in time and subsequent cancellation of the entire contract without alternate arrangements of compressors at GGS-II, led to avoidable flaring of gas of 5.07 crore cubic meters during the period from April 2000 to April 2003 (after considering one year from April 1999 for tendering procedure and installation of compressors). The resultant loss suffered by ONGC was Rs.10.65 crore*.

The matter was reported to the Ministry in June 2004 and May 2005; its reply was awaited (November 2005).

14.7.4 Wasteful expenditure on an ill-conceived Project

Approval of the Food Grade Hexane (FGH)/Special Boiling Point (SBP) solvent project without giving due consideration to the current demand situation and unauthorised use of these products led to wasteful expenditure of Rs.9.05 crore between 1998-99 and 2001-02.

Based on market survey carried out by the Indian Institute of Petroleum (IIP) in June 1997 and detailed Feasibility Report (September 1998) by Engineers India Limited (EIL), ONGC's Board of Directors approved a project (April 1999), in principle, for processing of Naphtha in the production of 20 thousand metric tonnes per annum (TMTPA) of Food Grade Hexane (FGH) and 136.5 TMTPA of Special Boiling Point (SBP) solvent. After finalisation of bid evaluation criteria, ONGC invited/reinvited the tenders in November 1999/October 2000 for award of contract on turnkey basis and the contract for Rs.52.17 crore was awarded in July 2001.

The viability of the project was based on demand growth in future. Even though the Feasibility Report (September 1998) showed a balance in demand and supply of these products, ONGC did not keep a close track of the current demand situation. The demand of these products from 1997 onwards showed a declining trend. Further, the Feasibility

* *after giving allowance for technical gas flaring at the rate of five per cent*

Report clearly mentioned the apprehension raised by the industry circle that a part of supply of these products was being diverted for adulteration. Despite this, the project was approved in April 1999.

In June 2000, the Ministry of Petroleum and Natural Gas issued 'Solvent Raffinate and Slop (Acquisition, Sale, Storage and Prevention of use in Automobiles) Order, 2000' which restricted the diversion of these products for unauthorised applications and adversely affected the demand for these products. However, without reviewing the current market trend and the impact of the Government's order of 2000 on the future consumption pattern of these products, the Executive Purchase Committee of ONGC approved the award of contract (June 2001) for FGP/SBP solvent project to M/s. MECON Limited.

In view of the surplus supply situation prevailing in the country and under-utilisation of existing facilities, the Chairman and Managing Director of ONGC advised in December 2001 that the project should be put on hold and ordered short-listing of credible buyers through pre-bid conference to establish product execution on a long-term contractual commitment basis. ONGC, however, found that in the absence of price formula and the surplus availability of the products in the immediate future, the parties were passive on the issue of long-term commitment. ONGC's Executive Committee, therefore, decided (May 2002) to drop the FGH/SBP solvent project. Accordingly, the contract with M/s. MECON Limited was terminated in January 2003 and the expenditure of Rs.9.05 crore incurred on the project was written off by ONGC.

The Management stated (May 2005) that the business decision was taken at a point of time based on certain parameters, which could change with the passage of time.

The reply is not tenable as:-

(i) At the time of approval of the project (April 1999) the market for FGH and SBP solvent was saturated and these products were being diverted for unauthorised purposes. ONGC proceeded with the project without considering how it would tackle the risk of excess supply situation in future and the unauthorised use of these products.

(ii) The decision of ONGC to award the contract to M/s. MECON Limited in July 2001, without reviewing the declining market trend and the apparent adverse impact of the Government's order of June 2000 on the future demand for these products, indicates lack of commercial prudence.

Thus, ONGC incurred wasteful expenditure of Rs.9.05 crore on the project due to its approval without any strategy to deal with excess supply situation and the award of contract without reviewing the current market trend.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

14.7.5 Wasteful expenditure on idling of rig

ONGC's failure to obtain prior clearance from forest authorities for drilling at a location forming part of 'Desert National Park' and non-provision of an alternative drilling location in its Annual Drilling Plan, led to idling of rig for 292 days in 2002 and wasteful expenditure of Rs.7.21 crore.

Under a notification issued by the Ministry of Environment and Forests on 4 May 2001, ONGC was required to obtain permission of the forest authorities for drilling in any location falling under the reserved 'Sanctuary and National Park'. The location MJAA (in Miajlar village) at Jodhpur Project was planned for drilling with rig E760-13 on 26 May 2001. The location formed part of the 'Desert National Park'. The necessary work order for 130 km of rig track civil works was awarded in November 2001. Civil work upto 75 Kms for the track and the site was completed and Rs.35.91 lakh was paid to the contractor. As ONGC did not obtain clearance from the forest authorities as required under the regulations, the work was stopped on 4 January 2002 by the forest authorities and the rig was held up there till 11 November 2002. The rig was then transported to another drilling location (CT-1 site) on 12 November 2002. In the process, the rig remained idle for 292 days (4 January 2002 to 11 November 2002 excluding 20 days for rig building), due to Management's failure to obtain prior clearance from the forest authorities; and non-existence of an alternative location built into the rig deployment plan. The idling of rig resulted in wasteful expenditure of Rs.6.85 crore apart from wasteful expenditure on civil works valued at Rs.35.91 lakh.

The Management stated (March 2004) that they were not aware of the fact that location MJAA was a part of 'Desert National Park' and efforts were made to get the clearance for drilling at the location MJAA. As regards civil works, the Management replied that the track would be utilised for transport of the rig to MJAA at Miajlar after permission of the Supreme Court. The Management also stated that the rig remained idle as it could not have been deployed elsewhere owing to its size and requirement of approach road. The Ministry endorsed (October 2005) the views of the Management.

The Management's/Ministry's reply is not tenable as:

(i) The location MJAA was notified as a Desert National Park way back in 1980. While selecting such sites for drilling, the Company should have obtained prior clearance from the competent authorities. The Company had not exercised due diligence, which is evident from the fact that the Petroleum Exploration Licence (PEL) also contained a stipulation that necessary approval should be obtained for any forest area included in the PEL.

(ii) The civil work being a 'Kachha' road, had become useless and a different road would be required for rig movement.

(iii) The rig remained idle because of non-existence of any alternative location in Annual Drilling Plan and not because of rig size or approach road.

Thus, failure to obtain prior clearance from forest authorities and absence of an alternative location led to idling of the rig for 292 days with consequential wasteful

expenditure of Rs.7.21 crore, underlining the need for streamlining the process of planning of drilling operations so that critical factors are not overlooked.

14.7.6 Loss due to delay in transport of rig material

ONGC suffered a loss of Rs.3.92 crore during the year 2003-04 on account of idling of rig due to delay in transportation of rig material.

In a drilling review meeting held in December 2002, ONGC decided that a desert rig at Rajasthan Project, Jodhpur after its conversion into conventional rig, would be deployed in Mehsana and Ahmedabad Assets to meet drilling targets of the year 2003-04. The Head Drilling Services (HDS)-Corporate Office, Mumbai suggested (April 2003) that necessary administrative approval for conversion of the desert rig and its transportation to Mehsana be granted expeditiously as any delay might result in loss to ONGC due to idling of the rig. Accordingly, the desert rig was released in April 2003 and dismantled by August 2003. Meanwhile, Basin Manager, Baroda approved (May 2003) the proposal for transportation of the rig to Mehsana on turnkey basis including loading and unloading of material, to ensure timely completion of the job.

On 22 May 2003, Head Forward Base, Jodhpur floated limited tenders for transportation of the rig on turnkey basis despite Mehsana Asset confirming (19 May 2003) the availability of crane for unloading even prior to issue of tenders. Bids were opened in June 2003 but the Tender Committee recommended (July 2003) re-invitation of tenders with loading and unloading rates to be taken separately on the grounds that Mehsana Asset had since confirmed availability of crane for unloading of the material. In July 2003, ONGC decided that Deputy General Manager (DGM), Incharge Logistic, Baroda would arrange for the transportation against their existing annual rate contracts. The DGM, Baroda issued two work orders on two transport contractors, but they were not willing to carry out the job under the prevailing annual rate contract. The work order was then issued in September 2003 to another transport contractor. The contractor completed the job in January 2004 at a cost of Rs.19.37 lakh, after a delay of more than a month due to the time taken in settlement of loads.

It was observed in Audit that due to not awarding the transport contract on turnkey basis, the transportation of the rig material was delayed by 84 days, which resulted in avoidable loss of Rs.3.92 crore towards idle cost of the rig after allowing normal time of 60 days required in transporting the rig material.

The Management/Ministry stated (August/October 2005) that:

(i) Against the tenders invited in May 2003, the lowest quote (Rs.24.80 lakh) was higher than the sanctioned cost (Rs.19.26 lakh) and as the tender committee also considered the information received from Mehsana Asset regarding crane availability for unloading, it was proposed to go for re-tendering.

(ii) As per decision of a Virtual Board meeting held in July 2003, the DGM, Baroda was asked to arrange the transportation of rig material under the then existing annual rate contracts to avoid further delay in re-invitation of tenders.

(iii) The transportation of rig material could be started only after the dismantling of rig equipment, which was completed in October 2003.

The above reply is not tenable in view of the following:

(i) The Company did not consider amendment in the tender documents, which were floated on 22 May 2003, despite receiving the information on 19 May 2003 from Mehsana Asset regarding availability of the crane. Further, considering the huge cost per day of an idle rig, it was not a judicious decision to delay the transportation work.

(ii) While seeking the approval in May 2003 for transportation of rig material through a turnkey contract, it was stated in the proposal that placement of trailer/trucks for long distance transportation through the annual rate contracts was irregular and the work had suffered in the past on this account.

(iii) Head Forward Base, Jodhpur had informed DGM, Baroda in August 2003 that the rig material was ready for transportation.

Thus, due to the delay in the transportation of rig material ONGC suffered an avoidable loss of Rs.3.92 crore towards idle cost of the rig.

14.7.7 Wasteful expenditure on procurement of defective Liquid Nitrogen Transportation Tanks

ONGC incurred wasteful expenditure of Rs.1.27 crore during 1999 to 2003 due to delay in examination of the third party inspection report against import of Liquid Nitrogen Transportation Tanks.

In September 1998, ONGC placed a purchase order on M/s. Marathon Marine Engineering (MME), Germany for supply and commissioning of eight Liquid Nitrogen Transportation (LNT) tanks at a cost of French Franc (FF) 2.82 million (equivalent to Rs.2.01 crore). The purchase order specified that (i) the material should be of recent manufacture, not older than one year from shipment date and (ii) the payment would be released against letter of credit (LC) on receipt of a set of specified documents including third party inspection by the bank. A copy of the same documents had also to be airmailed to ONGC by the party before sending the original documents through the bank for payment. The terms of payment against LC specified that (i) the material covered by the invoice had to pass the test and conform to contract specifications in every respect and (ii) all discrepant documents should be accepted strictly on collection basis by the negotiating bank so that payment to the supplier in respect of such documents could be made only after prior approval of the importer.

MME supplied eight LNT tanks in two lots. On 13 January 1999, ONGC's bank asked it for re-imbursement of an amount of Rs.69.74 lakh released to MME against the documents for the first lot of three tanks. Though ONGC had not received its set of documents required to be airmailed by MME, it did not obtain and examine a copy of the documents including the third party inspection certificate received by its bank but released the payment and then obtained the documents.

In March 1999, ONGC undertook a visual inspection of the three tanks received in February 1999 and found that all the three tanks were manufactured in 1992. ONGC then noticed that the third party inspection certificate indicated that the tanks were manufactured in 1998 but hydro test was conducted in 1992. As these two statements were contradictory, the three tanks were declared defective and unacceptable.

Meanwhile in February 1999, ONGC's bank released payment of Rs.1.17 crore against the second lot of five LNT tanks, which were certified as of recent make. ONGC made the payment to the bank and received these tanks in April 1999. It requested (July 1999 to March 2000) MME to replace the three defective tanks and depute engineers for commissioning of all the tanks, but there was no positive response from MME. In April 2000, ONGC got one of the five tanks of second lot tested through a third party and found that the tank had serious problem in external piping work due to manufacture defect. Despite this, ONGC did not take any effective action against MME except encashment of performance bank guarantee for Rs.13.35 lakh.

As MME was not responding to ONGC requests, the Company got the last five LNT tanks repaired at a cost of Rs.39.08 lakh and put these to use, one in January 2002 and four in April 2004, at the risk and cost of MME. The three tanks received in the first lot were lying unused. ONGC hired one LNT tank at a cost of US$ 79,970 (equivalent to Rs.31.99 lakh) during 1998-99 to 2001-02 for meeting its operational requirements.

At the time of receipt of bank's intimation regarding the supply of first lot of three LNTs, ONGC's failure to obtain and verify a copy of the documents including the third party inspection certificate, resulted in wasteful expenditure of Rs.1.27 crore[♣] on procurement of defective LNTs.

The Management stated (November 2005) that the discrepancy in the documents of first lot with respect to the year of testing/inspection being of 1992 and the year of manufacture as 1998 was immediately raised but by that time the shipment of the second lot of five tanks was already effected on 20 January 1999 and payment released by the negotiating bank. The Management stated that a case had been initiated to black list MME and the third party who issued the ambiguous inspection certificate.

The reply is not tenable as, at the time of the bank's intimation (13 January 1999) regarding the first lot of supply, if ONGC had obtained a copy of all the documents including the third party inspection certificate from the bank and examined the same before issuing the order (15 January 1999) for release of the payment, the fact that these tanks did not meet the contract specifications could have been detected before 20 January 1999 and payment towards the second lot stopped till replacement, repair and successful commissioning of the tanks by MME engineers. Thus, the wasteful expenditure of Rs.1.27 crore could have been avoided by putting effective pressure on MME.

The matter was reported to the Ministry in March 2005; its reply was awaited (November 2005).

[♣] ***Includes cost of three LNT tanks lying unused, repair charges of five tanks and hire charges of one tanks less encashed amount of performance bank guarantee.***

14.7.8 Irregular payment of Operational Allowance

ONGC made an irregular payment of operational allowance of Rs.51.10 lakh to ineligible employees during the period from February 2001 to January 2005.

In ONGC, 'Operational Allowance' is paid to those employees who are directly engaged in operational activities in onshore areas, in consideration of the arduous and/or hazardous nature of work and the extra time involved in travelling to and from their duty point. As per ONGC's office order of December 1997, employees so eligible for operational allowance should be directly connected with drilling or production activities in the field at drill sites/oil fields (*i.e.* in the open and not located at any office or storage shed) and attending duty in shifts.

Employees posted at Seismic Data Processing Interpretation Centre (SPIC) at Panvel and the Regional Office Building at Mumbai, who were paid operational allowance of Rs.51.10 lakh for the period February 2001 to January 2005, were neither directly engaged in operational activities nor were working in the open or carrying out arduous or hazardous work. These payments were based on an office order issued with the approval of the Executive Director, Mumbai Region (March 2001). As per ONGC's 'Book of Delegated Powers', the power with regard to payment of salaries, allowances etc. entirely vested with the Board of Directors. However, approval of the Board of Directors was not obtained for the above payments. The payment of operational allowance to these employees amounting to Rs.51.10 lakh was, thus, irregular.

In its interim reply, ONGC's Deputy General Manager (Finance and Accounts), Dehradun stated (September 2005) that as the employees working in SPIC and the Regional office were required to attend the office in shifts, including night shifts, it was considered by the local Management that their duties could also be treated as the duty eligible for operational allowance under the orders of 1997. However, in view of the Audit comment the payment had been stopped from February 2005 onwards till further decision.

The reply is not tenable as working in shifts alone did not entitle an employee to operational allowance, which was payable only to employees directly connected with drilling or production activities in the field like drill sites/oil fields in the open space and also attending duty in shifts. The payment was stopped from February 2005 without any office order and action to initiate recovery of the past payments was yet to be taken (September 2005).

The matter was reported to the Management in April 2005 and to the Ministry in May 2005; their replies were awaited (November 2005).

Oil India Limited

14.8.1 Wasteful expenditure on acquisition of petroleum properties

Oil India Limited purchased a project of petroleum properties from ONGC Videsh Limited without adequate assessment of its prospects. The project became unsuccessful due to absence of commercial gas zones leading to loss of Rs.31.55 crore.

Oil India Limited (Company), in pursuance of its objective to acquire petroleum properties and exploration acreage overseas, approved (January 2003) the proposal for purchase of the Sakhalin India Inc. (SII), Texas, USA, a wholly owned subsidiary of ONGC Videsh Limited, (OVL). SII held 10 *per cent* participating interest in an exploration acreage in North Hellhole Bayou Prospect, Vermilion Parish, in offshore Louisiana, USA. Accordingly, an agreement was signed on 7 March 2003 with OVL being effective from 10 March 2003. The cost of acquisition included US$ 1,000 (equivalent to Rs.0.48 lakh) towards equity capital and a loan of US$ 7.06 million (equivalent to Rs.33.70 crore) towards expenditure incurred by OVL for their participating interest.

It was noticed in Audit that the Management decided in January 2003 to examine geo-scientific data of the acreage through visit of a group of geologist and geophysicist. However, the Company did not carry out any technical evaluation separately on the exploration acreage and accepted the offer based on the technical report of OVL.

At the time of acquisition of SII (March 2003) the position of wells drilled was as follows:

(i) The first well had shown presence of gas but could not be tested properly due to well complications and was abandoned.

(ii) The second well had revealed poor reservoir quality. The Operator (M/s. Mc Alester Fuel Company) had proposed sidetrack well with the objective of penetrating the gas reserves of the first well. Sidetracking of the well started in January 2003 and the well reached the target in February 2003.The first test completed in March 2003 revealed meagre amount of gas/oil.

The exploration activities were discontinued shortly thereafter from April 2003 due to absence of any positive commercial gas zones. The Operator decided to abandon the project and surrender all leases in August 2003.The project was declared unsuccessful and it was decided (April 2004) to wind up M/s. Sakhalin India Inc. (renamed as M/s. Luit India Inc.) in due course. A part of the loan i.e. Rs.31.55 crore (US$ 7.13 million) extended to the project was written off by the Company in 2003-04. M/s. Luit India Inc. was dissolved in December 2004.

Thus, the Management acquired petroleum properties without adequate risk assessment, based on the data provided by OVL/Operator and incurred a loss of Rs.31.55 crore on the prospecting blocks.

The Management, while accepting the facts of the case, stated (December 2004) that due care was taken before acquiring the interest in SII. It further stated that decision was also taken keeping in view the national interest of acquiring stake by OVL in Sudan Project which resulted in the country's gain of three MMT per year of crude oil. The reply is not acceptable as the Management relied on the data/ analysis provided by OVL/operator and did not carry out any independent evaluation in this regard. Further, the Company's claim that the investment was made in national interest is an after thought since nowhere in the deliberations at the time of approval of the investment, the Board of the Company considered this aspect. In fact disinvestment in SII was the commercial decision of OVL since it was in the process of acquiring 25 *per cent* stake in the Greater Nile Project in Sudan and apprehended law suit because of OVL ownership of SII operating in USA. Moreover, it did not derive any benefit out of the accommodation thus extended to OVL. Instead it incurred a loss of Rs.31.55 crore in the acquisition of SII.

The matter was reported to the Ministry in February 2005; its reply was awaited (November 2005).

CHAPTER XV: MINISTRY OF POWER

NTPC Limited

15.1.1 Loss of interest due to overstocking of coal beyond CERC norms

Due to overstocking of coal beyond CERC norms, the Company could not get any return on excess funds blocked in coal stock and suffered an avoidable loss of interest of Rs.9.20 crore.

The tariff being recovered by NTPC Limited (Company) from beneficiaries is fixed by the Central Electricity Regulatory Commission (CERC), based on annual fixed charges and variable charges (fuel cost). Interest on working capital is one of the elements allowed in the tariff, which, *inter alia*, includes interest on funds blocked in coal stock. For calculation of interest on working capital in respect of funds blocked in coal, the fuel cost for one month and reasonable fuel stock as actually maintained but limited to 15 days for pit-head stations and 30 days for non-pit head stations corresponding to the target availability is allowed by CERC.

Review of coal stock position at seven pit-head stations[♣] during the three years ending 2003-04 revealed that there was excess stocking of coal[•] ranging between 0.12 lakh MT valuing Rs.1.10 crore and 2.57 lakh MT valuing Rs.25.05 crore, as compared to the 15 days actual consumption at pit-head stations. The overstocking of coal was avoidable in view of the following facts:

(i) The generating stations were situated very near the coal fields.

(ii) No major lead-time was involved in transportation of coal.

(iii) The Company has its own merry-go-round system for transportation of coal having dedicated railway lines, wagons, engines and manpower.

In its final tariff orders for pit-head stations (except Rihand and Kahalgaon) for three years ending 2003-04, CERC did not allow interest on working capital blocked in coal in excess of the lower of 15 days' requirements or actual stock. As a result, the Company could not get any return on the excess funds blocked in coal stocks at seven pit-head stations and suffered loss of interest of Rs.9.20 crore (calculated at a rate of 8 *per cent* per annum) on blocked funds during the three years ending 2003-04.

The Management stated (August 2004) that stocking of coal varied from month to month depending on various factors which were beyond its control and mines did not generate at

[♣] *Rihand, Vindhyachal, Talchar Super Thermal Power Station, Talchar Thermal Power Station, Singrauli, Farakka and Kahalgaon*

[•] *Worked out based on the actual consumption and monthly closing stock of coal for the respective years*

full capacity during summer and rainy seasons resulting in depletion of stock. They added that coal stock availability had accrued benefits by way of unscheduled interchange (UI) charges and incentive for higher generation and the loss due to overstocking was negligible as compared to these gains.

The reply is not tenable as the factors affecting coal supply are taken into account by CERC before fixing the limit of 15 days for pit-head stations and the annual coal requirement was worked out by CERC based on gross calorific value of coal, heat contribution, specific coal consumption etc. Further, loss due to overstocking of coal had been worked out based on the average actual consumption which included consumption for earning UI charges. Besides, the concept of UI was introduced by CERC to bring in grid discipline and as such, had no relation with coal stock. UI charges could also be earned with 15 days coal stock and the Management did not bring out any instance of loss of generation due to shortage of coal.

Thus, due to overstocking of coal beyond CERC's norms, the Company could not recover interest on the excess funds blocked in coal stocks and instead suffered an avoidable interest loss of Rs.9.20 crore.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

Power Finance Corporation Limited

15.2.1 Loss owing to undue benefit to a private party

Non-inclusion of hedging cost in foreign currency loan agreement and restructuring interest on rupee term loan in relaxation of its interest restructuring policy led to undue benefit to a private party and loss of Rs.13.48 crore to the Company.

Based on various requests of M/s Jindal Thermal Power Company Limited (borrower) for refinancing of Foreign Currency Loan (FCL) and Rupee Term Loan (RTL) taken by them, Power Finance Corporation Limited (Company) entered (February 2003) into an agreement with the borrower to refinance FCL of US$ 44.50 million and RTL of Rs.65.00 crore at interest rates of US$ LIBOR[♣] plus 2.4 *per cent* and 12.25 *per cent* respectively with the special condition that the disbursement of FCL would be from the proceeds of external commercial borrowing (ECB) programme of the Company. Accordingly, the Company disbursed FCL amounting to US$ 41.72 million (Rs.198.77 crore) from the ECB of 12 billion Japanese Yen and RTL of Rs.63.07 crore in March 2003.

It was observed in Audit that according to the Company's policy (internal circular dated 11 December 2002), the spread (2.4 *per cent* in the instant case) should be increased appropriately to reflect the hedging cost in case the lending was in a currency other than the currency of ECB raised, so as to cover the adverse exchange rate variation. However, the Company had not incorporated any clause in the loan agreement to this effect. The Company raised the first demand in November 2003 for US$ 0.86 million (Rs.3.92 crore)

[♣] ***London Inter Bank Offer Rate***

towards cross currency hedging cost for the period from March 2003 to October 2003. The demand was not accepted (December 2003) by the borrower as the same was not included in the terms of sanction letter/loan agreement.

An internal committee appointed by the Company concluded (May 2004) that the hedging cost was not recoverable in terms of the sanction letter and proposed to revise the margin to include the additional cost for being recovered from the borrower, which was not agreed to by the borrower.

Subsequently based on recommendations of another internal committee, the Company offered (October 2004) revised interest rate of US$ LIBOR plus 3.5 *per cent* and agreed (November 2004) to withdraw its demands totalling Rs.9.63 crore towards cross currency hedging cost for the past period from March 2003 to October 2004. The borrower (March 2005) accepted the same and paid lump-sum amount of Rs.3.58 crore being the difference of margin of 1.10 *per cent* (3.50 minus 2.40) in hedging costs, for the period from October 2004 to April 2008 [after taking into account net present value (NPV)]. Thus, the Company had to forego the amount of Rs.9.63 crore for the period from March 2003 to October 2004 due to not incorporating an enabling clause in the loan agreement for recovery of hedging cost.

Simultaneously, the Company restructured (April 2005) the interest on RTL from 12.25 *per cent* to nine *per cent* retrospectively from July 2004 by charging premium of Rs.1.65 crore only against NPV of Rs.5.50 crore. It was observed in Audit that the restructuring of interest was not in accordance with the Company's policy prevalent on the date of sanction of the loan, as RTL agreement did not contain any specific clause in this regard. However, the Company revised its policy in July 2004 and allowed benefit of restructuring to the borrower on the plea that the settlement on hedging cost was reached. Even the revised policy was relaxed to give benefit from back date. Besides, the Company did not obtain the consent of the lead financial institution for the interest restructuring, which was required in terms of the revised policy. This resulted in undue benefit of Rs.3.85 crore to the borrower.

Thus, lapse on the part of the Company in not incorporating the enabling clause in the agreement and restructuring of RTL in relaxation of its policy resulted in an undue benefit to the private party and loss of Rs.13.48 crore (Rs.9.63 crore plus Rs.3.85 crore) to the Company.

The Management stated (August 2005) that since settlement on the cross currency hedging cost was reached, the Company permitted restructuring of interest on RTL, which was earlier denied to the borrower because of default in service of FCL. They added that these were two different issues going on simultaneously and no undue benefit was given to the borrower.

The reply is not tenable as the Company failed to incorporate the clause for recovery of hedging cost in the agreement in deviation of its internal circular of December 2002, nor did it fix any responsibility for this lapse. As regards restructuring of interest rate on RTL, this was neither in accordance with the loan agreement, nor with the prevailing interest restructuring policy of the Company.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

CHAPTER XVI: DEPARTMENT OF PUBLIC ENTERPRISES

Hindustan Aeronautics Limited, Bharat Electronics Limited, Bharat Earth Movers Limited and Kudremukh Iron Ore Company Limited

16.1.1 Excess payment due to incorrect regulation of leave encashment

Four Companies made excess payment of Rs.34.35 crore due to adoption of 26 days as a month instead of 30 days for computation of encashment of leave.

As per instructions issued in April 1987 by the Department of Public Enterprises (DPE), any individual public enterprise, with the approval of the Board of Directors, may frame leave rules for its employees keeping the broad parameters of the policy guidelines laid down in this regard by the Government.

A review of regulation of encashment of leave in four Companies* during the years 1994-95 to 2004-05 revealed that these Companies made excess payment of Rs.34.35 crore due to adoption of 26 days a month instead of 30 days for computation of encashment of leave as detailed below:

Name of the Company	Excess payment (Rs. in crore)	Period covered
Hindustan Aeronautics Limited (HAL)	13.17	2001-02 to 2004-05
Bharat Electronics Limited (BEL)	13.06	1994-95 to 2004-05
Bharat Earth Movers Limited (BEML)	5.73	2000-01 to 2004-05
Kudremukh Iron Ore Company Limited (KIOCL)	2.39	1998-99 to 2004-05
Total	**34.35**	

The Managements of HAL, BEL and BEML stated (August 2004, May 2005 and October 2004 respectively) that initially the amount payable for a day's leave was arrived at by dividing the monthly salary by 30 days which was subsequently changed to 26 days based on Supreme Court Judgment (July 1980) in respect of Payment of Gratuity Act, 1972 on a civil appeal in Shri Digvijay Woollen Mills' case. The Management of KIOCL stated (October 2005) that leave rules had been amended and approved by the Board of Directors on 20 October 2005 to adopt 30 days a month for encashment of leave.

The Ministrv of Defence endorsed (August 2005) the reply furnished by the HAL Management. The Ministry of Defence, in respect of BEL, stated (August 2005) that DPE had been requested to clarify the method of calculation of earned leave encashment.

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* ***Hindustan Aeronautics Limited, Bharat Electronics Limited, Bharat Earth Movers Limited and Kudremukh Iron Ore Company Limited***

The reply furnished in respect of HAL, BEL and BEML is not tenable due to the following reasons:

(i) Generally a month means a period of 30 days unless otherwise stated. The judgment of the Supreme Court defining a month to mean 26 days was specifically for the purpose of calculation of gratuity payable under the Payment of Gratuity Act, 1972 and can not be applied automatically in other cases.

(ii) DPE instructions allowed PSUs to frame leave rules keeping the broad parameters of policy guidelines of Government and no Government guidelines exist for adoption of 26 days a month instead of 30 days for encashment of leave.

(iii) While effecting recovery from employees for absence without leave and leave without pay, HAL, BEL and BEML computed 30 days in a calendar month and not 26 days.

(iv) Even the DPE observed (February 1983) that the procedure adopted by BEL in calculating the rate of encashment by dividing the monthly emoluments by 26 days as incorrect and advised the Department of Defence Production to examine the issue. Action taken by Department is not available on the records of BEL.

Thus, by persisting with adoption of 26 days for a month in respect of leave encashment, these Companies had already incurred an extra expenditure of Rs.34.35 crore during 1994-95 to 2004-05 and would continue to incur extra expenditure even in subsequent periods.

The matter was reported to the Ministry in respect of BEML in May 2005, its reply was awaited (November 2005).

Airports Authority of India, Food Corporation of India, National Hydroelectric Power Corporation Limited, Power Finance Corporation Limited, National Insurance Company Limited, The New India Assurance Company Limited, The Oriental Insurance Company Limited, United India Insurance Company Limited

16.2.1 Recoveries at the instance of Audit

During test check in Audit, several cases were pointed out relating to non billing, short billing, non recovery, short recovery, excess payment, avoidable payment, short collection, under-charge, non-preference of claims and undue benefit to third parties in respect of Central PSUs. In 28 such cases pertaining to eight Central PSUs where Audit pointed out an amount of Rs.13.82 crore for recovery, the Management of the PSUs recovered an amount of Rs.12.38 crore during the years 2004 and 2005 as detailed in Appendix-I.

CHAPTER XVII: MINISTRY OF RAILWAYS

Indian Railway Finance Corporation Limited

17.1.1 Loss of Rs.2.96 crore due to non-prepayment of high-cost debt

The Company lost an opportunity for reducing the interest burden by not pre-paying the high-cost debt and suffered a loss of Rs.2.96 crore.

Indian Railway Finance Corporation Limited (Company) availed (September 2000) a loan of Rs.100.00 crore from Indian Bank at 12.50 *per cent* rate of interest for a tenor of 10 years. The Company had the option to prepay the loan at any time with a notice of 30 days. Based on the requests of the Company from time to time, Indian Bank reduced the rate of interest to 11 *per cent* (December 2002) on the total amount and to nine *per cent* on Rs.50 crore (March 2003). In March 2005, it further reduced the rate from 11 and nine *per cent* to 8.50 and 8.40 *per cent* respectively.

The Company subsequently availed (31 March 2003) a loan of Rs.100 crore from GE Capital at 7.20 *per cent*, which was utilised to pre-pay the loan of Rs.100 crore taken from Union Bank of India three days earlier (29 March 2003) at 7.25 *per cent*.

It was observed that though the Company was paying higher rate of interest ranging between nine *per cent* and 11 *per cent* to Indian Bank during the same period, it opted to pre-pay the loan of Rs.100 crore bearing lower rate of interest (7.25 *per cent*). By not exploring the possibilities of pre-paying the high-cost debt, the Company lost the opportunity to reduce its interest burden and suffered loss of Rs.2.96 crore till March 2005 on account of payment of extra interest on the loan availed from Indian Bank.

The Management stated (March 2004) that the Company being a repeat borrower could not take abrupt view of prepayment to any bank at any time with the sole purpose of reducing the cost. The Management added (May 2005) that the availment of loans from Union Bank of India and GE Capital towards the end of March 2003 was in pursuance of annual targets set by the Ministry of Railways for 2002-03 and it was not a case of prepayment of a loan but a case of returning money with the last minute reduction in borrowing target. They further stated that the loan from Indian Bank was restructured thrice bringing down the cost to 8.50/8.40 *per cent*. The Ministry endorsed (October 2005) the views of the Management.

The reply is not tenable as even if there was reduction in borrowing target, pre-payment of high cost debts should have been effected first, which would also have met the borrowing targets. Though the money received from GE Capital was not meant to prepay any loan, the same was utilised to return the loan to Union Bank of India without exploring the possibilities of repaying the high-cost loans. Further, the reduced interest rates of 8.50/8.40 *per cent* were still higher than the rate of 7.25 *per cent*.

Thus, the Company lost an opportunity for reducing the interest burden by not pre-paying the high-cost debt and suffered a loss of Rs.2.96 crore till March 2005 on account of payment of extra interest on the loan availed from Indian Bank.

IRCON International Limited

17.2.1 Blockage of funds of Rs.1.02 crore in purchase of disputed land

The Company blocked Rs.1.02 crore for more than four years and suffered loss of Rs.25.71 lakh due to failure to pre-check the title of the land and release of the final payment ignoring the disputed status of the land.

In order to construct an office building in Bangalore, IRCON International Limited (Company) participated (December 2000) in auction of certain plots on 'as is where is basis' conducted by Bangalore Development Authority (BDA) and got a plot measuring 399.07 square meters. As per the conditions of the auction, 25 *per cent* (Rs.24.54 lakh)[*] of cost of the plot (Rs.1.02 crore) was paid to BDA on 8 December 2000 and the balance amount was to be paid within 45 days from the date of receipt of confirmation letter.

Meanwhile, officials of the Company apprehended the disputed status of the plot during the site visit on 17 January 2001. The Company immediately took up the matter with BDA for providing unencumbered land. However, without waiting for the dispute to get resolved, the Company released the final payment of Rs.76.62 lakh on 25 January 2001. The Company is yet to obtain possession of the land (September 2005), as the occupants of the land had filed civil suits citing the Company as one of the defendants. An amount of Rs.0.35 lakh had been spent by the Company on litigation costs.

It was observed in Audit that the Company committed itself to significant capital investment without proper verification of the site, which was critical, as the sites were offered on 'as is where is' basis. Further, even after the Company's officials observed that the land was not free from encumbrances, it did not explore the possibility of deferring the final payment of Rs.76.62 lakh.

The Management/Ministry replied (July/October 2005) that there was nothing at the site to indicate the disputed nature of the plot on the date of auction and non-deposit of the balance amount would have resulted in imposition of penalty. While accepting that a third party was claiming ownership of the plot, they added that value of the plot had appreciated significantly.

The reply is not tenable since the land was under stay from 1 December 2000, i.e., before the date of auction. Further, after being aware of the disputed nature of the land, the Company should have demanded return of the amount already deposited if clear title was not ensured. As regards appreciation in the value of the land, this is not relevant as the purpose of purchasing the piece of land was to construct its office building in Bangalore and not to make profit on sale of land.

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[*] ***After adjusting Rs. one lakh paid for participating in the auction***

Thus, the Company blocked Rs.1.02 crore and did not get ownership of the land for more than four years, due to its failure to pre-check the title of the land and release of final payment ignoring the disputed status of the land. It also suffered loss of Rs.25.71 lakh* on account of interest on the blocked funds and litigation charges, which would further increase at a rate of Rs.0.45 lakh per month, till the final resolution of the issue.

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* ***Interest loss of Rs.25.36 lakh from January 2001 to September 2005 at a simple rate of 5.32 per cent per annum and litigation cost of Rs.0.35 lakh.***

CHAPTER XVIII: MINISTRY OF ROAD TRANSPORT AND HIGHWAYS

National Highways Authority of India

18.1.1 Blockage of funds due to non-utilisation of land acquired for construction of residential complex

The National Highways Authority of India lost Rs.1.05 crore towards interest for six years due to non-construction of residential complex on purchased land.

The National Highways Authority of India (Authority) acquired (August 1999) 6,225 square meters of land valuing Rs.2.53 crore at Dwarka, New Delhi on perpetual lease allotted by Delhi Development Authority (DDA) for providing residential accommodation to its employees. The Authority also spent (September 2002) Rs.29.88 lakh towards stamp duty and transfer duty. The Authority was required to complete the construction within a period of two years from the date of taking over possession of the land as per perpetual lease and could not sell, transfer, assign or otherwise part with the possession except with the consent of DDA.

The Authority took possession of the land in December 1999. It appointed a consultant (December 2001) to carry out the design, planning and supervising the construction of the building and incurred an expenditure of Rs.5.57 lakh towards the consultant's fee. The Authority considered (June 2002) constructing 106 flats in a phased manner during 2002-03 to 2004-05 at an estimated cost of Rs.19.96 crore and a budget allocation of Rs.4.00 crore was also made in 2002-03. Subsequently, the Authority decided (August 2003) to examine the possibility of leased housing in Dwarka for its employees and not construct residential flats for the staff. The Authority paid Rs.31.60 lakh towards ground rent for five years. The land has not been put to use till date (December 2005).

Thus, the Authority incurred an expenditure of Rs.2.88 crore towards cost of land, registration charges and consultancy charges and Rs.31.60 lakh towards ground rent for five years for acquisition of residential plot. This resulted in blockage of funds to the extent of Rs.3.20 crore with a consequential loss of interest of Rs.1.05 crore, besides annual commitment towards ground rent of Rs.6.32 lakh and liability to pay penalty of Rs.7.57 lakh per annum to DDA for not utilising the land.

The Ministry stated (November 2005) that the construction of residential accommodation for the employees was deferred as it was decided that providing leased accommodation to the NHAI employees was an economic solution. It further stated that by retaining the land, the Authority had the flexibility of construction of residential accommodation in proximity to the Corporate Office of the Authority as sufficient rental accommodation would not be available with the passage of time.

The reply of the Ministry confirms the audit contention that the land was purchased without framing a policy for providing residential accommodation to the employees and without any plan for construction even after more than six years of the purchase of the land. This led to blockage of funds of Rs.3.20 crore with a consequential loss of interest

of Rs.1.05 crore up to August 2005 and annual commitment of ground rent of Rs.6.32 lakh and annual liability of penalty of Rs.7.57 lakh till the construction.

CHAPTER XIX: MINISTRY OF SCIENCE AND TECHNOLOGY

Bharat Immunologicals and Biologicals Corporation Limited

19.1.1 Loss due to delay in utilisation of material

Delay on the part of the Company to decide and dispose of the material before its expiry resulted in a loss of Rs.91.39 lakh.

The Company had been formulating Oral Polio Vaccine (vaccine) with the bulk procured from M/s. IPVE, Moscow for supply to the Ministry of Health and Family Welfare, Government of India. In anticipation of supply of vaccine to the Government during 2001-02, the Company procured (November 2001) bulk for 10 million doses out of which it could utilise bulk for 3.851 million doses. Balance 6.149 million doses valuing Rs.91.39 lakh could not be used as the Government of India stipulated (March 2002) that the vaccine must be blended from a WHO approved bulk while the bulk procured by the Company from M/s. IPVE was not WHO approved.

The Company then decided (July 2002) to enter into trade market and invited sealed offers (December 2002) for appointment of super distributors/super stockists for marketing its vaccine in Delhi and Karnataka. The sealed offers were received in January 2003 but were opened in February 2003. The physical verification of the parties to verify the eligibility conditions was conducted by a committee of the Company in March 2003 and recommendations of the committee were examined in May 2003. The examination disclosed that the committee did not verify the validity of the drug licences of the tenderers to stock the product. Validity of licences was verified in July 2003 and the proposal was reconsidered in August/ September 2003. Stockist was decided in October 2003 but the clauses of agreement and retail price of the product were finalised in November 2003. The Company could finally appoint the distributor only in February 2004 by which time the bulk had already expired (October 2003). The material could not be used and was ultimately written off (July 2005).

The Management stated (May 2005) that the Company had been operating in the institutional market. This was the first time they made efforts to enter into the trade market and they had taken required steps for appointment of distributors within a reasonable time. The Ministry endorsed (September 2005) the reply of the Management.

The reply is not tenable because the delay was due to slow processing of activities of routine nature like verification of the licences of the parties, tender processing and price fixation of the vaccine.

Thus, the failure of the Company to decide and dispose of the material before its expiry resulted in a loss of Rs.91.39 lakh.

CHAPTER XX: MINISTRY OF SHIPPING

Dredging Corporation of India Limited

20.1.1 Loss of Rs.3.76 crore on account of failure to properly ascertain the site conditions through a comprehensive survey and delay in commencement of work

The Company did not carry out a comprehensive survey of the site on its own before undertaking a dredging contract. It also delayed the commencement of dredging. Due to these, there was significant under-achievement in production, which resulted in delay in completion of the work and consequently the Company incurred a loss of Rs.3.76 crore.

The Company entered (August 2003) into an agreement with Chennai Port Trust (CPT) for undertaking the work of 'Deepening of Dr. Ambedkar Dock Basin (ADB) and maintenance of dredging in outer harbour, entrance channel and sand trap' of the Chennai Port. As per the terms of the contract, the material to be dredged was to be of all types of soil such as loose or compact sand, silt mixed with/without clay etc. including any broken concrete pieces/debris in the basin and alongside berths. The Company did not carry out a comprehensive survey on its own to find out the extent of debris and relied upon the information given in the contract as well as upon the information given by National Institute of Ocean Technology (NIOT), which was engaged by it for surveying the area. NIOT in its report stated that the dredging operations in the area could be accomplished without much difficulty. To facilitate commencement of work during favourable weather conditions, CPT issued letter of acceptance in June 2003. The work was to be completed within six months and delay attracted levy of liquidated damages at the rate of 0.5 *per cent* of the contract price per week or part thereof subject to a maximum of five *per cent* of the contract price.

Despite clear indication from CPT that dredging in sand trap area was to be carried out only in favorable weather conditions, the commencement of work was delayed upto September 2003. During the execution of the contract, the dredgers encountered unusually high quantities of cylindrical concrete like pieces, debris, metal pieces, wire ropes, nylon ropes, coal, textile, waste etc. which clogged the drag heads of the dredgers, due to which an average daily production of 25,073 cubic meters per day could only be achieved as against the anticipated production of 35,000 cubic meters per day. This resulted in deployment of its dredgers for 93 days as against originally estimated 67 days and the work, which should have been completed by December 2003, was actually completed in November 2004. The Company incurred a total expenditure of Rs.17.53 crore on this work as against the net revenue of Rs.13.77 crore after deducting liquidated damages of Rs.0.40 crore, resulting in a loss of Rs.3.76 crore.

The Management stated (July 2005) that normally reliance is placed on the data regarding soil conditions given by the client because conducting comprehensive surveys to

ascertain the site conditions would be time consuming and costly. Further, time available for submitting tender does not permit a detailed survey. As regards delay in commencement of dredging, it stated that one of the dredgers could not be deployed due to operational reasons while another dredger had a major mishap in August 2003. It also stated that it had made a claim for Rs.18.74 lakh for reimbursement of port dues etc. and for Rs.1.11 crore towards additional cost under different clauses of the contract. The Ministry endorsed (November 2005) the views of the Management.

The reply is not tenable as in the past also, the Company had encountered problems in execution of dredging contracts due to incorrect assessment of soil conditions[♣]. In fact the Board of Directors of the Company had, while reviewing the progress report of a dredging assignment in November 2002, remarked that it had been repeatedly emphasising the need for proper survey of the site before commencement of work, but the same was being neglected and that the Company was expected to have adequate data in respect of each port in this regard by that time. Despite this, the Company failed to conduct comprehensive pre-bid survey in the case of CPT and encountered the same problem and incurred a loss. As regards delay in commencement of work due to the reason cited, the same reflects the lack of preparedness and planning in execution of a work, which is the prime business of the Company. Further, CPT was yet to accept the additional claims made by the Company. Moreover, these claims were far short of the excess expenditure of Rs.3.76 crore.

Thus, failure to ascertain the site conditions through a comprehensive survey on its own and delayed commencement of dredging in Chennai Port, resulted in delay in completion of work and loss of Rs.3.76 crore including levy of liquidated damages amounting to Rs.0.40 crore.

20.1.2 In-ordinate delay in retrieving a sunken pipeline resulted in avoidable loss of margin of Rs.71.34 lakh besides blocking up of funds

Non-retrieval of a sunken pipeline immediately upon completion of work resulted in loss of margin of Rs.71.34 lakh and blocking up of funds of Rs.3.75 crore with consequential loss of interest of Rs.47.40 lakh.

The Company laid (December 1998) 345 meters of sunken pipeline at Paradip port in connection with dredging work. It did not remove the same even after three years of completion of work. As a result, the pipeline got buried in the seabed. In May 2002, Paradip Port Trust (PPT) asked the Company to remove the sunken pipeline by the end of May 2002. The Company issued (August 2002) tenders for retrieving the same alongwith another 120 meters of pipeline laid in 1997. After evaluating the offers received, the Company decided to undertake the work departmentally on the ground that the rate quoted by lowest tenderer i.e. Rs.29.50 lakh was higher than the Company's own estimates by Rs.19.00 lakh. Accordingly, it diverted its Dredger V, which was in commercial operations at Haldia, to Paradip on 21 February 2003 for the purpose of removing the material lying over the sunken pipeline. Dredger V remained at Paradip from 23 February 2003 to 3 March 2003, but there was no appreciable effect on the

[♣] *Dredging undertaken for M/s. Hung Hua Construction Company Limited, Taiwan at Taichung harbour in the year 2001-02 and for Kandla Port Trust at Kandla in 2002-03*

overburden lying on the pipeline. However, in the process, the Company had to forgo a revenue of Rs.95.51 lakh and margin of Rs.71.34 lakh (after deducting the variable cost)[♣], which the dredger could have earned had it continued operations at Haldia.

PPT requested (June 2003) the Company again to expedite the removal of the pipeline and set a deadline of July 2003. The Company entrusted this work (August 2003) to a sub-contractor at a cost of Rs.22.00 lakh. The sub-contractor could remove only 393 meters (August and September 2003) of pipeline and thereafter it abandoned the work stating that the remaining pipeline could not be located.

On account of delay in retrieval of the sunken pipeline, PPT had withheld an amount of Rs.3.75 crore from the bills of the Company. The Company was yet to take a decision regarding retrieval of balance pipeline (June 2005).

Thus, failure to remove the sunken pipeline immediately after completion of the work resulted in loss of margin of Rs.71.34 lakh on account of unfruitful deployment of Dredger V at Paradip. Besides, it led to non-realisation of dues of Rs.3.75 crore and consequential loss of interest of Rs.47.40 lakh[♦].

The Management stated (June 2005) that Dredger V was withdrawn from operations on arrival of Dredger XV and the contractual requirement regarding deployment of five dredgers at Haldia was fulfilled. It also stated that apart from retrieval of sunken pipeline, Dredger V carried out capital dredging also at Paradip port. It further stated that the need for removal of sunken pipeline arose only in the year 2002 when PPT made the request. It also informed that the withheld amount included Rs.1.14 crore withheld towards liquidated damages and it was pursuing with PPT for release of the withheld payments.

The reply of the Management is not tenable as Dredger V was diverted to Paradip specifically for the purpose of removing the overburden lying on the sunken pipeline, which resulted in loss of revenue earning opportunity. During the period of deployment of Dredger V at Paradip, the Company lost 9 days and 16 hours on account of non-deployment of a fifth dredger at Haldia. Further, if Dredger V was engaged in capital dredging work at Paradip, there was no evidence of the Company having billed PPT for its services. Although, PPT asked the Company to remove the pipeline only in the year 2002, it should have also been clear to the Company that pipeline left in the sea bed would get buried and shift over a period of time and would be difficult to retrieve later. As regard liquidated damages, the withheld amount of Rs.3.75 crore does not include any amount towards liquidated damages.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

[♣] ***Calculated for 9 days and 16 hours from 23 February 2003 to 5 March 2003, during which the Dredger V could have been deployed at Kolkata had it not been diverted for Paradip***

[♦] ***Calculated at the rate of six per cent per annum which the Company is earning on its short term deposit receipts***

20.1.3 Loss of margin of Rs.1.14 crore due to idling of Dredger

The Company failed to deploy its Dredger XVII for a period of eight days after completion of repairs due to which it lost revenue of Rs.1.46 crore and a margin of Rs.1.14 crore.

The Company prepares dredger deployment schedules and dry dock schedules in advance in respect of all the dredgers to profitably utilise them without idleness. Further, the deployment scheduling is important, particularly for dry docking and loss of revenue on account of voyage to and from the repair yard is a factor for deciding the lowest offer for awarding dredge repairs contracts.

Dredger XVII of the Company was working for Kolkata Port Trust (KOPT) at Haldia and was earning revenue of Rs.18.30 lakh per day. The Company decided to dry-dock it for 30 days during April/May 2003 to rectify defects and to improve its performance. It was planned to re-deploy it at Haldia after repairs. Accordingly, after following the tender process, the dredger was sent (March 2003) to M/s. Colombo Dockyards Limited (CDL), Colombo.

The dredger reached Colombo on 30 March 2003 for dry-dock repairs, which were undertaken upto 13 April 2003. The dredger commenced its return voyage on 14 April 2003 and reached Chennai on 15 April 2003. Awaiting Management's instructions regarding further assignment, the dredger was anchored outside Chennai Port for six days from 16 April 2003 to 21 April 2003. Upon receipt of assignment, it commenced voyage from Chennai on 22 April 2003, reached Haldia on 24 April 2003 and commenced dredging operations with effect from 27 April 2003. As a result the dredger remained idle for six days at Chennai besides losing another two days due to the detour it had made to Chennai. Thus, in the process it lost eight days and corresponding revenue of Rs.1.46 crore and margin of Rs.1.14 crore.

The Management replied (June 2005) that there was no specific assignment for Dredger XVII in April 2003 and since Dredger XII which was working at Haldia was scheduled for dry-docking during April/May 2003, permission of KOPT for deploying Dredger XVII in place of Dredger XII was sought in April 2003 and thereafter, Dredger XVII was deployed at Haldia with effect from 27 April 2003. It further stated that there was no loss of revenue as five dredgers were continuously deployed at Haldia. The Ministy endorsed (November 2005) the views of the Management.

The reply of the Management/Ministry is not tenable as it approached KOPT for substitution of Dredger XII with Dredger XVII after Dredger XVII had already been anchored at Chennai port. Had this been done in advance the idling could have been avoided. As regards deployment of five dredgers continuously at Haldia, the contract with KOPT provided for deployment of a sixth dredger also in case the required depth of five meters was not achieved in a particular month. There was underachievement of depth in the month of April 2003, which provided scope for deployment of Dredger XVII.

Thus, idling of Dredger XVII led to a loss of revenue of Rs.1.46 crore and loss of margin of Rs.1.14 crore.

Inland Waterways Authority of India

20.2.1 Avoidable expenditure on procurement of Water Injection Dredger

Procurement of additional dredger for National Waterways–2 without adequate justification resulted in avoidable expenditure of Rs. 3.16 crore besides future liability of Rs.2.59 crore.

Inland Waterways Authority of India (Authority) was constituted (October 1986) under the Inland Waterways Authority of India (Authority) Act 1985 for the purpose of regulation and development of inland waterways for shipping and navigation. To facilitate shipping operations, least available depth (LAD) of two meters was to be maintained in National Waterways-1 (NW-1) and National Waterways-2 (NW-2) by carrying out dredging operations to remove the silt from the river bed. The Authority approved in June 1997 a scheme for purchase of two Water Injection Dredgers (WID) one each for NW-I and NW-2. In NW-2 it was to be deployed between Bangladesh Border to Pandu near Guwahati for a distance of 260 kms. The Government approved (February 1998) the proposal for purchase of two WIDs and an order was placed (September 1998) on M/s. Hoogly Dock & Port Engineers Limited (HDPE) for their purchase at a total cost of Rs.10.46 crore. The dredgers were delivered at Patna and Guwahati in March 2001 and February 2002 respectively for the exclusive use in NW-1 and NW-2 respectively.

Audit observed that the WID at Guwahati since its delivery was utilised for merely 58 dredging hours during the 33 months (August 2002 to April 2005) of its availability for operation in NW-2. The quantity of material dredged, was also not measurable by the Authority and the dredger was utilised for escorting cargo vessels, ensuring safe passage and also supplying bunker to different vessels as against the proposed utilisation of removing 6,16,500 cubic meters of silt during the period November to April each year. The reasons for such gross underutilisation as analysed by Audit were as under: -

(i) Out of the total length of 260 kms between Bangladesh border and Pandu, the dredging operation was required for the stretch of about 50 kms only since the LAD was more than two meters throughout the year in other stretches.

(ii) Cargo movement through NW-2 was less as compared to NW-1 and NW-3 thereby necessitating no dredging operations for the movement of cargo vessels in NW-2.

(iii) There was no commitment for cargo movement from the end users to utilise the waterways.

(iv) The dredger was utilised as escort and supporting vessel rather than for dredging.

While the Authority was unable to utilise fully the existing WID purchased in February 2002, it placed (March 2004) an order on M/s. HDPE for purchase of another WID for NW-2 to be delivered by April 2005 at a cost of Rs.5.75 crore. The dredger was yet to be delivered (October 2005). The Authority had paid Rs.3.16 crore till July 2004 (Rs.2.30 crore in March 2004 and Rs.0.86 crore in July 2004). The purchase of one more WID for

NW-2 at the cost of Rs.5.75 crore also lacked justification in view of the underutilisation of the earlier dredger purchased in February 2002 and the requirement of a dredger for 50 kms only.

The Management stated (May 2005) that the purchase of the first dredger was justified as it was procured for deployment at the time of emergency, when the vessels are stranded for the sudden development of inadequate depth at a location and was not meant for normal dredging operation. These dredgers were further kept as standby for rescue operation. However, no justification for the purchase of a second dredger was furnished by the Management.

The reply of the Management is, however, not acceptable as at the time of obtaining approval from the Government, the Authority had stressed the need for WID being flexible in dredging operation and the most cost effective inland dredging system which could ensure navigational depth throughout the year and had not proposed it for rescue operations during emergency or supporting vessel equipment. It was also not procured as standby equipment but for regular operations. With the first dredger being grossly underutilised even in the limited stretch of 50 kms, the procurement of a second dredger (March 2004) at a cost of Rs.5.75 crore lacked justification.

Thus, placing the order for the second WID inspite of under utilisation of first WID for NW-2, without adequate justification, resulted in avoidable expenditure of Rs.3.16 crore besides future liability of Rs.2.59 crore.

The matter was reported to the Ministry in July 2005, its reply was awaited (November 2005).

Hindustan Shipyard Limited

20.3.1 Loss of Rs.33.92 lakh due to the Company restricting sales tax to three per cent despite the customer's offer to reimburse the actual

Despite the customer's offer to reimburse sales tax on actual basis, the Company made a commitment to charge sales tax at a fixed rate of three *per cent* which resulted in a loss of Rs.33.92 lakh being the difference between the sales tax paid and sales tax recovered from the customer.

The Company signed an agreement (July 1999) with Mormugao Port Trust (MPT) for supply of two 45 tonne Bollard Pull Tugs at a negotiated price of Rs.37.70 crore which was later revised (March 2003) to Rs.37.42 crore. The price was inclusive of Andhra Pradesh General Sales Tax (APGST) amounting to Rs.1.10 crore at a rate of three *per cent* though the actual rate prevailing at that time was 10 *per cent*. The delivery of the tugs took place in March 2003 and December 2003. The Company incurred a total loss of Rs.9.15 crore in executing this contract.

On the above sale the Company paid APGST at the rate of four *per cent*, which amounted to Rs.1.44 crore while it could claim Rs.1.10 crore only from MPT as per the agreement. It was observed that before the award of work, the Company made an unnecessary commitment (November 1998) to MPT that the APGST would be charged at three *per*

cent only, in anticipation of its downward revision from the then prevailing rate of 10 *per cent*. This commitment was made despite the fact that MPT had agreed to pay APGST on actual basis on proof of payment. On account of this, the Company suffered a loss of Rs.33.92 lakh being the differential of APGST paid and recovered from the client.

The Management in its reply (April 2005) stated that it kept the sales tax component to three *per cent* anticipating its downward revision and to submit a competitive offer keeping in view stiff competition from other yards and also the fact that price including taxes would be considered for establishing L-1. Had this not been done, the Company would have lost the order and the resultant contribution as well.

The reply is not tenable because the Company was aware, while furnishing clarifications on 30 November 1998 to MPT that its offer was lowest even after considering the sales tax at 10 *per cent*; and therefore, the contention that otherwise the Company would have lost the order is not factual. Although the Company quoted the price with sales tax at three *per cent*, since MPT offered to reimburse the variations in taxes on documentary proof it should have accepted it. The Company's commitment to charge APGST at the rate of three *per cent* in anticipation of its downward revision from then prevailing rate of 10 *per cent* was unwarranted because while a downward revision was on the anvil, the Company had no reason to believe that it would be revised exactly to three *per cent*.

Thus, the unwarranted commitment on the part of the Management limiting the rate of sales tax to three *per cent* resulted in avoidable loss of Rs.33.92 lakh to the Company.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

CHAPTER XXI: MINISTRY OF SOCIAL JUSTICE AND EMPOWERMENT

National Scheduled Castes Finance and Development Corporation

21.1.1 Avoidable expenditure due to delay in shifting the office premises

Inordinate delay by the Ministry in dealing with a capital investment of Rs.5.41 crore, resulted in wasteful expenditure of Rs.52.53 lakh.

The Board of Directors (BOD) of National Scheduled Castes Finance and Development Corporation (Company) in its 73rd meeting approved (14 June 2002) a proposal for purchase of office premises measuring 1,202 square metre in Scope Minar, New Delhi at a cost of Rs.5.41 crore. The Company made the payment to SCOPE in two instalments in June 2002 and July 2002 and took over the possession in August 2002.

On 17 December 2002, the Ministry of Social Justice and Empowerment (Ministry) alleged serious lapses in the purchase of the office property, without, however, indicating specific cases of lapses and directed the Company not to proceed until further orders. The Company responded on the same day stating that the decision to purchase the office premises was the outcome of a transparent decision-making process. After almost five months, the Ministry sought (May 2003) clarification on certain issues pertaining mainly to the authority of CMD to incur capital expenditure, defect in the composition of BOD of the 73rd meeting and the support papers prepared for the proposal.

The Company communicated its reply to the Ministry in July 2003 after obtaining legal opinions on the regularity of its decision and establishing the cost-benefit of the proposal. After five months, the Ministry conveyed (January 2004) its clearance for shifting the office to the new premises.

As the validity of the earlier tender called for interior work had expired, the Company decided (May 2004) to entrust the interior work to CPWD and shifted to the new office in May 2005. During the intervening period of 17 months from January 2003 to May 2004, the Company continued to incur expenditure on rent, electricity and security, etc. for its rented office.

It was observed in Audit that the representatives of the Ministry were present in the 73rd meeting of BOD which approved the proposal for office premises. It was only after six months of the approval that the Ministry raised objections and took further five months in specifying the nature of lapses. Thus, there was inordinate delay on the part of the Ministry in dealing with the issue, which led to non-utilisation of building space involving an investment of Rs.5.41 crore and resulted in wasteful expenditure of Rs.52.53 lakh[♣].

[♣] *Rs.43.35 lakh as rent plus Rs.2.21 lakh on security plus Rs.5.30 lakh on account of electricity and generator charges for rented premises plus Rs.1.67 lakh towards legal fee*

The Management stated (February 2004) that the Ministry's action regarding not allowing the Company to shift the office was within the powers of the Ministry and that there was no delay on the part of the Company as the matter was taken up immediately with the Ministry on 17 December 2002.

Thus, inordinate delay on the part of the Ministry in dealing with the case involving an investment of Rs.5.41 crore, even when the nominee directors of the Ministry were present in BOD meeting, led to idling of investment of Rs.5.41 crore and wasteful expenditure of Rs.52.53 lakh.

The matter was reported to the Ministry in September 2004 and May 2005; its reply was awaited (November 2005).

CHAPTER XXII: MINISTRY OF STEEL

Hindustan Steelworks Construction Limited

22.1.1 Loss of Rs.40.64 lakh in the execution of a work order

Due to submitting the offer on the basis of the estimates provided by the client, the Company suffered a loss of Rs.40.64 lakh in the work of renovation of roads in the Visakhapatnam Steel Plant.

Hindustan Steelworks Construction Limited (Company) secured (October 2002) a work order from Rashtriya Ispat Nigam Limited (RINL) for renovation of certain roads in its Visakhapatnam Steel Plant at a cost of Rs.68.60 lakh. The rates were finalised on the basis of quotation made by the Company as per the estimates provided by RINL in the invitation of tender (July 2002), instead of on the basis of the Company's own cost estimates. The work was to be completed by February 2003.

For the purpose of execution of the job through offloading, the Company invited tenders (October 2002) and the lowest rate received was for Rs.72.10 lakh. Negotiations were held with the first two lowest parties (November 2002) during which both the parties refused to execute the work at their quoted rates. As the Company did not even start (December 2002) the work, RINL indicated that the work would be got done at the Company's risk and cost. Failing to locate any suitable contractor to offload the work, the Company, ultimately decided (December 2002) to get the work executed departmentally and finally completed the work in September 2003 by incurring an expenditure of Rs.118.44 lakh against the total amount of Rs.77.80 lakh admitted by RINL.

The Company, thus, suffered a loss of Rs.40.64 lakh by submitting its offer based on estimates provided by the client, which could have been avoided had it prepared its own realistic estimates. The rates submitted by the Company on the basis of RINL estimates were unrealistic, as was evident from the fact that even the L1 party subsequently refused to execute the work at its offered rate of Rs.72.10 lakh.

While accepting the facts, the Management contended (June 2005) that it felt that giving an offer close to RINL's estimates would give them a fair chance of clinching the job. The reply clearly indicated that its approach was only to clinch the job and was without any consideration of its financial impact.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

Kudremukh Iron Ore Company Limited

22.2.1 Loss due to defects in adopted technology

Due to defects in adopted technology, the Company could not achieve the desired objective of expansion of its pelletising capacity and suffered a loss of Rs.31.65 crore.

Kudremukh Iron Ore Company Limited (Company), decided (January 1995) to set up Vertical Shaft Pelletising Furnace Plant (SPF) of five lakh metric tonne (MT) capacity at an estimated cost of Rs.40 crore for expansion of its existing pelletising capacity. The decision of the Company was based on the proposal (August 1994) and feasibility study (December 1994) conducted by M/s. Maumee Research and Engineering, USA (MRE). The Project was justified by MRE, *inter alia*, on the grounds of low investment cost with a pay back period of five years, low operating cost, quick implementation time and low maintenance cost.

The Company considered MRE as the only firm having expertise and capability for supply and erection and commissioning of SPF. As per the agreement of November 1995, MRE was also responsible for design, drawings and preparation of specifications of the equipment for SPF. During the execution of the Project there were frequent changes and modifications to suit the site conditions indicating that the original designs as considered by MRE were faulty. As a result, the SPF was completed in November 1999 at a cost of Rs.57.15 crore as against the schedule completion of January 1998 at Rs.40 crore leading to time and cost over run of 21 months and Rs.17.15 crore respectively.

The SPF commissioned for regular operation in August 2001, could not be operated on a continuous and sustained basis due to various equipment failures and stoppages. The production achieved during 2001-02 and 2002-03, was 61,600 MT and 44,200 MT respectively as against the expected capacity of 5,00,000 MT. Due to non-stabilisation and frequent failures of the plant there was excess consumption of fuel and power by Rs.1.87 crore. The SPF, however, stopped working in April 2003.

M/s. JINAN Iron and Steel Group Corporation, China (JINAN) inspected (May 2004) the SPF and recommended certain modifications at a projected cost of US$ 339.80 million to revive it. As the cost projected was considered to be on the higher side and the fact that the Company might not have magnetite ore after December 2005, the proposal for its revival was not pursued. The Company decided (December 2004) to utilise certain equipment valued at Rs.16.78 crore in the existing pellet plant and wrote-off the balance equipment valued at Rs.31.65 crore in the accounts for the year 2004-05.

The Ministry stated (October 2005) that (i) SPF proposed by MRE was not an outdated technology but had been upgraded with a number of technological improvements and (ii) after ascertaining the reasonableness of cost of modifications projected by JINAN and acceptability of the ore offered by the South African company, the revival of the SPF will be considered.

The reply of the Ministry is not tenable as (i) MRE being considered as the only agency with expertise and having proposed the technology to the Company after conducting feasibility study should have been in a position to suggest appropriate designs and modifications taking into account the site conditions. On the contrary, the improved technology proposed by MRE was not found to be defect free resulting in subsequent technical problems. The Company could neither succeed in persuading MRE to rectify the problems nor could get it done through any other agency and (ii) the revival of SPF is still not achieved.

Thus, the failure to adopt defect free technology by the Company led to non-achievement of the desired objective of expansion of its pelletising capacity and resulted in a loss of Rs.31.65 crore.

MECON Limited

22.3.1 Loss of Rs.4.63 crore due to inefficient execution of contract

Due to poor bid estimation and inefficient execution of the contract for construction of retail outlets for Indian Oil Corporation Limited, the Company suffered a loss of Rs.4.63 crore.

MECON Limited (Company) accepted (September 2000) a work order from Indian Oil Corporation Limited (IOCL) for the construction of 23 retail outlets (ROs) in the States of Maharashtra and Gujrat at a lump sum value of Rs.18.97 crore. The work was to be completed within a period of 16 weeks from the date of letter of intent i.e. by January 2001. Subsequently, IOCL could not hand over the sites of four ROs to the Company and in terms of the option available in the work order, withdrew (February 2001) the same from the scope of work.

In order to execute the work through offloading, the Company approved the proposal of sub-tendering to eight parties in January 2001 and continued to place work orders upto May 2002. During a review (May 2001) of the progress of work, IOCL noticed poor progress ranging between zero to 14.17 *per cent* and accordingly took back (August 2001) the sites of 10 out of the 19 ROs for execution at the risk and cost of the Company. The price for the reduced scope of work for the remaining nine ROs was revised to Rs.7.27 crore. Of these nine also, the Company did not complete the work on seven ROs as per the scope of work and these were subsequently taken back by IOCL during August 2002 to February 2003. The remaining two ROs were completed and handed over by the Company to IOCL between September and November 2002.

The Company got the work executed through offloading at a total expenditure of Rs.9.61 crore, whereas against the revised contract value of Rs.7.27 crore, IOCL, remitted Rs.6.18 crore only in full and final settlement after making recoveries for the defects and incomplete work and treated the work order as closed. The Company thereby suffered a cash loss of Rs.3.43 crore. It also incurred man-hour cost of Rs.1.20 crore not included in the original estimates, making a total loss of Rs.4.63 crore.

The Management stated (July 2005) that (i) it had completed nine ROs fully and handed over the same to IOCL during September to November 2002 (ii) the Company had

bagged the job on percentage tender basis on fixed schedule of quantities indicated by IOCL, but during detailed engineering, the quantity of many items was found to have increased and some new items came into the picture which were not originally envisaged by IOCL. Also, the Company was pursuing extra claims for settlement with IOCL and (iii) the Company did not take into account the man-hour cost due to the reasons of compelling situation for entering the new market and to remain in competitive fray with a long term objective of securing more orders considering the recession in the steel sector during that period.

The contention of the Management is not tenable as (i) IOCL in their letter of June 2003 had clearly indicated that the Company could never complete the balance work as per specifications, due to which seven ROs were taken between August 2002 to February 2003 after making suitable deductions, (ii) acceptance of a work order on lump sum contract fee against the schedule of quantities fixed by the client indicated lack of financial prudence; further, after releasing final payment to the Company, IOCL had treated the work order as closed and (iii) man-hour cost being a major input cost in civil works, non-consideration of the same by an Engineering Company only to remain in the competitive fray was against the financial interest of the Company. Further, the reply is silent on the issue of taking back the site of 10 ROs by IOCL due to poor performance of the Company.

Thus, due to poor bid estimation and inefficient and delayed execution of job, the Company suffered a loss of Rs.4.63 crore.

The matter was reported to the Ministry in July 2005; its reply was awaited (November 2005).

22.3.2 Extra expenditure of Rs.3.40 crore in the execution of a contract

Due to inclusion of wrong estimates while submitting tender and failure to put completion schedule with its sub-contractors in line with the time schedule as per Indian Oil Corporation Limited work order, the Company incurred extra expenditure of Rs.3.40 crore.

MECON Limited (Company) secured a work order (December 2000) from Indian Oil Corporation Limited (IOCL) for design, engineering, erection, testing and commissioning of a Pipeline Tank Terminal at Lucknow on turnkey basis on a lump sum contract fee of Rs.29.10 crore to be completed by March 2002. Subsequently, due to certain deviations, deletions and addition of some extra items, the value of the work order was reduced to Rs.28.19 crore. The work order provided for liquidated damages (LD) at the rate of 0.5 *per cent* of the total value of the work order per week of delay subject to a total 10 *per cent.*

It was observed in Audit that though the Company completed the job by incurring a total expenditure of Rs.27.86 crore, it incurred extra expenditure of Rs.3.40 crore on account of the following:

(i) Expenditure of Rs.1.15 crore[♣] was incurred due to wrong calculation of estimates for land development work while submitting the offer,

(ii) Certain extra jobs were executed at an expenditure of Rs.1.25 crore[♦] that were not included in the original estimates,

(iii) Payment was made of net liquidated damages of Rs.84.00 lakh for 44 day's delay in completion schedule due to not conducting site acceptance test as per schedule and failure to keep the LD clauses with its sub-contractors in line with the LD clause of IOCL work order. Out of Rs.99.00 lakh paid to IOCL the Company could offload only Rs.15 lakh to its sub-contractors.

(iv) There was a loss of interest of Rs.16.00 lakh[♥] on the amount of Rs.3.53 crore which remained un-recovered from IOCL due to failure to settle the issues of retest of site acceptance, warranty period and annual maintenance contract in totality.

This loss could have been avoided had the Company (i) submitted its bid estimates after proper calculation for the land development work and (ii) protected its financial interest by putting the time schedule with its sub-contractors in line with the time schedule of IOCL work order.

The Management accepted (September 2004) the facts by stating that (i) wrong estimate for land development was submitted in the offer due to paucity of time in submitting the tender and (ii) it had contested the imposition of LD with IOCL.

The Ministry, while endorsing the views of the Management stated (September 2005) that there was a financial gain of Rs.33.00 lakh in the project.

The contention of the Ministry/the Management is not tenable, as IOCL had turned down the Company's request in April 2005 for return of the recovered LD and the matter stood closed at their end. Also the financial gain of Rs.33.00 lakh in the project would have increased to Rs.3.73 crore had the Company not incurred the extra expenditure.

Thus, due to submitting wrong estimates against the tender and failure to put completion schedule with its sub-contractors in line with the time schedule as per IOCL work order, the Company incurred an extra expenditure of Rs.3.40 crore.

22.3.3 Loss due to poor bid estimation

Due to poor bid estimation, MECON Limited suffered a loss of Rs.86.34 lakh.

MECON Limited (Company) entered (April 2002) into an agreement with Bihar State Hydroelectric Power Corporation Limited (purchaser) for setting up of Tejpura Small

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[♣] ***Expenditure on actual land development for 2,05,378 M^3 - Rs.1.54 crore minus admitted by IOCL Rs.0.39 crore (Rs.0.09 crore for original estimates of 12,740 M^3 plus Rs.0.30 crore for 39,735 M^3 for additional land) = Rs.1.15 crore.***

[♦] ***Expenditure on extra items – Rs. 1.53 crore minus Rs.0.28 crore reimbursed by IOCL = Rs.1.25 crore***

[♥] ***Interest of Rs.1.02 crore on amount due from IOCL minus interest of Rs.0.86 crore saved on withheld amount of Rs.2.98 crore due to its sub-contractors worked out at the rate of 10.5 per cent from January 2003 to September 2005.***

Hydel Project (2 X 750 Kw) on turnkey basis at a total cost of Rs.6.64 crore. The work was to be completed within 24 months from the date of payment of mobilisation advance. In terms of the provisions of the agreement, the Company received (May 2002) mobilisation advance of Rs.32.78 lakh after furnishing bank guarantee of equivalent amount to the purchaser. The Company also furnished another bank guarantee of Rs. five lakh as contract security. The scheduled date of completion of the project was May 2004.

However, until October 2003, the Company had only executed the job of detailed survey, layout preparation and engineering work on equipment and civil works after incurring an expenditure of Rs.86.34 lakh. Accordingly, the purchaser terminated the agreement in October 2003 alleging slow progress and encashed both the bank guarantees.

It was seen in Audit that the Finance department of the Company had reviewed the contract agreement in August 2002 and had noted that Rs.2.40 crore provided for civil works in the agreement (based on the rates estimated in-house on the cost of civil work as per bill of quantities provided by the purchaser) was on the lower side and it was likely to be in the order of Rs. five crore. It was further seen that (i) the agreement was signed by the Company without various annexures containing special terms and conditions relating to schedule of prices, break-up price etc. as indicated in para 11 of the agreement and (ii) the purchaser changed the project site in November 2002 from irrigation channel to navigation channel and also revised (January 2003) the capacity of the project from 2 X 750 Kw to 2 X 500 Kw.

Despite being aware of the fact in August 2002 that the agreed job was *ab-initio* a loss making venture and also that the purchaser was not finalising the annexures containing special terms and conditions due to persistent dispute, the Company chose to continue with the execution of the job without safeguarding its financial interest until the purchaser terminated it in October 2003. This resulted in a loss of Rs.86.34 lakh. The Company took up the issue of reimbursement of the entire expenditure with the purchaser in November 2003 but no amount had been realised so far (November 2005).

While accepting the facts, the Management stated (July 2005) that the Company had estimated the cost of civil engineering work based on the bill of quantities furnished by the purchaser and in its eagerness to successfully penetrate into this chosen field and that the Company had signed the agreement on the premise that purchaser was a government undertaking and all general and special terms and conditions would be fair to both the parties. The Ministry endorsed (November 2005) the view of the Management.

The reply of the Ministry/Management is, however, silent on the issue as to why it decided not to opt out of a project which was *ab-initio* a loss making venture even when it got the opportunity to do so in November 2002 followed by January 2003 when the purchaser changed its project site and project capacity respectively. The actions of the Management failed to safeguard the financial interest of the Company.

Thus, the Company suffered a loss of Rs.86.34 lakh due to poor bid estimation and lack of financial prudence.

National Mineral Development Corporation Limited

22.4.1 Loss of Rs.1.89 crore on account of delay in receipt of compensation for short lifting of iron ore due to lacunae in sale agreement

Due to lacunae in the agreement and consequent delay in realisation of the legitimate dues the Company incurred a loss of Rs.1.89 crore by way of interest.

The Company entered into an agreement (9 July 1993) with M/s. Essar Investment Limited, Mumbai (Customer) for supply of iron ore to its pellet plant at Visakhapatnam for a period of 10 years. The agreement was amended in March 2000 and was to remain in force till 31 March 2015. The agreement prescribed the minimum quantity to be lifted every year by the Customer. It also provided that in case the quantity lifted happened to be less than 80 *per cent* of the agreed quantity, the Customer would compensate the Company at the rate of Rs.10 per Wet Metric Tonne (WMT) of such short lifted quantity.

The Customer did not lift the agreed quantity in any of the years from 1996-1997 to 2003-2004. There was shortfall of 89.36 lakh WMT upto the year 2003-04 on account of which the Company was eligible for compensation amounting to Rs.8.94 crore. However, it could realise Rs.2.98 crore pertaining to 1996-97 to 2000-2001 and that too only in March 2003 with delay ranging from two to six years and another Rs.1.00 crore pertaining to the years 2001-02 to 2003-04 in April 2004. The Company was yet to realise the balance dues of Rs.4.96 crore pertaining to the years 2001-02 to 2003-2004 (October 2005).

It was observed in Audit that though the Company had been specifying a period of 15 days for payment of compensation, backed by bank guarantees in other contracts, no such provision was made in this contract. It also did not include any provision for levy of penal interest for the delayed payments. On account of this, the amount of compensation could not be recovered in time and consequently the Company suffered a loss of interest of Rs.1.89 crore[♣].

The Ministry stated (September 2005) that the claim for the period beyond October 1996 was under dispute and had been referred to arbitration. It assured that the Company would include a clause for penal interest on delayed payments while entering into fresh contracts with the customer and would take all legal measures for recovering dues including interest. It also informed that the Company would be advised to eliminate such loopholes, which were liable to be exploited.

Thus, due to lacunae in the agreement and consequent delay in realisation of the legitimate dues amounting to Rs.3.98 crore and blockage of dues amounting to Rs.4.96 crore, the Company incurred a loss of Rs.1.89 crore by way of interest. While the Ministry agreed with the need to plug the loopholes in future contracts, the loophole in the current agreement with the Customer would continue upto the year 2015.

[♣] *calculated at the rate of eight per cent*

Rashtriya Ispat Nigam Limited

22.5.1 Failure to retrieve the value of material held by a supplier and not invoking risk purchase clause

The Company failed to recover the value of its Imported Coking Coal amounting to Rs.34.70 crore, withheld by Indian Iron and Steel Company Limited. It also did not invoke the risk purchase clause under general conditions of the contract to recover an additional expenditure of Rs.18.49 crore which it had to incur on purchase of 22,794 MT of blast furnace coke on account of failure of IISCO to complete supplies.

The Company entered into a contract (March 2003) with M/s. Indian Iron and Steel Company Limited (IISCO), Kolkata for supply of Blast Furnace (BF) Coke by converting Imported Coking Coal (ICC), which was to be supplied by it. Under the contract, IISCO was to supply one MT of BF Coke for every 1.59 MT of ICC transferred by the Company at a conversion charge of Rs.1,000 per MT. The contract was valid for an initial period of six months extendable upto one year at the option of the Company. The contract was extended upto March 2004.

The Company transferred 2,04,292 MT of ICC during March 2003 to January 2004 against which IISCO was required to supply 1,28,485 MT of BF coke. IISCO supplied 1,05,692 MT of BF coke from March 2003 to November 2003 by utilising 1,68,050 MT of ICC. It neither supplied the balance 22,794 MT of BF coke nor did it return the unutilised 36,242 MT of ICC.

As the Company was facing shortage of BF coke, a team of the Company visited (February 2004) IISCO for resolving the issue and restoring the supplies. However, IISCO while expressing its inability to supply BF coke on conversion basis agreed to supply BF coke on direct sale basis. The Company placed (March 2004) a purchase order on IISCO for supply of 60,000 MT of BF coke at prices prevailing on the date of dispatch.

IISCO delivered 25,836 MT of BF coke from February 2004 to June 2004 at landed costs ranging from Rs.13,386 to Rs.17,546 per MT for which an amount of Rs.42.13 crore was paid. No further supplies were received and the contract was short-closed.

It was noted in Audit that in the above transactions, the Company failed to protect its interest, as neither did it get the value of the ICC amounting to Rs.34.70 crore lying with IISCO adjusted against the value of the coke purchased on direct sale basis nor did it invoke the risk purchase clause under general conditions of the contract and recover the extra costs of Rs.18.49 crore from IISCO. The landed cost of the coke on conversion basis was Rs.8,168 per MT of BF coke against the landed cost of Rs.13,386 to Rs.17,546 MT for the coke procured on direct sale basis.

Thus, the Company incurred an additional expenditure of Rs.18.49 crore on purchase of 22,794 MT of BF coke on direct sale basis, which it failed to claim from IISCO. It also failed to retrieve 36,242 MT of ICC valuing Rs.34.70 crore from IISCO.

The Management in its reply (May 2005) stated that since it was not in a position to supply further quantity of ICC to IISCO for conversion due to critical stock of ICC at plant, the risk purchase clause was not invoked. As regards the quantity held by IISCO, it informed that efforts were being made at higher levels to retrieve the same.

The reply of the Management is not tenable as there was no shortage of ICC. The Company sent about 3,000 MT of ICC every few days from March 2003 to January 2004. Yet IISCO stopped supplying BF coke from November 2003. As IISCO was already holding a quantity of 36,242 MT citing shortage of ICC did not arise. As regard retrieval of ICC, the same was yet to be effected (October 2005).

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

22.5.2 Extra expenditure of Rs.35.73 crore in procurement of US Coal

The Company procured US coal based on an incorrect assessment of requirement, which resulted in an extra expenditure of Rs.35.73 crore.

The Company mixes Imported Hard Coking Coal (ICC), Imported Semi Soft Coking Coal (SSCC) and Medium Coking Coal (MCC) in the ratio of 80:10:10 in its Coke Oven Batteries to produce Blast Furnace (BF) coke. The Company also procures BF coke directly to meet its requirements. Citing difficulties in supply of BF coke and shortage of ICC, the Company decided (February 2004) to set up an Emergency Raw Material Procurement Committee (ERMPC) to facilitate building up of safe levels of stock and to ensure continuity in production. ERMPC was authorised to finalise orders on nomination basis, if required.

In April 2004, ERMPC placed orders for the procurement of 2,20,000 MT of US Coal on three firms on nomination basis, based on voluntary offers received. The prices ranged from Rs.8,317 per MT to Rs.9,258 per MT. This was put up to the Board of Directors for ratification in May 2004. The Board was apprised that the requirement of ICC for the period April 2004 to August 2004, considering usage of the same at the rate of 90 *per cent* in the overall blend, would be 13,71,700 MT and on the basis of the stock on hand and expected receipts it was estimated that there would be a shortage of 2,98,300 MT of ICC (including SSCC) and to meet this shortage orders of US coal had been placed.

It was observed in Audit that the projected shortage of ICC was overstated to the tune of 1,65,917 MT on account of the following:

(i) The opening stock of Imported Coking Coal (including SSCC) was taken as 1,23,400 MT as against the physically verified opening stock of 2,17,778 MT.

(ii) While estimating the consumption, the Management did not consider the fact that 71,539 MT of Imported Coking Coal (including SSCC) would not be required due to capital repairs scheduled for a Coke Oven Battery in April 2004, resulting in overstatement of requirement to that extent.

Despite these facts, the Company did not restrict the order for US Coal to the required level of 54,083 MT and instead placed orders for 2,20,000 MT. The Company received 1,85,974 MT of US coal during the period July to August 2004. Due to delay in the supplies, the Company cancelled the order for the remaining quantity (January 2005). Thus the Company procured 1,31,891 MT of US Coal in excess of the requirement out of which it consumed only 40,363 MT of US coal during the distress period.

The Management stated (August 2005) that the opening stock of ICC was 1,23,400 MT. It also contended that the capital repair to Coke Oven Battery was originally envisaged in the month of December 2004. As regards utilisation it stated that the performance of US coal was not known at the time of import and the same was done with a view that it could be used as a substitute in case of emergency if found suitable and it was never envisaged that it would be used at the same rate in the blend at which Australian coal was being blended.

The reply is not tenable because as per the physical verification report, the opening stock of ICC (including SSCC) was 2,17,778 MT including the stock at plant and stock at port. As regards capital repairs, the works department of the Company recommended (March 2004) taking up of capital repairs to the Coke Oven Battery in April 2004 itself. Uncertainty regarding the performance of US coal at the time of import further substantiates the fact that the Company issued orders for US coal without a proper assessment of even its suitability.

Thus, the procurement of US coal in excess of requirement, for use during the period of distress resulted in extra expenditure of Rs.35.73 crore as compared to the cost of Prime Coking Coal procured during the same period from indigenous source.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

22.5.3 Failure to exercise freight option in time resulted in avoidable extra expenditure of Rs.8.77 crore

The Company incurred an avoidable extra expenditure of Rs. 8.77 crore, as it did not exercise the freight option within the validity period of offer.

The Company entered (May 2001) into an agreement with M/s. Emirate Trading Agency (ETA), Dubai for procurement of 10.00 lakh Metric Tonne (MT) of Low Silica (SMS Grade) Limestone on Free On Board (FOB) basis at prices ranging from US$ 7.95 per MT to US$ 8.15 per MT. The agreement provided for purchase of an additional quantity of two lakh MT provided the order for it was placed before 30 June 2003. The agreement gave another option to the Company to get the material supplied on Cost Freight Rate (CFR) basis at Visakhapatnam at an additional expense of US$ 8.95 per MT towards freight. The validity of this option was 18 months from the date of agreement or till the time of supply of six lakh MT, whichever occurred earlier. For import of material on CFR basis, the Company was required to obtain dispensation from Transchart, Ministry of Surface Transport.

ETA completed the supply of 10 lakh MT of the material by September 2003. As the validity for exercising the option for import of additional quantity had expired in June 2003, the Company requested (August 2003) ETA to extend its validity till 15 September 2003 and also to lower the freight. In response, ETA offered (August 2003) to supply the additional quantity and revised the freight rate to US$ 8.75 per MT for shipment of additional quantities provided acceptance for the same was communicated by 15 September 2003. The Company communicated (9 September 2003) its acceptance of additional quantity of two lakh MT through an amendment to the original agreement. It also added the words "all other terms and conditions remain unaltered" in its acceptance without stating anything specific with regard to freight.

After obtaining dispensation from Transchart in October 2003, when the Company re-approached ETA to supply the material on CFR basis, ETA refused (October 2003) on the ground that the Company had failed to exercise the option for freight before 15 September 2003. As a result, the Company had to import (November 2003 to March 2004) 1,81,761 MT of the material on FOB basis by paying freight charges ranging from US$ 15 per MT to US$ 21 per MT as against the ETA's offer of US$ 8.75 per MT and accordingly it incurred an additional amount of Rs.7.24 crore towards differential freight. In addition, it paid custom duty on the differential freight amounting to Rs.1.23 crore besides incurring stevedoring costs of Rs.30.00 lakh. Thus, the Company incurred an extra avoidable expenditure of Rs.8.77 crore which was yet to be recovered (October 2005).

The Ministry stated (November 2005) that the option for the freight offer was exercised within the validity period vide amendment issued in September 2003 by mentioning "all other terms and conditions remain unaltered", which implied that the offer of the supplier was accepted both on FOB as well as CFR basis. It also stated that the extra expenditure of Rs.8.77 crore was recoverable from ETA.

The reply of the Ministry is not tenable, as the option was exercised in October 2003, which was clearly beyond the period of validity and the seller was not bound to arrange the shipment at that rate nor could it be made liable for any breach of contract. Besides, legal experts had opined that by simply mentioning all terms and conditions remained unaltered, it could not be said that the Company specifically referred to the freight offer. On account of the adverse legal opinions, the Company had not gone in for arbitration against ETA.

Thus, failure on the part of the Company to exercise the freight option within the validity period of offer resulted in an avoidable extra expenditure of Rs.8.77 crore.

22.5.4 Loss of revenue of Rs.2.40 crore due to deviation from laid down procedure

The Company deviated from its own laid down procedure of selling pig iron through open tender and sold the same on spot basis, which resulted in loss of revenue of Rs.2.40 crore.

The Company issued (5 October 2002) a Notice Inviting Tender (NIT) for sale of 50,000 MT of pig iron for delivery during November and December 2002. Out of five bids received, bid of M/s. Stemcore, United Kingdom was highest at FOB price of US$

125.27 (equivalent to Rs.6,053) per MT. The Company accordingly awarded (29 October 2002) a contract for sale of 50,000 MT of pig iron to M/s. Stemcore, UK.

While the above sale was being finalised, the works department of the Company informed (19 October 2002) that another one lakh MT of pig iron would be available for sale upto the end of December 2002. Instead of issuing a fresh tender as required under the prescribed procedure, the Company decided (25 October 2002) to sell an additional quantity of 50,000 MT on spot basis to the parties who had participated in the above NIT on the ground that the price received in the previous NIT (5 October 2002) was lower than the highest price obtained in the preceding quarter indicating a downward trend. Accordingly an offer was made. Of the three parties that responded, M/s. Prime Trade AG, Switzerland offered highest FOB price of US$ 125.51 (equivalent to Rs.6,017) and US$ 125.28 (equivalent to Rs.5,991) per MT for deliveries during November and December 2002 respectively. A sale contract for 50,000 MT (+/-10 *per cent*) was awarded (2 November 2002) to M/s. Prime Trade AG, Switzerland at the above prices. The quantity was increased (18 November 2002) to 60,000 MT at the request of the customer.

After awarding the above contract, the Company issued another NIT (25 November 2002) for sale of 50,000 MT of pig iron for delivery during January 2003 to March 2003. This time M/s. Prime Trade AG whose offer was highest offered a rate of US$ 133.77 (equivalent to Rs.6,432) per MT. A sale contract was awarded (17 December 2002) to the party for the sale of 50,000 MT of pig iron at the above rate.

It was observed in Audit that due to deviation from the laid down procedure, the Company lost revenue of Rs.2.40 crore in the sale of 60,000 MT of pig iron to M/s. Prime Trade AG, Switzerland at US$ 125.51 (equivalent to Rs.6,017) and 125.28 (equivalent to Rs.5,991) per MT in November 2002 as against the market price of US$ 133.77 (equivalent to Rs.6,432) per MT obtained from the same party through fresh global tendering in December 2002.

On this being pointed out, the Management replied (April 2005) that as per the marketing procedure the sale could be made either through tender or on spot basis. It further stated that the expected increase in the holding of pig iron could not be accommodated in the stockyard of the plant without adversely affecting the operations and disposing the same through global tender would have taken four to five months.

The Management's reply is not tenable as the Company's Export Marketing Procedure (as amended at the instance of Chief Vigilance Officer in September 2002) does not provide for offering fresh quantities to the bidders of an earlier bid. In fact, it prescribes that in case the total quantity offered for sale against a tender can not be sold at H1 price, the tender shall be short closed and the balance quantity re-tendered or included in the next tender. As regard constraint in accommodating the quantity, it was noticed that while deciding to liquidate the additional quantity of pig iron expected to be available by December 2002, the Management assumed that there would be no domestic requirement during the period. The Company delivered 40,000 MT in November-December 2002 in the domestic market while the first and second consignments due to M/s. Prime Trade were delivered only on 24 December 2002 and 28 January 2003.

Thus, due to deviation from its own laid down procedure, the Company lost revenue of Rs.2.40 crore in sale of pig iron.

The matter was reported to the Ministry in May 2005; its reply was awaited (November 2005).

Steel Authority of India Limited

22.6.1 Loss of Rs.30.84 crore due to waiver of quantity option clause

The Company incurred a loss of Rs.30.84 crore in the procurement of silico manganese and ferro silicon due to not enforcing quantity tolerance at buyer's option for procurement cycle 2003-04 and purchasing the same at higher rate finalised for procurement cycle 2004-05.

Steel Authority of India Limited (Company) placed orders (April-November 2003) on various parties for procurement of a total quantity of 65,380 MT of silico manganese at an average basic price of Rs.22,680 per MT. As per the terms of the purchase order, the prices were firm and the Company had the option of quantity tolerance of plus/minus 25 *per cent*. Further, in case the seller failed to deliver the material, the Company had the option of purchasing the same at the risk and cost of the seller. The order was placed for the procurement cycle 2003-04 and the period of contract was between March 2003-April 2004 with delivery schedule as given by the respective steel plants of the Company.

Considering the rising trend in the price of the material, the Company exercised the quantity option clause and issued amendments (January-March 2004) to all suppliers enhancing the ordered quantity by 25 *per cent*. Suppliers, however, expressed their inability in continuing supplies at the contracted price for 2003-04 due to unprecedented increase in the price and some of them stopped the supplies while others supplied less than the scheduled quantity. After several meetings with the suppliers and apprehending disruption in production in case of disrupted supplies of the material, it was agreed that the suppliers would supply the balance quantity (24,577 MT) from the original ordered quantity of 65,380 MT at the existing rates and in turn, the Company would not insist for optional 25 *per cent* increase in quantity.

As such, the Company lost the opportunity of procurement of 25 *per cent* increased optional quantity of the original ordered quantity (16,345 MT) at lower price, that was ultimately procured at higher average price of Rs.39,660 per MT finalised for the procurement cycle 2004-05 instead of purchasing at the risk and cost of the suppliers and suffered a loss of Rs.27.75 crore in the procurement of silico manganese.

Similarly, in the purchase of 18,000 MT ferro silicon for the procurement cycle 2003-04, under the same terms and conditions, the Company did not invoke quantity option clause in its favour under the same circumstances and procured 4,500 MT (25 *per cent* of ordered quantity) at higher price of Rs.38,730 per MT finalised for the procurement cycle 2004-05 and suffered a loss of Rs.3.09 crore.

Thus, the Company incurred an extra avoidable expenditure of Rs.30.84 crore in the procurement of silico manganese and ferro silicon due to not enforcing the quantity

tolerance of plus 25 *per cent* option clause in its favour in terms of the contract and procurement of the same at higher price.

While accepting the facts, Management stated (August 2005) that though the quantity variation clause was enforceable, however, due to unprecedented increase in price, the supplies were disrupted by the parties, which might have led to disruption in the production of steel.

The reply is not tenable as the Company neither enforced the quantity variation clause nor enforced the risk purchase clause, which led to loss of Rs.30.84 crore.

The matter was reported to the Ministry in August 2005; its reply was awaited (November 2005).

22.6.2 Extra expenditure due to delay in procurement of hard coke

Despite being aware of the scarcity of hard coke due to price rise, Company delayed advance payments, which resulted in shortage of hard coke and an extra expenditure of Rs.2.32 crore with the consequential loss of contribution margin amounting to Rs.28.16 crore on account of production loss of saleable steel.

In order to meet its requirement in the event of heavy shortfall due to re-building of coke oven batteries, the Rourkela Steel Plant (RSP) of Steel Authority of India Limited (Company) entered (September 2003) into a Memorandum of Understanding (MOU) with Durgapur Projects Limited (DPL) for the purchase and uninterrupted supply of 2,40,000 to 3,60,000 MT of hard coke over a period of two years commencing from September 2003. In terms of the MOU, DPL was to supply 10,000-15,000 MT of hard coke per month with a minimum of 7,500 MT per month during the period September-December 2003.

Accordingly, RSP initially placed (October 2003) a purchase order for the procurement of 75,000 MT of hard coke at the rate of Rs.7,100 per MT, to be supplied over a period of six months commencing from September 2003 with the option of increase in quantity and period of supply to the MOU level. Payment was to be made either in advance or through letter of credit (LC).

It was observed in Audit that though the Company made advance payment (September 2003) for the first rake, it did not open LC for subsequent supplies on the plea that it would require amendment in purchase order for withdrawing the provisions of advance payment. It also made considerable delays in making advance payment for want of documents of previous supply/Proforma invoice from DPL. In the meanwhile, due to rise in price of imported coal from time to time, DPL increased the price of hard coke to (i) Rs.8,000 per MT with effect from 1 November 2003, (ii) Rs.10,000 per MT with effect from 1 January 2004 and (iii) Rs.11,000 per MT with effect from 1 February 2004 and availability of the material became scarce.

In the process, the Company could purchase only a small quantity of 19491.200 MT of hard coke upto February 2004 as against the ordered quantity of 75,000 MT. Out of the above, 9,412.600 MT was purchased at the purchase order price whereas the balance quantity of 10,078.600 MT was purchased at increased prices, due to which the Company

incurred an extra expenditure of Rs.2.32 crore. It also had to suffer acute shortage of hard coke and the Plant had to curtail hot metal production and suffered production loss of 93,045 MT of saleable steel directly attributable to the under procurement of 55,508.800 (75,000 MT minus 19,491.200 MT) of hard coke from DPL. This also resulted in loss of contribution margin amounting to Rs.28.16 crore*.

Thus, despite being aware of the scarcity of the material in the market due to price rise, the Company delayed in making advance payments to DPL resulting in extra expenditure of Rs.2.32 crore in the procurement of hard coke and consequential loss of contribution margin amounting to Rs.28.16 crore for the production loss of saleable steel due to shortage of hard coke.

The Management stated (July 2005) that there was no delay in processing the payments after receipt of the proforma invoice from DPL and the party did not supply hard coke due to global shortage of imported coal and other reasons at their end. The Ministry further stated (December 2005) that as per the standard procedure subsequent advances to a supplier against the same order can be made only after regularisation of the previous advances.

Reply of the Management/Ministry is not acceptable as according to the provisions of the purchase order advance payment of subsequent supplies was to be made against the documents of previous supply and not against Proforma invoice, which was to be issued by the supplier once in a month only.

22.6.3 Loss of Rs.10.15 crore in the sale of steel blooms

Due to acceptance of supply order without price escalation clause, the Company suffered a revenue loss of Rs.10.15 crore in the sale of steel blooms to Rail Wheel Factory during the year 2003-04.

The Alloy Steels Plant (Plant) of Steel Authority of India Limited (Company) secured (June 2003) a supply order from Rail Wheel Factory (RWF), Bangalore for the supply of 21,984 metric tonne (MT) of steel blooms of various specifications at basic prices ranging from Rs.24,500 to Rs.28,900 per MT (total value of Rs.71.09 crore). In terms of the supply order, deliveries were to be completed by January 2004 and prices were to remain firm till the supply was completed. Further, RWF reserved its right to increase/decrease the ordered quantity by 30 *per cent* at the same rates and on the same terms and conditions during the currency of the contract.

Meanwhile, with the increasing trend in the prices of input materials mainly Melting Scrap and Ferro Manganese, the Company increased the prices of blooms ranging from six *per cent* (May 2003) to 71 *per cent* (March 2004) over the price prevailing in March 2003. However, in the absence of any escalation clause in the supply order, the Plant could not revise the prices of blooms to be supplied to RWF. Instead, it had to accept the enhancement in the ordered quantity from 21,984 MT to 28,579 MT at the same price due to invoking of (October 2003) the quantity option clause by RWF.

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* ***Contribution Margin from 93,045 MT of steel – Rs.93.35 crore minus Rs.65.19 crore value of 55,500 MT of coke under procured = Rs.28.16 crore.***

The Plant took up the matter with RWF in November 2003 and March 2004 for increase in per MT price by Rs.3,300 and Rs.8,000 for the supplies effective from 15 November 2003 and 1 March 2004 respectively. However, in the absence of any price escalation clause, the request of the Plant for price amendment was not accepted by RWF. The Company, as such, had to supply 16,765.62 MT of steel blooms after 15 November 2003 at the existing rates and suffered a revenue loss of Rs.10.15 crore.

Thus, by non-including the price escalation clause in the supply order for the year 2003-04 the Company incurred a revenue loss of Rs.10.15 crore.

While accepting the facts, the Management stated (June 2005) that the price variation formula had been incorporated in the new contract for the year 2004-05. It further stated that there was a sudden and unprecedented increase in the input prices during 2003 which could not be foreseen at the time of quoting against the tender in March 2003 and the order was secured through competitive bidding against a global tender without any negotiation. The Ministry endorsed (October 2005) the views of the Management.

Thus, by not including the price escalation clause in the contract to take care of unforeseen eventualities of future price rises, the Company failed to safeguard its financial interest in the contract for the year 2003-04 and suffered a loss of Rs.10.15 crore.

22.6.4 Avoidable expenditure of Rs.1.29 crore

Procurement of iron ore lumps from outside source without considering the stock position at captive mines resulted in an avoidable extra expenditure of Rs.1.29 crore.

Iron Ore lump is one of the basic raw materials used in the production of hot metal in Steel Industry. The Bhilai Steel Plant (Plant) of Steel Authority of India Limited (Company) has its own iron ore captive mines[♣] to cater to the requirement of iron ore lumps. According to the records for the years 1999-00 to 2002-03, the average production of Blast Furnaces Grade iron ore lumps of the captive mines was about 9,500 MT per day and average consumption at plant was about 7900 MT per day. However, with the enhancement of production targets for the year 2003-04, the average consumption of iron ore lumps was increased to 9,000 MT per day during April 2003. On 19 April 2003, the Plant had a stock of 48,480 MT of iron ore lumps. Assuming that these stocks would last for about four days only, the Company, in order to have a buffer stock of iron ore for the forthcoming monsoon, placed (22 April 2003) a purchase order on National Mineral Development Corporation Limited (NMDC) for the procurement of 40,000 MT of iron ore lumps with delivery by 31 May 2003. Against this, it received 13,838 MT of iron ore lumps only (7,011 MT in May 2003 and 6,827 MT in August 2003) at a landed cost of Rs.1,349.64 per MT.

It was noticed in Audit that while going for the procurement of iron ore lumps from outside sources, the Company did not consider the stocks of 74,363 MT of iron lumps lying at its captive mines. With this, the total stock availability would have been 1,22,843

[♣] *Rajhara and Dalli Mines*

MT. The landed cost of iron ore lumps from its captive mines worked out to Rs.417.19 per MT; against this low cost, procurement of 13,838 MT of iron ore lumps from outside sources at a higher landed cost of Rs.1,349.64 per MT resulted in a loss of Rs.1.29 crore to the Company.

The Management stated (May 2005) that as per the directive of the Board of Directors of the Company (May 2000) a minimum of 11 days stock was to be maintained at Plant against which the stock of iron ore lump was sufficient for four days only. As such there was an urgent need to create the buffer stock which had helped in reducing the probable risk of low stock situation.

The reply of the Management is not tenable as the stocks of iron ore lumps at the mines could have been transported to the plant in order to bring the stocks to the optimum level of 11 days instead of procuring 40,000 MT from outside sources at a higher price. Even the procurement of the ordered quantity of iron ore lumps would have increased the level to eight days only against the optimum level requirement of 11 days. Further, the actual receipt of 7,011 MT in May 2003 and 6,827 MT in August 2003 neither met the objectives of urgent requirement nor created any buffer stock.

The Ministry stated (October 2005) that the production of BF grade iron ore from the captive mines was not more than the requirements of Blast Furnaces for Hot Metal production during the period of criticality.

The reply of the Ministry is not tenable, as production of BF grade iron ore during the month of April 2003 was 3,06,226 MT as against the consumption of 2,72,182 MT during the same month. Moreover, the Company did not consider the stocks lying its captive mines in the procurement proposal.

Thus, due to avoidable procurement of iron ore lumps without considering the stocks lying at captive mines, the Company suffered a loss of Rs.1.29 crore.

22.6.5 Loss of Rs.81.00 lakh in the sale of pipes

The Company suffered a loss of Rs.81.00 lakh due to supply of pipes to Delhi Jal Board below the prescribed specifications.

Steel Authority of India Limited (Company) received (March 2004) a supply order from Delhi Jal Board (DJB) for supply of 22,060 meters of spirally welded pipes of various sizes and specifications at a total value of Rs.14.56 crore.

The payment was to be made against delivery of material at Delhi. For the purpose of making payment to the Company, DJB opened (May 2004) a revolving letter of credit (LC) of Rs.4.85 crore upto a maximum amount of Rs.14.56 crore. In terms of the provisions of the LC, for the purpose of drawing payment from the bank, the Company was to produce certificate to the effect that goods were as per the purchase order.

On a joint inspection (June 2004) by the officials of DJB and the Company, it was found that all the pipes of 938 milli meter (mm) outside diameter inspected (252.38 meters) were below the specified thickness of 10 mm and were actually in the range of 9.1 mm to 9.6 mm. Accordingly, DJB made deductions of Rs.81.00 lakh for undersized thickness

and the Company received Rs.13.71 crore against the invoice value of the material supplied. In the process, the Company suffered a loss of Rs.81.00 lakh.

The Management stated (June 2005) that the pipes were supplied as per IS-code- 3589 which permitted wall thickness tolerances of minus 12.5 *per cent* and plus 20 *per cent* and DJB had not imposed any such specific restriction in the supply order. The Ministry endorsed (October 2005) the views of the Management.

The reply of the Ministry/Management is not tenable as the supply order of DJB categorically mentioned thickness of the pipes as 10 mm and not as per IS-code 3589, which was reiterated by DJB in June 2004 also.

Thus, due to supply of material below specification, the Company suffered a loss of Rs.81.00 lakh.

22.6.6 Irregular decision to sell goods to a private party

The Company suffered a loss of Rs.66.37 lakh as a result of an irregular arrangement with one of its customers under which it allowed establishment of letters of credit after despatch of goods.

The terms and conditions of sale obtaining in the Visvesvaraya Iron and Steel Plant (Plant), a Unit of Steel Authority of India Limited (Company) varied from customer to customer and commercial terms were generally negotiated with the party along with price and credit on a case-to-case basis. Accordingly, on the basis of negotiations (August 1997) with M/s. Trinity Forge Limited, Pune (customer) the Plant agreed to dispatch the material on credit basis and allowed the customer to open letters of credits (LCs) at a later date. Under the negotiated arrangement, LCs were not opened for despatches valuing Rs.86.20 lakh sold from September 2000 to January 2001. Since payment was not forthcoming, dispatches were stopped in January 2001 citing the very same reason viz. non-opening of LCs. Subsequently, the Plant could realise only Rs.39.07 lakh from the customer (March 2005). The Plant treated outstanding sales dues of Rs.47.13 lakh along with interest of Rs.19.24 lakh on belated settlement of old outstanding dues as doubtful of recovery and made a provision in the books of accounts of 2003-04.

While admitting (June 2005) that materials were indeed delivered to the customer even before LCs were opened, the Management stated that the decision was taken in response to depressed market conditions and as per industry practice.

The reply is not tenable as the same customer had defaulted in settlement of dues earlier also during 1998-99. Despite this, the Plant did not review the concessions and it failed to safeguard its own interest by allowing the customer to open LCs after dispatch of goods.

Thus, the Plant suffered a loss of Rs.66.37 lakh on account of unrealised dues for sales made during the year 2000-01 and interest levied for belated settlement of earlier dues.

The matter was reported to the Ministry in June 2005; its reply was awaited (November 2005).

22.6.7 Loss of Rs.65.39 lakh due to theft of equipment

Due to installation of solarphoto voltaic street lighting system in a theft prone area without insurance coverage and other safety measures, the Company suffered a loss of Rs.65.39 lakh as most of the equipment were stolen over a period of six months.

In order to conserve energy and reduce unauthorised power tapping, Bokaro Steel Plant (Plant) of Steel Authority of India Limited (Company) decided (July 2003) to provide 200 sets of solar photovoltaic (SPV) street lighting system in its township at a cost of Rs.70.83 lakh. Accordingly, the Plant procured (September 2003) 200 sets of solar street lighting system from Bharat Heavy Electrical Limited out of which 188 sets were installed and commissioned in April 2004 while the remaining 12 sets were installed by September 2004. The Company incurred a total capital expenditure of Rs.69.56 lakh on the procurement, installation and commissioning of the sets. However, during the period May-September 2004, 188 of these sets were stolen in full or in parts and only the balance 12 sets remained in working condition.

It was observed in Audit that though in the initial proposal, the Investment Planning Cell of the Plant had suggested an insurance cover for the equipment; the Plant Management ignored the suggestion and accorded (July 2003) sanction of the scheme without any insurance cover. In the absence of insurance cover, the Plant could not make any claim for the stolen equipment. It was further observed that in May 2004, when for the first time, theft of 21 photo voltaic plates and one complete set of lighting system came to notice, the Electrical department of the Plant had advised for providing anti-climbing system on each pole to check theft, which was also not done by the Plant Management on the plea that it would not stop theft.

The Company, thus, suffered a loss of the Rs.65.39 lakh incurred on the procurement, installation and commissioning of 188 sets, which were stolen subsequently. This could have been avoided, had the Company accepted the suggestion of Investment Planning Cell for taking insurance cover of the equipment to be installed in a theft prone area.

The Ministry stated (September 2005) that (i) for the security of the township area, the Plant was dependent on the State Administration and (ii) insurance of equipment like substations, transformers, distribution systems streetlights etc. in the township area was not taken considering the same as uneconomical.

The reply of the Ministry is not tenable in view of the fact that (i) it is the responsibility of the Company to take adequate steps for safeguarding its assets and security arrangements of State Government in general can not absolve the Company of this responsibility and (ii) the Company had not worked out any financial implications of the insurance cover at the time of deciding on the procurement.

Thus, due to installation of the system in a theft prone area without insurance coverage and other safety measures to protect its interest, the Company suffered a loss of Rs.65.39 lakh.

22.6.8 Loss of Rs.64.87 lakh due to payment of excess railway freight

Failure of the Company to monitor timely the changes in classification of commodities for payment of railway freight led to a loss of Rs.64.87 lakh.

Steel Authority of India Limited (Company) dispatches limestone and dolomite from its Bhawanathpur Limestone Mines to Bokaro Steel Plant by rail by paying railway freight at applicable rates for various classes of commodities. In March 2000, Railways revised the classification of limestone and dolomite from Train in load (TL) 125 to TL 120 with effect from 1 April 2000. The rail freight of commodities classified under TL 120 was lower (ranging from Rs.30.58 per quintal to Rs.32.45 per quintal) as compared to the commodities classified under TL 125 (ranging from Rs.31.75 per quintal to Rs.33.80 per quintal). The Company, however, without giving any cognisance to the revised classification, continued to pay higher freight as per classification code TL 125 instead of TL 120 till middle of August 2002 for the dispatches of limestone and dolomite. This resulted in payment of excess freight amounting to Rs.79.98 lakh on the dispatches of 6,59,987 MT of limestone and dolomite transported during the period 1 April 2000 to 12 August 2002.

Subsequently, the Company lodged (October 2002) a claim with Railways for the refund of excess freight paid. In terms of the provisions of Rule 106(3) of Indian Railway Act, 1989, claims for the refund of overcharges were acceptable if the notice to the railways had been served within a period of six months of such payments etc. The Railways, accordingly, after accepting the part claim amounting to Rs.15.11 lakh for the overcharges falling within six months period, rejected the remaining claim amounting to Rs.64.87 lakh as time-barred.

While accepting the facts, Management stated (July 2004) that the lapse was on the part of Railways, since there was a delay on their part in intimating the change in TL class from 125 to 120 and that the freight was paid as per the rates intimated by Railways. It further stated that the matter had been taken up with Railways for refund of the balance amount.

The reply is not tenable in view of the fact that (i) the Company has a Rail Movement Cell responsible for collecting railway circulars and intimating the unit offices and (ii) in other steel plants and mines of the Company, freight for the transportation of limestone was paid as per revised rates with effect from1 April 2000.

The Ministry endorsed (August 2005) the views of the Management but asked the Company to fix responsibility.

Thus, despite having a Rail Movement Cell, the Company failed to timely monitor the changes in classification of commodities for correct application of railway freight, which led to a loss of Rs.64.87 lakh.

22.6.9 Unfavourable terms of an MOU

The Company signed a Memorandum of Understanding (MOU) for entering into a strategic partnership with a foreign party for securing availability of imported coking coal in exchange for leveraging its iron ore resources without ascertaining the financial implications. The deal was not favourable to the Company.

Steel Authority of India Limited (Company) is engaged in iron and steel making with a hot metal output of 12-13 million metric tonne per annum (MMTPA). Coking coal is one of the major raw materials being used in Integrated Steel Plants (ISP) of the Company. The Corporate Plan 2012 of the Company aimed at reaching a level of 20 million metric tonne (MMT) of hot metal production and accordingly envisaged a requirement of 14.5 MMT of coking coal by that time. The Company was meeting its requirement of coking coal by outsourcing indigenously and through imports. With the deteriorating quality of indigenous coking coal, the Company's dependency on imported coking coal was increasing progressively. Further, to meet the increasing requirement of high grade iron ore, the Company was looking for strategic partners for development of most of its mines.

In order to obtain assured volumes of coking coal, the Board of Directors (BOD) of the Company decided (April 2004) to develop a strategic partnership which would ensure availability of coking coal, on a long term and sustainable basis, by leveraging its resources in iron ore. M/s. BHP Billiton Pty Limited (BHPB), an Australian company, was a supplier of coking coal to SAIL under Long Term coal agreements. Accordingly, the BOD approved (September 2004) the proposal of strategic partnership and entered into a Memorandum of Understanding (MOU). The MOU was to be implemented under two phases. The milestone for various activities under Phase-I was 27 months from the date of commencement and 42 months for phase-II activities.

The MOU, *inter alia* provided that under Phase-1, SAIL would incorporate a Special Purpose Company (SPC) and cause to initiate the process for de-notification of the Thakurani iron ore reserve in Orissa owned by it, with an estimated reserve of 75 MMT of iron ore, and transfer its Prospecting Licence in the name of the SPC to enable BHPB to carry out its prospecting. The SPC would be a joint venture with 50:50 shareholdings of SAIL and BHPB. The 50 *per cent* stake of BHPB in the SPC would be in exchange for SAIL's stake of equivalent value in BHPB's Maruwai Coal Resource, Indonesia (MCR).

Under Phase-II, the MOU provided that BHPB and SAIL would work together to identify and agree upon a major Indian iron ore reserve comprising around 700 MMT which should be the existing iron ore reserve at Chiria in Jharkhand or Rowghat in Chattisgarh or an iron ore deposit of similar size and quality. BHPB would again get 50 *per cent* ownership interest in such major iron ore reserve. In exchange, SAIL would get 20 *per cent* ownership interest in MCR having an estimated reserve of 100 MMT of coking coal. This 20 *per cent* ownership interest in MCR would be inclusive of SAIL's ownership interest under Phase-I.

It was, however, observed in Audit that the various parameters set out in the MOU were either not in the interest of the Company or were not on equal footing as under:

(i) Prospecting of Thakurani Reserve

The prospecting of Thakurani iron ore reserve would be carried out by BHPB, which would enable it to control the estimation of the total iron ore reserves and, thus, the valuation of Thakurani. There was no corresponding provisions in the MOU regarding the Company's role in the prospecting of MCR.

(ii) Sales

(a) Pre-determined quantities of iron ore (as would be mutually agreed upon between BHPB/ SPC and SAIL after taking into consideration the Company's requirements and project feasibility) would be sold to the SAIL on take or pay basis, which would make the Company liable to pay for the committed quantity even if it did not lift them during the stated period. In a cyclical industry like iron and steel, the 'take-or-pay' clause in the MOU ensured that the risks were transferred from the joint venture to the Company. By contrast, there were no such clauses protecting the Company's stake in MCR.

(b) BHPB would be appointed as Marketing Agent for third party sales of Thakurani iron ores whereas no such provisions existed in the MOU for the marketing rights of MCR coal by the Company.

(c) Sales of iron ore to the Company would be made at a price based on long term Indian domestic iron ore bench mark price, if available, or the benchmark export price or as agreed between BHPB and SAIL, unlike the existing transfer pricing. This would negate the advantage of low iron ore input prices.

(iii) Ownership of iron ore reserves/MCR

The ownership exchange between the two strategic partners was provided in the MOU without any cost benefit analysis. In exchange for 50 *per cent* ownership over the 775 MMT of iron ore reserves of the Company in India, the Company could get a maximum of 20 *per cent* ownership in the MCR of BHPB having an estimated reserve of 100 MMT of coking coal.

In the absence of any cost-benefit analysis by the Company, Audit worked out the financial implication on conservative basis by taking the price of coking coal at US$ 126 per MT (prevalent for 2005-06 delivery period and highest among the last three delivery periods) and iron ore at US$ 22 per MT (based on Ministry of Mines export price figures for 2003-04, which was lower than BHPB's own price in 2005-06). Based on the above benchmarks, BHPB's MCR was valued at US$ 12.6 billion against the Company's iron ore reserves covered by the MOU valuing US$ 17.05 billion. Thus, the estimates indicated that against the approximate overall value to be received by BHPB of US$ 8.53 billion, US$ 2.52 billion was to be received by SAIL over the life of the coking coal and iron ore reserves. The Management, thus, did not safeguard the financial interest of the Company while entering into the MOU.

(iv) Legal position of Iron ore Mines/MCR in their respective countries

In respect of the Indian iron reserves, the Company neither consulted nor informed the State Governments about the proposed transfer of leases to the joint venture involving a foreign party even though such transfers would require the approval of the concerned Governments. This was of special importance with respect to the Chiria iron ore deposit since out of the six leases, the Jharkhand State Government had refused to renew three expired leases. The Central Government, while overturning the rejection of two leases, on the revision applications made by IISCO, a subsidiary of the Company, highlighted IISCO's claim that the Company was sure to make full use of the mineral deposits in the leased area.

On the other hand, the MCR coking coal reserve was located in a protected forest area and the Company had not ascertained whether commercial open-cast mining of coking coal could be undertaken under the existing rule of the land. The Company also did not ascertain the quality of MCR coal to see whether it would meet the required specifications of the Company.

Thus, the Company signed an MOU, for a strategic partnership, for which it neither took into confidence the concerned State Governments nor ascertained the legal position of the properties in a foreign land. It also agreed to such provisions, which were heavily skewed in favour of the foreign party and were not in its financial interest.

The Management stated (August 2005) that:

(i) New reserves of iron ore were contemplated in the MOU; the size of these reserves as well as the quality of iron ore was not known either to SAIL or BHPB.

(ii) In respect of cost benefit analysis, the MOU envisaged valuation of iron ore reserves and MCR by an independent expert who would be appointed at the appropriate time.

(iii) The matter of obtaining approval from the State Governments requiring transfer of leases would be taken up at the appropriate time.

(iv) Company's due diligence would cover quality/quantity of coal and legal and regulatory framework in Indonesia and the stage of due diligence had not yet been reached.

(v) The MOU only provided the basic framework of the proposed strategic alliance and was not legally binding; at this stage only the broad parameters of understanding had been reached.

The reply of the Management is not tenable for the following reasons:

(i) the reference in the MOU to the independent expert is to independent review by an expert of the fairness of valuation, not to valuations themselves.

(ii) valuation of the reserves should have been done prior to entering into the strategic partnership to ascertain the financial impact so that an informed view could be taken,

(iii) the Company was aware of the estimated quantity of reserves of iron ore in India,

(iv) appropriate time for taking the steps mentioned at Sl. No. (iii) and (iv) of the Management reply was prior to signing the MOU so that the Company could enter into the strategic partnership with prior clarity on the issues.

(v) Though the MOU was not a legal binding agreement, the MOU would set the tone for negotiation and finalisation of the legally binding agreements, and it would be difficult to finalise agreements which were essentially different from the principles and parameters set forth in the MOU.

The matter was reported to the Ministry in October 2005; its reply was awaited (December 2005).

CHAPTER XXIII: MINISTRY OF TOURISM

India Tourism Development Corporation Limited

23.1.1 Loss of revenue on sale of air tickets due to deficiency in Debtors Control System

Failure of the Company to follow its own Credit Policy for recovery of debts coupled with ineffective recovery action resulted in accumulation of debtors of Rs.6.68 crore.

The Ashok Travel and Tours division of India Tourism Development Corporation Limited (Company) is engaged in the business of providing Air Tickets (national and international) to various Ministries/Government departments and private parties. On behalf of its clients, the Company purchases air tickets from Indian Airlines, Air India etc. and pays the cost of the same to the concerned Airlines on the due dates out of its own funds. The tickets sold to the private parties were on cash and carry basis whereas the authorised Government/PSU officials/delegates were extended 15 days' credit facility as per bills raised and thereafter an interest at 18 *per cent* per annum was leviable. Further if any department defaulted in payment regularly, the Company could stop the credit facility. The follow up of debtors was also regulated by giving first reminder after 30 days and thereafter reminders at every 15 days' interval. The Company could also file legal case as per the procedure prescribed after 75 days of the credit in case of defaulters.

Audit observed (February 2005) that an amount of Rs.6.68 crore (138 Government departments-Rs.6.18 crore, 18 PSUs-Rs.0.46 crore and two other parties-Rs. 0.04 crore) was outstanding as on 31 March 2005, out of which debts to the extent of Rs.3.24 crore were due for more than three years. Audit scrutiny of debtors revealed that the efforts to recover the debts as envisaged in their credit policy were not made by the Management and there was no system in place for debtors' control. The Ministry of Tourism was also not approached by the Company by furnishing all requisite details to assist in recovery of the dues as per Memorandum of Understanding with the Ministry. The credit facilities were not stopped by the Company in respect of 29 Government departments and one PSU even after default for more than three years. The Company did not even file any legal case.

Due to deficient recovery and poor follow up, the Company lost interest of Rs.2.62 crore on the outstanding amount calculated at 18 *per cent* with effect from 1 September 2000 as the break-up of outstanding before that date was not made available to Audit. Details of travel authorisation of Government departments amounting to Rs. one crore were not available with the Company as the bookings were stated to have been made over telephone/verbal requests from certain departments.

The Management initiated a proposal (August 2003) to write off the bad/irrecoverable debts amounting to Rs.1.58 crore which were more than five to 15 years old and made a provision of Rs.3.24 crore in the accounts for the year 2004-05 in respect of debts

outstanding for more than three years. The Company appointed (June 2004) a private agency viz. M/s. MALCHA International (Private) Limited for undertaking follow up work with the Ministries/ Government departments etc. for realising old outstanding dues but no dues could be recovered (July 2005).

While confirming the above factual position, the Management stated (April and June 2005) that letters were being issued to the concerned defaulters for charging the interest in cases where the dues were not received within the stipulated time. The responsibility on concerned officials could not be fixed as these officials extended credit facility to the Government departments on the proper authority given by the concerned department and it was the duty of the consumer department to pay the dues in time and suggestion of Audit had been noted for future compliance that letters be issued to the concerned Ministries/Government departments for charging interest in case payment was not received within the stipulated time.

The Ministry endorsed (September 2005) the reply furnished by the Management and further stated that most of the outstanding dues had become time barred and legal action at this stage could not be initiated.

The above replies confirmed that there was no system in place for timely recovery of debts. Thus, failure of the Company to follow its own Credit Policy for recovery of debts coupled with ineffective recovery action and weakness in internal control system resulted in accumulation of debtors.

23.1.2 Improper planning in construction of a new Hotel Project

The decision of the Company to take up the construction of a hotel at Chandigarh was not based on sound financial consideration resulting in loss of Rs.4.02 crore.

India Tourism Development Corporation Limited (Company) was allotted (June 1981) a plot of land measuring 2.91 acres in Chandigarh on 99 years' lease. The lease rent of the land was Rs.3.28 lakh per annum and a one time premium of Rs.36.58 lakh was charged. The Company kept the land idle for over 10 years though as per the Punjab Capital (Development and Registration) Building Rule, 1952, the construction of building was to be completed within three years of the auction. The Chandigarh Administration cancelled the allotment of land (October 1994), which was restored back to the Company (March 1996).

In June 1996, the Company approved the construction of a five Star Hotel consisting of two single storey blocks and one seven storey block with 130 guest rooms on the said plot of land at an estimated cost of Rs.33.95 crore which was to be met through internal resources of the Company. However, as per the construction plans approved (June 1998) by Chandigarh Administration, the shell structure for all 130 rooms was to be constructed and 100 rooms were to be furnished in the first phase. The contract was accordingly awarded (March 1999) to the lowest tenderer for Rs.17.76 crore to be completed in 18 months from the date of handing over of site to the contractor (April 1999).

In view of its financial position, the Company decided to stop the construction (December 2000) after completion of the structural work upto sixth floor as it was not

possible to continue to finance the hotel project from the internal resources. The Company could not also obtain funds from the Ministry. An expenditure of Rs.8.64 crore was incurred till such time. The Company then decided to sell the hotel project at the incomplete structure stage (September 2001) and forwarded the proposal for its disinvestment to the Ministry of Disinvestment through the Department of Tourism. The hotel was sold for Rs.17.27 crore in July 2002. As per the formula approved by the Cabinet Committee on Disinvestment, the entire unearned increase in the value of land accrued to the Chandigarh Administration and the balance bid amount accrued to the Company. Accordingly the sale proceeds were apportioned between Chandigarh Administration (Rs.12.65 crore) and the Company (Rs.4.62 crore).

It was observed in Audit that during the period from June 1996 (when the Company decided to construct with internal resources) to April 1999 (when construction actually commenced), the Company's profit had declined from Rs.54.72 crore in 1997-98 to Rs.12.02 crore in 1998-99. Moreover, no consideration was given to the Report of the Disinvestment Commission published in 1997, which had recommended privatisation of the Company hotels. Thus, the decision of the Management to take up (April 1999) the construction of the hotel at a time when the disinvestment policy for its hotels was known to it and the profits had declined was not based on sound financial considerations and resulted in a loss to the extent of Rs.4.02 crore (March 2005) with contingent liability amounting to Rs.12.55 crore.

The Management while confirming the facts stated (April 2004) that the Government accepted the recommendations of Disinvestment Commission in 1999 and the global advisors were appointed in July 2000. Thus, it was only in the middle of the year 2000 that Government's decision to disinvest the Company hotels became clear. Further, the Chandigarh project was not included in the 26 hotel properties to be disinvested and it was disinvested at the request of the Company.

The Ministry stated (November 2005) that the policy on disinvestment was implemented subsequently in 1999 with retrospective effect from the year 1997 and hence the decision taken by the Board of Directors in 1996 to construct the hotel in question, was in consonance with the situation prevailing at that point of time. The decline in profitability of the Company could also not be foreseen during this period, as the losses were incurred in the following years due to external factors.

The replies of the Management and Ministry are not tenable as at the time of awarding the construction work (March 1999), the Company's financial position was deteriorating and the Company did not consider the decline in profitability or its own internal resources before embarking upon the new construction. Thus, due to lack of planning in funding the project, it had to sell the incomplete structure and incurred a loss of Rs.4.02 crore with contingent liability of Rs.12.55 crore.

23.1.3 Avoidable expenditure on electricity charges

The Company's failure to convert its LT service connection into HT service connection in one of its hotels resulted in avoidable expenditure of Rs.69.53 lakh.

Hotel Samrat owned by India Tourism Development Corporation Limited (Company) was provided (1982) Low Tension (LT) electricity service connection by New Delhi Municipal Corporation (NDMC). As per the NDMC tariff structure, consumers of LT connection with connected load exceeding 100 KW were chargeable at High Tension (HT) tariff rates, besides an additional levy of 10 *per cent* surcharge on the total billed amount. Since Hotel Samrat had a connected load beyond 100 KW, NDMC collected electricity charges from the hotel at HT rates and 10 *per cent* surcharge on the total billed amount additionally because of its LT service connection.

In March 2000, NDMC took a policy decision that existing LT service consumers with a connected load of 100 KW or more could convert their existing service connections into HT. The Company applied to the NDMC (February 2001) to convert the LT service connection of Hotel Samrat into HT service connection. The Company could have saved payment of 10 *per cent* surcharge by this conversion. However, it failed to follow it up with the NDMC which resulted in avoidable payment of electricity surcharge amounting to Rs.1.35 crore (July 2000 to September 2005).

The Management stated (August 2005) that the Company had requested NDMC for switching over from LT to HT electricity service connection and were following up with the NDMC authorities for change over. The Ministry endorsed the reply of the Management (September 2005).

Thus, the absence of effective pursuasion by the Management with NDMC to convert the connection from LT to HT resulted in avoidable expenditure of Rs.69.53 lakh[♣] from July 2000 to September 2005 towards surcharge and the issue remained unresolved even after a period of five years.

♣ *excluding Rs.65.26 lakh which otherwise was required to be incurred on annual maintenance of transformer*

CHAPTER XXIV: MINISTRY OF URBAN AFFAIRS AND POVERTY ALLEVIATION

Housing and Urban Development Corporation Limited

24.1.1 Avoidable expenditure due to not retaining call option in bonds issue

The Company did not retain a call option in its infrastructure bonds issue, in spite of expert advice. Accordingly, the Company had to service the high interest borrowings in an era of falling interest rates, which resulted in an avoidable interest expenditure of Rs.48.98 crore.

Housing and Urban Development Corporation Limited (Company) offered (March 1997) 'Infrastructure Bonds' carrying tax benefits under the Income Tax Act for public subscription aggregating Rs.200 crore with a right to retain excess subscription upto Rs.50 crore. The bonds carried an interest of 15 *per cent* per annum and were redeemable on expiry of 10 years from the date of allotment. The bonds were oversubscribed and the Company retained (April 1997) Rs.250.11 crore as per terms of the bonds issue.

It was observed that while recommending the various features of the bonds issue, the lead manager to the issue (M/s. SBI Capital Markets Limited) had suggested, *inter alia*, to include a 'put and call option' in the bonds issue. While 'put option' extends right in favour of bondholders to exit after certain years, 'call option' bestows a right on the Company to redeem the bonds before the date of maturity to take advantage of any fall in the interest rates.

The Company, however, did not retain the 'call option' to be exercisable after certain years (say five years), but included the 'put option' in the terms of the bonds. By not retaining the 'call option' in an era of economic liberalisation, the Company had to pay 15 *per cent* interest to the bondholders, though the incremental borrowing cost after five years of issue of bonds came down to 9.98 *per cent* by 2001-02. The high interest obligation would continue till the maturity of the bonds in April 2007.

The Management/Ministry stated (May/July 2005) that the object of the bond issue was mobilisation of funds for financing infrastructure projects which required long-term resources, whereas inserting a call option would have reduced the tenure of bonds to five years. They added that the requirements and peculiarity of the Company's operations were perhaps not fully appreciated by the lead manager and at a time when the interest rates had been on a rising trends, it could not be assumed that the interest rate would fall in future.

The reply is not tenable as the Company allowed 'put option' to the bondholders giving them the right to redeem the bonds before the maturity date, while restricting itself to the full tenure of the bonds. Further, the lead manager, being a reputed firm, had handled various bonds issues successfully and was well aware of the tenure for which the loans

were to be mobilised. Besides, protecting the Company against high interest costs was as much a priority as ensuring success of the issue.

Thus, the Company had to service the high interest borrowings in an era of falling interest rates due to not retaining the call option in the bonds issue despite the advice of expert. As a result, the Company incurred avoidable interest expenditure of Rs.30.46 crore[♣] from April 2002 to October 2005 and would further incur expenditure of Rs.18.52 crore till the maturity of the bonds in April 2007.

24.1.2 Avoidable interest liability due to acceptance of oversubscription at higher rates of interest

The Company did not consider the downward trend of interest rates and accepted oversubscription of Rs.137.51 crore at higher rates of interest. Consequently, it incurred extra expenditure of Rs.13.29 crore till October 2005 and committed future liability of Rs.17.37 crore towards interest over the remaining tenure of bonds.

Housing and Urban Development Corporation Limited (Company) floated (June 2001) bonds issue ('XX' series) for Rs.500.00 crore under book building method with an option to retain excess subscription. As per the offer document, bidders for the bonds had to indicate the rate of interest from the given range of 10.15 to 11.25 *per cent*, the corresponding amount to be subscribed and the tenure of bonds:

The Company received a total subscription of Rs.835.66 crore. Against this, the Company retained (July 2001) Rs.637.51 crore[•] at rates ranging between 10.30 and 11.15 *per cent* as suggested by UTI Bank, the sole arranger appointed by the Company for raising these bonds. Accordingly, an oversubscription of Rs.137.51 crore was accepted by the Company.

It was observed that the Company accepted the amount of Rs.637.51 crore without carrying out any analysis with reference to future inflows and outflows of funds. In fact, in view of the softening trend in interest rates due to steady reduction in Cash Reserve Ratio as well as Bank Rate by Reserve Bank of India and no immediate requirement of funds, the Company could have restricted the subscription amount to Rs.502.16 crore matching the issue size of Rs.500.00 crore and raised the balance amount of Rs.135.35 crore through alternate means which were available at lower interest rates subsequently (viz. short term and medium term borrowings, roll over arrangement with the bankers etc.). By this way, it could have saved Rs.30.66 crore over period of 10 years, based on the rate of 10 *per cent* at which bonds were raised subsequently in March 2002.

The Management/Ministry stated (June/September 2004) that in the falling interest rate regime the subsequent issue was always at a lower rate but the financing organisations kept on borrowing from the market which was need-based. They added that the Company

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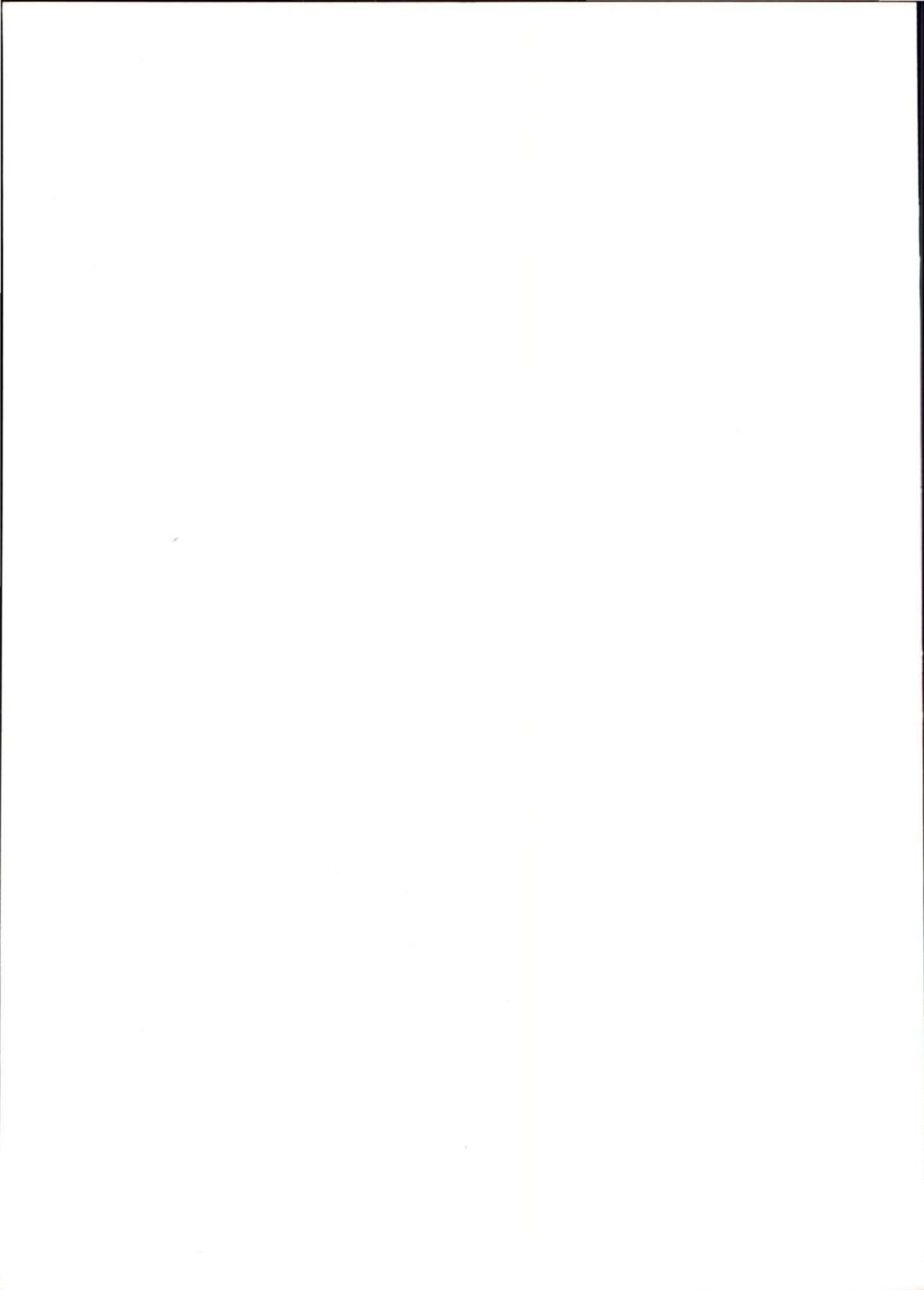
[♣] ***Calculated at a rate of 5.02 per cent (15 September 1998) and after taking in to account expenditure of Rs.13.13 crore likely to be incurred on raising funds, like arranger fee, brokerage etc.***

[•] ***Rs.166.65 crore for five years, Rs.26.80 crore for seven years and Rs.444.06 crore for 10 years***

decided to retain Rs.637.51 crore as the requirement of funds was for project releases especially long term funds of more than seven years.

The reply is not tenable since in the falling interest rate regime, as accepted by the Ministry, the Company should have adopted appropriate strategy to reduce the cost of borrowings within the various available modes of borrowing. Further, the Company had not prepared any cash flow statement or age-wise distribution of the loans, in the absence of which, neither the requirement of funds for long-term lending, nor justification for retaining the oversubscription of Rs.137.50 crore could be established.

Thus, by accepting oversubscription at higher rates of interest ignoring the downward trend of interest rates and not adopting alternative means of financing, the Company incurred extra expenditure of Rs.13.29 crore till October 2005 and committed future liability of Rs.17.37 crore on account of higher rate of interest over the remaining tenure of bonds.



SECTION II
IT AUDITS

CHAPTER XXV: MINISTRY OF FINANCE

Insurance Division

National Insurance Company Limited

25.1 Report on the General Insurance System Software

Highlights

Liquidated damages of Rs.17.32 lakh were short deducted.

(Para 25.1.5.1)

To assume risk from back date a facility, named Scroll, has been provided in General Insurance System (GENISYS). In 83 cases at Divisions –VII, IX and XI Kolkata–accidents occurred before accounting of cheques and generation of policies.

(Para 25.1.5.2)

Under GENISYS, books are allowed to be kept open up to seven days after transactions. As a result, back date entries in the Cash book can be made and policies with back date can also be generated. Scrutiny of the Inward Remittance Register of Division-XI, Kolkata and cross check with the System revealed that some of the cheques, entered in the Register, were not accounted for in GENISYS and no policy was issued against such cheques.

(Para 25.1.5.2)

In some cases effecting change in recovery of service tax at higher rate was delayed and the difference in collection amounted to Rs.1.24 crore up to 31 May 2003. Further, circulars modifying rates, conditions etc. were not incorporated in the system in time.

(Para 25.1.5.3)

There was no check, either manually or through computer system to see whether all the Cover Notes were accounted for and policies issued. In five cases, premium was collected through Cover Note but no corresponding policies were issued.

(Para 25.1.5.4)

25.1.1 Introduction

National Insurance Company Limited (Company) is engaged in general insurance business and had 24 Regional offices, 304 Divisional offices and 635 Branch offices as on 31 March 2005. The Board of Directors of the Company approved (December 2000) a proposal for procurement and implementation of the front office software 'General Insurance System' (GENISYS), from CMC Limited (CMC) at a cost of Rs.164.50 crore for implementation in 943 offices with interconnectivity.

The software runs on client server architecture in Local Area Network (LAN) set up, for which all the operating offices have been provided with -

(i) Pentium based system with Windows 2000 operating system for server and clients as hardware platform and,

(ii) Oracle database at back end and Developer 2000 at front end as Relational Data Base Management System (RDBMS) platform.

GENISYS facilitates processing of underwriting, claims, preparation of accounts and generation of reports and queries.

25.1.2 Scope of Audit

The scope of audit included examination of effectiveness of GENISYS in computerisation of various activities of the company through test check of records at Management Service Department (MSD) and analysis of data besides review of general and application control checks and data integrity.

25.1.3 Audit Objectives

The broad objectives of audit were:

(i) To review the procurement of Hardware and Software system.

(ii) To check the effectiveness of controls in the system.

(iii) To check the security controls in the system.

25.1.4 Audit Methodology

(i) Study and analysis of the files of Management Service Department at Head Quarters of the Company.

(ii) Testing of control checks of the system by using dummy data.

(iii) Analysis of offsite data pertaining to three Divisional Offices and two Branch Offices through Utility software prepared by the Management based on SQL queries framed by the CMC on the basis of specific requirement of audit. The Read Only report, thus generated, was password- protected by Management. This was, thereafter, copied in a separate Excel sheet for further analysis. Findings in

respect of a few selected cases were verified with on line data of respective operating offices and were followed by verification of relevant physical records.

25.1.5 Audit Findings

25.1.5.1 Review of Purchase orders

Non-recovery of liquidated damages of Rs.17.32 lakh

The GENISYS software was procured from M/s. COMPAQ. Terms of the purchase order provided (May 2001) that if the supplier failed to install any or all of the goods at the respective destinations within the time limits specified in the order, the company would deduct liquidated damages (LD) from the contract price. According to clause 39(b), in case the delivered goods and/or services could not be put to use without the undelivered parts or services, the damages would be calculated considering the total price of the component.

It was noticed that in respect of 106 offices under four Regional Offices, delivery of switches was delayed for periods ranging from two to 409 days. As a result, total components like LAN, Servers and Nodes could not be put to use and GENISYS was also not implemented in time. However, LD was recovered only in respect of value of undelivered goods/services instead of value of total components.

Thus, LD of Rs.17.32 lakh was not recovered.

The Management stated that the system delivered and installed could always be put to use on a standalone basis and this should not be linked to the performance of the vendor. Therefore, LD had been charged correctly.

The reply of the Management is not acceptable as the order on M/s. COMPAQ was placed for supply, installation and maintenance of hardware for Local Area Networking of the Company's offices. The part delivery of goods did not serve the purpose since GENISYS, essentially based on a networked system, can not run in isolation on standalone basis. Therefore, full value of the components (even if part of the hardware was delivered) should have been taken into account for the purpose of calculation of LD as per terms of the order.

25.1.5.2 Review of GENISYS System

Inadequate control mechanism in GENISYS application

While reviewing the control mechanism provided in the software, it was found that adequate control checks were not provided in the following areas.

Scroll Entry

According to Section 64VB of the Insurance Act, 1938, no risk can be assumed from a date earlier than a date on which the premium has been received in cash/cheque. In case, the premium is collected by Agent, it is required to be deposited within 24 hours of collection. In case the premium is received by post, the date of post will be reckoned as

date of receipt. To assume risk from back date, a facility, named 'Scroll', has been provided in GENISYS. The issuance of policy through Scroll from back date is fraught with the risk of any of the following misuses:

(i) The premium may be accounted for only after the claim becomes due.

(ii) If there is no claim, the cheque may be returned to the party causing loss of business to the company.

(iii) The cheque may be held if money is not available in the party's account.

Detailed scrutiny of records revealed the following irregularities under the above three situations.

Premiums accounted for after receipt of claims

In 69 cases at Division –XI, Kolkata, accidents occurred before accounting of premium and generation of policy. It was seen that in these cases cheques and cash were held for periods of one day to 164 days. Underwriting and claim files of 69 cases were requisitioned, of which only 13 claim files were produced to Audit and no underwriting file was made available. Audit observed that out of 13 claims

(i) nine cases relating to mediclaim policy were settled through Third Party Administrator (TPA). In the absence of detailed documents regarding settlement of these cases, no further audit observation could be made;

(ii) three cases related to Motor Policy, out of which in two cases there was no record to show that premium cheques were received before occurrence of accident;

(iii) in one case, Marine Cargo Specific Transit Policy was issued after expiry of the risk period, though cheque was received beforehand. The cheque was kept in hand without any entry in the system. The same was accounted for only after the accident occurred.

At Division –VII and IX, Kolkata, in seven cases each, policies were issued through Scroll where accidents occurred before accounting of premium and generation of policy.

In the absence of related files regarding claims and underwriting, circumstances under which policies were generated in these Divisions after the occurrence of the accident, could not be ascertained. It, however, further indicated a lack of validation control.

Return of cheques

On a test check of entries in the Inward Remittance Register (IRR)♠ of Division-XI with those in the System, it was seen that some of the cheques entered in the Register, were

♠ ***This is a manual register to record incoming premium, in cheque, pending generation of policy and recording in cash book. However, this has been dispensed with in most of the operating offices after introduction of GENISYS.***

not accounted for and no policy was issued against such cheques. Following four such cases relating to the year 2003, 2004 and 2005 were noticed:

IRR No.	Date/Time	Name	Cheque No and Date	Bank Name	Amount (Rs.)	Department
3536	11/08/2003 3.30 PM	Ransal India Private. Limited	442599 11/08/2003	Bank of Maharastra	1,695	Marine
3958	27/08/2003 0.55 PM	Kamrup Tea	492277 27/08/2003	Federal Bank Ltd	6,385	Marine
7106	23/11/2004 5.25 PM	Zenith Exports Ltd	361420 23/11/2004	Canara Bank Overseas	1,170	Marine
4019	27/07/2005 5.25 PM	Ajoy Automobiles	688252 27/07/2005	Bank of India	4,423	Motor (struck out)

It was observed that the above cheques were not deposited in the banks. The ultimate fate of these cheques could not be ascertained as the relevant documents were not produced to audit. It was also seen that many entries of the IRR were struck out without giving any remarks and authorisation.

Retention of cheques

It was seen that at Division-XI, Kolkata, in 20488 cases, cheques and cash were held for periods ranging from one day to 343 days. In 41 cases, where cash was received, there was a delay of three to 15 days in deposit of cash of Rs.0.40 lakh. In 111 cases, cheque dates were later than the Scroll date. Thus, there was no validation control between Scroll date and cheque date.

Assuming risk before receipt of premium violates provisions of 64VB of the Insurance Act 1938. Further, the system of issue of policy after occurrence of accident violates the basic rules of financial propriety.

At Division –VII, Kolkata, in 194 cases, cash was held for periods ranging from one day to 123 days and in 1,922 cases cheques were held for periods ranging from one day to 111 days. Delayed deposit of cheques resulted in unnecessary coverage of risk, in case cheques were dishonoured subsequently.

Opening of books

It was noticed that Under GENISYS, Books were allowed to be kept open up to seven days after the date of transaction in Division VII, IX, XI Kolkata and, Street Branch Bentinck, and MG Road Branch, Kolkata. This is fraught with risk as back dated entries in the Cash book can be made and policies with back date can also be generated.

When a separate facility of Scroll entry for generating policy with the date effective from an earlier date exists, system should ensure daily closing of Cash book to avoid manipulations.

Deficiencies in the system regarding Fire Policy

(i) Silent Risk

According to All India Fire Tariff (AIFT), in case of risk becoming 'Silent'♠, it shall not be entitled to any discounts. However, on a test check through dummy data, it was noticed that policy was generated allowing 15 *per cent* claim experience discount and 10 *per cent* Fire Extinguishing Appliances (FEA) discount for risk that fell in the category of 'Silent' risk.

The Management accepted the Audit observation and also stated that suitable rectification would be made in GENISYS.

(ii) Ratings

In GENISYS the 'Risk Code Menu' of the underwriting module, does not display description of all types of risks prescribed in the tariff. It was observed in Audit that the option to select storage risks outside the compound of industrial/manufacturing units was not available. Further, in the menu the system did not incorporate the list of hazardous goods issued by Tariff Advisory Committee (TAC). Thus, the user had to manually consult the tariff chart to identify the risk code applicable.

The Management stated that 'Risk Code Menu' against utilities located outside industrial and manufacturing risk was available in GENISYS. The Management's reply is not correct as on verification it was seen that 'Risk Code Menu' does not show the description of property. Thus, there is a chance of wrong classification and charging of wrong premium by the user.

Failure to cancel motor policies in respect of Cash Loss/Total Loss

In case vehicle is totally damaged/or when the net cost of repair is almost close to the Market Value or the Insured Estimated Value (IEV) or the vehicle is stolen, the claim can be considered as a Total Loss. If loss is extensive but does not warrant consideration of the claim on 'Total Loss' basis, claim can be settled on 'Cash Loss' basis. According to 'Claims Settlement Manual' of the Company, in these cases the policy should be cancelled and Regional Transport Office (RTO) should be informed by registered post about the cancellation of the policy in such cases.

It was seen that the GENISYS software did not have appropriate validation controls to ensure cancellation of the policy after settling such claims. On analysis of the data it was observed that in three cases of Division-VII, eighteen cases of Division-XI, two cases of Bentinck Street Branch, and four cases of MG Road Branch, Kolkata, claims were settled on 'Total Loss' basis but the policies were not cancelled leaving scope for further claim under the policy.

♠when a factory remains closed for a period more than 30 days

Mediclaim policy

In case of Mediclaim insurance policy, if there is any gap in renewal of policy, cumulative bonus can not be allowed unless it is approved by the competent authority. However, the GENISYS system allows cumulative bonus on renewal of insurance policy even though there is a gap in renewal and there is no approval of competent authority. In MG Road Branch, Kolkata, 25 Mediclaim policies were issued where there was a break in continuity. In test check of two of these cases, it was seen that cumulative bonus was allowed despite absence of approval of competent authority in the absence of appropriate validation check.

25.1.5.3 Delay in giving effect to modifications in the software

It was noticed from records that the Company launched new products without any provision in the GENISYS to underwrite the same.

The Management stated that there was some time gap between introduction of a product and incorporation of relevant module in the software.

Necessary provisions should have been incorporated in the GENISYS before launching the product.

As per the agreement entered with CMC, for making changes in the system at global level, patches/versions are prepared by CMC. This patch/version is thereafter sent to all operating offices to run and update the system.

The Government revised service tax from five to eight *per cent* on 14 May 2003. However, GENISYS version (5.9.1.2) for enhancing service tax was released by CMC on 19 May 2003.

On a test check of records it was noticed that there was delay in implementation and recovery of service tax at higher rate, which in some cases was delayed till 31 May 2003 and the difference in collection amounted to Rs.1.24 crore.

The Management stated that delay was due to failure of the operating offices in loading the patch in time. They also stated that there was no loss to the exchequer as service tax paid to service provider like Bharat Sanchar Nigam Limited could be set off against the collection of service tax on the insurance premium. The Management also stated that the differential Service Tax was collected and kept in excess premium account to be adjusted subsequently.

The reply is not tenable as the fact remains that there was a loss to the Company due to delay in communication and implementation of revision of service tax patch by the Company. The short collection of Rs.1.24 crore was arrived at after considering subsequent differential collections.

The Management of Bentinck Street Branch stated (December 2005) that excess commission paid due to delayed implementation of changes in GENISYS was adjusted/recovered subsequently.

Circulars modifying rates, conditions, etc. not incorporated in the system in time

With effect from August 2003, the agency commission on motor business was revised, and as a result, no commission was payable on Third Party (TP) portion of package policies irrespective of the insured category. It was, however, noticed that the system allowed agency commission on total amount of premium. The system, thus, lacked control in this regard. In Bentinck Street Branch, Kolkata and in M.G Road Branch, Kolkata, excess commission of Rs.0.61 lakh had been paid.

As per TAC direction, if claim experience ratio was more than 100 *per cent*, in case of Fire Policy, the matter was to be referred to TAC. This provision was changed with effect from 16 April 2004 and loading of slabs was introduced even in cases where claim experience was more than 100 *per cent*. On a test check with dummy data, claim experience was entered as 600 *per cent* and system did not impose any loading even though as per tariff 100 *per cent* loading was to be imposed. Therefore, this vital change was not incorporated in the system.

The Management accepted (March 2005) the audit observation.

TAC issued directions from time to time regarding tariff. On a test check it was found that the guidelines contained in the following circulars were not incorporated in the system.

(i) Circular dated 25 March 2004 regarding voluntary Deductibles regarding Act of God.

(ii) Circulars dated 31 March 2005 regarding clarification on risk code and rate code, clarification regarding tariff item namely "Dwelling, places of worships.........." and refund on cancellation of long term policy.

(iii) Company's guidelines issued on 13 March 2003 regarding prohibiting commission from second year in respect of package policy on commercial vehicle other than tractor.

25.1.5.4 Audit through GENISYS

Audit through Genisys revealed the following cases where mistakes occurred due to users' fault.

Cover Note

Cover Note is a vital document committing the Company to undertake the insurance of the risk. This is considered as a temporary policy. The Cover Notes are to be issued only when full particulars of insurance are gathered and the premium is calculated. Therefore, a close control is required to minimise the chance of fraud through misuse of the Cover Notes. Though there is a provision to enter Cover Note number in the system, it was not followed many times. As a result the register of Cover Notes, generated by the system, remained incomplete and effective control over the utilisation of Cover Notes could not be exercised.

On a test check of some Cover Notes issued by the agents of Division –XI, Kolkata, through the system, it was seen that in the following four cases premium was collected through Cover Note but no corresponding policies were issued.

Sl. no.	Cover note no.	Book no.	Amount (Rs.)	Name of the insured	Risk start date	Development officer/agent code
1	214888	8596	3,580	A.Keay Power Foods (P) Ltd.	28/08/2003	-DO-
2	401840	16074	7,515	Zulfikar Alam	17/08/2004	-DO-
3	214891	8596	847	Animesh Kr. Saha	28/08/2003	-DO-
4	401421	16057	1,567	Ganesh Mondal	06/12/2004	01075

It was further noticed that money collected by the agents in the above cases was not deposited with the Company and, at the same time, there was also no record that the above cover notes were cancelled subsequently.

Issue of policy in favour of National Insurance Company Limited

On data analysis of MG Road Branch, Kolkata, it was seen that a policy was issued in the name of the Company under which one TP claim and one Own Damage claim was settled TP was settled for an amount of Rs.31.12 lakh and the Own Damage claim was settled for Rs.0.89 lakh. On discussion, the Management stated that this dummy policy was generated to adjust the entire TP claim paid by the Divisional office on behalf of Branch office but regarding Own damage claim there was no explanation. However, no record was produced to Audit in favour of the arguments.

The Company may consider any other adjustment module for the purpose since a Company can not insure its own property with itself.

25.1.6 Conclusion

There was lack of control in the system to combat the following situations:

(i) risk was covered before receiving premium in violation of section 64VB of the Insurance Act 1938,

(ii) cash book remained open up to seven consecutive days with consequent risk of manipulation,

(iii) guidelines issued by the TAC and the HO of the Company were not incorporated,

(iv) agents collected money through cover note but did not deposit with the Company and data validation of scroll date with cheque date was absent.

25.1.7 Recommendation

(i) Business process should be re-engineered to ensure that Scroll entries and Cash book entries are made simultaneously on receipt of premium in the shape of either cheque or cash. Separate facilities may be provided to take care of situation where premium is collected by agent or by post.

(ii) The system should restrict any violaion of Section 64 VB of Insurance Act, 1938 which prohibits assuming risk before receipt of premium.

(iii) Periodical report on exception to the above should be generated and sent to Regional Office for investigation/reconciliation

(iv) Provisions contained in the tariff and changes made from time to time may be incorporated in the system instantly through a prompt change management system to avoid any financial loss (es).

(v) Adequate validation controls should be imposed to ensure that data received for processing was correct, complete, and without duplication.

(vi) Provision regarding keeping daily accounts open for seven days from the date of transaction may be reviewed and daily closing of Cash book may be ensured.

The matter was reported to the Ministry in December 2005; its reply was awaited.

CHAPTER XXVI: MINISTRY OF POWER

National Hydroelectric Power Corporation Limited

26.1 Taxability of perquisites

The Company was treating three taxable perquisites as non-taxable in contravention of the provisions of the Income Tax Act. On being pointed out by Audit, these perquisites were categorised as taxable income with effect from the financial year 2004-05, thereby avoiding recurring loss to the exchequer.

National Hydroelectric Power Corporation Limited (Company) developed a software system for calculating the income tax payable by employees as per the Income Tax Act. The system was designed with a flexible code structure so that any new rule related to income tax could be incorporated/deleted from the system without involving any change in the program or database. All the components of the salary of the individual employee were categorised as 'Earnings' or 'Deductions'. For the purpose of income tax calculation, these components were defined into three categories, viz. Taxable, Non-taxable and Rebatable.

While reviewing the database at Corporate Office of the Company, it was observed in Audit, as detailed below, that three perquisites, viz. lease maintenance, leave travel concession (LTC) and conveyance allowance, allowed to the employees were being treated as non-taxable in contravention of the provisions of the Income Tax Act:

(i) Employees availing the facility of leased accommodation were entitled to an amount equivalent to two months' rent per year for repair and maintenance of the house property on self-certification basis. While reviewing the system it was observed that the Company was treating this amount as non-taxable in the hands of employees.

(ii) The Company introduced (December 2000) LTC scheme under which the employees were allowed LTC for distance of upto 1,400 kilometres on the basis of self-certification. Though the amount payable under this scheme was taxable in the hands of employees, the same was categorised as non-taxable.

(iii) As per the Central Board of Direct Taxes (CBDT)'s circular dated 25 September 2001, the sum paid/various facilities provided by the employer to employees, over and above the prescribed limit, are treated as perquisites and are taxable in the hands of the employee. Regarding use of motor car, the circular provides that where an employee owns a motor car and the running expenditure is met or reimbursed by the employer and such reimbursement is for the use of the vehicle partly for official purpose and partly for personal purpose of the employee then the sum paid in excess of the limits specified in the circular would be treated as perquisites for the purpose of levy of income tax. It was seen that the entire conveyance allowance paid to employees was treated as non-taxable without

complying with the conditions stipulated by CBDT, such as maintaining user details in the form of log book, odometer reading etc.

On being pointed out in Audit, the Company revised (December 2004) the taxability of these perquisites by categorising the same as taxable income with effect from the financial year 2004-05, after taking the opinion of tax consultants.

The Management replied (May 2005) that the Company had recalculated the tax liability of the employees of the Corporate Office after re-categorisation of the three items. The difference between the tax liability before and after changing the taxability status of these three items was Rs.80.08 lakh (approximately) for the financial year 2004-05, which was deducted from the salaries of the employees (January to March 2005). Position regarding deduction of differential amount of tax in respect of other units of the Company was awaited.

Thus, by rectifying the category of perquisites at the instance of the Audit, recurring loss to the exchequer was avoided.

The matter was reported to the Ministry in December 2005; its reply was awaited.

CHAPTER XXVII: MINISTRY OF ROAD TRANSPORT AND HIGHWAYS

National Highways Authority of India

27.1 Assessment of Information Technology under Cobit Framework

Highlights

The Authority did not prepare a structured Information Technology plan.

(Para 27.1.5.1)

There was lack of planning and coordinated approach in the three major software applications leading to duplication of efforts.

(Para 27.1.5.2)

Since major software applications were developed against World Bank loan release commitments, there was little scope for the Authority to undertake cost benefit analysis.

(Para 27.1.5.3)

Expenditure of Rs.5.07 crore (Rs.2.07 crore and US$ 0.66 million[♣] equivalent to Rs.3.00 crore was rendered wasteful in development of technical assistance for 'operation and development of pilot corridor management units' as the system did not lend itself to integration with Road Information system and also because the database was to be eventually hosted on the servers located in a foreign country.

(Para 27.1.6.2)

27.1.1 Introduction

National Highways Authority of India (Authority) is a statutory authority established by the National Highways Authority of India Act, 1988 for the development and maintenance of National Highways. The main activities of the Authority are to:

(i) Upgrade and broaden existing National Highways corridors connecting the four metros of Delhi, Mumbai, Chennai and Kolkata of the country forming the Golden Quadrilateral (GQ) and Srinagar to Kanyakumari and Silchar to Porbandar that form North South East West (NSEW) corridor.

(ii) Undertake other highway projects such as connectivity to ports development of bypasses, etc.

[♣] *One US$ = Rs.45.61*

(iii) Implement externally aided road projects.

(iv) Improve, maintain and augment the existing national highways network including ensuring road safety measures and environmental management.

(v) Collect toll tax on highways on behalf of Government.

In 1995 the Government of India entrusted to the Authority the responsibility of implementing the externally aided projects of length around 333 kms. Later the Authority was entrusted the responsibility of upgrading and four laning of the following length of national highways:

(i)	NHDP Phase I (December 2000)	7,498 kms
(ii)	NHDP Phase II (December 2003)	6,736 kms
(iii)	NHDP Phase III (December 2004)	10,417 kms
Total	-	**24,651 kms**

27.1.2 Organisational set up of Information Technology and Planning Division

The Authority has Information Technology and Planning Division to look after development, procurement and customisation of IT systems/ solutions for office automation, computer based project monitoring and planning of the works. The Division functions under the directions of a Chief General Manager (CGM) who in turn reports to Member (Administration).

27.1.3 Audit objective and scope

The Audit of Information Technology focused on key information systems supporting the operations of the Authority *viz.* Project Financial Management System, Road Information System for planning and management of highways and high quality data collection for corridor management and toll collection.

The objective of Audit was to assess the extent to which information needs of the Authority under Information Technology had been aligned with its business objectives/ needs, IT related risks, existence of a regulatory environment to ensure strict control over information assets and value for money spent in the creation of information systems.

27.1.4 Audit Methodology

The Audit was conducted with reference to the benchmarked international standards for good IT governance – COBIT (Control Objectives for Information and Related Technology) which was used for assessing key aspects of Authority's systems.

The Audit was performed by walking through the systems of the Authority and study of the documentations and records available at the headquarters office of the Authority.

27.1.5 IT planning and organisation

27.1.5.1 A good IT planning and organisation set up assures the existence of sound control practices so that the information requirement necessary to achieve corporate objectives is achieved.

However the Authority did not follow an approach of preparing a structured IT plan which involved adoption of a methodology to formulate and modify plans. Though the Authority was set up in June 1989 and had an IT division within the organisation, it was yet to formulate an IT plan/ initiatives to support the organisation's mission and goals.

The Management stated (October 2005) that it had engaged a Consultant (M/s. Price Waterhouse Coopers) in June 2002 for studying the Authority's requirements and formulating plans for institutional strengthening of which Information systems, planning and communications formed a major part. It further stated that the Consultant did an extensive review of the existing IT systems of the Authority and formulated phased implementation plan comprising different functions such as office automation, executive functions, technical functions against immediate/ short term/ long term implementation by the Authority.

Though the draft report was available in 2003, neither the final report was available nor the acceptance of the same was available on record. The Authority also could not inform Audit of the initiatives taken by it after the Consultants submitted the report for institutional strengthening relating to information technology/ information systems.

27.1.5.2 The existing capacity planning of IT resources was either on the basis of *ad-hoc* requirement sought by the user division or at the instance of term lending institutions which insisted on creation of such IT facilities. The formulation of Project Finance Management System (PFMS) and Road Information System (RIS) were at the instance of the term lending institution - World Bank. The Electronic Drawing Management System, Payroll Accounting, Geographical Information system based Road Management and Construction System, Computerised Project Information system (CPIS) etc. were envisaged by the user divisions of the Authority.

Audit observed that there was lack of planning and co-ordinated approach in the following three major software applications being developed in the Authority, due to which same data was collected repeatedly during the development of the applications.

S. No.	Name of application	Area of computerisation
1.	Road Information System (RIS)	Collection and storage of highway related data
2.	Project Financial Management System (PFMS)	Financial Management
3.	GIS based Road Management System (GIS)	Road management system

The Authority's reply (October 2005) that the initiatives taken by it under various projects on strengthening the information systems such as PFMS, RIS, CPIS etc. were in line with the recommended IT plan on institutional strengthening of the Authority as

submitted by the Consultant were not borne out by facts. The development of PFMS and RIS, which was started in June 2000 and March 2002 respectively was at the instance of the World Bank and CPIS (development started in December 2002) was sought to be developed at the initiative of the Authority and the same were developed before the draft report of the Consultants.

The applications were non-integrating. This was evident from the fact that the Authority had taken up different projects without identifying the information requirements for the attainment of business objectives. In each of the above systems (PFMS, GIS, RIS) the Authority envisaged maintenance of separate database for capturing common data such as name of contractor, contract stretch, state, length of road, date of start/ completion, details of laning, NH number, chainage etc. The capturing of data in same fields across various systems was redundant and led to duplication of efforts.

The Authority stated (October 2005) that the databases created for hosting the IT applications and capturing the data relating to implementation of various projects were not integrated and the Authority was undertaking a feasibility study for implementing an Enterprise Resource Planning solution for synchronising the stand alone databases of different subsystems.

This indicated that the Authority did not envisage an integrated software application and instead created small projects thereby creating redundant data and individual applications which were non integrating and eventually had to plan for synchronising the stand alone databases.

27.1.5.3 The table below summarised the yearly budget for expenditure proposed by the IT Division, approved by the Finance Division and the actual expenditure incurred on information technology assets.

(Rs. In lakh)

Year	**IT Division Budgeted Expenditure**	**Finance Divison Budgeted Expenditure**	**Actual Expenditure**	**Actual expenditure in comparison to IT Division Budgeted Expenditure (in *per cent*)**
1999-2000	115.00	Not available	9.99	8.69
2000-2001	90.00	70.00	54.71	60.79
2001-2002	390.00	265.00	79.05	20.27
2002-2003	300.00	300.00	161.53	53.84
2003-2004	300.00*	300.00	151.20	50.40
2004-2005	Not available	Not available	40.38	--

Analysis of the budget provisions for expenditure on information technology asset creation revealed that there was non utilisation of 39 to 80 *per cent* of the budget estimates between 2000-01 to 2003-04 which indicated that the budgeting was not based on any scientific objective criteria, thus indicating faulty planning. Further Audit

* ***Finance Division Budgeted Expenditure***

observed that the Authority made only *ad-hoc* estimation of the expenditure for the projects on hand every year.

The Authority stated (October 2005) that its IT budget estimates were prepared yearly and the estimates were based on the likely expenses on the approved and on going IT projects and the cost benefit aspect of each IT project was discussed and documented. However, Audit was not provided access to any cost benefit study undertaken.

The reply of the Authority that a cost benefit study of each project was undertaken is also not borne out by facts as the software applications developed at the instance of the outside funding agencies had to be compulsorily implemented as part of the terms of loan agreement.

27.1.6 Wasteful expenditure in Development of Software Applications

27.1.6.1 Wasteful expenditure of Rs.26.59 lakh on development of Geographical Information System based Road Management and Construction System

A pilot project[♣], Geographical Information System based Road Management and Construction System, was conceived (July 2001) as a web based road management and construction system for executive decision support. The contract was awarded (September 2001) to M/s. Hope Technologies Limited at a cost Rs.26.59 lakh for supply of web interface software to have interactive access to design drawings, maps and data through internet and its installation. Besides data collection[♥] from Detailed Project Reports (DPRs) and conduct of ground survey for pavement condition after the date of completion of construction work it also included conversion, web designing, system integration and training. The data was proposed to be hosted on the webserver of the Authority. The entire work was completed in June 2002. Though the system envisaged updation of data by the user division, the same was not carried out both for the completed stretches and the stretches which were under construction as the Authority did not prescribe a mechanism for data collection and capturing of the same. Also, the Authority did not make any attempt to utilise the capability of the software in other completed stretches as well as in the stretches still under progress. As a result, the investment of Rs.26.59 lakh in the above system was rendered wasteful.

The Authority did not reply to the Audit observation nor did it state as to how the drawings for the completed and ongoing projects were captured in the electronic databases, if at all, to be available for future maintenance of road projects constructed at huge costs.

[♣] ***Two stretches – one completed stretch(Delhi-Jaipur) and another under construction (Sikandra-Bhaunti);***

[♥] ***pre constructions activities, geographical location of highway stretch, highway parameters such as pavement conditions, approach roads, speed, road side plantation and utilities, traffic details including accident data and construction/maintenance programme details***

27.1.6.2 Wasteful expenditure of Rs.5.07♣ crore due to abandonment of development of information solution of corridor management study

The Authority awarded (April 2002) a contract to Louis Berger Group Inc., USA (Contractor) for technical assistance for development and operation of pilot corridor management units• (CMU) at a cost of Rs.3.83 crore and US$ 0.84 million to be completed by August 2004. The scope of technical assistance also included High Quality Management System (HQMS)♠ to prioritise corridor and pavement maintenance schemes, procure and establish appropriate IT infrastructure and provide training and coordinate other relevant studies i.e. Road information, Minor Improvement to National Highways etc. being carried out by the Authority. However, there was no mention in the contract about the hosting of the data base for the HQMS.

Review in Audit of the deliverables showed that the Authority changed (August 2002) two stretches of the Delhi unit proposed to be taken up for data collection as long term operation and maintenance contracts had already been awarded thus making them unsuitable for consideration as pilots. It was also noticed in Audit that both the changed stretches had also been selected for data collection at the time of GIS (Delhi-Jaipur) and RIS (Barwa-Panagarh, Vijayawad-Chilkaluripet and Vijayawad-Eluru) software implementation, thus, resulting in duplication of efforts.

The Authority suspended (August 2003) the development of IT solution of HQMS as it did not provide possible integration with the RIS software concurrently under implementation. As a result, the amount of Rs.5.07 crore paid to the Contractor (upto December 2005) relating to data collection, development of IT solution, etc. which were required to facilitate the functionality of HQMS was rendered wasteful due to suspension of development of HQMS.

The Authority stated (October 2005) that the terms of reference of HQMS provided only for procurement and establishment of appropriate IT infrastructure and HQMS was proposed as possible software for the purpose by the Consultants. This was not found suitable by the Authority as the main domain was hosted in a third country and all the data was to be kept there and that integration of the software with Road Information System application was not an issue and no payments on account of procurement of HQMS was made by the Authority.

The contention of the Authority is not borne out of facts as the scope of study and duties of the Consultant included a clause to procure and establish appropriate IT infrastructure for operation of pilot corridor management units alongwith coordination with other relevant studies i.e. road information, minor improvement to National Highways etc. being carried out by the Authority. Thus, the amount had been paid towards development

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♣ *Comprising of Rs.2.07 crore and US$ 0.66 million equivalent to Rs. three crore (One US$ = Rs.45.61) – December 2003*

• *One at Delhi (Delhi-Agra section of NH 2 and Delhi-Jaipur section of NH 8) and another at Vijayawada (Vijayawade-Eluru section of NH5 and Vijayawada-Nandigama section of NH 9)*

♠ *prepare inventory and pavement condition data including locational referencing, highway patrolling, traffic accident management, land management, Right of width control including control of utilities, etc*

of IT solution even when the Authority itself had stated as early as August 2003 that the development of the software application be put on hold pending solution of the problem of its integration with Road Information system. Also the hosting of the database for the HQMS in a foreign country should have been known at the time of finalisation of contract. Thus, the eventual purpose of technical assistance for development and operation of pilot corridor management units, which also included cost for suggestion of suitable information system, was not met.

27.1.7 Conclusion and recommendations

27.1.7.1 Conclusion

As the Authority had not formulated a coherent IT strategy and IT plan, integrating its needs on the various facets of its operations, the result was:

(i) Duplication of efforts

(ii) Erection of different platforms and consequent training needs

(iii) Extra expenditure due to another effort to study the systems of the Authority

27.1.7.2 Recommendations

Audit recommends that:

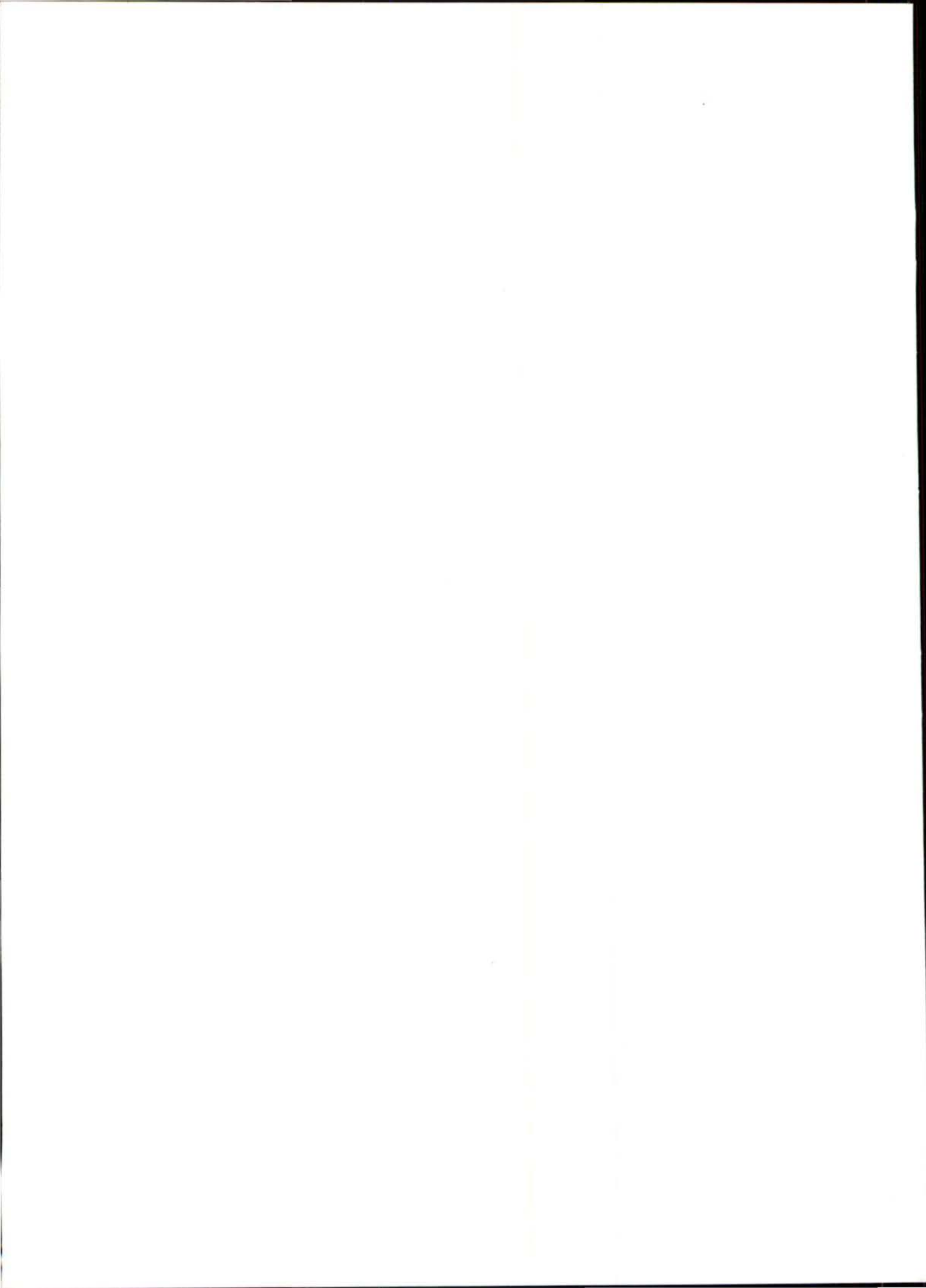
(i) The Authority should follow a structured information technology plan with a coordinated approach so as to gain from the huge investments made in information technology assets created so far which would lead to improving the Management Information system.

(ii) Authority should integrate the areas of Road Information system, Project Financial Management system and GIS based Road Management and Construction System so as to avoid duplication of efforts.

(iii) The Authority should plan and prepare realistic budgets after making cost benefit analysis of IT projects.

The matter was reported to the Ministry in December 2005; its reply was awaited.

SECTION III
GENERAL



CHAPTER XXVIII

Follow-up on Audit Reports (Commercial)

The Lok Sabha Secretariat requested (July 1985) all the Ministries to furnish notes (duly vetted by Audit) indicating remedial/corrective action taken by them on the various paragraphs/appraisals contained in the Audit Reports (Commercial) of the Comptroller and Auditor General of India as laid on the table of both the Houses of Parliament. Such notes were required to be submitted even in respect of paragraphs/appraisals which were not selected by the Committee on Public Sector Undertakings (COPU) for detailed examination. The COPU in its second Report (1998-99-Twelfth Lok Sabha) while reiterating the above instructions, recommended:

- setting up of a monitoring cell in each Ministry for monitoring the submission of Action Taken Notes (ATNs) in respect of Audit Reports (Commercial) on individual Public Sector Undertakings (PSUs);

- setting up of a monitoring cell in Department of Public Enterprises (DPE) for monitoring the submission of ATNs in respect of Reports containing paras relating to a number of PSUs under different Ministries; and

- submission to the Committee within six months from the date of presentation of the relevant Audit Reports of follow up ATNs duly vetted by Audit in respect of all Reports of the CAG presented to Parliament.

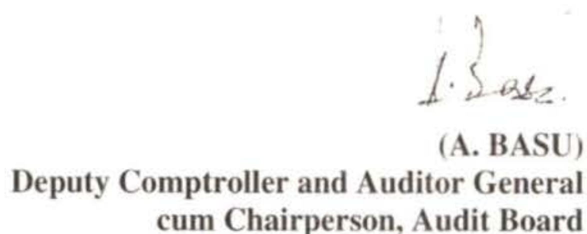
While reviewing the follow up action taken by the Government on its above recommendations, the COPU in its First Report (1999-2000 - Thirteenth Lok Sabha) reiterated its earlier recommendations that the DPE should set up a separate monitoring cell in the DPE itself to monitor the follow-up action taken by various Ministries/Departments on the observations contained in the Audit Reports (Commercial) on individual undertakings. Accordingly, a monitoring cell is functioning in the DPE since August, 2000 to monitor the follow up on submission of the ATNs by concerned administrative Ministries/Departments. Monitoring cells have also been set up within the concerned Ministries for submission of ATNs on various reports of CAG (Commercial).

A review in Audit revealed that inspite of reminders from Audit, the remedial/corrective action taken notes on the paragraphs/appraisals contained in the last five years' Audit Reports (Commercial) relating to the PSUs under the administrative control of various Ministries, as detailed in Appendix-II, were not received by Audit for vetting.

In respect of Audit Reports (Commercial) for the last five years (upto 2004), out of 404 paragraphs/ reviews on which ATNs were awaited, 32, 40, 77, 109 and 146 were awaited for Audit Reports (Commercial) of 2000, 2001, 2002, 2003 and 2004 respectively. For Audit Reports (Commercial) of 2005, which were presented to Parliament in March/May

2005, ATNs on 394 paras/reviews out of total 609 paras/reviews were awaited from various Ministries till October 2005.

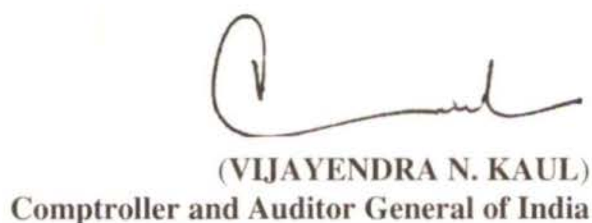
Out of 798 paragraphs on which ATNs are awaited, 104 paragraphs related to the PSUs under the Ministry of Finance (Banking Division), 100 paragraphs related to PSUs under the Ministry of Petroleum and Natural Gas, 83 paragraphs related to PSUs under the Ministry of Communications and 67 paragraphs related to PSUs under the Ministry of Steel.



(A. BASU)
Deputy Comptroller and Auditor General
cum Chairperson, Audit Board

New Delhi
The 17 March 2006

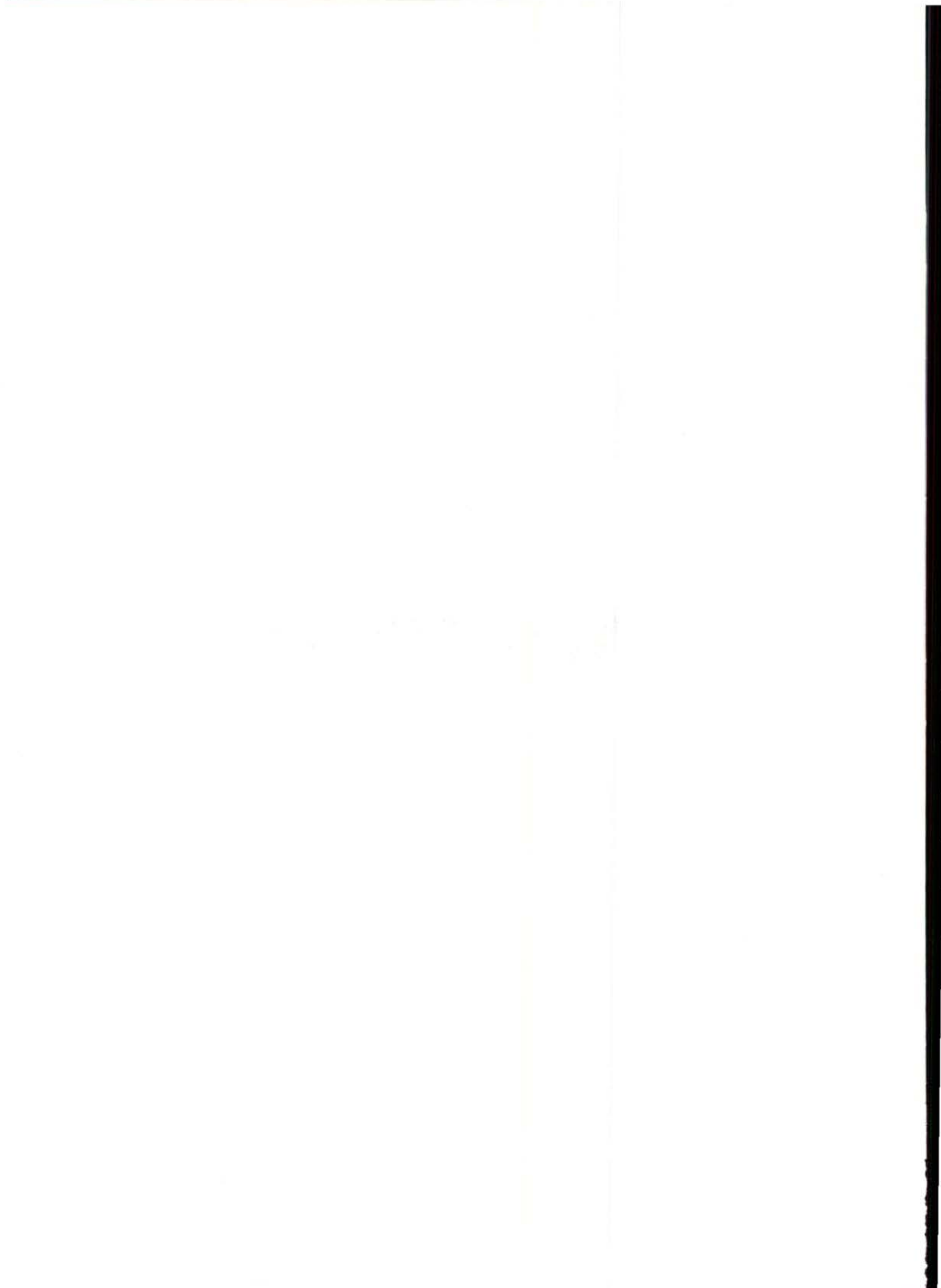
Countersigned



(VIJAYENDRA N. KAUL)
Comptroller and Auditor General of India

New Delhi
The 21 March 2006

Appendices



APPENDIX-I

(Referred to in para 16.2.1)

(Rs. in lakh)

Name of PSU	Audit Observation in Brief	Amount of recovery pointed out by Audit	Amount Recovered
1. Airport Authority of India	Short billing due to non-implementation of the annual escalation clause of car parking license contract at IGI Airport during the period from March 2004 to January 2005	40.95	40.95
2. Power Finance Corporation Limited	Excess payment of interest to banks due to ignoring change in the Prime Lending Rate	77.81	9.79
3. National Hydro Electric Power Corporation Limited	Undue benefit to contractor due to under insurance of works	161.00	150.00
4. United India Insurance Company Limited	(i) Short collection/ under charge of premium	21.20	20.57
	(ii)Excess payment of claim	2.26	1.54
	(iii)Avoidable payment of agency commission	0.12	0.12
	(iv)Non-recovery of terrorism surcharge	46.50	15.35
5. National Insurance Company Limited	(i) Short collection/ under charge of premium	5.83	5.83
	(ii)Excess payment of claim	46.02	35.73
	(iii)Excess payment of survey fees	0.36	0.33
	(iv)Non-recovery of terrorism surcharge	1.17	0.18
	(v)Non preference of claim from reinsurers	720.02	709.08
	(vi)Excess payment to Development Officers	4.43	0.40
6. The New India Assurance Company	(i) Short collection/ under charge of premium	1.67	0.88
	(ii)Non-recovery of terrorism surcharge	5.41	0.21

Limited	(iii)Excess payment of claim	34.82	34.82
7. The Oriental Insurance Company Limited	Issue of unviable Group JPA Policy to Steel Workers Union	200.12	200.12
8. Food Corporation of India	Non-recovery of loss from CWC, Dimapur due to not following proper procedure for preservation and issuance of stock by them	12.06	12.06
	Total	**1381.75**	**1237.96**

APPENDIX -II

(Referred to in Chapter XXVIII)

Statement showing the details of Audit Reports (Commercial) for which Action Taken Notes are pending as on 31 October 2005

No. and Year of Report	Name of the Report	Para No., if any
Ministry of Agriculture		
1. No. 3 of 2003	Transaction Audit Observations	Para 1.1.1
Department of Bio-Technology		
1. No. 2 of 2000	Comments on Accounts	Para 2.5.1
2. No.2 of 2002	Comments on Accounts	Paras 1.4.1, 2.1.2, 2.2.1, 2.3.3, and 2.8.1
3. No.2 of 2003	Comments on Accounts	Para 2.1.2
4. No.2 of 2004	Comments on Accounts	Paras 2.2.2 and 2.3.1
5. No. 2 of 2005	Comments on Accounts	Paras 2.1.2, 2.2.1
Department of Chemicals and Petrochemicals		
1. No. 2 of 2000	Comments on Accounts	Para 2.5.2
2. No. 6 of 2000	Appraisal on Hindustan Antiboitics Limited	
3. No.2 of 2003	Comments on Accounts	Paras 2.1.3, 2.2.4, 2.2.5, 2.3.2, 2.4.6 and 2.8.1
4. No.3 of 2003	Transaction Audit Observations	Para 3.1.1
5. No.2 of 2004	Comments on Accounts	Paras 1.2.1, 1.2.2, 2.1.2, 2.1.3, 2.4.2 and 2.5.2
6. No.3 of 2004	Transaction Audit Observations	Paras 1.1.1, 1.2.1, 1.3.1 and 1.4.1
7. No. 2 of 2005	Comments on Accounts	Paras 1.4.1, 2.1.3
8. No. 3 of 2005	Transaction Audit Observations	Paras 2.1.1, 2.1.2, 2.2.1
9. No. 4 of 2005	Review on HOCL Chapter-1	Paras 1.1, 1.2, 1.3, 1.4, 1.5, 1.6, 1.7

No. and Year of Report	Name of the Report	Para No., if any
Department of Fertilizers		
1. No.3 of 2003	Transaction Audit Observations	Para 10.2.1
2. No. 2 of 2005	Comments on Accounts	Paras 1.4.2, 1.4.3, 2.1.4, 2.2.2, 2.4.3, 2.5.1, 2.6.2 and 2.7.1
3. No. 3 of 2005	Transaction Audit observations	Paras 8.1.1, 8.1.2, 8.1.3, 8.2.1 and 8.3.1
Ministry of Civil Aviation		
1. No.3 of 2002	Transaction Audit Observations	Para 3.1.1
2. No.3 of 2003	Transaction Audit Observations	Para 4.1.4
3. No. 2 of 2005	Comments on Accounts	Paras 1.2.1, 1.4.4, 2.1.5, 2.1.6, 2.2.3, 2.3.1, 2.3.2, 2.4.5, 2.4.6, 2.5.17, 2.7.3, 2.7.4 and 2.7.33
4. No. 3 of 2005	Transaction Audit Observations	Paras 3.2.1, 3.2.2, 3.2.3, 3.2.4, 3.3.5 and 3.4.1
5. No. 4 of 2005	Reviews on AIL Chapter-II	Paras 2.1, 2.2, 2.3, 2.4 and 2.5
Ministry of Coal		
1. No. 7 of 2000	Appraisal on Eastern Coalfields Limited	
2. No.3 of 2002	Transaction Audit Observations	Para 4.6.1
3. No. 2 of 2005	Comments on Accounts	Paras 1.3.1, 1.3.2, 1.3.3, 1.4.5, 2.1.9, 2.1.10, 2.1.11, 2.1.12, 2.2.5, 2.4.8, 2.5.2, 2.5.3, 2.6.4, 2.6.5, 2.6.6, 2.7.2 (i), 2.7.2 (ii) and 2.7.2 (iii)
4. No. 3 of 2005	Transaction Audit observations	Paras 4.1.1, 4.1.2, 4.2.1, 4.2.2, 4.2.3, 4.3.1 and 4.5.1
5. No. 4 of 2005	Review on BCCL(Chapter III) (Performance of Madhuband Washery)	Paras 3.1, 3.2, 3.3, 3.4, 3.5, 3.6, 3.7 and 3.8
	Review of WCL (Chapter – IV) (Information Tech. Audit of Asset Accounting System)	Paras 4.1, 4.2, 4.3, 4.4, 4.5, 4.6, 4.7 and 4.8
Ministry of Mines /Department of Mines		
1. No. 2 of 2005	Comments on Accounts	Paras 2.5.13, 2.6.26, 2.4.23, 2.5.13 and 2.6.26

No. and Year of Report	Name of the Report	Para No., if any
2. No. 3 of 2005	Transaction Audit Observations	Para 14.1.1

Ministry of Commerce & Industry
Department of Commerce

No. and Year of Report	Name of the Report	Para No., if any
1. No. 2 of 2002	Comments on Accounts	Para 1.2.16
2. No. 3 of 2002	Transaction Audit Observations	Paras 5.2.1, 5.2.3 and 5.2.6
3. No. 2 of 2003	Comments on Accounts	Para 2.2.12
4. No.3 of 2003	Transaction Audit Observations	Paras 6.1.1 and 6.2.1
5. No.2 of 2004	Comments on Accounts	Paras 2.2.4, 2.2.5 and 2.3.4
6. No. 2 of 2005	Comments on Accounts	Paras 1.4.8,1.4.10, 2.1.15, 2.6.7 and 2.6.10
7. No. 3 of 2005	Transaction Audit Observations	Paras 5.3.1 and 5.3.2

Ministry of Communications
Department of Telecommunications

No. and Year of Report	Name of the Report	Para No., if any
1. No.2 of 2002	Comments on Accounts	Para 1.2.19
2. No.5 of 2003	Telecommunications Sector-	
	Chapter-2	Para 4 (Part), Para 3
	Chapter-3 (Review)	Paras 16.5.5, 16.7.6, 16.7.9.1, and 16.7.9.2
	Chapter-4	Para 42
3. No.2 of 2004	Comments on Accounts	Paras 1.2.10 and 2.4.8
4. No.5 of 2004	BSNL	
	Chapter-II	Paras 2.1, 2.2 and 2.10
	Chapter-III(Review)	Paras 3.5, 3.6, 3.8 and 3.11
	Chapter-IV	Paras 4.13, 4.17, 4.20, 4.22 and 4.32
	MTNL-Chapter-VII (1 Review)	Paras 7.14, 7.15, 7.16, 7.17, 7.18, 7.19, 7.20, 7.21, 7.22, 7.23 and 7.24
	Chapter-VIII	Paras 8.2 and 8.3
	Chapter-X	Para 10.3
	Chapter-XII	Para 12.1
5.No. 2 of 2005	Comments on Accounts	Paras 1.2.5, 1.2.6, 1.3.4, 1.4.11, 2.1.19, 2.1.20, 2.2.10, 2.2.11, 2.4.9, 2.4.10, 2.5.4, 2.5.5,

No. and Year of Report	Name of the Report	Para No., if any
		2.6.11 and 2.6.12
6. No.5 of 2005	Communication Sector	
	Chapter- I	Paras 1.3, 1.4, 1.6, 1.7
	Chapter- II	Paras 2.7, 2.9, 2.10, 2.11, 2.13, 2.16 and 2.17
	Chapter- III	Paras 3.1, 3.2, 3.3, 3.4, 3.5, 3.6, 3.7, 3.8, 3.9 and 3.10
	Chapter- IV	Paras 4.1, 4.2, 4.3, 4.4, 4.6, 4.7, 4.8, 4.9, 4.11, 4.12, 4.13, 4.14, 4.15, 4.16, 4.17, 4.18, 4.19, 4.20, 4.21, 4.24, 4.28 and 4.30
	Chapter- VI	Paras 6.1, 6.2, 6.3, 6.4, 6.13 and 6.14
	Chapter – IX	Paras 9.1 and 9.2
	Chapter – X	Paras 10.1, 10.2, 10.4 and 10.5
	Chapter- XI	Paras 11.1, 11.2, 11.3, 11.4, 11.5 and 11.6
	Chapter – XIII Follow up on Audit Reports	Para 13

Ministry of Consumer Affairs Food & Public Distribution

1. No.3 of 2002	Transaction Audit Observations	Para 7.2.3
2. No.3 of 2003	Transaction Audit Observations	Para 7.1.3
3. No.4 of 2003	Fraud Control in FCI	Para 2.1
	Internal Audit System in FCI	Para 2.2
4. No.2 of 2004	Comments on Accounts	Paras 1.2.11 and 2.2.9
5. No.3 of 2004	Transaction Audit Observations	Paras 5.2.2 and 5.2.6
6. No. 3 of 2005	Transaction Audit Observations	Paras 6.1.2, 6.1.3. 6.1.5, 6.1.6, 6.1.7, 6.1.9 and 6.1.12
7. No. 4 of 2005	Review on FCI (Chapter-V) (Export of food grains)	Paras 5.1, 5.2, 5.3, 5.4, 5.5, 5.6, 5.7, 5.8, 5.9, 5.10, 5.11and 5.12

Department of Defence Production and Supplies

1. No. 2 of 2003	Comments on Accounts	Para 1.4.9
2. No. 2 of 2005	Comments on Accounts	Paras 1.4.12 and 2.1.21
3. N0. 3 of 2005	Transaction Audit Observations	Paras 7.1.2, 7.3.1, 7.4.1, 7.4.2, 7.4.3 and 7.4.4

No. and Year of Report	Name of the Report	Para No., if any
4. No. 4 of 2005	Reviews	
	Chapter – VI (Bharat Electronics Limited)	Paras 6.1, 6.2, 6.3, 6.4, 6.5, 6.6, 6.7 and 6.8
	Chapter – VII (Bharat Electronics Limited)	Paras 7.1, 7.2, 7.3, 7.4, 7.5, 7.6, 7.7 and 7.8
	Chapter – VIII (Garden Reach Shipbuilders & Engineers Limited)	Paras 8.1, 8.2, 8.3,8.4, 8.5, 8.6 and 8.7
	Chapter – IX (Hindustan Aeronautics Limited)	Paras 9.1, 9.2, 9.3, 9.4, 9.5, 9.6, 9.7, 9.8, 9.9, 9.10, 9.11, 9.12 and 9.13

Department of North Eastern Development

1. No. 2 of 2002	Comments on Accounts	Paras 2.3.23 and 2.6.73
2. No. 2 of 2003	Comments on Accounts	Paras 1.2.15, 1.4.11, 2.3.16 and 2.6.75 (Para No. 2.3.16 and 2.6.75 transferred from Ministry of textiles in view of the letter no. 25012/9/05 – B&A dated 18th May 2005)
3.No. 3 of 2003	Transaction Audit Observations	Para 9.1.1
4. No. 2 of 2005	Comments on Accounts	Paras 1.4.37, 2.1.39, 2.3.11and 2.6.27

Ministry of Environment and Forest

1. No.2 of 2002	Comments on Accounts	Paras 2.4.19, 2.5.7 and 2.6.22
2. No. 2 of 2004	Comments on Accounts	Para 2.5.8
3. No.4 of 2004	Review on A&NIF&P Development Corporation Limited	Chapter-VI-Paras 6.1, 6.2, 6.3, 6.4, 6.5, 6.6, 6.7 and 6.8

Ministry of Finance (Banking Division)

1. No. 2 of 2000	Comments on Accounts	Paras 1.2.24, 1.2.25, 1.2.26, 1.2.27, 1.2.28, 1.2.29, 2.1.17, 2.2.22, 2.5.21, 2.6.19, 2.6.20, 2.6.21, 2.6.23, 2.6.26 and 2.6.27
2. No. 3 of 2000	Transaction Audit Observations	Paras 10.1.1, 10.1.2 and 10.1.3
3. No. 2 of 2001	Comments on Accounts	Paras 1.2.22, 1.2.23, 1.2.24,

No. and Year of Report	Name of the Report	Para No., if any
		1.2.25, 1.2.26, 1.2.27, 2.1.21, 2.1.22, 2.2.18, 2.2.19, 2.6.13, 2.6.14 and 2.6.16
4.No. 3 of 2001	Transaction Audit Observations	Paras 11.1.1, 11.2.1 and 11.3.1
5.No.2 of 2002	Comments on Accounts	Paras 1.2.24, 1.2.25, 1.2.26, 1.2.27, 2.1.14, 2.2.15, 2.2.16, 2.2.17, 2.2.18, 2.2.20, 2.6.23, 2.6.24, 2.6.25 and 2.6.27
6. No.3 of 2002	Transaction Audit Observations	Paras 11.1.1, 11.2.1, 11.3.1 and 11.4.1
7. No. 2 of 2003	Comments of Accounts	Paras 1.2.16, 1.2.17, 1.2.18, 1.4.12, 1.4.13, 2.1.22, 2.1.23, 2.1.24,2.3.5, 2.3.6, 2.6.21, 2.6.22, 2.6.23, 2.6.24, 2.6.25, 2.6.26, 2.6.27, 2.6.28, 2.8.10, 2.8.11, 2.8.12 and 2.8.13
8. No. 2 of 2004	Comments on Accounts	Paras 1.2.13, 2.1.14, 2.1.15, 2.2.11, 2.2.12, 2.2.13, 2.3.5, 2.4.11, 2.6.12, 2.6.13, 2.6.14, 2.6.15 and 2.6.16
9. No. 3 of 2004	Transaction Audit Observations	Paras 9.1.1, 9.2.1, 9.2.2 and 9.3.1
10. No. 2 of 2005	Comments on Accounts	Paras 1.2.11, 1.4.13, 1.4.14, 1.4.15, 1.4.16, 1.4.17, 2.1.24, 2.1.25, 2.2.12 and 2.2.13
12. No. 3 of 2005	Transaction Audit Observations	Paras 1.1.1, 1.2.1and 1.2.2
Ministry of Finance (Insurance Division)		
1. No. 2 of 2003	Comments on Accounts	Paras 2.1.26, 2.2.16, 2.6.30, 2.8.14 and 2.8.15
2. No.2 of 2004	Comments on Accounts	Paras 1.2.14, 1.3.12, 2.1.16, 2.2.14 and 2.6.17
3. No.3 of 2004	Transaction Audit Observations	Paras 8.2.1, 8.2.2, 8.2.3, 8.2.4, 8.2.5, 8.2.6, 8.2.7, 8.3.2, 8.4.1, 8.5.1, 8.5.2, 8.5.3 and 8.5.4
4. No. 2 of 2005	Comments on Accounts	Paras 1.2.10, 1.3.6,.1.3.7, 1.4.18, 1.4.19, 2.1.26, 2.1.27, 2.1.28, 2.2.14, 2.2.15
5. No.3 of 2005	Transaction Audit Observations	Paras 9.1.1, 9.2.1, 9.2.2, 9.2.3, 9.2.4, 9.4.1, 9.4.2, 9.4.3, 9.4.4,

No. and Year of Report	Name of the Report	Para No., if any
		9.4.5, 9.5.1, 9.5.2, 9.5.3 and 9.6.1
6..No. 4 of 2005	Review on Insurance Division Chapter- X	Paras 10.1, 10.2, 10.3, 10.4, 10.5, 10.6, 10.7, 10.8, 10.9, 10.10, 10.11 and 10.12
Ministry of Health & Family Welfare		
1. No. 2 of 2000	Comments on Accounts	Paras 2.6.28 and 2.8.8
2. No.2 of 2002	Comments on Accounts	Paras 2.1.15, 2.2.27 and 2.4.20
3. No.3 of 2002	Transaction Audit Observations	Para 12.1.1
4. No. 2 of 2003	Comments of Accounts	Para 2.6.32
5. No.3 of 2003	Transaction Audit Observations	Para 12.1.1
6. No.2 of 2004	Comments on Accounts	Para 2.6.18
7. No.3 of 2004	Transaction Audit Observations	Para 10.1.1
8. No.2 of 2005	Comments on Accounts	Paras 2.2.16, 2.4.13 and 2.6.19
Ministry of Home Affairs		
1. No. 2 of 2003	Comments on Accounts	Paras 2.6.76 and 2.8.24
2. No.2 of 2004	Comments on Accounts	Paras 1.2.20, 2.3.22 and 2.6.53
3. No.2 of 2005	Comments on Accounts	Paras 2.2.25
Ministry of Human Resource Development		
1. No. 2 of 2000	Comments on Accounts	Paras 1.2.43, 2.6.49 and 2.8.16
2. No. 2 of 2001	Comments on Accounts	Paras 2.1.34, 2.2.30 and 2.6.31
3. No.3 of 2004	Transaction Audit Observations	Para 12.1.1
4. No. 2 of 2005	Comments on Accounts	Paras 1.4.34, 2.1.37, 2.2.26 and 2.6.22
Ministry of Human Resources & Science Technology		
1. No.2 of 2001	Comments on Accounts	Para 2.1.35
2. No.2 of 2002	Comments on Accounts	Paras 2.1.21 and 2.6.42
3. No. 2 of 2003	Comments on Accounts	Para 2.2.26
Ministry of Heavy Industry & Public Enterprises		
1. No. 3 of 2003	Transaction Audit Observations	Paras 13.1.1 and 13.1.2
2. No.2 of 2004	Comments on Accounts	Para 2.3.14
3 No. 3 of 2004	Transaction Audit Observations	Paras 11.1.9 and 11.3.1

No. and Year of Report	Name of the Report	Para No., if any
4. No. 2 of 2005	Comments on Accounts	Paras 1.2.12, 1.2.13, 1.3.9, 1.3.11, 1.4.23, 1.4.24, 1.4.32, 1.4.33, 2.1.36, 2.2.17, 2.2.23, 2.2.24, 2.3.4, 2.3.5, 2.4.16, 2.5.9, 2.7.15, 2.7.17 and 2.7.20
5. No.3 of 2005	Transaction Audit Observations	Paras 11.1.1, 11.1.2, 11.1.3, 11.1.4. 11.1.5, 11.1.6, 11.1.7, 11.1.8 and 11.2.1
Department of Information Technology		
1. No. 2 of 2005	Comments of Accounts	Paras 1.4.35, 2.2.28, 2.3.10, 2.4.22, 2.6.24 and 2.6.25
2. No. 3 of 2005	Transaction Audit Observations Chapter- 13	Para 13.1.1
Ministry of Information and Broadcasting		
1. No. 2 of 2001	Comments on Accounts	Para 1.3.33
2. No. 3 of 2001	Transaction Audit Observations	Para 13.1.1
3. No.2 of 2002	Comments on Accounts	Paras 1.3.33 and 2.5.16
4. No.3 of 2002	Transaction Audit Observations	Para 14.1.1
5. No.2 of 2004	Comments on Accounts	Paras 1.2.21, 1.3.17, 2.1.21, 2.3.15, 2.6.27, and 2.7.6
6. No. 2 of 2005	Comments on Accounts	Paras 2.1.38, 2.2.27, 2.4.21, 2.6.23 and 2.7.21
7. No. 3 of 2005	Transaction Audit Observations Chapter- 12	Para 13.1.1
Ministry of Non-Conventional Energy Sources		
1.No. 3 of 2003	Transaction Audit Observations	Para 16.1.1
2.No. 3 of 2005	Transaction Audit Observations Chapter 15	Para 15.1.1
Ministry of Petroleum and Natural Gas		
1. No. 3 of 2000	Transaction Audit Observations	Para 16.3.3
2. No. 2 of 2001	Comments on Accounts	Paras 1.2.50 and 1.3.39
3. No. 3 of 2001	Transaction Audit Observations	Paras 17.2.2, 17.4.1, 17.6.2 and 17.8.2
4. No.2 of 2002	Comments on Accounts	Paras 1.2.37, 1.2.40 and 2.3.16
5. No.3 of 2002	Transaction Audit Observations	Paras 16.1.2, 16.1.4, 16.5.1,

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		16.6.2, 16.6.3, 16.6.4, 16.6.6 and 16.7.4
6. No. 2 of 2003	Comments on Accounts	Paras 1.2.27, 1.2.28, 1.2.32, 1.3.29, 2.2.30, 2.5.20, 2.5.21, 2.6.48 and 2.6.50
7. No.3 of 2003	Transaction Audit Observations	Paras 17.2.2, 17.6.1, 17.6.2, 17.6.5, 17.6.6, 17.7.4 and 17.7.6
8. No. 2 of 2004	Comments on Accounts	Paras 2.1.23, 2.6.32 and 2.7.7
9. No. 3 of 2004	Transaction Audit Observations	Paras 14.4.3, 14.5.3, 14.5.6, 14.6.1, 14.6.5, 14.6.6, 14.6.8 and 14.7.2
10. No.4 of 2004	Review on GAIL	Chapter-VIII- Paras 8.1, 8.2, 8.4,,8.6, 8.7, 8.10 and 8.11
11. No.4 of 2004	Review on Oil India Limited	Chapter-IX-Paras 9.1, 9.2, 9.3, 9.4, 9.5, 9.6 and 9.7
12. No. 2 of 2005	Comments on Accounts	Paras 1.2.17, 1.2.18. 1.3.16, 1.3.18, 1.4.38, 2.1.41, 2.2.30, 2.2.31, 2.3.12, 2.4.24, 2.4.26, 2.6.28 and 2.7.21
13. No. 6 of 2005	Petroleum Sector Profile	
	Chapter-1	
	Chapter –2	Paras 2.2, 2.3, 2.4 and 2.5
	Follow up action on reviews in the last five years Audit Reports	
	Chapter – 3 (Reviews)	Chapter – 3
	Review on branching and capacity augmentation of pipelines in Northern Region - IOCL	3.1
	Review on Arbitration Cases – ONGC	3.2
	Review on production sharing contracts with private exploration and production companies - ONGC	3.3
	Chapter – 4	Chapter – 4
		Paras 4.1, 4.1.1, 4.1.3, 4.1.4,

No. and Year of Report	Name of the Report	Para No., if any
		4.1.5, 4.1.6, 4.2, 4.2.2, 4.2.3, 4.2.4, 4.2.8, 4.3, 4.3.1, 4.3.2, 4.4, 4.4.1, 4.5, 4.5.1, 4.6, 4.6.1, 4.6.2, 4.6.3, 4.6.4, 4.6.5, 4.6.6. 4.7, 4.7.1, 4.7.2, 4.7.3 and 4.8
	Review on IT Audit	
	IT Review on re-engineering project – Manthan - IOCL	5.1
	Payroll application in mumbai region - ONGC	5.2
	Corporate Governance in Oil PSUs.	Chapter - 6
Ministry of Power		
1. No. 2 of 2001	Comments on Accounts	Paras 1.3.45 and 2.2.43
2. No.2 of 2002	Comments on Accounts	Paras 1.2.44, 1.3.43, 2.6.56 and 2.8.19
3. No.4 of 2002	Review on implementation of Rehabilitation Plan by THDC	Chapter 5
4. No. 2 of 2003	Comments on Accounts	Paras 2.1.44, 2.2.34, 2.6.57, 2.8.25, and 2.8.28
5. No. 2 of 2004	Comments on Accounts	Para 1.2.32
6. No. 2 of 2005	Comments on Accounts	Paras 1.2.20, 1.2.21, 1.2.22, 1.2.23, 1.4.39, 1.4.40, 2.1.42, 2.4.27, 2.4.28, 2.5.14, 2.6.30, 2.6.31, 2.6.32, 2.7.23 and 2.7.24
7. No. 3 of 2005	Transaction Audit Observations	Paras 16.1.1, 16.2.1, 16.2.2 and 16.3.1
Ministry of Railways		
1. No.2 of 2005	Comments on Accounts	Paras 1.2.24, 2.1.43, 2.2.33, 2.4.29, 2.5.15 and 2.7.27
Ministry of Road Transport and Highways		
1. No.2 of 2005	Comments on Accounts	Para 2.1.44
2. No. 3 of 2005	Transaction Audit Observations	Chapter – 18- Para- 18.1.1
3. No. 7 of 2005	National Highways Authority of India	Chapter – I – Paras 1.1, 1.2, 1.3. 1.4, 1.5, 1.6, 1.7 and 1.8
		Chapter – 2 – Paras 2.1, 2.2,

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		Chapter-4-Paras 4.1, 4.2, 5.1, 5.2,5.3 and 5.4
		Chapter – 6
		Chapter – 7 – Paras 7.1 and 7.2
		Chapter – 8- Paras 8.1, 8.2 and 8.3
		Chapter – 9 – Paras 9.1 and 9.2
		Chapter – 10
		Chapter – 11 – Paras 11.1, 11.2, 11.3, 11.4 and 11.5
		Chapter – 12
Department of Public Enterprises		
1. No.4 of 2003	Reviews on some of the activities of selected PSUs	Para 5.1
Department of Small scale Industries & Agro and Rural Industries		
1. No.2 of 2002	Comments on Accounts	Para 2.3.17
2. No. 3 of 2004	Transaction Audit Observations	Para 19.1.1
3. No. 4 of 2005	Review on National Small Industries Corporation Ltd.	Chapter – XIII- Paras 13.1, 13.2, 13.3, 13.4, 13.5, 13.6, 13.7, 13.8, 13.9, 13.10, 13.11, 13.12, 13.13, 13.14, 13.15 and 13.16
Ministry of Social Justice & Empowerment (Department of Welfare)		
1. No. 2 of 2000	Comments on Accounts	Paras 2.1.56 and 2.2.64
2. No. 3 of 2000	Transaction Audit Observations	Para 24.2
3. No. 2 of 2001	Comments on Accounts	Para 2.1.50
4. No.2 of 2002	Comments on Accounts	Paras 2.1.34, 2.2.43 and 2.6.63
5. No.3 of 2002	Transaction Audit Observations	Para 20.1.1
6. No. 2 of 2003	Comments of Accounts	Paras 2.1.52, 2.1.53, 2.2.41, 2.2.42, 2.3.15, 2.4.38, 2.4.39, 2.5.22, 2.6.63, 2.8.30, 2.8.31, 2.8.32 and 2.8.33
7. No.2 of 2004	Comments on Accounts	Paras 1.2.40, 1.4.26, 2.1.32,

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		2.2.33, 2.6.42, 2.7.10 and 2.7.11
8. No.2 of 2005	Comments on Accounts	1.4.45, 2.1.49, 2.1.50, 2.1.51, 2.2.36, 2.2.37, 2.2.38, 2.6.38, 2.6.39, 2.6.40, 2.7.28 and 2.7.29
Department of Space		
1. No. 2 of 2003	Comments on Accounts	Para 2.5.19
2. No. 2 of 2004	Comments on Accounts	Paras 2.2.21(i), 2.4.18 and 2.5.13
3. No. 2 of 2005	Comments on Accounts	1.4.36
Ministry of Steel		
1. No. 2 of 2001	Comments on Accounts	Paras 2.5.25 and 2.8.19
2. No. 3 of 2001	Transaction Audit Observations	Paras 21.3.2, 21.4.5, 21.4.6 and 21.4.7
3. No. 4 of 2001	Review on Execution of CCP of Rourkela Steel Plant by MECON	Chapter 7
4. No.2 of 2002	Comments on Accounts	Paras 1.2.54 and 2.6.12
5. No.3 of 2002	Transaction Audit Observations	Paras 21.2.1, 21.5.2, 21.6.2, 21.7.1 and 21.7.9
6. No. 4 of 2002	Review on Modernisation of BSP-SAIL	Chapter 6.1
	Review on Township Management in SAIL	Chapter 6.2
	Review on R&D Centre for Iron & Steel-SAIL	Chapter 6.3
7. No. 2 of 2003	Comments of Accounts	Paras 1.3.37, 1.3.39, 2.1.54, 2.4.40, 2.6.65, 2.6.66, 2.6.67 and 2.6.70
8. No.3 of 2003	Transaction Audit Observations	Para 23.5.5
9. No.4 of 2003	Business Restructuring Plan of SAIL	Para 3.1
	Rail and Structural Mill of Bhilai Steel Plant of SAIL	Para 3.2
10. No.2 of 2004	Comments on Accounts	Paras 1.2.45, 1.3.29, 1.4.30, 2.1.36, 2.2.34, 2.2.35, 2.2.36,

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		2.2.37, 2.5.17, 2.5.18, 2.6.43, 2.6.44, 2.6.46, 2.6.47 and 2.7.12
11. No.4 of 2004	Review on NMDC	Chapter-XIII-Paras-13.1, 13.2, 13.3, 13.4 and 13.5
12. No.6 of 2004	Steel Sector-Chapter 2 (SAIL)	Review on Captive Mines of SAIL
	Chapter-3	Paras 3.2 and 3.7
	Section-II, Review on the working of MECON	Chapter-4 Paras 4.1, 4.2, 4.3, 4.4, 4.5, 4.6, 4.7, 4.8, 4.9 and 4.10
	Section-III HSCL Limited (Review)	Chapter-6 Paras 6.1, 6.2
	Section-IV, RINL	Chapter-8 Paras 8.1and 8.2
	Section VI-NMDC	Chapter-12 Para 12.1
13. No.2 of 2005	Comments on Accounts	Paras 1.2.29, 1.3.21, 1.3.24, 2.1.53, 2.2.44 and 2.6.41
14. No. 3 of 2005	Transaction Audit Observations(Chapter-20)	Paras 20.1.1, 20.2.1, 20.2.3, 20.3.1,20.4.1, 20.4.2, 20.4.4, 20.4.5 and 20.5.1

Ministry of Shipping

1. No.3 of 2004	Transaction Audit Observations	Para 18.2.2
2. No.4 of 2004	Review on Hindustan Shipyard Limited	Chapter-XI-Paras 11.1, 11.2, 11.10, 11.12, 11.14, 11.15 and 11.16
3. No. 2 of 2005	Comments on Accounts	1.4.42, 2.1.47, 2.1.48 and 2.6.36
4. No.3 of 2005	Transaction Audit Observations	Chapter 19- Paras 19.1.1, 19.2.1 and 19.3.1
5. No.4 of 2005	Review on Dredging Corporation of India Limited	12.1, 12.2, 12.3, 12.4, 12.5, 12.6, 12.7, 12.8, 12.9, 12.10, 12.11 and 12.12

Ministry of Science & Technology

1. No. 2 of 2005	Comments on Accounts	2.1.45, 2.1.46, 2.2.34 and 2.4.30

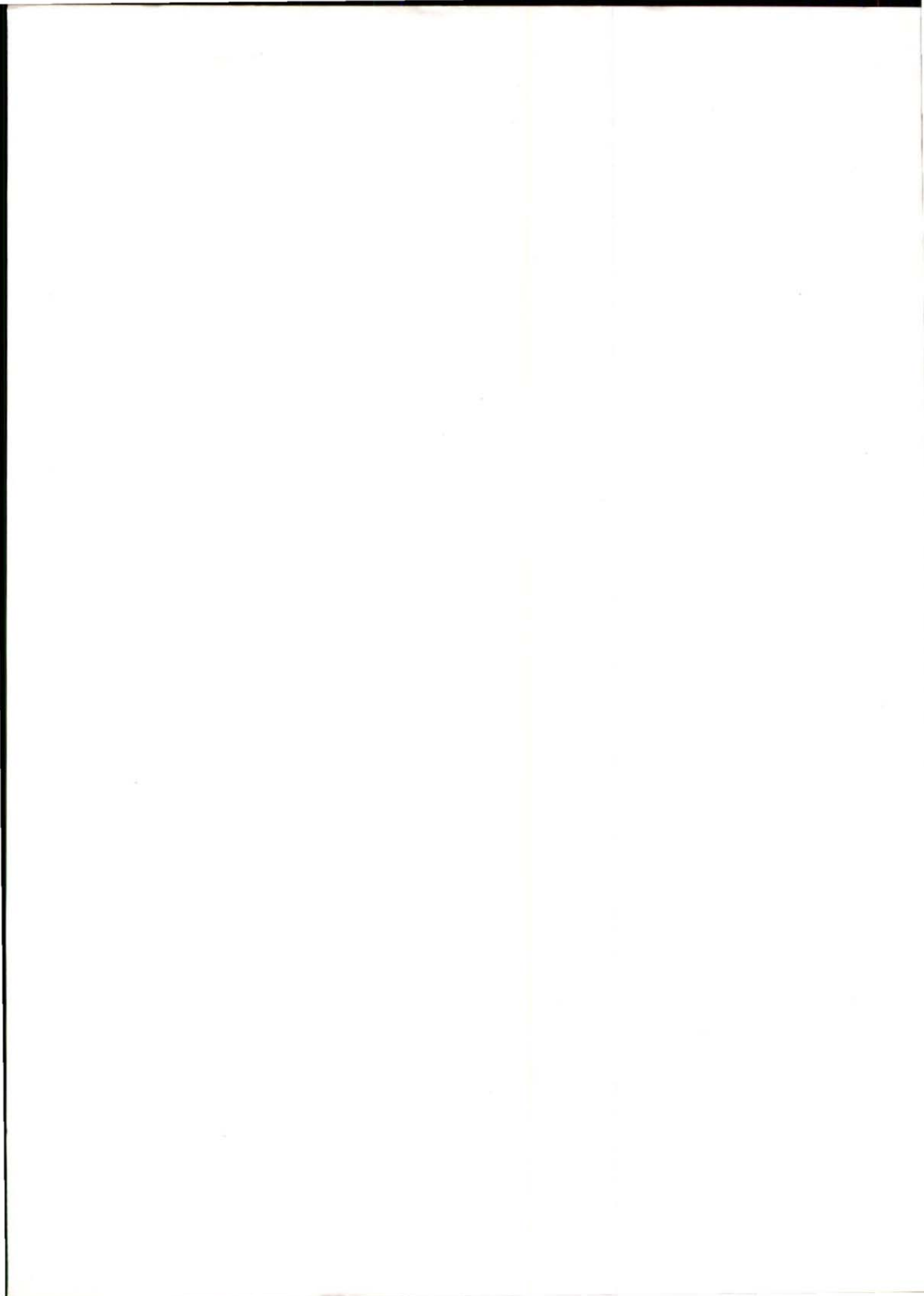
No. and Year of Report	Name of the Report	Para No., if any
Ministry of Surface Transport		
1. No.4 of 2003	Working of River Service Division of Central Inland Water Transport Corporation Limited	Para 4.1
Ministry of Textiles		
1. No. 2 of 2005	Comments on Accounts	Paras 1.4.50, 2.1.54, 2.6.47, 21.1.1, 21.1.2 and 21.2.1
2. No.3 of 2005	Transaction Audit Observations	Chapter 21- Paras 21.1.1 and 21.1.2
3. No. 4 of 2005	Review on National Textile Corporation (APKK&M)	Chapter XIV- 14.1, 14.2, 14.3, 14.4, 14.8 and 14.9
Ministry of Urban Development and Poverty Alleviation		
1. No. 2 of 2001	Comments on Accounts	Para 1.2.65
2. No. 3 of 2001	Transaction Audit Observations	Para 24.1.1
3. No.2 of 2002	Comments on Accounts	Para 1.2.61
4. No.2 of 2004	Comments on Accounts	Paras 1.2.48, 1.4.35, 2.1.41 and 2.2.40
5. No.3 of 2004	Transaction Audit Observations	Paras 20.1.1 and 20.2.1
6. No.2 of 2005	Comments on Accounts	Paras 1.2.31, 1.2.32, 1.4.56, 1.4.57, 2.1.57 and 2.6.52
7. No.3 of 2005	Transaction Audit Observations	Chapter 22 - 22.1.1, 22.1.2, 22.1.3
Ministry of Water Resources		
1. No.2 of 2004	Comments on Accounts	Paras 1.2.49 and 1.4.36

GLOSSARY

AAI	Airports Authority of India Limited
APCS	Air Pollution Control System
APGST	Andhra Pradesh General Sales Tax
ATN	Action Taken Note
AY	Assessment Year
BEML	Bharat Earth Movers Limited
BEL	Bharat Electronics Limited
BG	Bank Guarantees
BIFR	Board for Industrial and Financial Reconstruction
BOD	Board of Directors
CERC	Central Electricity Regulatory Commission
CFR	Cost Freight Rate
CHP	Coal Handling Plant
CMDs	Chairmen cum Managing Directors
CMWSSB	Chennai Metropolitan Water Supply and Sewerage Board
COD	Commission Operated Depot
CPP	Captive Power Plant
CPT	Chennai Port Trust
DECL	M/s. DSS e Contact Limited
DJB	Delhi Jal Board
DO	Divisional Office
DVC	Damodar Valley Corporation
DPC	Dabhol Power Company
DPL	Durgapur Projects Limited
DPCL	DLF Power Company Limited
ETA	M/s. Emirate Trading Agency
FCL	Foreign Currency Loan
EDC	East Donger Chikhli
FO	Furnace Oil
GEB	Gujarat Electricity Board
GENISYS	General Insurance System
GGS	Group Gathering Station
GIT	Group-Inclusive Tour
GJPAP	Group Janata Personal Accident Policy
GMP	Group Mediclaim Policy
GMSC	Golden Multi Services Club
GR	Guwahati Refinery
GTFS	Golden Trust Financial Services
HAL	Hindustan Aeronautics Limited
HO	Head Office
HOSI	M/s. Halliburton Offshore Services Inc.
HPCL	Hindustan Petroleum Corporation Limited
HPFR	Hindustan Petroleum Fuel Refinery
HSD	High Speed Diesel
HUDCO	Housing and Urban Development Corporation Limited

HQMS	High Quality Management System
IAL	M/s. Ispat Alloys Limited
IAR	Industrial All Risk
ICC	Imported Coking Coal
IOCL	Indian Oil Corporation Limited
IPC	International Potash Co (UK) Limited, London
IISCO	M/s. Indian Iron and Steel Company Limited
ISP	Integrated Steel Plant
IT	Information Technology
KfW	Kreditanstalt fur Wiederaufbau, Germany
KPT	Kandla Port Trust
KVA	Kilo Volt Ampere
KWH	Kilo Watt Hour
LD	Liquidated Damages
LC	Letter of Credit
LPG	Liquified Petroleum Gas
LNT	Liquid Nitrogen Transportation Tanks
MCR	Maruwai Coal Resource, Indonesia
MIADS	Malabar International Airport Development Society
MDI	Methylene Di-Phenyl Di-isocyanate
MME	M/s. Marathon Marine Engineering
MMSCMD	Million Metric Standard Cubic Meters per Day
MMTPA	Million Metric Tonne per annum
MOU	Memoranda of Understanding
MPT	Mormugao Port Trust
MT	Metric Tonne
NAAS	M/s. North American Aviation Services
NDMC	New Delhi Municipal Corporation
NIA	New India Assurance Company Limited
NIC	National Insurance Company Limited
NOIDA	New Okhla Industrial Development Authority
ONGC	Oil and Natural Gas Corporation Limited
OVL	ONGC Videsh Limited
PD	Public Deposit
PMT	Per Metric Tonne
PPL	Paradeep Phosphates Limited
PPT	Paradip Port Trust
PSU	Public Sector Undertaking
PU	Polyurethane
RINL	Rashtriya Ispat Nigam Limited
RLA	Residual Life Assessment
RMT	Reservoir Monitoring Tool
ROs	Retail Outlets
RTL	Rupee Term Loan
SCM	Standard Cubic Meters
SCP	Special Contingency Policy
SIIL	Sterlite Industries (India) Limited, Tuticorn
SPC	special purpose company

SRU	Sulphur Recovery Unit
SSPC	Standing Sales Purchase Committee
TD	Term Deposit
TAC	Tariff Advisory Committee
TL	Train in Load
TMTPA	Thousand Metric Tonne Per Annum
TNEB	Tamil Nadu Electricity Board
TSED	Tripura State Electricity Department at Rokhia, Tripura
UDAF	User Development Additional Fee
VDA	Varanasi Development Authority
VRS	Voluntary Retirement Scheme
WBSEB	West Bengal State Electricity Board
WID	Water Injection Dredgers



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