

CHAPTER - II

2. Review relating to Government Companies

2.1 Review on “Power Purchase Agreements entered into by MP Power Management Company Limited/ Board/ Government of MP with Private Power Producers for purchase of power and its operationalisation” during the period from 2008-09 to 2012-13

Executive Summary

Introduction

MP Power Management Company Limited (Company) under the administrative control of Department of Energy, Government of Madhya Pradesh (GoMP) is entrusted with the responsibility of assessing the demand of power in the State and make arrangements for meeting the demand by pooling all power purchases from different sources.

The Review conducted during May 2013 to July 2013 covers Power Purchase Agreements (PPAs) entered into by GoMP Company with Independent Power Producers and operationalisation of PPAs during the period from 2008-09 to 2012-13 including planning and procurement of power.

Against the planned procurement of 1009 MW capacity of power through IPPs on long term basis, the Company could procure only 207 MW during the period of review

The Company paid idle capacity charges to the extent of ₹ 66.77 crore during the period from November 2011 to March 2013 for scheduling lower capacity from a gas based Power Project.

Deviation from terms and conditions of Memorandum of Understanding and Implementation Agreement in respect of PPA with BLA Power Private Limited resulted in additional expenditure of ₹ 1.53 crore due to purchase of two and half per cent of power at regulated tariff rate instead of concessional tariff rate and committed additional cost of ₹ 73.83 crore.

The Company was deprived of availing cheap power from Sasan Power Ltd., for a period of 15 months due to postponement of commissioning date (COD) in all the six units of a power project resulting in potential loss of ₹ 1252.46 crore on account of purchase of power from other sources.

The Company did not impose liquidated damages of ₹ 10.89 crore as per PPA for tariff based power for the delay in commissioning of the Bina Thermal Power Project beyond the extension granted.

Due to removal of capping of fixed charge rate, the Company had to incur an additional expenditure of ₹ 24.51 crore and committed to incur an additional cost of ₹ 145.96 crore towards fixed charges on procurement of power from Torrent.

There is no mechanism to verify landed cost of coal and its gross calorific value.

Due to deficiencies in the billing, payment procedure and deviation from norms, the Company could not avail Rebate amounting to ₹53.02 lakh from developers and also incurred avoidable LPS of ₹6.97 crore.

Introduction

2.1.1 The Government of India (GoI) notified a National Electricity Policy (NEP) in February 2005 with the main objective to supply reliable and quality power in an efficient manner and at reasonable rates. MP Power Management Company Limited¹ (Company) under the administrative control of Department of Energy, Government of Madhya Pradesh (GoMP) is entrusted with the responsibility of assessing the demand of power in the State and make arrangements for meeting the demand by pooling all power purchases from different sources.

The unrestricted maximum demand² (UMD) for power in the State during 2007-08 was 7200 MW and the Company/ State could meet the demand to the extent of 6436 MW resulting in a shortage of 764 MW, which was managed through load shedding. In 2012-13, while the UMD increased to 9804 MW, the demand met was 9412 MW leaving a shortage of 392 MW. Thus, the Company has been able to largely meet the power requirements of the State as at the end of March 2013. Considering the improved power availability, GoMP in 2013, launched Atal Jyoti Abhiyan with a view to provide 10 hours power supply to agricultural consumers and uninterrupted supply of power to other consumers of the State.

In order to meet the gap between UMD and availability of power, the Company prepares plans for procuring power from the different sources viz., State owned generating stations, Central Generating stations and generation by Independent Power Producers (IPPs) from which the demand would be met. The plan prepared by the Company is submitted to GoMP for approval.

Power from IPPs is obtained through long term agreements and short term arrangements. Long term agreements are entered into by the Company either through the process of bidding or on the basis of Memorandum of Understanding (MoUs) entered into by GoMP. MoUs are signed between the GoMP and the IPPs proposing to set up power projects in the State and under the MoU, GoMP undertakes to provide facilities such as providing land for the project from its own sources or through acquisition, allotment of water for the project, assisting in GoMP clearances for the project etc. In lieu of the facilities/ assistance from GoMP, the IPP is required to provide five³ per cent of the power generated from the project at concessional rate (Concessional power⁴) considering only the cost of fuel. Besides, the MoU provides for first right of allocation of upto 30 per cent of

¹ As a part of power sector reforms, Madhya Pradesh Power Trading Company Limited, Jabalpur, was incorporated on 2 May 2006. The name of the Company was since changed to Madhya Pradesh Power Management Company Limited (Company) with effect from 10 April 2012.

² The actual point of peak demand is a single half hour or hourly period which represents the highest point of customer consumption of electricity without any restriction.

³ 7.5 per cent, if the fuel is obtained from captive coal block situated in Madhya Pradesh.

⁴ Concessional power represents the power agreed to be supplied by IPP on variable cost i.e., cost of fuel.

power of the Power Station's installed capacity (tariff based power⁵) to the GoMP or its nominated agency at rates as determined by the Madhya Pradesh Electricity Regulatory Commission (MPERC). In pursuant to the terms of MoU, GoMP and IPPs sign the Implementation Agreements (IA). On the basis of the MoUs/ IAs signed between the GoMP and IPPs, the GoMP enters into Power Purchase Agreements (PPAs) for concessional power and the Company enters into PPAs for tariff based power. The Company being the nominated agency of the GoMP receives the concessional power. Thus, through long term PPAs, the Company obtains concessional power, tariff based power and bid based power⁶.

The details of long term agreements (PPAs) entered into by the Company for procurement of power from conventional sources⁷ during the period 2006-07 to 2012-13 are given in *Annexure-2.1.1*. Besides, the Company has also entered into 98 PPAs for procurement through non conventional sources⁸.

Organisational set up

2.1.2 The management of the Company is vested in a Board of Directors (BoD) comprising of Chairman, Managing Director, Director (Commercial) and five Non-Executive Directors. The day-to-day operations of the Company are carried out by the Managing Director, who is the Chief Executive of the Company with the assistance of eight Heads of the Department⁹ and Company Secretary.

Capital Structure of the Company

2.1.3 The Authorised and Paid up Capital of the Company at the time of incorporation was ₹ 10.00 lakh each, which stood at ₹ 6500 crore and ₹ 4012.36 crore respectively by the end of March 2013.

Scope and Methodology of Audit

2.1.4 The Review conducted during May 2013 to July 2013 covers PPAs entered into by GoMP/ Board¹⁰/ Company with IPPs and operationalisation of PPAs during the period from 2008-09 to 2012-13 including planning and procurement of conventional and non-conventional power. The review also covered the Power Sale Agreements (PSAs) entered into with the PTC India Ltd. (PTC), which had entered into PPAs with IPPs.

⁵ Tariff based power represents the 30 per cent of the power generated by IPP on which first right of allocation vests with the Government or its nominated agency on which rate of supply is to be determined by MPERC.

⁶ Bid based power represents the power that is contracted on the basis of bidding.

⁷ Conventional sources represent the power generated through thermal and hydel.

⁸ Non-conventional sources represent the power generated through Solar, Wind and Bio-mass/gas.

⁹ (i)Executive Director (Finance and Administration) (ii)Executive Director (Power Management) (iii)Executive Director (Investment Promotion Cell) (iv)Chief General Manager (Regulatory) (v)Chief General Manager (Human Resources) (vi)Chief General Manager (Commercial) (vii)General Manager (Public Relations) (viii)Director General (Enforcement).

¹⁰ Board represents erstwhile Madhya Pradesh Electricity Board from which the responsibility of power procurement was taken over by the Company.

Twelve out of 23 PPAs for conventional power and 24 out of 98 PPAs of non-conventional power entered into by the Company were randomly selected for scrutiny.

Entry conference was held with Management/ Government in May 2013. Audit findings were reported to the Company and Government in August 2013. Replies were received between August 2013 and November 2013. Findings were also discussed with the Principal Secretary (Energy) and Managing Director of the Company in an exit conference held in December 2013. Replies of the Company/ Government have been appropriately incorporated in the Report.

Audit Objectives

2.1.5 The objectives of the Review were to assess whether:

- The GoMP/ Company assessed the demand for power and planned for creation of generation capacities under IPP mode in accordance with National Electricity Plan/ Policy;
- The provisions of the Memorandum of Understandings (MoUs)/ Implementation Agreements (IAs)/ Model PPAs/ PPAs entered into by the GoMP/ Company were in line with established guidelines/ rules/ regulations and not detrimental to the interest of the Company;
- PPAs were operationalised as per its terms and conditions; and
- An effective monitoring mechanism was in place.

Audit Criteria

2.1.6 The audit criteria for assessing the performance were:

- Electricity Act 2003 and Electricity (Supply) Act 1948;
- National Electricity Policies and Tariff Policies issued by GoI from time to time;
- Guidelines, Terms and Conditions of Tariff issued by Central Electricity Regulatory Commission (CERC)/ Madhya Pradesh Electricity Regulatory Commission (MPERC) from time to time;
- Standard Bidding documents, Model PPAs framed by GoMP/ GoI, MoUs and PPAs; and
- Decisions of the BoD and Management Information System reports.

Audit Findings

2.1.7 The Audit findings are discussed below:

Planning

Target for procurement of power through long term agreements

2.1.8.1 As per NEP, the progress of implementation of capacity addition plans and growth of demand would need to be constantly monitored and necessary adjustments would be made from time to time.

Non-achievement of targeted procurement of power through long term PPAs resulted in additional financial burden of ₹ 288.16 crore.

The details of capacity addition planned vis-à-vis actual achievement and shortfall during the period from 2008-09 to 2012-13 are given in *Annexure-2.1.2*. It could be seen from *Annexure-2.1.2* that against the planned additional capacity of 1009 MW on long term basis, the Company could add only 207 MW resulting in shortfall of 802 MW in capacity addition to the end of March 2013. The shortfall was mainly due to delay in completion of the projects planned. This resulted in increased load shedding or purchase of power through short term arrangements.

We noticed that while the Company made plans to meet its entire demand without any procurement from short term arrangements, the Company had to resort to short term purchase of 2361.93 MUs at an average cost of ₹ 4.86 per unit during the period from 2008-09 to 2012-13. We observed that the average cost per unit of power procured through long term basis during the above period was ₹ 3.64 per unit.

The Principal Secretary (Energy), during exit conference in December 2013, stated that the responsibility of timely execution of the projects is entirely that of the concerned IPPs and the GoMP or Company has a very limited role. He further stated that the shortfall in long term procurement with reference to plan might have resulted in resorting to load shedding etc. and the short term power purchases were primarily to meet peak demand and therefore should not be linked to shortfall in procurement on long term basis.

The fact however remained that the Company had to resort to short term procurement at higher cost, though no such procurement was planned. Besides, if supply had materialized through long term PPAs as planned, the Company would have at least been able to reduce its short term purchases.

Delay in completion of Shri Maheshwar Hydel Power Project

2.1.8.2 PPA between the erstwhile Madhya Pradesh State Electricity Board (Board) and Shri Maheshwar Hydel Power Corporation Ltd (SMHPCL) was signed in November 1994, which was further amended in September 2005 due to non-achievement of financial closure¹¹. As per the terms and conditions of PPA, the scheduled Commercial Operation Date (COD) was March 2010 and extended to October 2012 due to force majeure conditions. However, the COD has so far (December 2013) not been achieved in the project.

The PPA, as amended, provides for termination of the contract in the event of failure on the part of IPP in achieving COD as scheduled.

We observed that the project cost, which was estimated at ₹ 736 crore in 1993 rose to ₹ 3993 crore in 2011. The Company estimated in October 2011 that the tariff¹² would increase from ₹ 1.51 per unit to ₹ 8.21 per unit due to increase in project cost. We further observed that the expenditure incurred on the project till March 2012 was ₹ 2917.70 crore, representing 73 per cent of the estimated project cost. Thus delay in the project might result in further increase in the overall

¹¹ Execution of all Financing Agreements required for Power Station.

¹² Average fixed and variable cost over the entire term of the PPA adjusted for inflation.

project cost and tariff. In spite of the defaults and non-achievement of COD by the IPP, the Company has not terminated the PPA.

The Government replied (October 2013) that the proposal for financial restructuring of the project was under consideration and it has been decided that a committee would be formed by the Ministry of Power (MoP), GoI to facilitate a decision regarding the tariff for power to be produced from the project.

The fact remains that further delay in commissioning of the project would increase the project cost leading to higher tariff as already estimated by the Company. The Principal Secretary (Energy) in exit conference agreed to review the case and take necessary action to protect the interest of the State.

Contract for purchase of power from an expensive source

2.1.8.3 The Company entered (16 January 2007) into a Power Sale Agreement (PSA) with PTC for purchase of 100 MW power, which had a back to back procurement arrangement (August 2005) from the 1100 MW gas based power project with Torrent Power Generation Limited (Torrent).

As per the provisions of the PPA between PTC and Torrent, Torrent was to ensure fuel supply to meet the contracted capacity of 100 MW. Torrent had tied up for 4.2 Million Metric Standard Cubic Meter Per Day (MMSCMD) (for 77 per cent of capacity) of gas as against total 5.45 MMSCMD of gas required for the project. As Torrent could not enter into long term arrangement for supply of remaining 1.25 MMSCMD (23 per cent) of gas, it sourced the same from open market. Torrent intimated (November 2011) PTC about the reduction in linkage of gas from existing long term sources also and requested permission to procure the remaining gas from spot market. As it would increase the weighted average Energy Charges Rate (ECR) from ₹ 2.70 to ₹ 3.55 per Kwh, the Company decided (November 2011) to procure only 77 per cent of contracted capacity from Torrent. Thus, due to failure on the part of the Company to insert a clause for long term fuel supply arrangement, the Company had to pay idle capacity charges¹³ to the extent of ₹ 66.77 crore during the period from November 2011 to March 2013 (*Annexure-2.1.3*).

Failure on the part of the Company to insert a clause in PPA for long term fuel supply arrangement, resulted in payment of idle capacity charges of ₹ 66.77 crore.

Thereafter, the Company entered (April 2012) into another agreement with PTC to purchase 35 MW power from the 382.5 MW gas based expansion project of Torrent based on PPA (April 2012) between PTC and Torrent.

We observed that at the time of entering into subsequent agreement for purchase, the Company was already aware of the problems of insufficient availability of gas faced by the IPP and was already paying idle capacity charges. Therefore, entering in to subsequent agreement for purchase of 35 MW power from the gas based project when the IPP had not secured long term gas linkage lacked justification.

The Government replied (October 2013) that there was a demand gap of around 2000 MW between off-peak and peak hours and as gas plants were suited to cope

¹³ Generation Capacity not utilised to full extent.

with such instant variation, reserving capacity from such plants was desirable. During exit conference, the Managing Director stated that supply of power from 1100 MW project were reasonable for a gas based power plant meant for supplying peak power, till the signing of agreement for purchase of 35 MW from the expansion project.

The reply is not acceptable as the Company was well aware about the worsening situation of gas market at the time of entering into agreement in April 2012 and the Company was paying idle capacity charges from November 2011 due to non-availability of sufficient long term gas linkage. Reserving capacity from gas based plants on the ground that it was meant for supplying peak power is not justified as the Company had contracted for 24 hour supply for a period of 25 years and not for supply during peak period.

Procurement of power through PPAs

2.1.9 The GoI has issued (January 2005) detailed guidelines for tariff based bidding process for procurement of power competitively except in cases of expansion of existing projects or State owned projects etc. As per clause 5.1 of the Tariff Policy issued by the GoI in January 2006, all the future requirements of power should be procured competitively by Distribution licensees.

GoMP notified Madhya Pradesh (Investment in Power Generation Projects) Policy 2010 (Power Policy) for procuring power from IPPs that are establishing the power stations in the State through MoU route.

We noticed that out of 20 PPAs signed for total contracted capacity of 3365.5 MW of Thermal Power during 2006-07 to 2012-13 (*Annexure-2.1.1*), the capacity contracted through competitive bidding was only 4.46 *per cent* from one bidder during 2010-11 at a levelised tariff¹⁴ of ₹ 2.45 per unit. After 2010-11, the Company did not initiate any action for procurement of thermal power through competitive bidding. Instead, the GoMP/ Company signed 22 MoUs with IPPs during the period subsequent to the date of notification of Power Policy till March 2013. Audit findings on the inadequacies in operationalisation of the PPAs are discussed in succeeding paragraphs.

2.1.9.1 Deviation from MoU for procurement of concessional power

In pursuant to the terms of MoU signed by GoMP in August 2007, the Company entered (January 2011) into a PPA with BLA Power Private Ltd. (BLA) for supply of 'tariff based' power for 20 years. In May 2011 another PPA was signed by GoMP for supply of five *per cent* of net power generated as 'concessional power'. The COD of Unit-I (45 MW) of the Project was declared in April 2012 and the Company received 13.60 MUs being the five *per cent* of net power generated as concessional power (value ₹ 3.03 crore) and 82.62 MUs tariff based power (value ₹ 37.10 crore) during the period from April 2012 to March 2013.

¹⁴ Levelised tariff means average fixed and variable cost over the entire term of the PPA adjusted for inflation.

Deviation from provisions of MoU/ IA resulted in additional expenditure of ₹ 1.53 crore and committed additional cost of ₹ 73.83 crore.

On scrutiny of records, we observed that GoI had allotted a coal block in June 1996 for captive dispensation¹⁵ to BLA Industries Limited, a sister company of the IPP. GoMP granted (May 1998) a mining lease for the coal block. BLA entered into an agreement with BLA Industries Limited for supply of coal from the coal block to the power project in April 2011. In terms of the MoU, if the IPP was to obtain fuel supply for the project from captive coal block, the GoMP/ Company would be eligible for concessional power of 7.5 per cent of the net generated power from the project. Though at the time of signing of PPA for concessional power, the fuel linkage from the coal block allotted as captive dispensation to the IPP's sister company was already in existence, GoMP did not insist on supply of 7.5 per cent concessional power. This had resulted in foregoing two and half per cent of concessional power and consequential additional expenditure of ₹ 1.53 crore¹⁶ to the Company for the period from April 2012 to March 2013. Besides, the committed additional cost during remaining agreement (PPA) period of 19 years amounted to ₹ 73.83 crore¹⁷ at current tariff.

The Government stated (October 2013) that coal mines allotted to BLA Industries Ltd. by Ministry of Coal (MoC), GoI in May 1998 did not specify captive use for generation of power by BLA.

The reply is not acceptable. MoC, GoI's letter September 2012 clarified that coal mine allotted to BLA Industries Limited was for Captive Dispensation. Further, in exit conference, it was stated that the Company requested IPP to provide 7.5 per cent of concessional power, which was not agreed to by the IPP. As BLA had been consuming the coal extracted from the captive mine allotted to its sister Company in the state of MP, the GoMP/ Company should have effectively negotiated for 7.5 per cent of net generated power at variable cost as per provisions of MoU.

2.1.9.2 The GoMP entered into the MoU with Reliance Power Limited, Mumbai (RPL) in September 2007 for setting up 6X660 MW Thermal Power Project by RPL which was to remain in force for a period of one year and the Government may extend for such further period, as may be mutually agreed upon. As per MoU, the GoMP/ Company was entitled to procure 5/ 7.5 per cent concessional power and 30 per cent tariff based power for a period of 20 years. We observed that the GoMP/ Company had not signed PPA with RPL so far (July 2013). We further noticed that the validity period of MoU with RPL had lapsed in June 2010. We also noticed that MoU did not contain any protective clause to ensure that it does not lapse if there was delay in signing of PPA by the IPP. Absence of such clause resulted in RPL getting the requisite assistance¹⁸ for the project from Government without corresponding benefits to the State.

¹⁵ Captive Dispensation means coal extracted from the mine allocated may be utilised for cement, steel, power plant etc. which does not require rail transportation.

¹⁶ 6.80 MUs (13.60/2 x ₹ 2.26 (Avg. total cost at tariff rate ₹ 4.49 per unit – Avg. variable cost ₹ 2.23 per unit)

¹⁷ (45 MW x 85% PAF x 2.5% Variable Portion x 19 Years x 365 Days x 24 Hours x 1000 Units x ₹ 2.26 per unit) + (45 MW x 85% PAF x 2.5% Variable Portion x 20 years x 365 days x 24 hours x 1000 units x ₹ 2.26 per unit).

¹⁸ The GoMP will facilitate the Company in land acquisition, water allocation, coal linkage, captive coal block allocation, statutory and other clearances required for Central and State laws for implementation of the project.

In exit conference, the Principal Secretary (Energy) stated that the matter of allocation of coal was sub judice in the Honourable Supreme Court and the IPP may come forward for signing of PPA in case of decision in favour of IPP. He assured that in case of non-signing of PPA by the IPP, the department would move the Government to withdraw the facilities provided to IPP as per the terms of MoU.

The fact remains that till date GoMP has not been able get the PPA signed to safeguard the interest of the State and the MoU has lapsed.

Procurement of Power through bidding process

2.1.9.3 MoP, GoI issued (January 2005) guidelines for procurement of power through competitive bidding on long term basis as per the provisions of Section 63 of the Electricity Act 2003. The guidelines specify that procurement of power by bidding can be through Case-1¹⁹ and Case-2²⁰ mechanisms.

The Company under Case-1 for supply of capacity up to 2000 MW of power on long term basis invited bids in June 2006. Reliance Power Limited, Mumbai (RPL) after negotiation, agreed (April 2008) to supply 1241 MW at levelised tariff of ₹ 2.45 per unit from its Chitrangi Power Project in MP. The Company had also entered into a MoU²¹ with RPL for supply of 1188 MW of tariff based power in September 2007 from the same project.

In October 2010, the Company requested RPL to sign the PPA for the 1241 MW power offered through bidding process. RPL however informed the Company that it would be willing to sign the PPA, only if the Company foregoes its right to obtain 1188 MW of tariff based power under MoU obligation. The Company informed (December 2010) RPL that the offer against bidding process (Case-1) was independent and had no relation with the 'tariff based' power offered through MoU route. RPL had however not signed PPA so far (July 2013). Delay in signing the PPA and implementation of the Project would deprive the Company of getting 1241 MW of power at low cost²² for 25 years besides restricting/ derailing the process of procurement through competitive bidding route.

We further observed that while RPL was not coming forward for signing PPA, they were extending the validity of their bid and Bank Guarantee (BG) for ₹ 37.50 crore towards bid bond from time to time. The Company has however not forfeited the bid bond by encashing the bank guarantee.

The Government replied (October 2013) that RPL had not signed the PPA due to non availability of full linkage coal and non achievement of financial closure of

In spite of not signing PPA by IPP the Company had not forfeited the Bid and Bank Guarantee for ₹ 37.50 crore.

¹⁹ Where location, technology or fuel is not specified by the procurer.

²⁰ For hydro power projects, load center projects or other location specific projects with specific fuel allocation such as captive mines available, which the procurer intends to set up under tariff based bidding process.

²¹ The Government or its Nominated Agency shall have first right to purchase power up to 30 per cent {1188 MW (3960 MW * 30 %)} of the aggregate capacity of generating units for a period of 20 years at the rate to be approved by Appropriate Electricity Regulatory Commission (AERC).

²² @ ₹ 2.45 per unit against the average cost of ₹ 3.64 per unit for power procured through long term sources during 2008-09 to 2012-13

the project. It was further replied that after invoking bank guarantee, it may not be possible to force RPL to sign the PPA. The reply is not relevant as successful bidder is required to sign the PPA even if the coal linkage and financial closure had not been achieved. The Company should consider the feasibility of invoking bank guarantee for the failure in signing PPA, while reserving its right to enforce the signing of PPA.

PPAs under Non-Conventional energy sources

2.1.10 Ministry of New and Renewable Energy (MNRE)²³ issued (September 1992/ November 1994) guidelines for procurement of power from Non-Conventional Energy sources.

Renewable Energy Purchase Obligation

2.1.10.1 MPERC through its Regulation (Co-generation and Generation of Electricity from Renewable Sources of Energy) (Rev1) 2010 (November 2010) specified the minimum quantum of electricity to be procured from the renewable sources by all the Obligated Entities²⁴ {Renewable Purchase Obligation²⁵ (RPO)}. The targets fixed vis-à-vis actuals during the years 2011-12 and 2012-13 for solar and non solar RPOs are as follows:

Year	Actual Annual Energy Requirement (MUs)	RPO of Solar power				Short fall in (per cent)	RPO of Non Solar Power				Short fall in (per cent)
		In (per cent)	In (MUs)	Actuals	Shortfall (MUs)		In (per cent)	In (MUs)	Actual	Shortfall (MUs)	
2011-12	40410	0.40	162	0	162	100	2.10	849	540	309	36.39
2012-13	44590	0.60	268	6	262	98	3.40	1516	699	817	53.89

Source: Compiled from Company records

It is seen that there was a shortfall of 36.39 *per cent* in procurement of Non-solar power against the RPOs during the year 2011-12, which increased to 53.89 *per cent* in 2012-13. In respect of Solar RPOs, there was 100 *per cent* and 98 *per cent* shortfall in meeting the targets during 2011-12 and 2012-13 respectively. We further noticed that shortfall in meeting the RPOs was mainly due to shortfall in entering into PPAs for solar and non-solar power.

Procurement of Power from Non conventional sources

2.1.10.2 During the period 2007-08 to 2012-13, the Company entered into eight PPAs with an installed capacity of 205.25 MW for procurement of Solar based power, out of which two PPAs with an installed capacity of 125 MW were entered through bidding process and the remaining six PPAs with installed capacity of 80.25 MW through MoU route. Similarly, Two PPAs with installed capacity of 2.4 MW and 86 PPAs with installed capacity of 286.06 MW were entered into for

²³ Previously known as Ministry of Non-Conventional Energy Sources.

²⁴ Company is the obligated entity because the power is being purchased on behalf of three Discoms in the State.

²⁵ It is minimum percentages of the total power that electricity distribution companies need to purchase from renewable energy sources.

procuring bio-mass and Wind Electric Generators (WEGs) based power through MoU route.

In February 2012, the Company initiated bidding process for procurement of 200 MW solar power on long term basis. The tariff for solar power in terms of MPERC tariff orders at the time of invitation of tenders was ₹ 15.35/ 13.94 per unit. After evaluation of bids, the Company entered into PPAs in October 2012 with Alfa Infraprop Limited and Welspun Solar Madhya Pradesh Private Limited, for supply of 20 MW and 105 MW solar power respectively at their quoted tariff of ₹ 7.90 per unit and ₹ 8.05 per unit respectively. The tariff obtained through bidding was thus lower by 48.53 and 42.25 *per cent* of the MPERC determined tariff.

We noticed that out of 98 PPAs entered into during 2007-08 to 2012-13, 96 PPAs were entered through MoU route against the spirit of Tariff Policy 2006²⁶ and guidelines for bidding issued by MNRE, GoI, and thus lost an opportunity to obtain lower prices as seen in above two PPAs.

The Government stated (October 2013) that the tariff determined by MPERC for Wind and Biomass projects was not very high as not much enthusiasm was shown by generators on these projects. It further stated that availability of renewable power to the extent of RPO had not yet been achieved and in the circumstances, exploration of possibility to get power at rates less than MPERC tariff was not feasible. Further during the exit conference it was stated in respect of non solar based plants that the MNRE has not issued specific guidelines for purchase through bidding.

Reply is not acceptable as the Company had so far not initiated the process of bidding to determine the cost for bidding based power. The fact that the cost of power through bidding in conventional and solar projects was less than prescribed tariff decided by MPERC²⁷ indicate that the Company might have obtained lower rates if it had opted for procurement through bidding. In bidding process, it would be open to many generators resulting in lower rates as seen in the above two cases. Further there was no restriction in attempting procurement of power through bidding process for wind/ bio-mass plants.

Deviations in the provisions of PPAs/ Model PPAs

2.1.11 The Company is required to execute PPAs on long term basis for procurement of tariff based and concessional power as per the Model PPAs approved (February/ June 2011) by GoMP.

Commercial Operation Dates

2.1.11.1 Commercial Operation Date (COD) is the date on which the power supply would start from any unit of the power project. Timely completion of the works is the essence of any agreement. Thus, fixation of COD in the PPA would be a vital aspect as the power supply at a contracted capacity would start from this

²⁶ All the future requirement of power should be through competitive bidding route.

²⁷ MPERC determined the levelised tariff for entire life period of the Projects.

date. We noticed instances where scheduled CODs were delayed due to delay in providing the infrastructure and other facilities by GoMP/ Company. The delay in COD would result in either procurement of power at higher rates through short term sources or load shedding. The cases of delay in scheduled COD and non-levy of Liquidated Damages (LDs) are discussed below:

Delay in providing land and other clearances by GoMP

Delay in facilitating handing over of land and other clearances etc., by the GoMP/ Company, the scheduled COD was not achieved which had resulted in depriving of availing cheap power from Sasan and a consequential potential loss of ₹ 1252.46 crore.

2.1.11.2 The Company entered into a PPA with Sasan Power Limited (Sasan) in August 2007 for 1485 MW power out of the total capacity of 3960 MW of Sasan UMPP. In terms of the PPA, the Company was required to hand over possession of land for the power station and site clearance from Ministry of Environment and Forest etc. The PPA also provided that the Power producer would have the option to prepone COD. Sasan exercised the option to prepone the COD, which was agreed to by the Company and accordingly a supplementary agreement was entered into between the two parties in October 2008.

The details of scheduled CODs as per PPA, preponement of CODs at the request of Sasan and the revised CODs due to default of the Company are given in the ***Annexure-2.1.4***. Sasan requested (July 2008) the Company to provide land and forest clearances in terms of the supplementary agreement.

Citing delay in meeting the obligations on handing over of land (9 months), forest clearance (21months), interconnection/ transmission facilities by GoMP/ Company as per the terms of the PPA etc., Sasan requested the Company to postpone the CODs. The Company accepted (September 2010) the request of Sasan and accordingly revised the CODs. As a result, the Company was deprived of cheap power from Sasan for a period of 15 months resulting in potential loss of ₹ 1252.46 crore on account of purchase of power from other sources during the corresponding period as detailed in the ***Annexure-2.1.5***.

The Government stated (November 2013) that there was no loss as the project was completed as per the originally scheduled COD and that the delay cannot be attributed to delay in providing land as 95 *per cent* of the land required for the project was already made available to the Sasan on time. Further during exit conference Managing Director stated that Sasan attempted to aggressively bring forward the commissioning date, which did not materialize as planned.

The reply is not acceptable as the Company accepted the plea of Sasan that the COD was delayed due to Company's failure in meeting its obligations and accordingly revised the COD. Further Unit I was delayed by four months from original COD and Unit II, originally scheduled for COD in December 2013 had not achieved COD till January 2014.

Delay in commissioning

2.1.11.3 The Company entered into a PPA (January 2011) with Bina for purchase of concessional power (five *per cent*) and tariff based power (65 *per cent*) from

their 1250 MW Thermal Power Project²⁸ to be established at Sirchopi, Tahsil Bina, District Sagar, Madhya Pradesh. In terms of PPA for tariff based power, Bina was liable to pay LD for delay in achieving COD as determined in the PPA.

The Bina sought (January 2012) four months extension for the COD of Unit-I (Phase-I) due to unprecedented heavy rainfall. Company accepted to the request and accordingly the COD was revised to July 2012. Bina achieved COD with a delay of 30 days from the extended COD. No LD was however imposed for delay beyond the period of extension granted by the Company.

Similarly, extension for COD of Unit-II (Phase I) sought by Bina was accepted by the Company and COD was revised to February 2013. Bina however achieved COD on 7 April 2013 with delay of 37 days. In this case also, no LD was imposed by the Company for delay beyond the extension granted.

The Company failed to impose LD of ₹ 10.89 crore for the delay as per provisions of PPA.

Thus, delay in achieving COD by the Developer for Unit-I & II resulted in delay in availing energy from the units. Besides, the Company failed to impose LD of ₹ 10.89 crore for the delay as per provisions of PPA.

We further observed that the Company did not include the clause of LD in the PPA for concessional power. As a result, the Company could not impose LD for the delayed CODs.

The Government stated (November 2013) that an agreement was reached not to levy LD as the Company had also defaulted in providing letter of credit (LC) on time in terms of the PPA for which LD amounting to ₹ 98.60 crore was payable by the Company.

Reply is not correct as the penalty for not providing LC was payable only if there was delay in commissioning test due to default of the Company. We did not find any evidence that the commissioning test was delayed due to failure of the Company to provide LC and thus the Company was not liable for any penalty.

Non-recovery of Liquidated Damages for short supply of power

2.1.11.4 As per PPA with Bina, the Developer was liable to pay LD to the procurer at the rate of ₹ 10000 per day/ MW for delay of 60 days and ₹ 15000 per day/ MW for delay in making the required availability of contracted capacity. However, the Developer was given option to supply energy from alternative generation source at par with agreed rates up to the period of 12 months.

In spite of short supply of 6719.60 MW, the Company did not levy LD of ₹ 6.72 crore.

Unit-I of Phase-I (250 MW) started power supply from 31 August 2012. We noticed that 26920.32 MW was required to be supplied by Bina as per PPA for the period from 31 August 2012 to 31 March 2013. The Developer however supplied only 20200.92 MW due to difficulties in stabilisation of the plant. LD of ₹ 6.72 crore leviable in terms of the PPA for the short supply of 6719.60 MW was not levied by the Company.

²⁸ Consists of two phases i.e. Phase-I for 500 MW (2X250 MW) and Phase-II for 750 MW (3X250 MW).

The Government stated (November 2013) that the Company would source the shortfall in supply by the IPP as and when the power position so warrants. In exit conference the Principal Secretary (Energy) stated that Bina was a revival project and it was a conscious decision of the Government to give relief to the Developer to make it possible for the Project to be revived. Reply confirms the fact that LD was not levied as provided in the PPA and any relief beyond what is provided for in the PPA amounted to undue benefit to the developer and had an impact on the cost of procurement of power by the State.

Additional expenditure on Operation & Maintenance Expenses

2.1.12.1 PTC India Limited(PTC) entered (August 2005) into a PPA with Torrent Power Generation Ltd. (Torrent) for purchase of power of 100 MW initially for five years and to be reduced to 50 MW for ten years thereafter from their gas based Thermal Power Project (1100 MW) established in Gujarat State. In January 2007, PTC entered into an agreement with the Company for supply of power of same capacity. As per the agreement entered into by the Company with PTC, the PPA between PTC and Torrent was an integral part of the contract.

The Company did not appeal to CERC against the additional burden without any visible benefits, resulting in additional expenditure of ₹ 25.69 crore and committed additional expenditure of ₹ 8.39 crore.

Tariff for power from the project was to be determined by CERC on an application/ petition filed by Torrent in terms of the PPA. Based on the petition filed by the Torrent in June 2009, CERC approved the Capital Expenditure and determined the tariff in January 2010. In its petition, Torrent claimed O&M expenses, which were higher than the normative O&M expenses of ₹ 14.80 lakh/MW to ₹ 18.49 lakh/MW fixed by CERC for the period between 2009-10 and 2013-14. Higher claim was made by Torrent on the plea that advance class machine/ technology was used in the power plant, which would increase the plant availability from 85 to 88 per cent. The CERC, considering the plea, relaxed the norms by invoking its power²⁹ under CERC (Terms and Conditions of Tariff) Regulations 2009 and approved O&M expenses at rates between ₹ 26.70 lakh/ MW and ₹ 29.68 lakh/ MW, which was 60 to 69 *per cent* higher than the norms.

The Company accepted the additional burden of ₹ 25.69 crore for the period from April 2011 to June 2013 and committed additional expenditure of ₹ 8.39 crore for the remaining period of nine months (July 2013 to March 2014).

We observed that the higher plant availability would result in higher generation and as a result higher revenues to the developer without any corresponding benefits to the Company, which had to pay higher O&M expenses. The Company however did not approach CERC for sharing of benefits accruing to the developer. During the exit conference the Principal Secretary (Energy) accepted the facts and stated that the Company would consider the feasibility of filing an appeal against the CERC's order.

²⁹ The CERC may relax any of the provisions of these Regulations on its own motion or on an application made by an interested person.

Capping of Fixed Charges

2.1.13 The Annual Fixed charges were determined based on the financial parameters outlined in MPERC/ CERC and the rate fixed in the PPAs should not exceed in any case.

2.1.13.1 According to the PPA between Torrent and PTC, based on which agreement for purchase of power between Company and PTC was drawn, the fixed charges would not exceed as initially agreed between the parties. As per Schedule-E annexed to the PPA between Torrent and PTC, the annual fixed charges for the period commencing from the date of COD of the Project to fifteenth anniversary of the COD would be ₹ 0.83 per unit.

Torrent, however, requested PTC to increase the fixed charges due to increase in the rate of interest on borrowing, working capital and increase in O&M expenses etc. and PTC accordingly requested (June 2009) the Company either to increase the tariff from ₹ 0.83 to ₹ 1.12 per unit or to accept the tariff as approved by CERC. The Company sought (September 2009) opinion on the PTC's request from its legal advisor, who opined (November 2009) that the Company should insist for enforcement of original PPA with capping of fixed at ₹ 0.83 per unit. The Company without waiting for receipt of legal opinion, acceded to the demand of PTC (October 2009).

Failure of the Company to insist on terms agreed in the PPA/ PSA resulted in additional expenditure of ₹ 24.51 crore towards fixed charges and committed to incur an additional cost of ₹ 145.96 crore.

CERC determined (January 2010) the fixed charges at ₹ 1.08 for the period from March 2011 to March 2013 and the Company had started paying fixed charges accordingly from March 2011.

Thus, due to failure of the Company to insist on terms agreed in the PPA/ PSA, the Company had to incur an additional expenditure of ₹ 24.51 crore (*Annexure-2.1.6*) towards fixed charges for the period from March 2011 to March 2013 and also committed to incur an additional cost of ₹ 145.96 crore (*Annexure-2.1.6*) for the remaining period up to 15th anniversary of the COD as envisaged in the PPA.

During the exit conference the Principal Secretary (Energy) stated that the rates of power shall be decided under Section 62 and 63 of the Electricity Act 2003 and there was no provision for capping of fixed cost in the Electricity Act 2003. Reply is not acceptable as the Company's own Legal advisor had opined that Company should insist for enforcement of original PPA with capping of fixed charges and no records were produced to Audit to show that capping of fixed charges was against the provisions of the Electricity Act.

Commission paid to an intermediary for inter-state power purchase

2.1.14.1 The Company entered four agreements with PTC for procurement of power, based on the PPAs between PTC and IPP. Thus, the PPAs were integral to the agreements with PTC. The details of the agreements entered are detailed in *Annexure-2.1.7*.

It could be seen from the *Annexure-2.1.7* that the Company has to pay trading margin to the PTC for power supplied from IPPs through the agreements. Till

May 2013, the IPPs have supplied 2033.43 MUs and the Company paid ₹ 10.17 crore towards trading margin to PTC.

Had the Company considered the option to enter into PPA directly with IPPs established outside the State, it could have avoided the payment of ₹ 10.17 crore towards trading margin to PTC and prospective avoidable payment of trade margin of ₹ 875.48 crore.

We observed that there was no provision/ condition in any of Regulations/ Acts/ Notifications compelling the Company to have PPAs from outside State through PTC. It could therefore have considered the option to enter into PPA directly with IPPs established outside the State as it did in the case of Jharkhand Integrated Power Limited in September 2008 and avoided the payment towards the trading margin to PTC. The prospective avoidable payment on trading margin to PTC worked out to ₹ 875.48 crore for the remaining tenure of the agreements as detailed in *Annexure-2.1.8*.

The Government stated (November 2013) that at the time of execution of the agreements with PTC, the financial position of the Company was not sound and Developers were not willing to enter into agreement with the Company directly, as PTC was willing to supply power, agreements were executed with PTC for procurement from IPPs on long term basis.

The reply is not acceptable as there was no evidence to show that the Company attempted but failed to enter into PPAs due to its financial position. As IPPs within the State did not have reservations in entering into PPAs with the Company, the Company would have been able to enter into interstate PPAs also, if it had intended to. This is further evidenced by the fact that the Company entered into 117 PPAs (including one PPA entered for procuring power from outside the State) with IPPs without any intermediary and only four agreements were entered into through PTC.

Miscellaneous

Non-inclusion of clause relating to sharing of penalties levied by the Developers on the fuel suppliers for short supply of fuel

2.1.15.1 Bina Power Supply Company Limited entered into Fuel Supply Agreement (FSA) with Central Coalfields Limited (CCL) / South Eastern Coalfields Limited (SECL) for procurement of coal for its 1250 MW thermal power project. According to the FSA with CCL/ SECL were liable to pay compensation to the Bina, if they deliver the coal below Annual Contracted Quantity (ACQ). We observed that Bina received coal from CCL and SECL below the ACQ due to which Bina had to purchase the deficit quantity of coal from open market/ through imports. As a result, the rate of energy charges increased from ₹ 2.708 per unit to ₹ 3.144 per unit during September 2012 to January 2013. Due to higher rate of energy charges, the Company decided to draw less power than contracted from February 2013 and paid idle capacity charges to the extent of ₹ 36.38 crore (*Annexure-2.1.9*) based on 100 per cent of the contracted capacity during the period from February to May 2013.

Further, we observed that while the Company allowed Bina to procure coal from open market/ imported coal to meet shortfall in supply and also paid idle capacity charges, the Company had not included an enabling clause for sharing of compensation received by Bina from the fuel supplier as per the terms of FSA.

Due to higher cost of energy charges, the Company scheduled lower capacity than the contracted capacity and paid idle capacity charges to the extent of ₹ 36.38 crore.

The Government stated (November 2013) that the credit from fuel supplier was received by the IPP for grade-slippage, oversized stones, short delivery etc. was already being adjusted in landed price of primary fuel and therefore, non-inclusion of this clause would not affect the energy charges annually. It was also stated that there was a three year moratorium on compensation from CCL to Jaypee Bina. The reply of the Government is not relevant as FSA did not cover short supply with reference to agreement quantities. Further, according to FSA, for short supply/ lifting, a separate claim has to be preferred for compensation and there was no evidence from the record made available to audit that such compensation was adjusted by Bina in the bills. Further, the moratorium on adjustment of shortfall of supplies safeguards the interest of CCL and the IPP, but the additional cost on open market purchase/import of coal due to shortfall in supply will have to be suffered by the procurer. Therefore, the Company should take necessary steps to insulate it from the burden arising from FSA by suitable changes to the PPA, which was agreed to by the Managing Director.

Excess Land Allotment

2.1.15.2 As per PPA for procurement of grid connected solar power on long term basis, land was to be allotted/ acquired at the rate of two hectares per MW for Solar Photo Voltaic (PV) projects. We observed that in case of Acme Solar Energy Private Limited, as against 50 hectares to be allotted, 74.914 hectares was allotted, whereas in case of Welspun Solar M.P. Limited, as against 50 hectares to be allotted 98.279 hectares was allotted by GoMP for their 25 MW each capacity Solar PV Projects. Thus, land to the extent of 73.19 hectares was allotted in excess of requirement.

Similarly, as per CEA Guidelines 2007, the land required for 6X660 MW Thermal Power Station at Chitrangi with indigenous coal was 3280 acres (0.83 Acres/MW), against which, 3466 acres were allotted by GoMP to RPL, resulting in excess allotment of 186 acres.

The Government stated (November 2013) that the State Nodal Agency for new and renewable energy viz., MP Urja Vikas Nigam provides necessary support to facilitate land acquisition for solar projects and total land to be allotted for solar developer depends on the terrain of the land as it would not be possible to install solar panels on undulated land. In case of the thermal power project, Government stated that land requirement was dependent on the location of the associated auxiliaries like location of the reservoir, distance of coal mine from plant etc. Reply confirms the fact that land was allotted in excess of requirement for the Projects as per PPA and CEA guidelines. Allotment of land in excess of the provisions results in higher cost of project and resultant higher tariff.

Monitoring and Control

2.1.16 Energy bills would be raised by the IPPs on the Company on the seventh day of each month basis for the concessional and tariff based power supplied during the previous month. On receipt of power bills from the IPPs, the Company scrutinises the bills, passes them and makes payment after pre-audit. On scrutiny

of the bills passed and payments made by the Company, the following deficiencies were noticed in Audit:

2.1.16.1 There was no mechanism for technical verification of landed cost of coal/ gas, Gross Calorific Value (GCV) of primary fuel and secondary fuel being used and claimed as energy charges by the IPPs in their bills, either by the Company or a third party Agency. In the absence of the said mechanism, the possibility of payment of un-authenticated claims cannot be ruled out.

The Government stated (November 2013) that after amendment to the regulation by CERC in December 2012, the information was being submitted by the generators along with the monthly bills. The Managing Director during the exit conference stated that the Company was trying to improve the procedure for payment of power procured and verification of landed cost of coal, GCV etc.

The reply confirms that the accuracy of bills of IPPs was not being verified to prevent the possibility of payment in excess of due.

2.1.16.2 For PPAs entered into with the IPPs for procurement of tariff based power, rebate clause for payment of any Bill before Due date was included, whereas no such clause for rebate was included for concessional power. In two of the eight PPAs³⁰ for concessional power, supply had commenced. We noticed that the Company in certain cases, had paid bills in advance of the due date for concessional power by one to 30 days.

The Government stated (November 2013) that the model PPA for concessional power specifically excluded the rebate clause. During exit conference, the Managing Director stated that the Government did not consider it appropriate to provide for Rebate clause, since only payment made for concessional power was for fuel, which was essentially reimbursement for the fuel used in the plant.

Reply is not acceptable as the Company/ Discoms are paying interest on loans taken for working capital needs and therefore payment of bills before due date was not in the financial interest of the Company/ Discoms when there is no rebate clause for early payment. Hence, the Company should either make payment only on the due date or should consider inclusion of rebate clause in concessional power PPA to reduce its financing cost.

2.1.16.3 In terms of a PPA entered into with Bina for procurement of 65 per cent of the installed capacity of power, rebate was to be allowed if the payment was made within 21 days from the date of receipt of bill as compared to 30 days allowed in model PPA. Due to changes in PPA with reference to model PPA, the Company had foregone a rebate of ₹ 53.02 lakh on rebate during the period from December 2012 to May 2013.

The Government stated (November 2013) that being a revival project, it was agreed to provide payment within 21 days instead of 30 days. As the payment period and rate of rebate considered for the purpose of tariff was not as per model PPA, entering into PPA with terms beneficial to the IPP resulted in foregone

Due to changes incorporated in the Rebate Clause, the Company had foregone an amount of ₹ 53.02 lakh.

³⁰ (i) BLA Power Pvt. Ltd. (ii) Bina Power Supply Company Ltd.

rebate and the fact that this was a revival project was not relevant. During exit conference the Principal Secretary (Energy) agreed with audit view and directed the Company to consider this aspect at the time of filing petition before MPERC for tariff fixation in future.

Payment of surcharge due to default in making timely payment

2.1.16.4 As per provisions of PPAs entered into with IPPs for procurement of non-conventional source of power, when payment of any bills payable under the Agreement was delayed by the Company beyond due date, Late Payment Surcharge (LPS) would be payable by the Company to IPPs at prescribed rates.

Due to default in making timely payment of energy bills in respect of 12 IPPs, the Company incurred LPS of ₹ 6.02 crore.

Test check of energy bills submitted by the IPPs during the period from April 2012 to June 2013, indicated that the Company had defaulted in making timely payment of energy bills in respect of 12 IPPs and incurred LPS amounting to ₹ 6.02 crore (*Annexure-2.1.10*).

The Government stated (November 2013) that the receipts of the Company had always been short of payment requirements and therefore delay in payments could not have been avoided. It further stated that LPS has not been paid to any IPP except Manganese Ore Industries Limited. The fact however remains that the Company had paid bills in advance of the due date to IPP as commented in para 2.1.15.2 *ibid* and therefore the reply that the Company could not have avoided delay in payments was not borne out of facts.

Payment of LPS due to deviation from norms

Deviation in the norms for number of days allowed for payment of energy bills resulted in avoidable LPS of ₹ 94.97 lakh

2.1.16.5 On scrutiny of PPAs, it was noticed that the Company had agreed for payment period as 30 days instead of 60 days as prescribed in MPERC (Terms and Conditions for Determination of Generation Tariff) Regulations 2009/ CERC (Terms and Conditions of Tariff) Regulations 2009. As a result, the Company had incurred an avoidable LPS of ₹ 94.97 lakh in respect of four PPAs, from which power supply had started. Besides, by adopting payment period at variance with regulations, the Company would incur additional LPS in all the PPAs during the currency of the contracts.

The Government during exit conference replied that the matter would be brought before the MPERC for factoring the reduction of due days for making payment of bills from 60 days to 30 days while determining the final tariff.

2.1.16.6 Internal Audit is an essential tool to strengthen the management by constructive appraisal of the operations including the review of internal control, policies, plans and procedures.

We observed that the Company did not have an internal audit wing and the work of internal audit was carried through Chartered Accountant firms. Scope of Internal Audit work did not include the work relating to core activities of the Company viz., billing and payments made to power suppliers, purchase of power, sale of power, letter of credit or escrow agreements entered by the Company etc, and was limited to assistance in preparation of accounting statements, statutory

compliances and other issues in connection with the Company's financial statements.

Due to narrow scope of internal audit, the work of audit committee of the Company regarding review of internal audit report and action taken thereon was also very limited.

The Statutory Auditor in his report on the Annual Accounts for the year 2011-12 opined that the scope of internal audit was insufficient and not commensurate with the size and nature of the business of the Company and needs further strengthening.

Thus, there is a need for strengthening of internal audit to address the risk areas in the changing business environment.

During exit conference, the Principal Secretary (Energy) agreed to strengthen the monitoring and control of the Company.

Conclusion

The Company failed to achieve the targeted procurement of power on long term basis. The Company deviated from MoU/ IA/ Model PPAs/ PPAs entered into with IPPs and failed to enter into agreement with RPL even after finalisation of bids.

The Company failed to insist on terms agreed in the PPA/ PSA resulting in additional expenditure towards fixed charges on procurement of power due to removal of capping of fixed charges. It incurred avoidable expenditure on commission due to procuring power through intermediary instead of procuring directly. The Company failed to include the clause relating to sharing of penalties levied by the Developers on the fuel suppliers for short supply of fuel.

The Company did not levy liquidated damages for delay in commissioning beyond the period for which extension was granted. Monitoring mechanism for processing of bills and payment procedure were deficient resulting in loss of rebate and avoidable payment of LPS. Scope of work for Internal Audit is not commensurate with the size and operations of the Company.

Recommendations

The Company needs to

- adhere to its planning in procurement of power and ensure compliance of the Guidelines/ Policy issued by Central/ State Governments from time to time;
- implement and adhere to the provisions of the Acts/ model PPAs/ PPAs;
- explore an alternative system to avoid purchasing power to meet long term power needs through power trading company;

- insert a suitable clause in the PPA to insulate it from the loss arising due to the failure of the Fuel Supplier/ IPPs in delivering/lifting the contracted quantity of fuel.; and
- strengthen its monitoring mechanism and internal audit.

2.2 Review on the working of Madhya Pradesh Laghu Udyog Nigam Limited, Bhopal

Executive Summary

Introduction

Madhya Pradesh State Laghu Udyog Nigam Limited (Company) was incorporated in December 1961 as a wholly owned Government Company to promote Small Scale Industries (SSIs) by providing marketing, financial, technical and managerial assistance. The Government of Madhya Pradesh has reserved 149 items, for preferential purchase from SSI sector of the State, through the Company only, under its Store Purchase Rules (SPR). The Company collects Service Charges/Commission from Suppliers on supplies made by the suppliers to the Government Departments, which is a prime source of its income.

Planning

Company had not prepared any promotional plan including financial plan for the development of SSI units in the State. The Company did not assess the impact of the fairs and Reverse Buyer Seller Meets. The actual achievement of business targets ranged between 80.50 and 120.51 per cent during the period 2008-09 to 2012-13. The Company could not achieve the targets fixed in MoU during the years 2009-10, 2011-12 and 2012-13. The percentage of SSIs availing the marketing assistance ranged between 0.28 and 0.49 per cent of total SSI registered with Department of Industries, GoMP.

Marketing Activity

The business of Marketing department decreased from ₹ 667.15 crore in 2008-09 to ₹ 529.60 crore in 2012-13 due to decrease in business of reserved items. The penalty deducted for delay in Government supplies amounting to ₹ 1.68 crore, till March 2012 has not been paid to Government departments. The Company did not evolve a system to verify the eligibility of SSI units with reference to Industrial Development Act for allowing proper price preference of 10 per cent to state based units over all India tender.

The Performance of other departments of the Company

The divisions of Estate and Construction Department (E&C) split up the deposit works in parts and kept the Probable Amount of Contract very proximate to ₹ five lakh and avoided publishing in news papers. The E&C Department adopted differential practice for deduction and remittance of royalty to the government exchequer. The Company failed to include an interest clause for delayed payments of bills in respect of construction of Navodaya Vidyalaya buildings

The profitability of the emporia was mainly due to inclusion of commission earned on sales of marketing items to Government Departments, agencies, bodies etc. for which marketing wing of the Company was established. In Delhi and Rewa emporia, the stock holding was more than their turnover. The Company has not framed any policy for disposal of non- moving stock. The agreements entered into for renovation of five of its emporia did not provide for levy of penalty in case of delay in completion.

The Raw Material Depot, Bhopal earned profit and Indore, Jabalpur and Gwalior Depot earned profits due to inclusion of commission from marketing of products

manufactured by SSIs. There was shortfall in lifting of iron and steel items against the quantities to be supplied by steel manufacturers, as the number of SSI units procuring iron and steel items reduced from 146 in 2008-09 to 102 in 2012-13. The procurement of coal ranged from 72.45 to 86.26 per cent against the allotment and the Company could assist only 455 coal consuming units as against total 19471 units in the State.

The turnover of the Company increased from ₹ 151.92 crore in 2008-09 to ₹ 223.05 crore in 2011-12 (46.82 per cent), while the net profit of the Company increased only from ₹ 13.18 crore in 2008-09 to ₹ 13.76 crore in 2011-12 (4.40 per cent). The profit is mainly due to income earned through interest on Fixed Deposit Receipts, while its operational activity was decreasing. The Receivables of the Company as at the end of March 2008 was ₹ 5.72 crore, which increased to ₹ 9.44 crore as on March 2012. The Company did not frame any long term investment policy to invest its surplus fund.

Manpower Management

The Company had not done reassessment of its manpower requirement.

Monitoring and Internal Control

There was no mechanism to ensure procurement of reserved items directly by the government departments which were reserved for procurement through the Company. The Company also does not have a system of verifying whether the beneficiary units were SSIs in terms of Micro Small and Medium Enterprises Development Act, 2006. The Company does not have an independent IT Cell/Wing to implement the information technology system. The Company did not have a separate internal audit wing and the internal audit work was assigned to the CA firms. The scope of internal audit is limited to physical verification of stock and preliminary checking of accounts, leaving core area of activities unaudited.

Introduction

2.2.1 The Madhya Pradesh Laghu Udyog Nigam Limited (Company) was incorporated (December 1961) as a wholly owned Company of the Government of Madhya Pradesh (GoMP) with a view to promote Small Scale Industries (SSIs) by providing marketing, financial, technical and managerial assistance. Activities of the Company include finalising rate contract for reserved items under Stores Purchase Rules (SPR) as well as non reserved items¹, civil construction works and renovation works of Government Organisations, selling handloom and handicraft items, arranging procurement of raw material² required by the SSIs, extending testing facilities³ for the products, etc. Thus, the working of Company is multi-dimensional. The Company has three Regional Marketing Offices⁴, four Raw

¹ Items which are not covered under SPR

² Iron & Steel and coal

³ mechanical, electrical, pharmaceuticals, civil works material etc.

⁴ Gwalior, Indore and Jabalpur

material depots⁵, eight Emporia⁶, eight Estate and Construction Divisions⁷ and two Testing Laboratories⁸.

To ensure the growth of Company, the GoMP fixes targets every year for various activities of the Company and signs a Memorandum of Understanding (MOU) with the Company. The GoMP has reserved 149 items, for preferential purchase from SSI sector of the State, through the Company only, under its SPR. The Company is recognised as a nodal agency not only for procurement of reserved items but also for the non reserved items not covered under SPR. In order to meet its expenses, the Company collects service charges/commission from Suppliers on the supplies made by the suppliers to Government Departments/ State Public Sector Undertakings etc. which is a prime source of income to the Company. Further, the Company earns supervision charges on the construction works executed on deposit work basis. The Company operates emporia for the sale of handloom and handicraft items.

The Management of the Company is vested in a Board of Directors (BoD) consisting of six Directors⁹ (March 2013). The Managing Director (MD) is the Chief Executive Officer and is assisted by five Chief General Managers¹⁰ followed by Deputy Chief General Managers and General Managers as per organizational chart at *Annexure-2.2.1*.

The Paid-up capital of the Company was ₹ 2.83 crore as on 31 March 2013. The Company finalised its accounts up to 2011-12 and earned profit after tax of ₹ 13.76 crore against turnover of ₹ 223.05 crore as on 31 March 2012. Against the sanctioned strength of 535 employees, 346 employees were working in the Company as on 31 March 2013.

Scope and Methodology of Audit

2.2.2 The working of the Company for the period 2003-04 to 2007-08 was earlier reviewed in the Audit Report of the Comptroller and Auditor General of India (Commercial) for the year 2007-08 Government of Madhya Pradesh. The Committee on Public Undertakings (COPU) discussed (July 2011) the Review and its recommendations are awaited. We reviewed the action taken on the assurances given by the Management before COPU and these have been incorporated under the relevant paragraphs in the present Review. The present Review, conducted during April to July 2013, assessed the performance of the Company during the period 2008-13 covering 14¹¹ of the 25 units for detailed field study selected based on its turnover.

⁵ Bhopal, Gwalior, Indore and Jabalpur

⁶ Bhopal, Gwalior, Indore and Jabalpur, Rewa, New Delhi and Kolkata (two)

⁷ Bhopal (two), Gwalior (two), Indore, Jabalpur, Satna and Raipur (now situated at Bhopal)

⁸ Indore and Jabalpur.

⁹ Six directors consisting of Chairman, Managing director, two executive (GoMP) nominated by GoMP from the executives of Commerce & Industry and Finance Department respectively and two non executive directors

¹⁰ Finance and Accounts, Emporium, Estate and Construction, Marketing, Technical and Coordination

¹¹ Regional Marketing Offices-Gwalior, Jabalpur, Indore, Mrignayni Emporia at Bhopal, Indore, Gwalior and Jabalpur, Testing lab-Indore, Estate & Construction divisions-Bhopal-I, Bhopal-II, Gwalior-I, Gwalior-II, Jabalpur and Indore

The audit methodology adopted with reference to the audit criteria consisted of scrutiny of records at the Head Office¹² and the selected units, interaction with the audited entity's personnel, analysis of data obtained from the Management Information System (MIS) with reference to audit criteria etc.

2.2.3 We explained the audit objectives to the Company during the Entry Conference held on 18 April 2013, which was attended by the Managing Director of the Company and representatives of Government. Audit findings emerging from the Review were reported (August 2013) to the Company and the State Government and discussed (November 2013) in the Exit Conference, attended by the Additional Chief Secretary (ACS), Department of Commerce and Industries, GoMP and Managing Director of the Company. The views expressed by the Management/Government in the Exit Conference and through their replies (October 2013), have been taken into consideration while finalising the report.

Audit Objectives

2.2.4 The objectives of the Review were to ascertain whether:

- Long term and short term plans were prepared to achieve the objectives of State Industrial policies and MoUs for providing assistance in procurement, financial, marketing and technical and management matters in respect of the small scale industries;
- the marketing activity was carried out with reference to provisions of Stores Purchase Rules and Memorandum and Articles of Association of the Company;
- the operation of various departments of the Company was carried out economically, efficiently and effectively in providing adequate/ reasonable assistance to SSIs in the State and compliance to the provisions of Public Works Department manuals;
- the Company had an effective and efficient financial management system;
- manpower management in the Company was effective and efficient for its operation; and
- adequate system of monitoring and internal control were in place.

Audit Criteria

2.2.5 The audit criteria adopted for deriving audit findings were drawn from:

- Industrial Promotion Policies-2004 and 2010 framed by the GoMP for the promotion of SSI units;
- Annual Memorandum of Understanding (MoU) entered into between the Company and GoMP;
- SPR and provisions of Micro, Small & Medium Enterprises (MSME) Act, 2006;
- Memorandum and articles of association of the Company;
- General principles of contract as well as provisions of State and Central Public Works Department manuals; and
- Agenda and minutes of meetings of Board of Directors of the Company.

¹² At Bhopal.

Audit findings

Planning

Industrial Promotion Policies

2.2.6 Department of Commerce, Industry & Employment (C&I), Government of Madhya Pradesh (GoMP) framed Industrial Promotion Policy in 2004, which was subsequently revised in 2010 with the main objective of promoting industrial investment in the State with special attention on promotion of small and medium enterprises. As determined by the above Industrial Promotion policies, the Company was required to take steps on the following:

- to establish vendor development and linkage between SSI and other units in developed industrial growth centres such as Pithampur, Malanpur, Mandideep to achieve zero inventory level for improving competitiveness and work efficiency of SSI & tiny sector units;
- to extend uninterrupted and easily available financial support to small industries through banks and financial institutions;
- expansion of marketing activities by organisation of buyers-sellers meet, trade fairs etc. and establishment of Urban hats (Mela) at Indore and other suitable places for expansion of marketing and display of small scale industries products under the marketing scheme of Development Commissioner (Handicrafts), Government of India.
- In the interest of small scale industries, complete transparency would be brought in working procedure of the Company and getting store purchase rules amended to increase supplies through SSI.

Audit analysis revealed the following:

The Company had not prepared any promotional and financial plan for development of SSIs with reference to vendor development as desired in Industrial Promotion Policy

- The Company had not prepared any promotional and financial plan for the development of SSI units in the State. Further, Company had not planned for vendor development and establish linkage between SSI and other units in developed industrial growth centres to achieve zero inventory level of SSIs for improving its competitiveness and work efficiency of SSI and tiny sector units as desired in the industrial policy.
- The Company organised six international and ten national fairs during the period covered under Review. However, the Company did not assess the impact of the fairs and inadequacies in its exhibition to improve the performance through the trade fairs and fact remained that the Company did not have a mechanism to evaluate the impact of fairs in development of micro & small industries in the State.
- The Company organised four Reverse Buyers Sellers Meet¹³ (RBSM) during the period covered under Review and executed 237 MoUs

¹³ RBSM presents a unique opportunity to major international buyers to interact with SSIs for sourcing their product requirement from Madhya Pradesh.

amounting to ₹ 2082.58 crore in these RBSMs. However, the Company did not maintain data base of the MoUs, which had actually translated into business for the State. Absence of a system to monitor and pursue materialisation of business arising out of the meets, would deprive the Government from assessing the impact of the efforts of the Company in development of industries in the State.

- There were 1181732 unregistered SSI units¹⁴ as per fourth all India census (2006-07) of MSME. While the Company had been doing business of marketing, raw material supply assistance, etc with the units registered with DoI, it has not so far developed any long term/ short term plan for assisting the unregistered SSI units so as to make them eligible for the financial/technical support from the Company/Government.
- The all India SSI census (2006-07) also indicated that 44.5 *per cent* and 15.01 *per cent* units were sick due to marketing problems and non availability of raw materials respectively. The Company had not made any efforts to identify such sick SSI units for assistance.
- Though the Company's marketing department invites tenders on e-portal for procurement and supplies to Government department, it did not display the details of SSI unit wise supply orders, quantity, and value placed for ensuring transparency. Besides, product range and capacity of the suppliers to execute the orders in terms of quantity and value was also not displayed.

The Government in its reply stated (October 2013) that the Company has organised RBSM, Micro Small Medium Enterprise Summits etc. by inviting prospective buyers of products manufactured by SSI units. It further stated that tender notices, rate list and details of units/products for which agreements were entered into had also been displayed on e-portal.

The Company however did not ensure transparency as envisaged in the industrial promotion policy by displaying distribution of supply orders in terms of quantity, value and capacity of the units. The reply had not addressed the absence of vendor development programme, financial and promotional plan for development of SSI units and assistance to unregistered SSI units.

ACS in Exit Conference (November 2013) stated that the Government was looking at the role of the Company as a promotional agency of SSI units instead of the presently predominant role as suppliers to the Government.

Targets and achievements

2.2.7 The Company enters into MoU every year with the GoMP, which contains targets of business, profit, dividend to GoMP, timely completion of projects etc. to be achieved. However, audit scrutiny of targets revealed that there was no linkage in fixing targets with reference to Industrial promotion policy of the Government other than target fixed for enlistment of 5000 new SSI units in 2012-13. The

MoU was not drawn with reference to objectives/targets set in the Industrial Promotion Policy

¹⁴ Units which are not registered with Directorate of Industries, (DoI) GoMP.

performance of the Company vis-à-vis the targets fixed in MoU did not thus ensure fulfillment of policy objectives of the Government.

The particulars of targets in terms of overall business vis-à-vis achievements¹⁵ there against and percentage thereof is given below for the period 2008-09 to 2012-13:

Table number 2.2.1					(₹ in crore)
Particulars	2008-09	2009-10	2010-11	2011-12	2012-13
Targets	876.33	1093.05	889.80	1032.95	1113.00
Achievements ¹⁶	1056.03	879.86	997.43	960.64	1076.83
Percentage	120.51	80.50	112.10	93.00	96.75

Source: Data furnished by the Company

The targets and achievements of the Company in various segments of its activities for five years ending 31 March 2013 are given in **Annexure-2.2.2**. The actual achievement of targets ranged between 80.50 and 120.51 *per cent* during the period 2008-09 to 2012-13. However, the Company could not achieve the targets fixed in MoU during the years 2009-10, 2011-12 and 2012-13. We observed that the reason for shortfall in the business was direct procurement by the major indenting departments¹⁷ even for items¹⁸ which were reserved for procurement through Company. Further, decrease in sale of iron and steel as discussed in **Para No 2.2.12**. We further observed that the Company was entering into MoU with the Government without ascertaining the annual requirement of the indenting departments.

The Government in its reply stated (October 2013) that the procurement budget of various departments were not known to the Company and major indenting departments have been placing work orders on contractors registered with Public Works department of GoMP, which included supply of reserved items for which the Company has no control.

As the Company was entrusted with the responsibility of assisting in growth of SSI in the state it should have taken up with the Government to ensure that orders for supply of items reserved for SSI units of the State are not procured from other sources.

Growth of SSI

2.2.8 As per Memorandum and Articles of Association (MoA) of the Company, the Company was responsible for promotion and assistance of SSI units by providing marketing, financial, technical and managerial assistance. However, we observed that the company provided mainly marketing assistance to the SSI units. The details of number of SSI registered with the Directorate of Industries (DoI),

¹⁵ Contains monetary targets of various departments of the company i.e marketing, estate & construction, emporia, raw material, business development cell and technical department.

¹⁶ The achievements represent overall business undertaken by the Company and will not match with turnover shown at annexure 2.2.6 as the latter includes only the commission on direct business.

¹⁷ Public Health Engineering (PHE), Irrigation/Water resources and Local Administration.

¹⁸ Galvanised Iron pipe/reinforcement Cement Concrete pipe Hume/ Unplasticised poly vinyl chloride (UPVC) pipe

GoMP vis a vis number of SSI assisted through marketing activities by the Company during the period from 2008-09 to 2012-13 are given in table 2.2.2:

Table 2.2.2

Year	Registered with the DoI	Assisted by the Company	Percentage of assistance
2008-09	117592	580	0.49
2009-10	137336	660	0.48
2010-11	157038	655	0.42
2011-12	177138	611	0.34
2012-13	197024	560	0.28

Source: Data furnished by the company and Directorate of Industries. (DoI)

SSI units availing marketing assistance from the Company decreased from 0.49 per cent (2008-09) to 0.28 per cent (2012-13) of total SSIs registered with Department of Industries, GoMP

We observed that SSI units availing marketing assistance from the Company decreased from 0.49 *per cent* (2008-09) to 0.28 *per cent* (2012-13) of total SSIs registered with Department of Industries, GoMP. The main reasons for declining percentage in assistance rendered to SSI units as observed in Audit were reduction in the business of reserved items and Company's failure to explore the market for unreserved items produced by the SSI units of the State.

The Government stated (October 2013) that information regarding number of registered units dealing with the products marketed by the Company was available with GoMP. The reply confirms that the Company did not have information on the products manufactured by SSI units registered with the Government to render assistance. As a result, the Company provided assistance only to units which approached them due to which, assistance rendered by the Company has been consistently decreasing.

Marketing activity

Marketing Assistance

2.2.9 The Company finalises rate contract for reserved and unreserved items, which are valid for one year. An element of service charges/commission¹⁹ receivable by the Company from the suppliers is also included in the rates finalised against the tenders floated. The finalised rates of various products are circulated for the benefit of buying departments and are notified on the website of the Company.

The business of marketing department was decreased due to decrease in business of reserved items

The overall business through the Marketing department of the Company decreased from ₹ 667.15 crore in 2008-09 to ₹ 529.60 crore in 2012-13 and the business of reserved items²⁰ through SSI units during the same period decreased from ₹ 455.21 crore to ₹ 355.20 crore.

While GoI, had reserved 350 items for exclusive purchase through SSI units, GoMP reserved only 149 items through SPR. The matter for enhancement of the list, deletion of obsolete²¹ items and addition of new items were not taken up by the Company with GoMP.

¹⁹ two per cent

²⁰ Medicines, GI pipes, ISI mark hume pipes, Cast Iron Detachable (CID) joints etc.

²¹ About 20 items which are no longer in demand, like typewriter, gland rope, ink and ribbons etc.

The Government stated (October 2013) that the major indenting departments have been placing work orders on contractors including supply of reserved items for which the Company has no control. It further stated that the matter regarding revision of SPR was under consideration of GoMP.

The reply confirms that the Company had not so far (December 2013) devised a plan to increase the business of SSI units either by ensuring procurement of reserved items through the Company or by taking steps enlarge the basket of items reserved for procurement from SSI units.

Improper management of indents

2.2.9.1 Store Purchase Rules-14²² provides for placing of indents by the indenting Departments on the Company for supply of reserved items. The State Government directed (October 2007) all the indenting departments to send the indents electronically to the Company to make the process more transparent and to avoid receipt of indents from departments by the Company through unauthorised intermediaries²³. In compliance to the above Government order, the Company intimated all the indenting departments, in February 2009, that indents be sent through electronic means.

We observed that:

- The company continued to receive indents by post and through messengers, which amounted to violation of Government instructions. The Company had not received any indents through electronic means till March 2013. Thus, the Government's objective of keeping intermediaries/mediators away and bringing transparency to the process had not been ensured by the Company. Besides, this also resulted in extra expenditure to the departments as discussed in succeeding paragraph.

The Government accepted (October 2013) the fact and stated that the Company has started (April 2013) obtaining indents through electronic medium.

- In 53 cases of the supply of cement during the period 2011-12 and 2012-13 and the supply of RCC fencing poles during the year 2011-12, indents obtained from the department were retained by mediators/suppliers for periods ranging from 14 days to 310 days in case of Cement and for periods ranging from 50 days to 83 days in case of supply of RCC fencing poles. After the rates for the items were revised upwards by the Company, the indents were submitted to the Company for issue of supply orders. This resulted in extra cost of ₹ 23.20 lakh on cement and ₹ 3.67 lakh on procurement of RCC fencing poles to the departments and corresponding undue benefit to the suppliers.

The Government in its reply (October 2013) stated that the respective departments and not the Company was responsible for the belated receipt of indents. Further, Company stated that it brought the issue to the notice

²² Articles produced or manufactured by SSIs shall be purchased through the Company only.

²³ Like SSI units, agents etc.

of indenting departments. The fact remained that the Company has failed to ensure that only indents received through electronic means were accepted and as a result intermediaries continued to influence the submission of indents and issue of supply orders.

Allowance of price preference to ineligible units

2.2.9.2 The Company invited²⁴ tenders for procuring galvanised mild steel tubes; un plasticised poly vinyl chloride rigid pipes/casing pipes etc. to meet the requirement of various Government Departments on all India basis. As per the prevailing policy of the GoMP, in respect of all India tender, price preference was to be given to state based SSI units up to 10 *per cent* over the lowest offer received against the tender.

The Industries (Development and Regulation) Act, 1951 (IDA) read with notifications/clarifications/orders issued from time to time, defines SSI and ancillary industrial undertaking.²⁵

The Company placed²⁶ supply orders on M/s. STL Exports Ltd by giving price preference for SSI unit of the State. Besides, orders were also placed on M/s. STL Extrusion Pvt. Ltd and M/s. Siddhartha Marketing Services Ltd. All the three companies were part of the Siddharth Group of Industries as some of the Directors of these companies were having business interest in other group companies by way of directorship/equity holding.

The Company passed price preference to the ineligible unit to the extent of ₹ 11.63 crore

We noticed that the companies of this group do not fall under the definition of SSI in terms of the IDA and therefore ineligible for price preference, as the gross block of assets and investment in plant and machinery of Siddharth Group was more than ₹ 5 crore as per their Balance Sheet for the year 2007-08 to 2011-12. Price preference given to M/s STL Exports Ltd in procurement of GI pipe to the extent of ₹ 11.63 crore was therefore not in order. This not only resulted in undue benefit to the supplier but also resulted in extra cost in the form of price preference to the indenting departments of the Government.

The Government in its reply (October 2013) stated that these companies were SSI units and have no relation with each other and not being managed and controlled by Directors of other related companies.

The reply is not acceptable as the group companies have significant influence in each other as per records available. Besides, we noticed that the Company did not verify the investment in Plant & Machineries from the audited Balance Sheet of

²⁴ December 2010 and August 2012

²⁵ Investment in plant & Machinery more than twenty five lakh Rupees but does not exceed five crore Rupees determined as SSI. Further, where an industrial undertaking is a subsidiary of, or is owned or controlled by, any other industrial undertaking or undertakings and if the total investment in fixed assets in plant and machinery of the first mentioned industrial undertaking and the other industrial undertaking or undertakings clubbed together exceeds the limit of investment prescribed.

²⁶ During the years 2011-12 and 2012-13

the above mentioned three companies to determine their eligibility for price preference as SSI units.

ACS in Exit Conference (November 2013) instructed the Company to examine the issue and take necessary action.

Irregularities noticed in finalisation of tenders by marketing department

2.2.9.3 Tender for supply of laptop, computers and desktop with peripherals was invited in March 2008, wherein eligibility for participation was limited to firms having turnover of not less than ₹ 500 crore. One SSI unit viz. HLBS Pvt. Ltd. Bhopal, which had a turnover of less than ₹ 500 crore offered its rate against the tender, though the firm did not fulfill the eligibility criterion. The Company however considered the offer as it was from a SSI unit and placed (2008-09) orders on the firm for supply of computers valued at ₹ 18.90 lakh. Changing the eligibility criteria at the time of placement of order not only vitiates the tender process but also result in depriving other SSI units an opportunity to participate in the tender. Besides, inviting bids from non-SSI units, when such items are being manufactured by SSI was against its own objective of promotion and development of SSIs in the State.

The Government stated (October 2013) that the offer of HLBS Tech. Pvt. Ltd. was considered as it was a SSI unit in the State and after this tender, the Company has incorporated the relaxed criteria of past performance and qualification for SSI units of the state in the tender document. The fact remained that the Company deviated from its objective of promoting SSIs in the State by incorporating a condition of turnover. Further, finalising the procurement without giving opportunity of participation to other SSI units led to undue benefit to the firm.

Supply of DI pipes from the firms having doubtful business integrity

2.2.9.4 The Company invited (March 2012) all India tender for supply of duct iron pipes to meet the requirement of Government Departments.

We noticed that during the process of evaluation of the tender, the Company became aware that one of the tenderers M/s Rashmi Metalics Limited, Kolkata had been black listed by Government/ Government bodies in some states due evasion of revenue, involvement in fraud and irregularity in supplies. The Company, however, placed orders of ₹ 1.06 crore on the firm during 2012-13. This not only resulted in undue benefit to the firm but also risked the interest of the indenting departments in obtaining quality supply on time.

The Government in its reply (October 2013) stated that there was no provision in special terms and conditions of tender documents and general terms and conditions of the tender to debar the firms that were involved in evasion of Government revenue and the firm therefore could not be debarred by the Company. It was further stated that the point was noted for future compliance.

The reply is not acceptable as the Company was aware that the material supplied by the firm to various Government undertaking/Departments in the country were sub-standard and of poor quality. The Company should therefore have re-invited

bids after incorporating necessary conditions as placement of order on such firm would lead to compromising quality, which is against the interest of GoMP.

Performance of other departments of the Company

Performance of Estate & Construction (E&C) Department

2.2.10 The Company has an Estate and Construction wing (E&C). As per the articles of Association of the Company, civil works relating to construction, maintenance and administration of industrial estates and industrial areas for small scale industries are only permitted to be undertaken.

The Company however, under took construction of schools, hostels, Primary Health Centers of Government on deposit work basis. The wing also undertook interior decoration and renovation work of offices of other Corporations/offices and gets supervision charges as remuneration. The Company received funds of 174.79 crore and utilised ₹ 163.00 crore during 2008-09 to 2011-12²⁷.

Execution of deposit works

2.2.10.1 As per the requirement of the depositing agency, the Company prepares estimates (including contingencies and supervision charges) and accordingly, receives funds for the execution of deposit works after getting Administrative Approval from the concerned agency. The work is generally executed as per provisions of the Public Works Department (PWD) Manual of the State/Schedule of Rates (SoR) and other related orders and instructions of the PWD department/ Company from time to time. The works awarded by the Company to contractors were also based on SoR of PWD.

We observed that the Company had so far (December 2013) not adopted some of the provisions of manual and orders of the PWD department as discussed below:

- The PWD introduced (April 2010) the system of e-tendering for the tenders where estimated cost was ₹ 10.00 lakh or above. In May 2012, e-tendering was introduced for all works irrespective of value. The Company however introduced (September 2011) e-tendering only for the works where estimated cost was in excess of ₹ 25 lakh.
- The GoMP also started (February 2007) a portal for e-procurement in construction works, supply of materials etc. by the government departments, agencies, boards, public enterprises and other organizations of the State, where tenders could be uploaded for better transparency and wider publicity. The Company however uploaded only the tenders where estimated cost was above ₹ 25 lakh.
- As per the PWD Manual, tenders were to be accepted by the competent authority as per actual cost²⁸ of the work and not as per the Probable Amount of Contract (PAC) of the work. We however noticed in 35 test checked cases, where the actual cost of the work ranged between ₹ 25.47 and 34.77 lakh, that the tenders were accepted by the CGM (E&C)

²⁷ Information for the year 2012-13 not available due to non finalisation of Accounts.

²⁸ Probable Amount of Contract (PAC)+/- rates quoted by the contractor (in percentage w.r.t. SOR)

considering Probable Amount of contract (PAC) as the basis, though the competent authority as per actual cost of work was the Managing Director.

The Government in its reply (October 2013) stated that the Company had issued (August 2013) orders to follow e-tendering for all the works, irrespective of the amount involved and assured compliance of PWD manual for acceptance of tender in excess of ₹ 25 lakh.

Lack of transparency in tender publication in News Papers

2.2.10.2 As per the decision (March 2010) of the Managing Director, in line with the provisions of PWD manual, all the works relating to construction activities whose estimated cost of works exceeded ₹ five lakh were to be published in news papers for wider publicity.

The Company kept the PAC below ₹ five lakh in order to avoid publishing tenders in news papers.

During test check of tenders invited by the divisions, we observed that in 790 cases, the divisions recorded the PAC below ₹ five lakh (ranged between ₹ 4.50 lakh and ₹ 4.99 five lakh) and avoided publishing in news papers. In 13 test checked cases, we noticed that the actual expenditure ranged between ₹ 7.23 lakh and ₹ 24.96 lakh.

We further observed that the deposits received from various Government agencies/departments against works were in lump sum and estimates were also prepared for the entire work to be executed for the same client and at same premises²⁹. The works were however split up for finalisation of tenders in parts and thereby the requirement of sanction from higher authorities and publication in news papers were avoided. Three test checked cases, where the works were split into 34 parts are given in ***Annexure-2.2.3***.

The Government in its reply (October 2013) accepted the fact and stated that the Company had issued (August 2013) orders to follow e-tendering for all the works, irrespective of the amount involved and publication of tenders in news paper. Managing Director agreed in exit conference (November 2013) with the views of the audit and assured to enquire the details of works which were split up to avoid approval by higher authorities.

Deduction of royalty from the final bills

2.2.10.3 The Mining Resources Department, GoMP directed (July 2004) that the minor minerals used in the construction works attracts advance deposit of royalty and the royalty deducted from contractors' final bills would not be refundable till Non objection Certificate (NoC) from the Mining department is produced by the contractor.

We observed that divisions of the E&C department of the Company adopted differential treatment for deduction of royalty with reference to material utilised in the works. While Indore Division retained royalties of ₹ 34.48 lakh during the period from 2008-09 to 2012-13 against works completed, Gwalior, Satna and

²⁹ The estimates of a particular deposit work were split up though the deposit was received for a composite work which was to be executed in the premise.

Bhopal divisions obtained *affidavits*³⁰ from the contractors at the time of settlement of final bills instead of retention of the amount of royalty.

As the orders of the GoMP will prevail over the order of the Company, final payment to contractor based on submission of affidavit was not in line with Government orders.

The Contracts did not contain a clause prescribing the time limit within which NOC of Mining Department should be produced, failing which the amounts would be credited to Government Account. As a result, the amounts withheld since 2008-09 by Indore division remained to be credited to the Government account.

The Managing Director in exit conference assured to adopt uniform treatment of royalty withheld by all the divisions.

Non inclusion of interest clause in the agreement

2.2.10.4 The Company entered in to agreements for construction of Navodaya Vidyalaya building in various districts of Madhya Pradesh, Chhatisgarh and Odissa with Navodaya Vidyalaya Samiti. The terms and conditions of the agreements included payment to the Company by Navodaya Vidyalay Samiti on presentation of monthly RA bills.

We noticed that against various works executed by the Company relating to the agreements, ₹ 10.01 crore was pending for payment by the Samiti for periods ranging from 3 to 32 months, for which specific reasons were not available on record. We further noticed that the Company failed to include a clause for timely payment of bills and interest for the delayed payments by the Samiti. The loss of interest on blocked capital calculated at the rate³¹ of eight *per cent* per annum worked out to ₹ 72.24 lakh for the period from August 2011 to November 2012.

Chief General Manager (E&C) in exit conference (November 2013) stated that the matter is being pursued with the concerned department. The Company being a commercial organisation should have executed the works only on deposit basis and not by employing its own funds.

Performance of the Emporium Department

2.2.11 The Company operates eight emporia engaged in sale of handloom and handicraft items. The handloom/handicrafts items are normally purchased from weavers and artisans of the state and the selling price is fixed by increasing the purchase price by 60 *per cent*. Besides, some items reserved for procurement under Store Purchase Rules were also handled (April 2001) by the Emporium Department. The business of emporium department increased from ₹ 28.23 crore in 2008-09 to ₹ 112.64 crore in 2012-13 as shown in *Annexure-2.2.2* and achieved targets fixed in MoU except in the year 2012-13. The profit of the emporium department increased from ₹ 0.76 crore in 2008-09 to ₹ 2.99 crore in 2012-13.

The Company could not recover an amount of ₹ 10.01 crore, which was pending for payment by Navodaya Vidyalaya Samiti for the period ranging from 3 to 32 months.

The increased profitability of the emporia was mainly due to inclusion of commission earned on sales of marketing items.

³⁰ stating that contractor paid royalty on material used and in case any dues are found he will be responsible and will make himself present in the Office as and when called for.

³¹ Minimum interest rate of FDRs during review period.

We observed that the increased profitability of the emporia was mainly due to inclusion of commission³² earned on supply of marketing items³³ to Government departments. Bhopal and Kolkata emporia earned profits even after excluding marketing commission during review period but other five emporia³⁴ incurred continuous losses if the commission earned on marketing items, were excluded.

The Government in its reply (October 2013) accepted the fact and stated that profitability of certain emporia was due to the commission earned on MVS.

Inventory management in Emporia

2.2.11.1 The term inventory management describes the effective method of controlling objects and activities and ensuring that they get to the right place at the right time all within a cost parameter. The emporium-in-charge procures materials based on the market trend, price, previous rate, quality, customer demand of goods to be sold etc. The inventory held by different emporia during the period 2008-09 to 2012-13 has been tabulated in ***Annexure-2.2.4***.

We noticed that:

- The Company was not having norms prescribed for holding of stock in various emporia either through purchase manual or through executive instructions.
- The percentage of closing stock to sales was maintained by Bhopal emporia was the lowest among the emporia which ranged between 11.33 and 18.22 *per cent* during the year 2008-09 to 2012-13.
- The closing stock in Rewa (2011-12 and 2012-13) and New Delhi (2008-09 and 2009-10) was more than their annual turnover leading to unwanted accumulation of stock and resulted in blockage of funds apart from deterioration of stock which was alarming.

The Government in its reply (October 2013) stated that the Company considers its inventory as a whole and examines the inventory on the basis of year wise inventory level.

As the emporium wise inventory level during the period covered under the review was alarming, the Company needs to fix norms for inventory holding for individual emporium.

Lack of policy in disposal of old inventory

2.2.11.2 The Company in physical verification stock statement incorporates the position of stock remaining unsold. We noticed that stock to the extent of ₹ 1.10 crore was lying unsold for more than two years as at the end of March 2013. The following is the position of inventory at cost price in emporia in table 2.2.3:

The stock to the extent of ₹ 1.10 crore was lying unsold for more than two years as at the end of March 2013

³² Two percent on reserved items and five percent on non-reserved items.

³³ Stationery, phynial, soap, toys etc.

³⁴ Indore, Jabalpur, Gwalior, Rewa, New Delhi

Table 2.2.3

(₹ in lakh)

Name of emporiums	Stock 1-2 years old	Stock 2-3 years old	Stock 3-5 years old	Stock 5-10 years old	Above 10 years old
Emporium, Indore	24.55	2.10	0.60	1.35	1.41
Emporium, Jabalpur	12.99	1.95	1.37	0.43	0.26
Emporium, Gwalior	3.13	3.14	0.81	0.50	Nil
Emporium, Bhopal	11.42	3.42	2.12	1.40	0.28
Emporium, Rewa	17.07	1.02	0.25	10.54	Nil
Emporium, Delhi	264.56	20.15	8.08	4.99	2.19
Emporium, Mrignayni-Kolkata	28.25	15.45	4.01	1.73	5.61
Emporium, Awanti-Kolkata	13.41	6.30	5.19	3.32	Nil
Total	375.38	53.53	22.43	24.26	9.75
Grand Total			109.97		

Source: Information furnished by the Company

We further noticed that:

- The Company has also not analysed reasons for non movement of stock for the period exceeding ten years.
- The Company has not framed any policy for disposal of non- moving stock.
- Above inventory also includes damaged stock of ₹ 32.53 lakh as on March 2013, however, the realisable value of the same was ₹ 19.54 lakh. Thus, the Company suffered a loss of ₹ 12.99 lakh on damaged stock due to reduction in realisable value of the stock. The Company has not taken any action for early disposal of the stock so far (November 2013).

The Government in its reply (October 2013) accepted the fact and stated that a policy in this regard will be formed.

Goods sent on approval not returned

The durable goods worth ₹ 24.41 lakh were sent on approval of customers, but were not returned or adjusted through sales in the stock statement as on March 2013.

2.2.11.3 The term ‘Goods sent on approval’ means arrangement under which items of durable nature are provided to a prospective customer for a pre purchase trial. These items are returnable in resalable condition within seven days from the date of issue, if not accepted for purchase. If the goods are not returned within seven days, the goods are liable to be billed.

We observed that non durable goods worth ₹ 24.41 lakh were sent on approval to customers but were not returned or adjusted through sales in the stock statement as on March 2013.

The Government in its reply (October 2013) stated that the goods sent on approval had been reduced to ₹ 5.12 lakh (October 2013) by either billing the customers or by obtaining return of goods. While action for liquidating the balances of the goods sent on approval had been taken by the Company, after being pointed out by the Audit, no details as to how much was sold or taken back and physical condition thereof was furnished. Further, the Company had not introduced a monitoring mechanism for regular adjustment of goods sent on approval.

Assistance to emporia weavers/craftsmen

2.2.11.4 One of the objectives of the Company was development of weavers and artisans through sale of their products in emporia by marketing support. However,

we observed that growth in the number of vendors to whom marketing support was provided by different emporia was very low and in some emporia it had actually decreased. The Company continued to procure items from same vendors particularly Indore, Jabalpur and Gwalior emporia. It was also observed that there were 251 vendors (2008-09) in eight emporia which marginally increased to 312 (2012-13).

The Government in its reply (October 2013) stated that the emporia normally purchase their products through weavers and artisans of MP, the decision is being taken purely on commercial basis and the purchase cannot be driven by objectives of their development only, though the number of weavers and artisans can be increased subject to availability and the quality of products offered.

The objective of the emporia was to promote the weavers and artisans of the State, but the Company procured material mainly from manufacturers and suppliers instead of weavers and artisans. Thus, the objective of providing marketing assistance to weavers and artisans had been very limited.

Renovation of emporia

2.2.11.5 With a view to cater to the demands of changing shopping habits of the consumers and increasing the turnover, Company decided to renovate its emporia to make it more consumer friendly with the core objective of promoting the products of the weavers and artisans of the state. The Company accordingly, took up work of renovating six³⁵ of its emporia during the period from 2008-09 to 2012-13 at a cost of ₹ 3.55 crore. While sales and profit after renovation increased in two³⁶ emporia, it decreased in Jabalpur emporium. In respect of remaining three emporia, renovation work was completed only during 2013-14.

The Company enters into agreement with the contractors entrusted with the work of renovation specifying the time period for completion. As the company is in the business of trading handicraft and handloom products through its emporia, any delay in completion of renovation work will have direct impact on its sales and profit arising from such sales.

We noticed that in the agreements entered into for renovation of six of its emporia, no clause for levy of penalty in case of delay in completion of work was incorporated in five³⁷ contracts. In the case of renovation of Indore Emporium, the agreement with M/s Antique Interior Designer, Gwalior contained a penalty clause according to which, a penalty of ₹ 10000 for each day of delay was leviable. The renovation work of Indore Emporium was completed by the contractor after a delay of six and half months for which penalty amounting to ₹ 19.70 lakh was leviable. The Company however levied a penalty of only ₹ 4.20 lakh. This resulted in short levy of penalty of ₹ 15.50 lakh and undue advantage to the contractor to that extent. Besides, due to delay in renovation work, Company lost consignment sale of ₹ 57.00 lakh in Indore emporium.

The Company short levied the penalty of ₹ 15.50 lakh on account of delay in renovation of Indore

³⁵ Emporia- Bhopal, Kolkata, Indore, Jabalpur, Gwalior and Rewa

³⁶ Bhopal and Kolkata

³⁷ Emporia- Bhopal, Kolkata, Jabalpur, Gwalior and Rewa

In the absence of an enabling clause for levy of penalty, in respect of Bhopal and Jabalpur emporia the Company could not secure its interest though the renovation work was completed after delay of 10 and 12 months respectively.

The Government in its reply (October 2013) accepted the fact and stated that the tender condition related to renovation of emporium have been revised and suitable penalty clause would be included in future renovations. Further, it stated that the committee considered the delay of 42 days for penalty in respect of Indore emporium and imposed penalty of ₹ 4.20 lakh.

The reply is not acceptable as penalty leviable as per the agreement was ₹ 19.70 lakh against which the company levied only ₹ 4.20 lakh. Further, the agreement did not stipulate any clause under which either time extension can be granted or delay in execution could be condoned/reduced. We recommend that the Company may consider uniform clauses in the agreements entered into by all the emporia after ensuring that financial interests of the Company are secured.

Performance of Raw Material Department

2.2.12 The activities of the Company include assistance to SSI units dealing with procurement of iron and steel required by the units as raw material. The Raw Material Department (RMD) sells iron & steel allotted by Steel Authority of India Limited (SAIL) to the Company for supply to SSIs. Further it is also engaged in supply of reserved³⁸ and non-reserved³⁹ items to Government Departments.

The details of business done by the Raw Material Department (RMD) during the period covered under Review are mentioned in *Annexure-2.2.2*. It was observed from the *Annexure-2.2.2* that business of RMDs decreased to ₹ 192.74 crore in the year 2012-13 from ₹ 253.87 crore in the year 2008-09 due to reduction in sale quantity of iron & steel to the SSI units as discussed below.

Table 2.2.4

Year	Allocation of steel in MT by main producer	Availed/lifted quantity in MT	Shortfall in lifting (in MT)	Shortfall in lifting in percentage
2008-09	25694	16158.420	9535.58	37.11
2009-10	25695	15223.645	10471.355	40.76
2010-11	25695	11040.906	14654.094	57.04
2011-12	25695	14496.512	11198.488	43.58
2012-13	25695	12329.384	13365.616	52.02
Total	128474	69248.867	59225.133	

Source: Data furnished by the Company

We observed that the percentage of shortfall in lifting of Iron & Steel against allocated quantity varied from 37.11 to 57.04 *per cent* during 2008-09 to 2012-13. We further noticed that the number of SSIs getting supplies through the Company had reduced from 146 in 2008-09 to 102 in 2012-13. The Company did not have information on the number of SSI units requiring Iron & Steel for

³⁸ 51 items out of 149 reserved items

³⁹ cement etc.

their production activities to determine the scope for improving the performance of its depots and in turn increase its assistance to SSI units of the State.

The profitability of Raw Material depots were mainly due to inclusion of commission from the marketing of reserved and non-reserved items indicating that depot's main activities continued to incur losses.

The Government in its reply (October 2013) accepted the fact and stated that the GoI has decontrolled (1992) the iron and steel business and the low off take was due to competition from private dealers. Fact remained that the Company failed to review the need for continuance of its depots, if the business of Iron & Steel by the Company, after decontrol was not contributing to the growth of the SSI units.

Further, only the Bhopal depot was earning profit from sale of raw material items to SSIs. We observed that though the RMD at Indore, Jabalpur and Gwalior reported profits, the profit of the depots were due to inclusion of commission from the marketing of products manufactured by SSIs. Thus the depots are incurring losses in its main activity viz. sale of raw material to SSI units.

The Government in its reply (October 2013) stated that the working results of RMDs were improving. The reply is however silent on the fact that the depots were suffering losses in their main activity. Reply also did not address the issue of RMD undertaking marketing activities when a separate marketing department was already in existence.

Cancellation of supply orders placed on SSI units

2.2.12.1 The Company executes annual rate contract with SSI units for supply of stainless steel utensils, which is an item reserved under Store Purchase Rules (SPR). Indents for procurement of utensils are mainly received from Woman and Children Welfare Department (WCWD), GoMP. We noticed that Company placed supply orders of ₹ 47.10 crore for the supply of stainless steel utensils, of which orders amounting to ₹ 19.87 crore were cancelled by WCWD during the period covered under Review, on the ground that the quality of utensils supplied was poor. The Company did not take up with WCWD against cancellation as the defective quantity could have been replaced under the terms of agreement with the SSI units, besides imposition of penalty on them.

Further, this was a reserved item under SPR and it is obligatory on the departments to procure the same from the Company only. The Company however did not watch if the requirements for cancelled items were met by WCWD through procurement from the market subsequently. As SSI units would have already mobilized resources to supply material to WCWD as per orders placed, cancellation of order without compensation to SSI units would affect the growth of the SSI units in the State. We however noticed that no provision existed in the agreement between WCWD and the Company for imposing penalty on cancellation of order.

The Government in its reply (October 2013) stated that WCWD, at its own discretion cancelled the order and Company was left with no option but to cancel the supply orders given to the SSI units. Further, it was also stated that the matter of compensation to SSI units would be taken up with the concerned department.

Performance of Business Development Cell (BDC)

2.2.13 As per the coal supply policy, the Company was nominated by the GoMP for supply of coal to small and medium enterprises in the State. The Business Development Cell (BDC) of the Company carries out the activities to assist SSI units in procurement of coal. The Company enters into a Coal Supply Agreement with the South Eastern Coalfields Limited (SECL)/Western Coalfields Limited (WCL) for procurement of coal to be allotted to SSI units of the State. The Company earns five *per cent* as commission on the basic price of coal. The position of allocation by coal companies and distribution of coal to SSI units is given in the table 2.2.5:

Table 2.2.5

Year	Allocation of quota in MT by Coal Companies	Availed/lifted quantity in MT	Shortfall in MT	Percentage of lifting to total allocation
2008-09	349999	268199	81800	76.63
2009-10	565000	459342	105658	81.30
2010-11	616000	531382	84618	86.26
2011-12	667000	483240	183760	72.45
2012-13	667000	538530	128470	80.74

Source: Data furnished by the Company

The short lifting of coal was ranged from 72.45 to 86.26 *per cent* against allocation during 2008-09 to 2012-13.

It could be seen from the above table that the lifting of coal against allocation ranged from 72.45 to 86.26 *per cent*. The Company assisted only 455 coal consuming units as against total 19471 units⁴⁰ in the State, which represented only 2.33 *per cent* of units having coal as main source of power. The reasons for short lifting were mainly due to inferior grade of coal.

We further observed that, as per the coal allotment procedure, the utilization of coal for every quarter by the units has to be verified by the General Manager (GM) of the District Trade and Industries Center (DTIC) and the Company before allotment of next quarter coal. The Company, however, did not have a system of verification and is relying on the certificate given by the unit and countersigned by the GM (DTIC).

The Government in its reply (October 2013) accepted the fact and the CGM (BDC), in the exit conference stated that due to inferior grade of coal, the lifting was at lower side and also assured to take up the matter with coal companies.

The Company should devise a mechanism to make it possible for the small scale units to draw coal under this arrangement so that the entire quantity allotted is lifted, which in turn would assist the development/growth of SSI units.

Performance of Technical Department

2.2.14. Technical cell performs the duty of making specifications for articles to be supplied and pre-inspection before its supply and estimation of work for determining the reasonability of tendered rates and preparation of feasibility report of SSI/MSI units, for which fees at specified rate is recovered. There are two testing laboratories at Indore and Jabalpur opened for sample testing of

⁴⁰ As per SSI census 2006-07 by GoI

government/non government organization under the Technical cell. The details of the sample received from the Government and private parties are given in the table 2.2.6:

Table 2.2.6

Year		No. of samples received and tested				
		2008-09	2009-10	2010-11	2011-12	2012-13
Testing Lab, Indore	From Government Deptts.	1274	2323	1676	1397	2148
	From Private parties	1228	1104	1653	1274	1580
	Total	2502	3427	3329	2671	3728
Testing Lab, Jabalpur	From Government Deptts	2287	1855	1638	1814	1800
	From Private parties	292	549	791	705	461
	Total	2579	2404	2429	2519	2261

Source: Data furnished by the Company

We noticed that:

- the facility intended for aiding the small/medium sector units in testing of samples was primarily used for testing samples received from Government departments/organisations.
- testing fees structure was revised only once in 2010-11 during the period of 2008-09 to 2012-13, though there was regular increase in staff and establishment cost.
- the testing labs did not maintain records of the samples brought to the lab that could not be tested due to non-availability of facilities.

The Government (October 2013) accepted the facts and stated that the rates of testing charges were revised in 2010-11 and in the view of increase in expenditure under various heads, the rates would be revised. It further agreed to maintain records of samples brought at the lab but could not be tested due to non availability of facilities.

Financial Management

Financial position and working results of the Company

2.2.15 The financial position and working results of the Company for 2008-09 to 2011-12 as per audited accounts are given in *Annexure 2.2.5 and 2.2.6*.

We observed that:

- The turnover of the Company increased from ₹ 151.92 crore in 2008-09 to ₹ 223.05 crore in 2011-12 (46.82 *per cent*), while the net profit of the Company increased only from ₹ 13.18 crore in 2008-09 to ₹ 13.76 crore in 2011-12 (4.40 *per cent*). The rate of growth in profit was lower due to higher rate of increase in administrative expenses and employees cost, imposition of service tax on supervision charges earned by E & C department from 2010-11.
- Profit includes income from deposits held by the Company which increased from ₹ 8.24 crore (2008-09) to ₹ 15.59 crore (2011-12). Thus, if

interest income is excluded, the profit would have been ₹ 12.13 crore in 2008-09, which would further decrease to ₹ 8.37 crore in 2011-12.

- The return on Capital employed decreased from 28.56 *per cent* in 2008-09 to 18.01 *per cent* in 2011-12, indicating deteriorating performance of the Company.

Failure to monitor realisation from Sundry Debtors

The Company did not have any age wise and party wise records of Sundry Debtors and system for timely reconciliation of the same.

2.2.16 The Company did not have any age wise and party wise records of Sundry Debtors. The sundry debtors of the Company stood at ₹ 5.72 crore, ₹ 7.28 crore, ₹ 7.31 crore and ₹ 9.44 crore during the year 2008-09, 2009-10, 2010-11 and 2011-12 respectively. The debtors of ₹ 3.06 crore of New Delhi emporium represented 48.96 *per cent* of all the emporia debtors of ₹ 6.25 crore as on March 2012.

The Company did not have a system of obtaining confirmation from the debtors on the dues receivable to make necessary adjustment to the receivables. As a result, name of parties from whom ₹ 11.42 crore was receivable and name of parties to whom 12.94 crore recorded as payable were not known to the Company. The Government in its reply (October 2013) accepted the fact and CGM (F&A), in exit conference, stated that the work of reconciliation was under progress.

Fund Management

The Company did not frame any long term investment policy to invest its surplus fund and a mechanism to assess the requirement of fund for ongoing deposit works to derive maximum return through prudential investment plan.

2.2.17 The Company had been investing its internally generated surplus funds and unspent deposits received from various Government departments for execution of civil works in Fixed Deposits (FDs). The investment in FDs increased from ₹ 116.27 crore (March 2009) to ₹ 209.18 crore (March 2013) and the Company earned interest of ₹ 46.35 crore during 2008-09 to 2011-12. The Company did not frame any long term investment policy to invest its surplus fund and a mechanism to assess the requirement of fund for ongoing deposit works to derive maximum return through prudential investment plan.

The Government in its reply (October 2013) assured to frame a long term policy for investment of surplus funds.

Non remittance of penalties recovered from SSIs

2.2.18 As per clause 23(1) of the agreements executed between the Company and SSIs, in case supplies are delayed or not found according to the specification/substandard supplies or for any other reason, a penalty equivalent to two *per cent* per month subject to maximum of 10 *per cent* of the value of supplies is to be imposed and recovered from SSIs. We noticed from the records of the Company that penalty deducted against supplies to Government departments was ₹ 1.68 crore as on 31 March 2012, which included ₹ 1.45 crore pertaining to the period prior to 2008-09.

We further noticed that the Company retained above amounts without any specific consent or approval of the State Government and had shown the same as liability not remitted (as on March 2012) into the accounts of the State exchequer. This resulted in unauthorised retention and use of penalties by the Company as its working capital.

The ACS in Exit Conference (November 2013) directed the Company to sort out the issue at the earliest with concerned departments.

Charging of excess commission

The emporium department of the Company charged service charges/commission in MVS scheme at the rate five *per cent* on unreserved items. As a result, excess commission of ₹ 3.45 crore was recovered from the Government departments.

2.2.19 The Company introduced (March 2001) Mrignayani Vipnan Seva (MVS) scheme for the supply of various items⁴¹ to the Government Departments through its Emporia and also issued⁴² instructions for its implementation. The main objectives of the scheme were to fulfill small requirements of the Government Departments at regional level. Initially, 17 items were identified to be covered under the scheme for marketing and supply purpose. During the period 2009-13, five emporia at Bhopal, Indore, Gwalior, Jabalpur and Rewa secured business of ₹ 122.37 crore and earned services charges/commission of ₹ 5.90 crore.

As per the Rule 16 of the SPR, the service charges/commission charged by the Company should not exceed two *per cent*. The emporium department of the Company charged service charges/commission in MVS scheme at the rate five *per cent* on unreserved items and two *per cent* on reserved⁴³ items. As a result, excess commission of ₹ 3.45 crore was recovered from the Government departments.

Thus, charging of excess three *per cent* commission was against the rule 16.

The Government in its reply (October 2013) stated that charging of five *per cent* service charges was decided by the BoDs of the Company and MVS tenders were now floated through e-tendering system. However, MD in exit conference (November 2013) agreed to review the rates of commission and take corrective action.

It is true that five *per cent* service charges were approved by the BoDs but, relevant provision of Rule-16 of SPR was not mentioned in the Agenda items.

Human Resource Management

2.2.20 Management of manpower is one of the important factors in achieving the organizational objectives of a Company. The Company's sanctioned staff strength was fixed at 535 in 1986 and same has not been reassessed so far (March 2013). The working manpower position is detailed in Table 2.2.7

Table 2.2.7

Sl. No.	Cadre	Sanctioned strength	Regular Working strength	On deputation	On contract after retirement	Total men in position
1.	CGM, Dy.CGM, GM	45	36	01	01	38
2.	Managers	85	36	01	--	37
3.	Assistant Managers, Accountants etc.	296	194	03	05	202
4.	Others	109	80	--	--	80
	Total	535	346	5	6	357

Source: data furnished by the Company

⁴¹ All textile materials, uniforms, musical instruments, stationary, door mates etc.

⁴² March 2001 and revised in April 2007 and December 2009

⁴³ The items specified in rule 14 of SPR as amended from time to time, if any, are only reserved item. Rests of the item of supplies are treated as unreserved.

As the business of the Company is decreasing as discussed in Para No.2.2.7, the Company should have reviewed its manpower requirement and the activities that requires prioritisation for development of SSI units in the state considering the changes in the industrial environment since 1986.

The Government in its reply (October 2013) accepted the fact and stated that the Company is trying to meet its manpower needs by outsourced employees. Reply is however silent about reassessment of manpower requirement in view of decreasing business.

Monitoring, Internal Control and Internal Audit

Lack of monitoring by management

2.2.21 The units/field offices prepare periodical performance reports manually and submit to Head Office of the Company. We, however, noticed that the monitoring mechanism in the Company suffered from the following deficiencies, which had impact on its objective of assistance in development and growth of SSI:

- There was no mechanism to assess the quantum of direct purchases made by Government departments of items that were reserved for procurement through the Company in terms of the SPR. As a result, the Company was unable to take up this issue with the Government for ensuring that the business reserved for the Company is not diverted by the department/agencies of the Government.
- The Company did not get the SPR revised for the last more than 20 years though many of the items reserved for procurement through the Company have become obsolete and not being indented by the departments. Some of the new items dealt by the Company are unreserved items and it would help the SSI sector, if such items are got reserved by revision in the SPR.

Implementation of Information Technology System

2.2.22 The Company does not have an independent IT Cell/Wing to implement the information technology system in the Company, despite having turnover of ₹ 223.05 crore in 2011-12 under different segments of business. Further, 25 units located in and outside of the State have not been connected through a centralised server and management has to depend on different software installed at different departments to gather information. The Marketing department of the Company through e-portal published tenders, monitors supplies⁴⁴. The system however does not exhibit on e-portal, the value of supply orders placed on different units as a measure of complete transparency despite its requirement in industrial policy of GoMP. Therefore, the system in use needs up gradation to suit the working of the Company and should be compatible with entire working to save time, cost and access by all officers/genuine users.

⁴⁴ Tender wise, supplier wise, value wise, item wise

Internal Control

2.2.23 Internal control system is an essential part of the Management activity. An efficient and effective system helps the Management to achieve its laid down objectives, procedure and financial proprietary discipline. We observed the following deficiencies in the internal control system-

- There was no internal control for recovery and adjustments of very old sundry debtors. (Para number **2.2.16**)
- Systems for timely disposal of non-moving, damaged and surplus inventory accumulated in the emporiums of the Company were not in place. (Para number **2.2.11.2**)
- The Company does not have a system of verifying a unit as SSI with reference to MSMED Act, 2006 with the related audited balance sheet of the unit from time to time. As a result, the Company is not in a position to ensure that the benefits meant for SSI are not availed by the units which had become medium enterprises. (Para number **2.2.9.2**)
- As per the coal allotment procedure, the utilization of coal for every quarter by the units has to be verified by the GM (DTIC) and the Company before allotment of next quarter coal. The Company however did not have a system of verification and is relying on the certificate given by the unit and countersigned by the GM (DTIC). The Company does not also check with the DIC as to whether the countersignatures were made on verification. (Para number **2.2.13**)
- The tenders floated by marketing, emporia, RMD and E&C departments were not routed through pre audit at corporate level and concurrence of finance department H.O. was not obtained before finalisation thereof. The system needs to be introduced for avoiding any leakage of revenue, extra cost or deviation from compliance of statutory provisions/manual.
- There was no structured mechanism for analysing the reasons for unit wise variance between actuals and budget which would make it difficult for the Company to take effective financial measures for overcoming inadequacies and fund management.
- Absence of a purchase manual relating to emporia business and accounting/ audit manual of the company.

Internal Audit

2.2.24 To keep proper watch on various activities performed by various wings, an adequate internal audit system which is commensurate with the size and nature of business of the Company is essential. It was noticed that the Company had a separate Internal Audit Wing headed by General Manager (Internal Audit) and a Manager, which undertakes physical verification of stock. The Company also use the services of CA firms for audit of cash book, Bank book with related vouchers, Bank reconciliation, advances to employees etc. Thus, the internal audit in the Company is limited to physical verification of stock and preliminary checking of accounts leaving scrutiny of core area of contracts, tenders etc. unaudited.

The Company had also not framed any Internal Audit/Accounts Manual and the internal audit reports had not been submitted to the BoDs. Thus, internal audit system was deficient and ineffective.

The Government in its reply (October 2013) stated that due to shortage of staff, internal audit wing could not be continued and internal audit work has been assigned to Chartered Accountant firms. The Statutory Auditors in their Audit Report for the year 2011-12 also expressed that the internal audit system needs to be further strengthened

The reply was not acceptable as the work assigned to internal auditors was restricted up to preliminary checking of transactions leaving scrutiny of contracts and tenders unaudited.

Conclusion

The Company had not prepared any promotional and financial plan for the development of SSI units in the State and did not assess the impact of the fairs and RBSPs. The Company could not achieve the targets of business fixed in MOUs during the three years up to 2012-13. The percentage of SSIs availing the marketing assistance was insignificant.

The business of marketing department of the Company decreased due to decrease in business of reserved items, non-adherence to the GoMP orders regarding management of tenders. The company did not evolve a proper system to verify the eligibility of SSI units for allowing price preference.

Civil deposit works were split up in parts to avoid publishing tenders in news papers and the Company also failed to introduce e-tendering system fully to make the entire process of finalization of tenders and issue of work order transparent and free from defects. The E&C divisions adopted differential practice for deduction and remittance of royalty to the government exchequer and non-inclusion of interest clause in the agreement.

The profitability of the emporia was mainly not due to counter sales. There was no policy for disposal of non- moving stock, goods sent on approval. Company did not levy penalty as per clause of agreement against renovation work of emporia.

The Company could not lift the total quantity of iron and steel allocated by steel manufacturers. Similarly, it could not also lift the total allocated quantity of coal and thus could not provide assistance to SSIs as planned. The testing fee structure was not revised since 2011-12 in respect of Technical labs.

The profit of the Company was mainly due to income earned through interest on FDRs, while its operational profit was in decreasing trend. The receivables management was poor and lacked timely reconciliation. The company has not done reassessment of manpower.

The Company does not have an independent IT Cell/Wing to implement the information technology system and the functioning of internal audit wing was deficient and ineffective.

Recommendations

The Company should endeavor to:

- plan and implement for promotion of SSIs through financial assistance;
- increase the number of SSIs under its marketing activities;
- develop a mechanism to trace out the direct purchases, follow up the revision in SPR with GoMP;
- execute deposit works in more economical and transparent manner by fully utilising the available funds, avoiding splitting of works and framing terms and conditions of contracts to secure interest of depositor departments/institutions with proper application of delegation of powers of executives;
- increase business of emporia by analysing causes of losses, fixing norms for inventory holding and speedy realisation/adjustment of sundry debtors;
- lift and distribute the total allocated quantity of iron & steel and coal to broad base its assistance to SSIs; and
- establish an independent IT Cell/Wing to implement the information technology system, sound internal control and effective internal audit.

2.3 Review on Materials Management of Madhya Pradesh Power Generating Company Limited.

Executive Summary

Introduction

The Madhya Pradesh Power Generating Company Limited, in order to operate and maintain its three thermal plants (total capacity of 3687 MW) and seven hydel plants located in the State, through its 21 stores is providing raw materials/inputs such as coal, oil and critical inventory/spares. Hence, effective management of inventory ensures timely availability of essential items for efficient operations with minimum blocking up of capital by ascertaining needs of stores on time and arranging such materials in the most efficient, economical and expeditious manner.

In order to review status of materials management in the Company a review on this subject, covering transactions from 2010-11 to 2012-13 in respect of all stores attached to three thermal plants was conducted in April to July 2013. The main findings, conclusions and recommendations arising out of the review are summarised below.

Planning and scheduling for Procurement of material

In the absence of any norms fixed in terms of days for publication and awarding of tenders from the date of receipt of indent from user department, the Company had taken time ranging from 38 days to 246 days in publishing Notice Inviting Tender (NITs) and a total of 238 days to 510 days for placing purchase orders, thus affecting its annual planned requirement.

Procurement of materials

In 43 cases where the value of Purchase Order (PO) exceeded ₹ five lakh, the requirement was not published in newspapers as required under its established procedures. Further, the Company had not only foregone an opportunity to obtain competitive rates, but also failed to develop a secondary source of supply to overcome possible contingencies due to placement of 66 POs on single tender basis.

Materials/spares valued ₹ 9.75 crore, was procured without assessing the actual requirement and were found to be lying in excess and inactive at various stores, resulting in blocking up of Company's funds.

Coal losses written off in excess of limits permitted by Madhya Pradesh Electricity Regulatory Commission (MPERC) amounted to ₹50.14 crore (2010-11), ₹35.19 crore (2011-12) and ₹40.50 crore (2012-13) respectively.

Due to excess holding of secondary oil beyond 60 days, the additional carrying cost amounted to ₹ 1.40 crore to ₹ 2.76 crore during 2010-13.

In 164 purchase orders valued ₹ 102.84 crore, the Company waived the tender condition for collecting 10 per cent security deposit of ₹ 6.64 crore from the suppliers. In respect of 52 purchase orders, material was not supplied even after lapse of two to three years.

Irregularities in inspection, receipt and issue of materials

As against Company's clear instructions to issue Material Receipt Certificate (MRCs) within seven days from the date of receipt of material at stores for processing payments to suppliers, in respect of 325 supplies against POs, the management delayed issue of MRCs for periods up to 209 days (Sarni), 918 days (Birsingpur) and 101 days (Chachai) respectively.

Introduction

2.3.1 Madhya Pradesh Power Generating Company Limited (Company) is a wholly owned Company of Government of Madhya Pradesh (Government) and is engaged in generation of electricity. It is the successor entity of erstwhile Madhya Pradesh State Electricity Board (MPSEB) and came into being w.e.f. 1 June 2005.

Management of the Company is vested in a Board of Directors (BODs) appointed by the State Government. The day to day operations are carried out by the Managing Director who is the Chief Executive of the Company and is assisted by the Executive Directors, Chief Engineers, Superintending Engineers and Executive Engineers.

To operate and maintain its three thermal plants and seven hydel plants (total capacity of 3687 MW) located in the State, the Company is maintaining 21 stores (thermal- 11 and hydel-10) to provide coal, oil and other critical inventory/spares. Besides, open land/stock yard/tanks are also being used for storing coal and oil.

While on one hand it is essential to ensure availability of raw materials viz. coal and oil, stores and spares for uninterrupted operations and maintenance of generating power stations, on other hand excess inventory holding leads to additional carrying cost on account of interest, storage and handling charges, insurance, record keeping, inspection and risk of deterioration in quality, which adversely affects the profitability of the organization. Hence, management of inventory ensures timely availability of essential items with minimum blocking up of capital in the most efficient, economical and expeditious manner.

Audit Objectives

2.3.2 The objectives of audit were to examine whether:

- system of planning and scheduling for procurement of material existed and was adequate and required funds were provided for procurement;
- inspection, receipt and issue of materials were according to prescribed procedures and

- system for identifying and timely disposal of obsolete, slow and non-moving materials was adequate.

Audit Criteria

2.3.3 Audit criteria, for the purpose of audit were derived from following sources:

- orders and guidelines of Government of Madhya Pradesh Electricity Regulatory Commission (MPERC), MPSEB Purchase and Stores manual/procedures of Company, terms and conditions of tender/supply etc;
- norms laid down by the Management for holding raw material and stock of spares and categorisation of slow moving, non-moving and obsolete items;
- Agenda and Minutes of BoDs meetings.
- delegation of financial powers at various levels for procurement.

Scope and Methodology of Audit

2.3.4 We reviewed records and systems/procedures relating to procurement and storing of coal, oil and stores/spares for three years 2010-11 to 2012-13 of 11 stores¹ of three thermal plants.

The scope and methodology of Audit were explained to the Management in an entry conference held in April 2013. The audit was conducted during April to July 2013. Audit findings arising out of audit were discussed in an exit conference held with the Government and Management on 21 October 2013. The views and replies of the Government/Management on audit findings have been appropriately incorporated in the review.

Acknowledgement

2.3.5 We acknowledge the co-operation extended by Government and the Company in providing necessary information, records and clarifications for smooth conduct of the review.

Audit findings

Analysis of closing inventory/spares

2.3.6 In terms of MPERC regulations, carrying cost of stores and maintenance spares held in stock to the extent of 20 *per cent* of normative Operation & Maintenance (O&M) expenses would be eligible for tariff fixation. Carrying cost of stores and spares held in excess of the limits prescribed will have to be absorbed by the Company. The table no. 2.3.1 indicates the available closing inventory/spares from 2010-11 to 2012-13.

¹ Includes merged construction division stores

Table 2.3.1				(₹ in crore)
Sl. No.	Particulars	2010-11	2011-12	2012-13
1	Coal	74.25	199.39	267.83
2	Oil	34.06	55.77	75.53
3	Stores & Spares	231.17	216.62	269.04
	Total	339.48	471.78	612.40
4	Non-moving stores & spares	44.11	53.28	37.99
5	Percentage of non-moving to total spares	19	24	14
6	Spares qualifying for tariff fixation as approved by MPERC	138.78	145.55	164.66
7	Excess Stock of spares (Sl.No.3-6)	92.39	71.07	104.38
8	Excess carrying cost @ 9 per cent p.a.on Sl.No.7	8.31	6.40	9.40

Source : i) Data as obtained from Finance and Stores wing and figures as submitted to MPERC for tariff fixation by the Company.

It can be observed from the above table that even though there is a decline in holding of non-moving inventory/spares from 19 to 14 *per cent* during the last three years, the Company is holding inventory/spares beyond MPERC allowable limits of maintenance spares at the rate of 20 *per cent* of the normative O&M Expenses. The cost of carrying stores and spares in excess of limits worked out to ₹ 8.31 crore, ₹ 6.40 crore and ₹ 9.40 crore during the years 2010-11, 2011-12 and 2012-13, respectively.

While the overall holding of stores and spares ranged between 1.5 and 1.7 months' consumption during the period covered in audit, we observed that inventory holding of some high value items exceeded 24 months' consumption and even beyond. Few such cases are listed in the Annexure 2.3.3 of the Report.

Planning and scheduling for procurement of material

2.3.7 Timeframe for planning of procurement of material

2.3.7.1 Up to 2012-13, the Company has not evolved any policy to have an Advance Procurement Plan in place. However, the user departments on the basis of Anticipated Annual Requirement (AAR) of the items mandated for centralised procurement and also the other spares and stores that are required in a year, send indents to the Material Management (MM) department at Corporate Office who is

responsible for centralised procurement² of goods. The requirement of users is compiled and consolidated by MM department before publication of Notice Inviting Tender (NIT). Thereafter, the tendering procedures are followed and with the prior approval of competent authority, orders are placed on the successful suppliers/ bidders.

The MM department has taken 38 to 246 days to publish NITs and 238 to 510 days to award PO's from the date of receipt of indents.

During test check of AAR of centralised items, which were consolidated and finalised by Chief Engineer/Material Management (CE/MM), Jabalpur, we noticed that no time limit for sending the annual requirements was prescribed by the MM department. Time limit or norms were also not fixed for finalising indents. In the absence of time limit, the indents of spares required in a year are received from user departments after the commencement of the year for which indents are made, thereby defeating the purpose of preparation of annual indents. We further noticed that in 15 out of 141 cases of centralized purchases test checked, the time taken by the MM department to publish the NIT ranged from 38 to 246 days from the date of receipt of indents and 238 to 510 days for award of purchase orders (POs) (*Annexure-2.3.1 & 2.3.2*). Similarly, for procurement of stores and spares other than centralised items like grinding balls, other than mill bearing spares etc., the MM department took 30 to 160 days from the date of receipt of indents for publishing NITs and 210 to 441 days for award of POs (*Annexure-2.3.1 & 2.3.2*).

We further observed that the delivery schedules in respect of 8 out of 47 POs test checked and placed by MM Department spilled over to the subsequent year. Abnormal time taken for placement of order and spilling of delivery schedules to subsequent year would defeat the objective of procurement based on Anticipated Annual Requirement planning and the need/requirement of generating stations are not met affecting efficiency of plants, which would result in further wear and tear.

The Management stated (July/October 2013) that inviting tenders after ensuring actual requirement at site, evaluation and vetting of indents and re-confirmation of requirements from user departments normally required six to eight months. It was also stated that compilation and consolidation of requirements was a time consuming process and there could be further delays on account of clarifications obtained from bidders. The fact remains that Para 2.5 of the Memorandum on Purchase Procedures clearly stipulates that the time required for various factors having a bearing on supply should be centralised and indents raised accordingly to ensure that supply materialised as per requirement.

Fixation of norms of various inventory levels

2.3.7.2 In terms of MPSEB stores manual, minimum stock level, maximum stock level and average consumption levels for the items to be maintained in all the stores should be fixed. As the levels were not fixed in terms of the manual in all the stores, the Additional Secretary of the Company directed (August, 2009) all

² Like pulveriser mill grinding elements/components, mill bearing, air heater tubes, conveyor belts, oil & lubricants, control power cables etc.

concerned authorities in charge of stores to ensure compliance of the provisions of the manual. We noticed that the management of none of the three generating stations test checked had so far (June 2013) adhered to these directions.

While accepting the audit observation, the Management stated that (October 2013) stock levels would be fixed under the new Enterprises Resource Planning (ERP) system which is to be introduced soon.

Procurement of materials

2.3.8 Placement of purchase order on single tender basis

2.3.8.1 As per the established purchase procedures, the Company had to call for tenders/quotations from at least three approved vendors/parties and wherever, the value of materials indented exceeds ₹ 5.00 lakh, tenders were to be published in at least two daily newspapers.

We noticed that in respect of 66 cases quotations were called for from single party only and in respect of 43 cases where estimated value of materials exceeded ₹ 5.00 lakh, the Company failed to publish NITs in news papers.

We observed that while the MM department publishes NIT for centralised procurement, there was no practice of publishing tenders exceeding ₹ 5.00 lakh by the generating plants. We also observed that quotations were being called from a single supplier by the generating plants. During test check of 235 purchase orders³ relating to three thermal plants, we noticed that 66 tenders were called from a single party only, of which in 43 cases⁴, though estimated value of supply exceeded ₹ 5.00 lakh, tenders were not published in news papers.

It was replied (October 2013) by the Management that critical items of special/proprietary nature where reverse engineering could not be done are being procured from OEMs on single quotation basis. However, audit observed that even the suppliers of commonly used spares/consumables were being treated as OEMs and single tender was invited. Further, the Company failed to explore alternate sources of supplies from open markets to increase its vendor base by publishing tenders and was dependent on single source. This not only resulted in violation of established procedures and resultant foregone opportunity to obtain competitive rates but also in failure to develop a secondary source of supply to overcome possible contingencies.

Unwarranted procurement of materials/spares resulted in non-moving of inventories and blocking of funds

2.3.8.2 A review of Purchase Orders placed by the three test checked generating stations (thermal) during the period covered under audit and the stock holding of the items procured indicated that the items that were to be procured through centralised purchase were directly procured on the plea of urgent need/critical for operations. However, we observed that many of these items were not utilised by the concerned plants for periods ranging from one to twelve years resulting in blocking of Company's funds. Details in respect of few purchase orders, where

³ value ranging between ₹ 1.70 lakh and ₹ 83.55 lakh

⁴ value ranging between ₹ 5.67 lakh and ₹ 83.55 lakh

the procurement resulted in accumulation of non-moving inventories are given in **Annexure 2.3.3.**

Unwarranted procurements of materials resulted in blocking of funds amounting to ₹ 9.75 crore (slow moving ₹ 6.74 crore and non-moving inventory ₹ 3.01 crore).

The above cases includes inventory of ₹ 9.75 crore (slow moving inventory ₹ 6.74 crore and non-moving inventory ₹ 3.01 crore). These procurements and their non-utilisation indicates that the Company had failed to make proper assessment before placing indents/orders by taking past consumption pattern into account and decision to procure additional quantities (especially Alloy Steel Tube & Electric Resistance Welded pipes) are thus unjustified.

The Management stated (October 2013) that most of the items were insurance spares⁵ and were either required for planned overhauls or regular maintenance. The reply is not acceptable to audit as insurance spares are capitalised as part of assets and the audit observation do not relate to insurance spares but to spares lying in inventory that have been procured for overhauls/maintenance. As procurement has to be timed with the schedule for overhauls, procurement well in advance/delayed procurement has resulted in accumulation of inactive/non-moving inventory.

Coal losses on account of transit, stacking and handling exceeding MPERC norms

2.3.8.3 Coal is one of the major inputs and important raw material required for generation of power and consumes the major portion of Company's working capital. Adequate planning and proper arrangement for timely supplies is required to ensure uninterrupted operation of the generating plants.

The Company, to meet its coal requirements, procures coal from the mines of South Eastern Coalfields Limited and Western Coalfields Limited located at a distance of 70 to 450 Km from the three thermal power stations. During transportation of coal and its handling at the plant, some quantity is lost by wind, moisture, spontaneous combustion and as carpet coal⁶. Besides, loss also occurs due to inaccuracies found in weighment process. Taking all these factors into consideration, the Madhya Pradesh Electricity Regulatory Commission (MPERC) has fixed a normative allowable loss of 0.2 *per cent* for pit head and 0.8 *per cent* for the non-pit head generating stations. As any loss exceeding permissible limits will have to be absorbed by the Company, it is necessary for the management to take concrete steps to arrest/reduce these losses.

The table 2.3.2 indicates the total coal procured and losses incurred on transit, Stacking and Handling (S&H) of coal during last four years ending 31 March 2013.

⁵ Insurance spares are mandatory spares which are either supplied during erection & commissioning of plants or replaced during capital overhauls and are capitalised to assets, whereas consumption of O&M spares are charged to P&L account.

⁶ Carpet coal : Formation of soft carpet, comprising of coal and dust which result in loss of coal

Table 2.3.2

Sl. No.	Particulars	2010-11	2011-12	2012-13
1	Total Quantity Received (MT)	13622422	13251387	14349795
2	Actual Loss on account of			
	(i) Transit (MT)	43326	50363	51665
	(ii) S&H (MT)	336200	187133	183009
	Total Loss (MT)	379526	237496	234674
3	Permissible limits for losses by MPERC (MT) (0.2 to 0.8)	127110	100472	107113
4	Loss in excess of norms fixed by MPERC (MT) (Sl. No. 2 – 3)	252416	137024	127561
6	Loss charged to P&L Account in excess of permissible limit (₹ in crore)	50.14	35.19	40.50

Source: Data as provided by Finance & Accounts wing of the Company.

Coal losses written off in excess of permissible limits amounted to ₹ 50.14 crore (2010-11), ₹ 35.19 crore (2011-12) and ₹ 40.50 crore (2012-13).

It can be observed from the above that the losses during transit and S&H though marginally decreased in 2011-12 when compared to 2010-11, it increased marginally in 2012-13. The total coal losses during 2010-11 which stood at ₹ 50.14 crore increased by 38.39 *per cent* over 2009-10 losses (₹ 36.23 crore). Thereafter, it decreased by 29.81 *per cent* (₹ 35.19 crore) in 2011-12 and increased by 15.09 *per cent* (₹ 40.50 crore) in 2012-13 respectively. Out of three thermal plants reviewed in audit we noticed that the transit and S&H losses was high in SGTPS, Birsinghpur and worked out to ₹ 28.05 crore (56 *per cent* of the total coal losses), ₹ 23.82 crore (68 *per cent*) and ₹ 23.78 crore (68 *per cent*) respectively during the last three years up to 2012-13 in excess of permissible limits.

No adequate measures were taken and implemented by the Company to arrest coal losses.

In order to study the causes for such losses, the Company constituted (March/April 2008) a committee of Engineers who recommended creating sufficient infrastructure by providing concrete flooring of coal yards, fencing, training personnel in stacking and handling etc. Similar measures to control coal losses were also recommended (November 2010) by the Director (Vigilance). Audit observed that even after a lapse of three years except for work undertaken to construct a compound wall, no other recommendations were implemented by the Company.

We also observed that even though MPERC has not fixed separate norms for carpet coal losses as it is a part and parcel of stacking and handling process, for which norms already existed. The Company however conceptualized and provided for the carpet coal losses accumulated for over 47 years at 14 coal yards in its three thermal plants in the books of accounts for the year 2009-10 and wrote off (March/July 2012) 114217 MTs valued ₹17.82 crore As carpet coal losses was not separately allowable in terms of MPERC regulations, the Company had absorbed this additional loss on account of carpet coal from its own accruals.

The Management replied (October 2013) that MPERC has gradually reduced the norms for coal losses. It was also stated that boundary walls were being constructed and security arrangements enhanced, to further reduce losses. The fact remains that non adherence to norms fixed by MPERC would result in increased losses to the Company and steps to minimize coal losses as per recommendations

made by consultants/vigilance department has not been taken by the Company so far (October, 2013).

Excess inventory held in respect of secondary oil

2.3.8.4 After coal, the second most consumable inventory in power plants both in physical and financial terms is secondary oil which includes furnace oil (FO), High Speed Diesel (HSD) and Light Diesel Oil (LDO), which is used alternatively to ignite/fire to maintain the required temperature/heat in the boilers. Secondary oil is being procured from centrally owned PSUs on rate contract basis. The annual consumption of secondary oil was about 59933 KL, 57204 KL and 49924 KL during the years 2010-11, 2011-12 and 2012-13, respectively.

MPERC allows holding of inventory of 60 days of consumption of oil for the purpose of determining the cost of working capital. Thus, the Company, by efficient management in procurement and distribution of oil to the generating plants, could improve its profitability.

A review of monthly consumption of secondary oil vis- a- vis stock of closing balances of inventory held in terms of number of days indicated that the holding of secondary oil was in excess of the norms prescribed by MPERC for calculating the interest on working capital. The details of inventory held and the impact in terms of carrying cost in the generating stations is given in ***Annexure 2.3.4.***

Due to excess holding of secondary oil beyond 60 days, the additional carrying cost amounted to ₹ 1.40 crore to ₹ 2.76 crore during 2010-13.

It can be observed from the Annexure 2.3.4 that all the three thermal plants were holding an average excess stock of secondary oil (worked out at 85 *per cent* Plant Availability Factor)⁷ ranging from 434 KL to 2351 KL (FO) and 555 KL to 1016 KL (LDO) considering the requirement for 60 days. The excess holding was to the extent of 16 to 336 days requirement (i.e., even after holding inventory upto 60 days) respectively. Based on their value, the additional carrying cost on holding stock in excess of sixty days requirement amounted to ₹ 1.40 crore, ₹ 1.75 crore and ₹ 2.76 crore during the years 2010-11, 2011-12 and 2012-13 respectively.

While accepting the audit observation, the Management replied (October 2013) that necessary action to bring in improvement would be undertaken.

Receipt of materials/spares after attending Annual Overhaul (AOH)

2.3.8.5 In order to maintain minimum spares of hydraulic coupling to meet any emergency/ preventive maintenance clubbed with its planned Annual/ Capital overhaul of Unit-5 (1 x 500 MW), the CE (Generation), Birsinghpur invited a single bid in September 2010 from Voith Turbo Private Limited, Hyderabad (VTPL). Accordingly, a purchase order valued at ₹ 23.57 lakh was placed (April 2011) with VTPL. Supply was received on 30 August 2012.

⁷ As per Annual Revenue Requirement (ARR) for tariff fixation, PAF considered is 85% - 88% depending on the capacities of power stations.

Receipt of material/spares after attending Annual Overhaul rendered an investment of ₹ 23.57 lakh idle.

In this connection, we observed that the spares stated to be required during AOH⁸ between 30-08-2012 and 15-09-2012 were inspected on 22-09-2012, after completion of AOH and remained idle thereafter in the stores. The likelihood of its utilisation would arise only after three to five years when the schedule for next AOH becomes due. Thus, the plant was made operational without complete replacement of materials during overhaul and has defeated the objective of procurement. Thus, the spares required for preventive maintenance and also to meet emergency were received after completion of AOH rendering the procurement redundant with unnecessary blocking up of Company's funds amounting to ₹ 23.57 lakh.

The Management stated during exit conference (October 2013) that due to financial difficulties the delay occurred. The reply is not acceptable to audit as whenever AOH are planned by the Company, it should ensure availability of funds so that the procurement process of critical items are either not stalled or delayed jeopardising operations. As these items are plant specific, their alternate use was not possible till next overhaul after three to five years. Hence, financial planning for receipt of materials and its utilisation should have been ensured/prioritised.

Non-compliance of guidelines/instructions

2.3.8.6 Government of M.P. issued directions (August/September 2010) to introduce E-Tendering system in the Company from October 2010. The Company has not introduced E-Tendering for orders placed till June 2013, which not only amounted to non-compliance of instructions but also deprived the Company of the benefits of competitive bidding and strengthening of vendor base.

We observed that with the approval of Government, the Company started the e-tendering process from July 2013 by uploading tenders in the GoMP website.

The Management stated (October 2013) that procurement through e-tendering system has commenced from 1 July 2013. The fact remains that the Company started the e-tendering system only after a delay of over 30 months after issue of instructions by GoMP in September 2010, while the Government departments had started e-tendering from October 2010 itself.

Irregular exemption and waiver of Security Deposit and Earnest Money Deposit

2.3.8.7 As per Clause 15 of standard tender document and circular instructions issued from time to time, the Company has to collect 10 *per cent* of cost of purchase order value as Security Deposit (SD) against performance Guarantee (PG) from the suppliers. The Company also has the system of collecting one time fixed amount ranging from ₹ 3 lakh and ₹ 5 lakh towards permanent of security deposit (PSD) from the suppliers and exempt them from paying SD for each order

⁸ The material/spares required during overhaul cannot be put to use till next overhaul due after three to five years.

placed with them. Besides, Public Sector Undertakings like Bharat Heavy Electricals Limited, Indian Oil Corporation Limited, Hindustan Petroleum Corporation Limited, etc. are exempted from payment of SD. The tender notices issued for procurement included the condition for payment of security deposit amounting to 10 *per cent* of the value of order.

In deviation to Purchase Policy, the Company waived to collect 10 *per cent* of security deposit amounting to ₹ 6.64 crore in respect of 164 POs.

During test check, we observed that in 164 purchase orders (Centralised-1 No and Local- 163 Nos) valued ₹ 102.84 crore placed on private suppliers between April 2010 and March 2013, the Company did not collect 10 *per cent* of SD amounting to ₹ 6.64 crore (includes 5 *per cent* differential SD of ₹ 3.64 crore in one case on ₹ 72.80 crore) as contemplated in the tender documents. In 52 of these purchase orders, value ranging between ₹ 0.14 lakh and ₹ 98.69 lakh, the ordered materials was not supplied even after lapse of two to three years.

We further observed that the Company decided to exempt the suppliers from payment of SD at the time of placing orders.

This not only defeats the objective of protecting Company's financial interest through assured supply of prescribed specifications but also resulted in extending undue favour to suppliers.

2.3.8.8 The first criteria/step to open quotations and tenders is submission of Earnest Money Deposit by the bidders who are not exempted from such deposit (firms registered as SSI units and central PSUs are exempted from deposit of EMD). We observed in audit that in respect of four tenders (value ranging between ₹ 3.75 lakh and ₹ 20.95 lakh), payment of EMD from bidders who were not under the exempted category, was waived by the Company.

We further observed that while the terms and conditions of tender document provide for collection of EMD/SD/PBG, the Delegation of Powers (DOP) of the Company provides powers to officers for approving waiver from payment. We are of the opinion that the powers delegated were meant to be exercised for making changes in the tender documents before inviting bids, as granting waiver after receiving bids tantamount to extension of undue favour to suppliers. Since the condition was incorporated to protect defects during the liability period, any such waiver subsequent to calling and finalisation of tender is an undue favour and hence waiver is unjustified. We also observed that this exemption is granted on the grounds that the supplier is an Original Equipment Manufacturer (OEM) (including authorized dealers). We however noticed that even for consumables materials like nuts, bolts, electrodes, caustic soda lye etc., SD is being waived considering the supplier as OEM. Waiver of the condition to some bidders could also invite litigations, when it is approved after invitation of tender.

During exit conference, the Government stated (October 2013) that the existing system of waiver of SD would be reviewed. It was further stated that compliance to instructions on collection of SD would be ensured in future.

Irregularities in inspection, receipt and issue of materials

2.3.9 Inordinate delay in issue of Material Receipt Certificate (MRCs)

2.3.9.1 MPSEB issued instructions in December 1996 to HODs at site to strictly adhere to the time limit of seven days from the date of receipt of material prescribed for issue of MRCs by duly completing entire process of receipt and inspection of materials. These instructions were also adopted by the Company since its incorporation.

A test check of MRC Registers maintained by all the thermal plant stores indicated that out of 4997 items for which MRCs were issued during 2010-13, there was delay in inspection and issue of MRC in respect of 325 items of material (STPS, Sarni-120, SGTPS, Birsinghpur-124 and ATPS, Chachai-81), as detailed below in table no 2.3.3.

Table No. 2.3.3

Sl. No.	Area Stores	2010-11		2011-12		2012-13	
		Range of Delay (in days)	Range of PO (₹ in Lakh)	Range of Delay (in days)	Range of PO (₹ in Lakh)	Range of Delay (in days)	Range of PO (₹ in Lakh)
1	STPS, Sarni						
	(i) EE (O&M), Store-I	8-195	0.10-15.90	8-103	0.05-35.42	10-150	0.09-11.00
	(ii) EE (O&M), Store-II	12-209	0.33-20.94	12-57	0.02-62.72	8-209	0.02-112.38
2	SGTPS, Birsinghpur						
	(i) EE (O&M), Store-I	12-604	0.13-12.03	15-139	0.14-68.00	16-222	0.10-17.67
	(ii) EE (O&M), Store-II	30-649	0.12-27.66	17-918	0.07-83.43	20-107	0.06-3.94
3	ATPS, Chachai	10-45	0.14-5.71	16-70	0.03-19.11	15-101	0.03-44.40

Source: Data prepared out of Daily Receipt Register, Inspection notes and Material Receipts Certificate issued by concerned stores of the Company.

As against a time limit of seven days for issue of MRCs, the Company has taken a maximum of 101 to 918 days. The delay in conducting inspection of material also ranged between 10 days and 918 days.

It can be observed from the above table that in preparation of MRC's by STPS, Sarni, SGTPS, Birsinghpur and ATPS, Chachai there was delay of up to 209 days, 918 days and 101 days respectively. Audit further observed that inordinate delays were found while conducting inspection of materials and the delays ranged between 9 to 207 days (Sarni), 10 to 918 days (Birsinghpur) and 8 to 90 days (Chachai) respectively which clearly indicates that the delay was by the indenting divisions themselves and procurement of material thus does not appear to be need based.

While accepting the audit observation, the Management stated (October 2013) that practice of periodic (weekly) reporting has been introduced from May 2013 and the ERP system which is proposed to be implemented would reduce the delays.

Material at Site

2.3.9.2 According to the Manual of Instructions of Stores of erstwhile MPSEB and as adopted by the Company, when material is required for works, it is issued to the works either from stock or through purchases and the items so issued is kept in the Material At Site account pending capitalisation/consumption. Further, all surplus materials at site, works on which have been completed or stopped or on

which outlay has been prohibited for any considerable length of time, should be transferred to other works in progress or brought on to the stock account. The stores/spares dismantled or removed due to replacement during regular maintenance/ overhaul should be brought back to stock either as scrap or reusable stores. An illustrative list of materials replaced during regular maintenance/ overhaul is listed out in the **Annexure- 2.3.5** some of the inadequacies noticed by Audit in the maintenance of MAS are as under:

We observed that materials drawn for replacements and repairs by various divisions either remained unreplaced or if replaced were not devoluted back to stores. Reconditioned materials which were stated to be required for reuse were not accounted for as spares.

- We observed that materials drawn for replacements by Boiler Maintenance Division (BMD), Turbine Maintenance Division (TMD), Electrical Maintenance Division (EMD), Coal Handling Plant (CHP) etc., were not devoluted back to stores as scrap. We also observed that the replaced materials/spares were being kept at site citing reasons that they can be re-used on repair and reconditioning. Retaining the material at site instead of bringing it to stock of the divisional stores and holding material without inspection as to their serviceability would impact the process of procurement planning. We further noticed that physical verification of the stores/spares replaced and at site was not conducted.
- During a test check of MAS maintained by all the three thermal plants, we noticed that in SGTPS, Birsinghpur discrepancies/differences in closing balances of materials/spares found in respect of 'O' Ring Insert (8 Nos), Steam Globe V/V 2500 Class (2 Nos), Globe valve 1' (7 Nos), Tungston Carbide TC (Ring) Dura (2 Nos), Pump Shaft (2 Nos), Vinton 'O' Ring (1 Nos), Sleeves Packing (12 Nos) in physical verification remained to be adjusted. In the absence of specified time frame for transfer of all items on completion of work to stores and reconciliation of the discrepancies/differences, the Company may not be in a position to ensure that the material at site are properly accounted for and stored for future use.
- There were instances of high value materials/spares (valued ₹ 1.43 crore) drawn for regular maintenance and for immediate replacement remaining unutilized for periods ranging from one to four and over five years from their drawl from main stores. We further noticed that even consumable items like HPSV lamps, which can be purchased at short notice, were kept in MAS for long periods.

While accepting the audit observation the Management stated (October 2013) that efforts were being made to overcome these deficiencies which will be taken care of once ERP system is introduced by the Company.

Non-coverage of insurance of assets/property and stores

2.3.9.3 A review of the Company's record indicated that as at the end of 31 March 2013, the Company was holding total inventory/stocks valued ₹ 1363.82 crore (Coal and Oil- ₹ 343.36 crore and Capital and O&M spares/materials- ₹ 1020.46 crore). However, it is observed in audit that despite stocking of combustible and hazardous materials and high value inventories, there is no practice in the Company to obtain insurance policy/coverage against theft, burglary, fire accidents and other perils of nature. Besides, it is also learnt that the total tangible

assets (net block)/ property valued ₹ 4437.91 crore (excluding capital work-in-progress- ₹ 7035.64 crore)) of Company is also not covered through any insurance.

It was replied (July/October 2013) by the Management that Public Liability Insurance Policy (covering hazardous materials) was being obtained regularly and work in progress of ongoing projects was also covered through insurance. It was further stated that action to cover other assets/property and stores of running power stations was under active consideration. Further progress is awaited in audit.

Non-disposal of scrap

2.3.10 Non disposal of scrap/obsolete materials

2.3.10.1 Due to continuous operation of plants, wear and tear of machinery/equipments and other material occurs, which on replacement were scrapped and handed over by Return Indent (RI) to the concerned stores.

For disposal of scrap material the Company has entered into an agreement with MSTC Limited⁹. In this regard, guidelines were issued (January 2007) by MSTC for preparation of lots for the purpose of e-auction, who acts on the basis of the list of disposable materials received from its principal (Company). MSTC was entitled for a service charge at the rate of three *per cent* on the sales realisation.

Scrutiny of records at Corporate Office, Jabalpur indicated that as at the end of March 2013, scrap/obsolete items valued at ₹ 4.66 crore (thermal- ₹ 4.40 crore and hydel - ₹ 0.26 crore) in 255 lots (thermal- 119 and hydel-136) was lying un-auctioned in all the power houses.

The Management replied (October 2013) that except for 28 *per cent* of scrap which were not purchased by buyers/not sold by the Company due to unacceptable prices, the balance scrap was sold and lifted till October, 2013. The undisposed scrap of 28 *per cent* valued at ₹ 1.22 crore included scrap valued at ₹ 1.12 crore (scrap of ₹ 0.26 crore lying undisposed since April 2010) at STPS, Sami.

Conclusion:

We found that the norms on time limits for publishing NITs and placing POs from the receipt of indents from user departments were not fixed and there were several instances of orders being placed after the close of the year for which requirement was assessed. The Company (especially the plant management) had constantly deviated its purchase procedures/policy by placing purchase orders based on single tender basis. The Company had not also standardised the stocks levels to avoid unnecessary holding of stocks. Many instances of inactive and non-moving inventory were primarily due to unplanned/ unwarranted procurements resulting

⁹ A Government of India Enterprise

in blocking of Company's funds, besides coal losses beyond MPERC norms/limits, excess inventory of secondary oil was also noticed. Materials/spares were being received and inspected after completion of Annual overhauls for which procurement was made and consequent retaining of spares for long periods without use. The Company is exempting/relaxing the condition on recovery of SD/EMD from its suppliers and as a result, the Company has not been able to bind the supplier to financially indemnify in case of default/sub-standard supply and lack of seriousness in supply etc.

Instances of inordinate delay in issue of MRCs, non-devolution of materials, non-accountal of spares/re-usable items and other discrepancies in MAS were also noticed.

Recommendations:

In order to have an efficient material management the Company should:

- fix timeframe for assessment of requirement, inviting tenders and awarding of purchase orders so as to achieve objective of planned purchases and avoid delay in purchases;
- consider fixing stock levels for different categories of stores and spares to minimise inventory holding in excess of limits allowed by MPERC;
- introduce a mechanism to ensure that purchases by power stations are not made on a single tender basis when items are not of proprietary nature;
- create sufficient infrastructure facilities for stacking and handling of coal so as to arrest/minimise coal losses; and
- ensure compliance to its own policy/guidelines in collection/waiver of security deposits for protecting its financial interest.

2.4 Review on Evaluation and Management of Build, Operate and Transfer scheme of Madhya Pradesh Road Development Corporation Limited

Executive Summary

Introduction

Madhya Pradesh Road Development Corporation Limited, incorporated in July 2004 under the Companies Act, 1956, is engaged in strengthening, upgradation and development of the state highways and major district roads (MDR) in the State of Madhya Pradesh. The Company is mandated to provide an efficient, adequate and proper road infrastructure in the state.

During 2009-10 to 2012-13, the Company completed 16 project highways under different models of Build Operate and Transfer (BOT) Scheme under Public Private Partnership (PPP).

Overview of executed road projects

Out of the 16 completed projects, the Company completed 11 projects within the scheduled period of completion. There were delays of 67 days to 564 days in achieving Commercial Date of Operation in remaining five projects. The major reasons for delays were delay in financial closure, delay in handing over of site and problems associated with Right Of Way

Erroneous Treatment of Environmental Mitigation cost

The Company allowed 25 per cent escalation on the environment mitigation cost also treating it as construction cost. This resulted in higher payment to concessionaries amounting to ₹62.71 lakh towards Viability Gap Funding.

Increase in project cost due to adoption of higher specification

Considering the present and projected traffic on the road, two lane standard on the Khimlasa-Malthon section of the Bina-Khimlasa-Malthon project highway was not warranted. Developing this section on two lane standard thus resulted in unwarranted and avoidable expenditure of ₹14.37 crore towards proportionate VGF

Payment of bonus and annuity under BOT (Toll plus Annuity) model

For the development of three project highways the Company formulated a new model of PPP viz. BOT (Toll plus Annuity). Due to not reducing the construction period as recommended by the Consultants payment of bonus for early completion resulted in unintended benefit of ₹16.82 crore to the Concessionaires.

Selection of Public Sector undertaking as partner under PPP

Contrary to the principles of PPP the Company selected a public sector entity for the development of the Bina-Kurwai-Sironj Project highway.

Incorrect fixation of toll

The Company did not formulate and document standard procedure for fixation of toll rates. This resulted in unintended benefit to concessionaire to the tune of ₹ 37.43 lakh towards higher toll rates.

Delayed remittance of premium by the concessionaire

The concessionaire of the Indore-Ujjain project highway did not remit to the Company the premium amounting to ₹ 7.69 crore as on 30 September 2013

Introduction

2.4.1 Madhya Pradesh Road Development Corporation Limited, Bhopal (Company) under the administrative control of Public Works Department, Government of Madhya Pradesh was incorporated on 14 July 2004 as a wholly owned government company under the Companies Act 1956, with the objective of executing roads and allied infrastructure projects or for objects, as envisaged in public-private or joint venture basis.

The Company was notified (October 2005) as the State Highway Authority under Madhya Pradesh Rajmarg Adhiniyam, 2004 and given mandate to develop and operate State Highways. The Company is engaged in strengthening and development of State Highways and Major District Road (MDR) projects. Majority of these are on "Build Operate and Transfer (BOT) contracts under "Public Private Partnership" (PPP) Model.

The Company is required to follow guidelines and "Model Concession Agreement" (MCA) of the Planning Commission, Government of India issued (between 2006 and 2008) for BOT contracts under PPP Model. The Company followed BOT (Toll)¹, BOT (Annuity)² and BOT (Toll plus Annuity)³ models for contracts with concessionaire⁴ for construction and development of highways.

During the period from 2009-10 to 2012-13, the Company completed 16⁵ project highways at an estimated cost of ₹ 3,803.81 crore⁶ as detailed in **Annexure 2.4.1**. Apart from these, 14 project highways⁷ were ongoing.

¹ Under this Model, Concessionaire is allowed to collect and keep Toll charges for specified period with 'Viability Gap Funding' to him or 'Premium' to be paid by him.

² Only a fixed sum as annuity is paid to Concessionaire every six months during the concession period.

³ Besides annuity, Concessionaire is allowed to collect Toll also during the concession period.

⁴ Concessionaire is the Private Sector Partner who undertakes investments and operates the facility for a fixed period of time after which the ownership reverts back to the public sector.

⁵ 13 on BOT (Toll) and 3 on BOT (Toll + Annuity) model

⁶ ₹ 3,596.37 crore (BOT Toll) plus ₹ 207.44 crore (BOT Toll + Annuity)

⁷ Damoh-Jabalpur, Satna-Chitrakoot, Bina-Kurwai-Sironj, Bhopal bypass, Jhabua-Kukshi, Damoh-Hirapur, Sarangpur-Shujalpur, Seoni-Maharashtra Border, Khandwa-Burhanpur Road, Lakhnadon-Seoni Border, Rau-Mandleshwar, Patan-Raheli Road, Bhopal-Sironj, Ishagarh-Guna

Organisational set-up

2.4.2 The Management of the Company is vested in a Board of Directors comprising nine Directors⁸ including a Chairman. The day-to-day operations of the Company are carried out by the Managing Director, who is the Chief Executive of the Company, with the assistance of a Technical Adviser, Chief Engineer (BOT), Chief Engineer (Procurement), Chief Engineer (Maintenance/MDR), Chief General Manager (Human Resource Development), Deputy General Manager (Highways), Deputy General Manager (National Highway), Deputy General Manager (BOT), Chief Accounts Officer and Company Secretary. As at the end of March 2013, the operations of the Company are spread over in 13 Divisions⁹, each headed by Divisional Manager/General Manager. The organisation chart is indicated in *Annexure 2.4.3*. The Company after due tendering process and evaluation of offers also engaged an Independent Engineer or Supervision and Quality Consultant (SQC) for each project highways, for supervision, monitoring and quality control of the works.

Scope and Methodology of Audit

2.4.3 During the period from 2009-10 to 2012-13, out of 16 project highways completed, 13¹⁰ were selected on random basis for scrutiny. Apart from these, three¹¹ out of 14 on-going projects were also selected on random sampling basis for such scrutiny.

A Review on Construction and maintenance of Roads and Bridges under the BOT Schemes in the State of Madhya Pradesh for the period April 2004 to March 2009 was included in the Report of the Comptroller and Auditor General of India (Civil), Government of Madhya Pradesh for the year ended 31 March 2009 in which findings relating to Company were also reported. The audit findings of the review were discussed in the meeting of Public Accounts Committee (PAC) held in May 2012 and their recommendations are awaited (December 2013).

We explained the audit objectives, scope of audit and methodology of audit to the Company and Government during an 'Entry Conference' held on 8 November 2012.

The methodology adopted for audit consisted of explaining audit objectives to top management, scrutiny of records at Head Office and at divisional offices, interaction with the personnel of audited entity and analysis of data with reference to audit criteria and raising of audit queries.

Transactions relating to selected project highways were reviewed in the audit. Records maintained in the Head Office of the Company and in six¹² out of 13 Divisions were examined.

⁸ Government nominees

⁹ Bhopal, Indore (I and II), Jabalpur, Rewa (I and II), Gwalior, Sagar, Ujjain (I and II), Chambal, Narmadapuram and Chhindwara

¹⁰ 10 project highway on BOT (Toll) viz Mandsour-Sitamau, Bhopal-Dewas, Chandpur-Badwani, Indore-Ujjain, Bhind-Gopalpur, Matkuli-Chhindwara, Bina-Malthon, Sagar-Damoh, Mhow-Ghatbillod, Ujjain-Unhel-Nagda-Ghiloda, and three project highway on BOT (Toll+Annuity) viz Badwani-Sendhawa, Sardarpur-Badnawar, Mandsour-Pratapgarh detailed in *Annexure 2.4.1* and *Annexure 2.4.2*

¹¹ Satna-Chitrakoot, Bina-Kurwai-Sironj and Damoh-Jabalpur

¹² Bhopal, Indore (I and II), Ujjain (I and II) and Sagar

Audit findings were reported to the Company and the State Government in June 2013. Replies of the Company and the State Government to the audit findings were received in July 2013 and December 2013 respectively. Audit findings were also discussed in 'Exit Conference' held on 5 September 2013 with the Principal Secretary (PWD) of the GoMP and the Managing Director of the Company. Views expressed by the Government/Company in the exit conference and reply given by the Government/Company have been considered while finalising the review.

Audit Objectives

2.4.4 The objectives of the review were to assess whether:

- the execution of project was in accordance with terms and conditions of the concession agreements entered into with concessionaires;
- estimates of the project highways were in accordance with the guidelines contained in the model Request for Proposal (RFP) promulgated by the Planning Commission in July 2009;
- concession agreements were as per the model Concession Agreement (MCA) of April 2009 of the planning commission;
- toll was fixed in accordance with the guidelines issued by GoMP;
- premium offered by the Concessionaires was remitted by them in terms of the concession agreement; and
- operation and maintenance requirements were complied with by the Concessionaires.

Audit Criteria

2.4.5 The audit criteria were sourced from the following:

- Guidelines contained in the model RFP;
- Provisions of the model Concession Agreement;
- Instructions issued by the State Government for implementation of BOT projects;
- Recommendations and publications of the Indian Roads Congress (IRC¹³); and
- Provisions of concession agreements governing execution and maintenance of roads.

Audit Findings

Audit findings are set out in the succeeding paragraphs.

Overview of executed road projects

2.4.6 According to the concession agreements, concessionaires were required to complete project highways within two years. During the period 2009-10 and 2012-13, the Company completed 13 project highways on BOT (Toll) and three project highways on BOT (Toll *plus* Annuity) model of PPP as detailed in *Annexure 2.4.4*.

¹³ A Technical body of highway engineers, registered as a society devoted to the cause of better roads in India and provides a forum to sharing of knowledge on the range of subjects dealing with construction of roads and bridges in India.

Out of the 16 completed projects, the Company completed 11 projects within the schedule period of completion whereas there were delays of 67 days to 564 days in achieving COD in other five¹⁴ projects taken up under BOT (Toll). The main reasons for delay in execution of the projects as seen from the records of the Company were delay in financial closure and problems associated with Right of Way.

Estimation of project cost

Erroneous Treatment of Environmental Mitigation Cost

Treatment of environmental mitigation cost had increased the VGF to the Concessionaires by ₹ 62.71 lakh.

2.4.6.1 The Company appoints a technical consultant for each project highway on the basis of tender and enters into an agreement for preparation of cost estimates for the project. According to Clause 3.14 of model Request for Proposal for selection of technical consultants, technical consultants would prepare cost estimates based on indicative Bill of Quantities (BOQ) of various components. The consultant may add 25 *per cent* of such construction cost as a lump sum provision for meeting out any physical and price contingencies, interest during construction, other financing cost and pre-construction expenses etc.

We noticed in respect of four out of 16 test checked project highways mentioned in the Table No 2.4.1 that environmental mitigation cost¹⁵ was also included as construction cost and 25 *per cent* contingencies were considered on such construction cost. Whereas in respect of other project highways¹⁶, the Company did not add environment mitigation cost for providing contingencies of 25 *per cent*. Thus, the Company did not follow a uniform practice for treating the environmental mitigation cost.

This treatment of environmental mitigation cost had increased the total cost of the four project highways and consequently increased the Viability Gap Funding to the Concessionaire by ₹ 62.71 lakh as detailed in the Table No 2.4.1.

Table No 2.4.1 (₹ in lakh)

Sl. No.	Project highways (all were under BOT (Toll) model)	Environmental mitigation cost	Extra Provision on cost (Provided 25 <i>per cent</i>)	Grant demanded (<i>per cent</i>)	Impact
1	2	3	4 (3 x 25%)	5	6 (4 x 5)
1	Sagar-Damoh	207.70	51.925	38	19.73
2	Damoh-Jabalpur	207.70	51.925	39	20.25
3	Pina-Malthon	108.41	27.103	38.01	10.30
4	Bhind-Gopalpur	130.01	32.503	38.25	12.43
	Total				62.71

The Government replied (December 2013) that since the environment mitigation cost was borne by the concessionaire, it was considered a component of civil cost and there was no over costing of project cost. In the Exit Conference the Managing Director explained that environment mitigation cost is treated as construction cost

¹⁴ Chandpur-Badwani, Makuli-Chhindwara, Lebad-Jaora, Jaora-Nayagaon and Ujjain-Unhel-Nagda-Ghiloda project highways

¹⁵ Environmental Mitigation Cost consists of cost for reduction of noise/dust pollution, plantation of trees, etc.

¹⁶ Labad-Manpur and Indore-Ujjain project highway

primarily because the same is incurred during the construction period of the project highway.

The reply is not acceptable as the inclusion of the environment mitigation cost in construction cost had resulted in increase of VGF to the Concessionaires and the Company itself did not treat environment mitigation cost as construction cost in other project highways.

Increase in project cost due to adoption of higher specification

2.4.6.2 The Company decided (June 2008) to take up Widening, Strengthening, Maintaining and operating of Bina-Khimlasa-Malthon 37.63 km project highway on two lane standard on BOT (Toll) basis. The project road consisted of two stretches of road. One Stretch was a Major District Road (MDR) from Bina to Khimlasa chowk¹⁷(BK) and the other was State Highway 42 from Khimlasa chowk to Malthon¹⁸(KM). The estimated project cost was ₹ 69.11 crore.

The Company signed the concession agreement (CA) with concessionaire Essel Bina Khimlasa Malthon Toll Road Limited on 7 August 2009 with a concession period of 25 years. Financial closure¹⁹ was achieved by the concessionaire on 25 May 2010. Provisional completion certificate²⁰ for the road was issued by the Independent Engineer in December 2011. Accordingly, the concessionaire commenced collection of toll from December 2011.

We noticed that:

The traffic as per 2008 estimates on BK section was 3722 PCU²¹ and on KM section 892 PCU. It was projected that the traffic on BK section would increase to 18722 PCU in the year 2034. In the same proportion, the traffic on KM section was expected to increase to 4487 PCU. According to IRC64:1990²², for the traffic of 18000 PCU, the standard of the road would be “two lane *plus* paved shoulder” and for the traffic of 4487 PCU, the standard would be “single lane”. So by the year 2034, the BK section of the road would require a two lane *plus* paved shoulder standard, whereas single lane standard would suffice for the KM section.

In spite of the vast difference in the traffic on the two sections of the road, for the purpose of the project, the traffic on the BK section only was considered and both the sections were developed on “two lane *plus* paved shoulder” standard.

Thus, the KM section of the road, where single lane standard would suffice even up to the end of the concession period, was also developed on a two lane standard, thereby

¹⁷ BK Section - length 17.04 Km

¹⁸ KM Section - length 20.59 Km

¹⁹ Financial closure is the date on which arrangement for financing the project highway is completed by the concessionaire.

²⁰ The Independent Engineer may issue a provisional certificate of completion all parts of Project can be legally, safely and reliably opened for commercial operation though certain works or things forming part thereof are not yet complete.

²¹ All types of vehicles passing are converted into a standardised unit for ease of comparison. Such unit is Passenger Car Unit counted on per day basis.

²² IRC 64:1990 issued by IRC specifies standard of road (two lane *plus* paved shoulder) according to the density of traffic.

Adoption of higher standard for project resulted additional burden of ₹ 14.37 crore to Public.

rendering the related expenditure on proportionate VGF amounting to ₹ 14.37 crore unwarranted and avoidable.

The Government replied (December 2013) that the standard and specifications of the road was not compromised in view of present traffic. It was also stated that by development of this project highway, the distance between Jhansi and Bhopal would be reduced by 26 KMs and additional traffic was anticipated because of this reduced distance. In the Exit Conference the Managing Director stated that the project highway was declared as a State Highway.

The reply is not acceptable as development of the KM section to a higher standard was not in accordance with the norms of IRC in view of the low density of traffic. Besides, if additional traffic was anticipated by the Company, the estimated increase in collection of toll from additional traffic should have been considered and VGF should have been reduced accordingly. Due to adoption of higher standard with reference to IRC norms without justified reasons on record, the Public exchequer suffered an additional burden of ₹ 14.37 crore.

2.4.6.3 Execution of road projects

According to the concession agreements, the concessionaire was required to complete the project in 24 months and for delays beyond the scheduled date of completion, damages at the rate of 0.1 *per cent* of the Performance Security²³ for each day of delay was leviable. Compensation was also payable by the Company in the event of delay in handing over the site/right of way to the concessionaire. The agreements also prescribe time frame for completion of different activities of the project and the concessionaire would be liable for damages for delay in adhering to the time frame prescribed.

Out of the 16 test checked project highways (13 completed and 3 ongoing projects), we noticed delays in five completed projects. While in five completed works, damages were levied as per agreement, in following two cases damages had not been levied as and when due as discussed below:

- The work of strengthening and reconstruction of Bina-Kurwai-Sironj project highway taken up under BOT (Toll) was awarded (November 2010) to Telecommunications Consultants India Ltd, New Delhi (TCIL). There were delays from the beginning in execution of the project. The Independent Engineer reported (June 2012) that the Concessionaire had not achieved Project Milestones²⁴ I and II and stated that the Company might resort to claiming damages in terms of the Concession Agreement. As of December 2012, only 17 *per cent* of the work was completed but the Company had not claimed damages of ₹ 73.90 lakh (up to April 2013) from TCIL.

After being pointed out (February 2013) by us, the Company called upon (April 2013) the concessionaire to deposit the damages. Progress of recovery is awaited (January 2014).

²³ Performance security is five *per cent* of project cost.

²⁴ Concessionaire shall have commenced 10 *per cent* and 35 *per cent* of the project cost expended on the 180th and 365th day from the appointed date for achieving milestone I and II respectively

- The Article 14.4.1 of the concession agreement for the Bina-Khimlasa-Malthon project highway stipulates that all items listed in the Punch List²⁵ shall be completed by the Concessionaire within 90 days of the date of provisional certificate, failing which the Company shall be entitled to recover damages from him. The Provisional certificate was issued in December 2011. Thus the items in the Punch List were to be completed by March 2012. We observed that Completion Certificate was not issued so far (September 2013) to the concessionaire even after a lapse of more than fifteen months from the date of issue of provisional certificate indicating non completion of items listed in the Punch List. The Company however had not claimed damages of ₹ 2 crore²⁶ for non-completion of punch list items²⁷.

The Company and Government did not reply to the observation.

Inclusion of the provisions relating to payment of Bonus and fixing the construction period at 730 days, resulted in unintended benefit to the concessionaires to the tune of ₹ 29.27 crore in the form of Bonus.

Payment of bonus and annuity under BOT (Toll plus Annuity) model

2.4.6.4 The project highways Mandsaur-Pratapgarh, Sardarpur-Badnawar and Badwani-Palsod-Sendhwa were developed (June/ July 2012) on BOT (Toll plus Annuity) model of PPP. Keeping in view of low density of traffic and lesser toll revenue in respect of these three project highways, the Company decided (January 2011-March 2011) to develop these project highways under BOT (Toll plus Annuity) Model. The State Level Empowered Committee on Public Private Partnership Projects decided (December 2010 and January 2011) that these project highways would be taken up on equated fixed annuity as discovered through tender mechanism.

Payment of bonus

The details of the project highways, scheduled period of completion as per CA, construction period as recommended by the Consultants, actual period of construction and bonus²⁸ granted for early completion are indicated in the table No 2.4.2.

Table No 2.4.2

Name of the project highway	Length (KMs)	Scheduled Completion period as per concession agreement (months)	Construction period recommended by the Consultants (months)	Scheduled and Actual Commercial Operation Date (COD)	Actual period of completion of projects highways (months)	Bonus granted for early completion (₹ in crore)	Amount of Bonus if Construction period fixed as per Consultants recommendation (₹ in crore)	Extra Bonus granted by the Company (₹ in crore)
Mandsaur-Pratapgarh	11.526	24	12	10 September 2013 and 18 June 2012	9	2.86	0.53	2.33
Sardarpur-Badnawar	42.990	24	18	14 December 2013 and 9 June 2012	6	14.16	9.47	4.69

²⁵ Punch List contains the details of items of work not completed as on the date of Provisional Completion Certificate.

²⁶ Damages is 0.1 per cent of the performance security or 0.2 per cent of the cost of completing such items as estimated by the IF, whichever is lower. IF did not work out such cost. Therefore, audit took 0.1 per cent of the performance security.

²⁷ Items are incomplete construction of shoulder, side slope, junction, bus bay, RCC drain, lane stretches, signage boards, truck lay bye, tree plantation, toll plaza, metal crash barrier, median and pedestrian railing

²⁸ Bonus calculated by the Company: Amount of per day Annuity * Number of days saved in schedule completion.

Badwani-Palsod-Sendhwa	56.880	24	12	2 October 2013 and 3 July 2012	9	12.25	2.44	9.81
Total						29.27	12.45	16.82

It may be seen from the table no 2.4.2

- The Schedule completion period for these project highways was allowed 24 months in the concession agreement whereas Consultants suggested 12 months to 18 months as completion period. Reasons for allowing more time than that was recommended by consultants were not on records made available, particularly when payment of bonus for early completion was provided for in the agreement.
- The Concessionaires completed the project highways within six to nine months against the scheduled completion period of 24 months.
- In cases of contracts involving payment of Annuity, Toll is not collected by the concessionaire and he is allowed a Bonus for early completion as specified by the Planning Commission in the model agreement. However in these cases, the concessionaires were also to collect Toll. Since the concessionaire would collect additional toll by achieving COD ahead of scheduled COD, he would any way draw incremental revenue and such commencement of toll collection ahead of scheduled date of COD would be incentive enough for early achievement of COD. Thus, inclusion of the provisions relating to payment of Bonus for early achievement of COD and not fixing the construction period as recommended by the consultant, resulted in unintended benefit to the concessionaires to the tune of ₹ 16.82 crore in the form of Bonus.

The Government replied (December 2013) that (i) the Model Concession Agreement (MCA) provides for the construction period of two years and (ii) payment of Bonus was as per the MCA, which was an incentive to the concessionaire for completing the project speedily.

The reply is not acceptable because the MCA for this type of PPP Model was not in place and the Company could have fixed the construction period as recommended by the consultant. By providing a longer construction period than that was recommended by consultant, the Company had committed to pay bonus for early completion to the extent of six to 12 months, even before commencement of work.

Payment of Annuity

The project highways taken up under BOT (Toll) are eligible for a Viability Gap Funding (VGF), which is usually restricted to 40 *per cent* of the cost of the project. According to the note submitted (October 2010) by the Company to the Director, Institutional Finance, GoMP, where the projects to be taken up under BOT (Toll *plus* Shadow Fees²⁹) with a VGF of 40 *per cent*, the quantum of the Shadow Fees was to be restricted to 10 *per cent* of the project cost, so that VGF and Shadow Fee together do not exceed 50 *per cent* of the project cost.

²⁹ Shadow Fees is a type of annuity in the form of compensation paid to the concessionaire in lieu of non levy of Toll from vehicles other than Commercial Vehicles.

The details of estimated cost, Annuity payable, present value of such future Annuities and Toll and the total present value as a percentage of estimated cost in respect of the three project highways is indicated in the Table No 2.4.3.

Table No 2.4.3

Name of the project highway	Estimated cost (₹ in crore)	Amount of Annuity payable on six monthly basis (₹ in crore)	Present value of the 26 instalments of Annuity [*] (₹ in crore)	Present value of estimated Toll* (₹ in crore)	Amount of Bonus paid (₹ in crore)	Total of present value of Annuity, Toll and Bonus	Present value and Bonus as a percentage of estimated cost
Mandsaur-Pratapgarh	21.90	1.17	15.21	10.24	2.86	28.31	129.27
Sardarpur-Badnawar	83.66	4.71	61.25	105.55	14.16	180.96	216.17
Badwani-Palsod-Sendhwa	107.11	4.97	64.63	72.95	12.25	149.83	139.89

^{*}The discounting rate of 12 per cent considered for present value calculation.

It may be seen from the Table No. 2.4.3 that in respect of the three projects under BOT (Toll *plus* Annuity), VGF in the form of Annuity exceeded 50 *per cent* of the project cost and ranged from 60 *per cent* to 73 *per cent*. The total present value of Annuity, Toll and Bonus in respect of the two projects accounted for 140 *per cent* to 216 *per cent* of the project cost against 129 *per cent* in respect of one project. This indicates that project wise evaluation of financial implications was not adequate resulting in very high return to the concessionaires, particularly in Sardarpur-Badnawar project highways and consequential higher VGF and extra burden to the Government.

In the Exit Conference, the Managing Director stated that experience proved that through the method of Annuity, there was lesser burden on the exchequer and more number of project highways could be developed.

The reply given in the exit conference however does not give justification for payment of annuity in excess of 50 *per cent* of the project cost in deviation of its own commitment to GoMP.

Selection of Public Sector undertaking as partner under PPP

Selecting of TCIL being Government Company for contract through PPP was contrary to the objectives of utilising funds through private enterprises.

2.4.6.5 According to the Secretariat for the Committee on Infrastructure, Government of India, PPP means “an arrangement between a government or statutory entity on one side and a private sector entity on the other, for the provision of public assets”. Public private partnerships are a tool to bring together the strengths of both sectors. In addition to maximising efficiencies and innovations of private enterprise, they provide much needed capital to finance government programmes and projects, thereby public funds could be available for core economic and social programs.

The Company signed (November 2010) concession agreement with Telecommunications Consultants India Ltd, New Delhi (TCIL). TCIL being the best bidder for the work of strengthening and reconstruction of two lane standard Bina-

Kurwai-Sironj project highway (total length 56.180 KM). The work was estimated to cost ₹ 95.10 crore. TCIL being Government Company, its selection for contract through PPP was contrary to the objectives of utilising funds through private enterprises.

In the Exit Conference the Managing Director stated that the Company was not aware of this and this would be considered for future contracts.

Incorrect fixation of toll and realisation of Premium

Incorrect fixation of toll

2.4.6.6 The State Government approves the levy of toll on the project highways being developed under BOT scheme for various types of vehicles for a road or part thereof (Homogeneous Section) from the date of COD issued by the Independent Engineer of the project highway concerned. The rates of toll are fixed based on the length of the road/Homogeneous Section on a “per trip per vehicle” basis.

The toll is collected by the concessionaire. The toll rates are revised every year and are computed on the basis of Wholesale Price Index (WPI) and are rounded off to the nearest five rupees. The revised toll rates, based on the WPI for the year ending 31 March of the previous year, are made effective from 1 September every year³⁰. We noticed that, there were no instructions or directions about the source of WPI. Lack of such instructions resulted in fixation of higher toll rate as stated below:

- There was no uniformity in computation of toll for the year 2011-12³¹ in case of four³² project highways.
- In case of the project highways Labad-Manpur, Bina-Khimlasa-Malthon, and Sagar-Damoh, the values for basic (WPI (A)) and WPI considered for the relevant year (WPI (B)) were the “Monthly” values for the month of March 2007 and March 2011 respectively published by the office of the Economic Adviser, Ministry of Commerce and Industry Government of India, instead of yearly value of WPI as per State Government notification.
- In case of the project highway Bhind-Mihona-Gopalpur, though the values of WPI adopted were “yearly”, however, these were based on the base year 1993-94 instead of latest WPI available for base year 2004-05.

This resulted in fixation of higher toll rate and consequently higher collection of toll by the concessionaire from the users. Such collection of higher toll during the period from September 2011 to August 2012 on these four project highways worked out to ₹ 37.43 lakh as detailed in **Annexure-2.4.5**

The Government stated (December 2013) that though the values of WPI (A) and WPI (B) were being adopted as was prescribed for some time, it was realised that the value of WPI (B) might be considered as the average of the WPI from April to March of that particular year. It was further stated that from September 2012, the WPI with

Fixation of higher toll rate resulted higher collection of toll of ₹ 37.43 lakh by the concessionaire from the users.

³⁰ Basic toll rates were the toll notified with effect from 1 September 2007.
revised toll rate = basic toll rate * WPI for 31st March of previous year (WPI(B))/WPI of 1.09.2007 (WPI(A))

³¹ applicable from September 2011 to August 2012

³² Lebad-Manpur, Sagar-Damoh, Bina-Khimlas-Malthon and Bhind-Mihona-Gopalpur project highway

latest series was being adopted consistently from the website of Ministry of Commerce and Industry, Government of India.

In the Exit Conference, the Managing Director informed that the Company had since standardised the procedure and this would be formally documented with the approval of the Board of Directors.

Delayed remittance of premium by the concessionaire

2.4.6.7 The Company decided to take up the work of “Widening, Upgradation and Strengthening” of the existing two lane Ujjain-Indore project highway to four lane standards under BOT (Toll).

The Company signed concession agreement with Mahakaleshwar Tollways Private Limited (concessionaire) on 17 September 2008 and financial closure was achieved by the concessionaire on 26 May 2009. As per clause 26.2.1 of the concession agreement, the concessionaire was to pay a Premium of 26.38 *per cent* of the total toll revenue in first week of the following month, which would increase at the rate of one *per cent* per annum. Independent Engineer issued provisional completion certificate on 15 November 2010 and the concessionaire commenced toll collection from that date.

Concessionaire collected toll but had not deposited the amount of premium of ₹ 7.69 crore with the Company.

We noticed (February 2013) that the concessionaire had paid the premium to the Company up to March 2012. For the year 2012-13 and 2013-14³³, the concessionaire collected ₹ 26.76 crore towards toll but had not deposited (September 2013) the amount of premium of ₹ 7.69 crore³⁴ with the Company on the grounds of insufficient collection of toll due to the non payment of toll by certain users and not getting support from Administration for toll collection.

The Management stated (April 2013) that the collection of toll by the Concessionaire was less than his financial obligation. It further stated that legal opinion on non-payment was being sought. In the Exit Conference, the Managing Director explained that all the revenues generated through toll were deposited by the concessionaire in an escrow account. From this account, by way of a waterfall arrangement, the monies were appropriated towards operation and maintenance of the project highway, toll collection expenses, interest, other expenses of the SPV and only after this, it could be appropriated towards premium and lastly to the concessionaire.

The reply is not specific as to how the Company proposed to ensure that the premium due to the Company in terms of concession agreement was realised on time.

Operation and Maintenance

Absence of Annual Maintenance Programme for roads constructed

2.4.6.8 According to the Concession Agreements entered into with the concessionaires, the concessionaire has to operate and maintain the project highway during the period of operation. The concessionaire should at all times during the operation period ensure that the project highway conforms to the maintenance

³³ Up to September 2013

³⁴ 28.38 *per cent* of ₹17.26 crore for the year 2012-13 and 29.38 *per cent* of ₹9.50 crore for the year 2013-14 of the toll collected

requirements set forth in concession agreement. Concession agreement also provides that on or before COD and no later than 45 days prior to the beginning of each accounting year during the operation period, the concessionaire shall provide to the Company and the Independent Engineer, its proposed annual programme of preventive, urgent and other schedule maintenance (the Maintenance Programme) to comply with the maintenance requirements.

The Table No 2.4.4 below depicts date of commercial operation in respect of the six projects highways.

Table 2.4.4

Sl. No.	Name of the Project Highway (road)	Date of commercial operation
1	Mhow-Ghatabilloid (Toll)	30 December 2012
2	Badwani-Sendhwa (Toll + Annuity)	3 July 2012
3	Sardarpur-Badnawar (Toll + Annuity)	9 June 2012
4	Mandsour – Sitamau (Toll)	5 February 2009
5	Mandsour– Pratapgarh (Toll + Annuity)	18 June 2012
6.	Bhopal-Dewas (Toll)	30 April 2010

It may be seen that though the commercial operation of the project highways mentioned in the Table No 2.4.4 had already commenced, the concessionaires did not submit their proposed Annual Maintenance Programme by the due date as envisaged in the concession agreements. On being pointed out by us no records showing conduct of annual maintenance was produced. In absence of the annual maintenance of the project highways, quality of roads may deteriorate.

After this was pointed out by Audit, the Company obtained (May 2013) annual maintenance programme in respect of four³⁵ project highways. Status in respect of the remaining two Project highways was awaited (December 2013).

Roughness test not conducted

2.4.6.9 The concession agreements for BOT (Toll) provide that the concessionaire shall comply with the Operation and Maintenance requirements set out in the schedules. It provides that the road roughness³⁶ value shall be measured at least twice in a year by a properly calibrated vehicle mounted bump integrator Road Measurement Data Acquisition System (ROMDAS) before the monsoon and soon after the monsoon, preferably in the months of April and October every year and that the concessionaire shall ensure that at no point during the operation period, the roughness in the road index shall exceed 3000 mm per km and 1000 mm in any 200 m length.

The details of Project Highways and the date of commencement of their commercial operation under the jurisdiction of the Indore (1 and 2) and Ujjain (1 and 2) divisions of the Company are indicated in the Table No: 2.4.5

Table No 2.4.5

Sl. No.	Name of the Project Highway (road)	Date of commercial operation
1	Lebad-Manpur (Toll)	30 November 2011
2	Mhow-Ghatabilloid (Toll)	30 December 2012
3	Mandsour – Sitamau (Toll)	5 February 2009
4	Indore – Ujjain (Toll)	19 November 2010

³⁵ Serial number 1, 3, 4 and 5 of the table No 2.4.4

³⁶ Surface roughness is a measure of the texture of a road surface. It is quantified by the vertical deviations of a real road surface from its ideal form.

5	Mandsour– Pratapgarh (Toll + Annuity)	18 June 2012
6	Badwani-Sendhwa (Toll + Annuity)	3 July 2012
7	Sardarpur-Badnawar (Toll + Annuity)	9 June 2012

We noticed that:

- No such tests were conducted by the concessionaire except for the road at Sl. No. 1 of the table on the due dates.
- Though on Lebad-Manpur project highway commercial operation commenced in November 2011, measurement of roughness values which were due in April 2012 and October 2012, were conducted in April 2013 and the roughness values per km were indicated instead of roughness values in 200 metre lengths.
- In case of the project highways Badwani-Sendhwa, Mandsaur-Pratapgarh and Sardarpur-Badnawar developed on Toll plus Annuity model, though the schedule to CA provided that roughness value more than 3000 mm/km should be corrected/repared within 180 days, the periodicity of conducting the roughness index test itself was not specified in the concession agreement. In these three project highways, first roughness tests were carried out after 11 months³⁷ against the maximum six months in respect of project highways on toll basis.

After this was pointed out, the Government obtained (May 2013) results of the roughness tests in respect of four³⁸ project highways only. In the Exit Conference the Managing Director stated that the roughness test in case of project highway Lebad-Manpur was not carried out in April 2012 and October 2012 because the project highway was commissioned recently.

The reply is not acceptable as roughness tests were to be conducted as per schedule documented in the concession agreements as cost of the tests must have also been taken in to account by the concessionaire while submitting proposal for projects.

Structural evaluation using deflection study not conducted

2.4.6.10 The Annexure I of Schedule K of concession agreement provided that the Characteristic Deflection Test as per IRC-81-1997 was to be carried out every year after rainy season. High values of deflections indicate that the road is structurally weak, whereas, low value deflections points to a structurally sound road. We noticed that such test was not carried out in respect of any of the 16 completed project highways during the review period.

The Government replied (May 2013) that this test was conducted only if any severe distress or sign of premature failure of crust is found. It was further stated that during inspection by officials/Independent Engineer, no sign of severe distress or premature failure of crust was found.

The reply is not acceptable because the concession agreement provided that the Characteristic Deflection Test as per IRC-81-1997 was to be carried out every year after rainy season.

³⁷ Test due in October 2012 and conducted in May 2013

³⁸ Serial number 4, 5, 6 and 7 of the Table No 2.4.5

Safety audit not conducted

2.4.6.11 According to the Standard Concession Agreement, the concessionaire shall *inter alia* comply with safety requirements set forth in Schedule L appended thereto. According to the Schedule L (Safety measures during Operation Period), once in every accounting year, a safety audit shall be carried out by the safety consultant and the Safety Audit Reports would recommend improvements to the road, markings, signs, project facilities etc.

We noticed that such safety audit was not carried out in respect of the project highways completed between 2009-10 and 2012-13.

The Government replied (May 2013) that (i) the compliance of safety requirement was taken care of by appointing a safety consultant in the staff of the Independent Engineer who was responsible for the compliance of safety requirements during construction as well as O & M period, (ii) the Divisional Managers of the Company work as the Independent Engineer during O & M period, (iii) independent safety consultant was appointed for the project highway Lebad-Jaora to review the design from safety point of view and (iv) the safety requirement was also being addressed in the larger perspective through the implementation of Accident Response System for which an agency had recently been fixed.

The facts remained that no safety audit report was produced to us.

Conclusion:

There were delays in completion of project highways due to delay in financial closure, delay in handing over of sites and problems associated with right of way.

For providing contingencies, uniform practise was not followed in respect of environmental mitigation cost. Khimlasa Malthon section of a project highway was developed on a two lane standard in spite of low density of traffic resulted in proportionate VGF unwarranted and avoidable.

Non deletion of provisions relating to payment of Bonus for early completion and not reducing construction period as recommended by the consultant under a new model of BOT with Toll *plus* Annuity resulted in unintended benefit to the concessionaires in the form of Bonus.

There were no instructions or directions about fixation of toll in case of project highways which resulted in fixation of higher Toll rate and consequently higher collection of toll by the concessionaire from the users of four project highways.

Roughness test were not conducted on the due dates in respect of six project highways. Characteristic Deflection Test, which was to be carried out every year after rainy season, was not carried out in respect of any of the project highways completed during the review period. Safety audit was not carried out in respect of the project highways completed between 2009-10 and 2012-13.

Recommendations

The Company should ensure that:

- the elements of total project cost is computed uniformly and adopted in all project highways;
- project highways are developed in terms of guidelines of Indian Roads Congress commensurate with the density of traffic;
- the construction period is fixed as recommended by the consultant of the project highways;
- price index are uniformly adopted for fixation of Toll; and
- prescribed periodical tests to ensure quality and safety audit are conducted.