

CHAPTER IV: NAVY

Procurement

4.1 Injudicious expenditure on procurement and overhaul of helicopter engines

Despite the fact that two Kamov 25 helicopters with the Navy were old and in a poor material state with virtually no product support, Ministry of Defence concluded a contract with a foreign firm for their overhaul at a cost of Rs 10.38 crore. Not only was the quality of the overhaul poor but expenditure amounting to Rs 8.14 crore became unfruitful as flying operations on these two helicopters were discontinued due to severe defects in their engines. Related procurement of spare KA 25 engines also became wasteful as the engines could not be utilised.

Indian Navy acquired in 1980 seven Kamov 25 (KA 25) helicopters from a Russian Company (Kamov Co) which were fitted on board the Rajput class of ships. With the loss of one helicopter at sea, IN was left with an inventory of six such helicopters. By 1986, it also stopped production of GTD-3M engines, which powered these helicopters. By 1997-98, the OEM also ceased all product support services for these helicopters.

In February 2005, Headquarters Naval Area, Goa proposed the overhaul of two helicopters by M/s Spetstechnoexport Ukraine (M/s STE). Product support for these helicopters was available only from this Company. Integrated Headquarters (Navy) advised in April/May 2005 against such overhaul on the grounds that (a) these helicopters were already too old, (b) maintenance, even after the overhaul would be difficult, as engines, main gear box and rotor blades would be only refurbished and they would not be new, and (c) proposed overhaul of these helicopters would not be economically viable proposition.

Notwithstanding such reservations, the case was processed and Ministry of Defence in December 2005 issued the Request for Proposal (RFP) to

M/s STE. The contract was finally concluded in May 2006 for an amount of US \$ 2.32 million (Rs. 10.38 crore¹). The overhaul was to be completed by January and March 2007 with a post overhaul life of 500 hours/five years. An agreement for some additional works was concluded in January 2007 for another US \$ 606,450 (Rs. 2.73 crore²). Delivery schedule of both the helicopters was later revised to May 2007.

The helicopters were received in April 2007 but could be accepted only by June 2007 as several defects found by the Test Team had to be rectified. Finally, the Test Team found that (a) the material state of the helicopter after the overhaul was satisfactory (b) all other structural fittings and state of on board equipment were satisfactory and (c) husbandry state of the helicopter was found to be satisfactory. However, due to the presence of minor defects detected during the assembly and acceptance, the test team recommended a requirement for improvement in quality of overhaul. The Indian Navy also observed in another correspondence a conspicuous deterioration in observance of quality standards by the Ukrainian company. In fact, in less than one month of its acceptance, the parts of engine exhaust of one helicopter shroud blew off. Both the engines were replaced, one of which again developed defects in July 2007. The engine was repaired again. In July 2008, engine of the other overhauled helicopter caught fire. In September 2008, merely within a year of the overhaul, all flying operations of the Kamov fleet were discontinued.

Indian Navy had separately procured four refurbished GTD-3M engines with a minimum residual life of 500 hours from M/s Hazel UK Ltd, Ukraine at a cost of US \$373,440 (Rs.1.74 crore³). Of these four, two were fitted in one of the overhauled helicopters. The other two engines had never been put to use. Thus, the decision of the Indian Navy and Ministry of Defence to overhaul two helicopters despite their 1970 vintage and lack of facilities for such overhauling led to an expenditure of Rs13.11 crore without any commensurate benefits.

Ministry of Defence stated, in January 2010, that the KA helicopters were procured as an integral part of the first three Kashin class destroyers and it was

¹ 1 USD = Rs 44.74

² 1 USD = Rs 45.02

³ 1 USD = Rs 46.59

envisaged that the helicopters would be in operation till the ships were in operation. Further, the shelf life of the operation of one of the ships has been extended to 2018 and similar extensions were being planned for other two ships. It was, therefore, decided to keep the helicopters in operation till such time the ships were decommissioned. The Ministry also confirmed that the flying operations of KA 25 fleet had to be stopped due to sudden spurt in defects in the engines due to ageing of internal components.

Ministry's intention that the helicopters should be kept in operation as long as the Rajput class of ships were in operation should have had a reality check as by the time it took the decision to overhaul the last two helicopters, the OEM had stopped production and support. The decision also ignored the opinion that such overhauling was not economically viable. Indian Navy and Ministry were also aware that the overhauling would be done by refurbished parts as new parts were not available. An expenditure of more than Rs. 13.11 crore thus did not bring any benefit whatsoever to Indian Navy.

4.2 Excess procurement of Electronic Warfare Systems

Ministry incurred an infructuous expenditure of Rs 19.19 crore on procurement of Electronic Warfare Systems for non-existent or already phased out aircraft. Besides, given the phase out schedule of the aircraft fleet, two AES-210 systems and three HOMI systems procured for Tu-142 M aircraft would be exploited for less than 50 per cent of their useful life.

As a part of the Naval Integrated Electronic Warfare Programme (NIEWP), the Indian Navy was to induct and fit Electronic Warfare (EW) Systems, during 1994-2003, on eight Tu-142M, its maritime patrol aircraft. The plan involved indigenous development of EW systems. In June 1995, Ministry of Defence (Ministry) sanctioned Project Sangraha for the indigenous development of EW systems by DRDO⁴ for various platforms of the Indian Navy. The project, *inter alia*, included development of the airborne ESM-HOMI (Homi) system for fitment on the Tu-142M. The system was to be

⁴ Defence Research and Development Organisation, an entity under the Ministry of Defence

productionised by Bharat Electronics Limited, Hyderabad (BEL). Under the project, five Homi systems were to be made available to Navy by June 2000.

Prior to this, in October 1994, in order to bridge the gap between the operational requirement and indigenous development, Navy proposed the procurement of six EW systems through import. Owing to the limited inventory of the Tu-142M aircraft with Navy and the on-going indigenous development of the Homi system, DRDO in February 1996 recommended procurement of only two imported systems. Consequently, Ministry in 1998 assured that any import of EW systems in excess of these two or after 2000 would be undertaken only after consultation with DRDO. Thereafter, Ministry (August 1999) concluded a contract with M/s Elisra Electronics Systems Ltd, Israel (Elisra) at a cost of USD 4,562,150 (Rs 19.92 crore⁵) for the supply of two AES 210 ESM / ELIINT systems and associated modification of four Tu-142M aircraft on the ground that the two systems could be removed and refitted on the four aircraft on an 'as-required' basis. The modification also implied that these Tu-142M aircraft would be compatible only with the AES 210 ESM / ELIINT systems and hence, would not be able to carry the indigenous Homi system.

Despite the assurance given to DRDO, the Ministry, in January 2006, concluded another contract with Elisra for procurement of two more AES 210 systems and spares for supporting all the four originally modified aircraft at a total cost of USD 4,150,000 (Rs 19.09 crore⁶), on the plea that the frequent removal and re-fitment adversely affected the efficiency of the systems. This was done despite the fact that IN had drawn-down one aircraft in 2006 and was holding only three Tu-142M aircraft which were compatible with the AES-210 system. Resultantly, Navy was left with one AES-210 system in excess of the requirement leading to an infructuous expenditure of Rs 9.55 crore.

Ministry, in their reply, of October 2009 stated that the decision to 'draw down' one aircraft was taken much later than the decision for installation of EW systems and that the 'drawn down' aircraft had not been removed from the inventory and should there be need in future, it would be recovered and

⁵ 1 USD = Rs 43.66

⁶ 1 USD = Rs 46.00

exploited. The reply is not tenable as the life of the aircraft was not extended after 2003 which indicates that the possibility of bringing the aircraft back into service is remote.

Meanwhile, the development and installation of the Homi system, which was to have been completed by 2000 was also delayed. Ministry could conclude the contract with BEL for five systems only in October 2002 at a cost of Rs 48.21 crore. However, the system was proven successful in flight trials in January 2005 and, thereafter, in August 2006 Navy placed a supply order at a cost of Rs 3.11 crore for installation of the Homi systems on four Tu-142 aircraft. Thus, as Navy held only four aircraft for which five Homi systems were ordered, the procurement resulted in excess procurement of one Homi system costing Rs 9.64 crore.

IHQ MOD (Navy) stated, in April 2009, that one Homi system would be maintained as a 'hot spare'. The reply is not tenable as the concept of holding a 'hot spare' was never deliberated at the time of conclusion of the contract. Besides, the second contract concluded for installation material and commissioning included charges for five systems. Moreover, it was noted that the first system delivered by BEL was used for trials and was planned to be removed and sent for training purpose to Naval Aircraft Yard while the fifth and last system would be installed later on the same aircraft.

Audit also observed that the systems (AES-210 and Homi) both have a useful life of 12 ½ years. The utility of the systems procured in 2006 and installed after 2006 would be restricted in view of the limited residual life of the Tu-142M aircraft as the three Tu-142M aircraft compatible with the AES-210 systems are scheduled to be 'drawn-down' by 2010-11. As regards the aircraft on which the Homi is installed, the life of one aircraft is till 2010, up to 2011 for another aircraft and upto 2017 for the remaining two aircraft.

In brief, Ministry incurred an infructuous expenditure of Rs 19.19 crore on procurement of two systems in excess of requirement. Besides, two AES-210 systems and three Homi systems will be exploited for less than 50 *per cent* of the full span of their useful life.

4.3 Injudicious procurement of pumps

Naval authorities ignored clear evidence that pumps offered by a vendor were unsuitable and instead purchased 44 such pumps worth Rs 4.56 crore from the vendor. Subsequent to delivery, the pumps could not be installed on-board the ships they were meant for due to fitment problems. Thus, these ships, even six years after many of the pumps being declared ABER⁷, continue to operate with the old pumps.

The Veer and Abhay class of ships, of Russian origin and commissioned in the Indian Navy (IN) since 1988, have on-board different types of pumps. Replacement of these pumps by the Original Equipment Manufacturer (OEM) has not been possible due to their obsolescence and difficulty in procurement. In 2003, Integrated Headquarters (IHQ) Navy directed Headquarters Western Naval Command (HQWNC) that a board of officers (board) may be constituted to examine the feasibility of installing indigenous pumps as replacement for the Russian-made pumps. Accordingly, HQWNC constituted a Board of Officers (Board 'I') in July 2003 to carry out a study to identify a suitable indigenous substitute out of the offers received from three firms, namely, M/s BE Pump, M/s Sehra Engineering and M/s Johnson Limited.

In respect of a critical auxiliary pump, i.e. the Fire Main Pump, the Board ('I') found that the technical specifications of the pumps offered by all three firms matched those of the existing pump, however, pumps offered by M/s Johnson required modifications to be made on the ship by the Navy while the pumps offered by the other firms were one-to-one replacements. Therefore, the Board ('I') recommended (February 2004) that the pumps be trial evaluated by installing on-board an operational platform for six months for performance monitoring and evaluation. HQWNC, while concurring (February 2004) with the Board ('I') findings recommended that the firm offering a one-to-one replacement and willing to undertake replacement on a turn-key basis be given preference.

Though, one-to-one replacements were available, in May 2004, IHQ Navy, citing reasons of 'standardisation', directed HQWNC to carry out another

⁷ Anticipated Beyond Economical Repair

feasibility study of the pump offered by M/s. Johnson *only*. In September 2004, HQWNC confirmed the suitability of the Johnson-make pump and IHQ Navy also gave approval for its installation. However, as this study had not considered the feasibility of actual fitment on-board the Veer and Abhay class of ships, in February 2005, HQWNC issued directives and constituted another Board of Officers (Board 'II') for certifying the suitability of installation of the Johnson-make pumps. The Board ('II') re-confirmed the findings of the first Board (2004) that the pump was not a one-to-one replacement and observed that the pumps were dimensionally bigger than the existing pumps fitted on the ships in all respects (i.e. length, height and breadth). The Board ('II'), however, stated that installation would be possible with certain limitations.

While the Board Proceedings were yet to be approved, Material Organisation, Mumbai (MOM) placed a supply order in May 2006 on the firm for procurement of 23 pumps at a cost of Rs 2.33 crore. In September 2006, however, HQWNC informed the Board ('II') that the Johnson-make pump had not been assessed as per technical drawings and suggested that the suitability of the pump be re-assessed. In contradiction of their earlier recommendations, in October 2006, the Board ('II') through an addendum to the original Board proceedings stated that the replacement of existing pumps with the Johnson-make pumps was a final solution. Consequently, MOM placed two further supply orders for 21 pumps at a cost of Rs 2.23 crore in February 2007. The entire quantity, against all the orders, was received during August 2007 - May 2008. Out of 44 pumps, 18 were issued between August 2007 and March 2008 for installation on-board various ships.

In the context of the Board findings, audit observed that, at the time of installation, Naval Dockyard, Mumbai intimated (February 2008) HQ WNC that physical dimensions of the supplied pumps were much bigger than the existing pumps and would have adverse impact on the fitment and the maintenance of other equipment fitted in the vicinity. The Dockyard stressed that in terms of naval specifications regarding design and installation for maintainability, adequate space would not be available for fitment of the pumps even after major modifications. As such, there would be future problems and delays each time the pump required over-hauling. Hence, HQWNC constituted a third Board ('III') in June 2008 to re-evaluate and reassess the feasibility of pumps as ABER replacement on platforms *other*

than the Abhay and Veer ships. The Board ('III') found that the pumps could not be fitted on-board any other ship based at Mumbai as they were suitable for replacement for fire pumps only on the Abhay class of ship.

The matter was referred to Ministry of Defence (September 2009). In reply, Ministry stated (December 2009) that the Board had overlooked certain areas of installation/integration leading to difficulty in installing the pumps onboard the Veer class and the same was under examination by HQWNC. The Ministry defended HQWNC's decision not to insist upon user trials as user trials of a similar pump had been performed on-board the INS Ajay and anticipated that the pumps would be installed during the next refit of the ships, possibly during their Medium Refits in 2010-12.

The fact remains that Navy over-looked the recommendation regarding one-to-one replacement pumps. Also, Navy did not exercise due diligence by performing subsequent user trials on-board the ships for which the pumps were meant (Veer class) and instead relied upon user trials held for a pump with different dimensions on-board a different class of ships (Abhay class) even though there was a vast difference in the dimension between the existing pump and the Johnson pumps. Ministry's assertion that these pumps will be utilised is in contradiction of Board ('III') findings regarding non-compatibility of these pumps with other ships and Dockyard observation that there will be maintainability problems in case the pumps are installed on-board the Veer class of ships. Incidentally, the guarantee of the pumps also expired in November 2009.

Thus, Navy's decision to purchase a particular make of pump despite the selected pumps not conforming to the required specifications in terms of dimensions has led to non-utilisation of 40 pumps costing Rs 4.15 crore. Out of the 44 pumps procured, two pumps have been installed on-board Abhay class of ships and the two on the LST class of ships as a *fait accompli*, while the Veer class of ships continue to function with the ABER pumps.

Contract Management

4.4 Mid Life Upgrade of Mine Sweeper ships

Upgradation of Indian Navy's four minesweeper ships, sanctioned at a cost of Rs 517 crore, has been completed in the case of three ships without fitment of vital MCM suite and weapon systems valuing Rs 170 crore. Advantages accruing from the subsequent installation of the equipment will be off-set by the limited residual life of the ships.

In January 2004, Ministry accorded approval for the Mid Life Upgradation (MLU) of four mine sweepers, inducted in Indian Navy between October 1987 and December 1988, at a total cost of Rs 516.67 crore (Foreign Exchange Rs 400.14 crore) to be carried out at Naval Dockyard, Visakhapatnam / Hindustan Shipyard Limited (HSL), Visakhapatnam. The MLU project, scheduled between December 2004 and July 2009, envisaged *inter alia* upgradation of Mine Counter Measure capability by providing them with a state-of-the-art Mine Counter Measure System Suite⁸ (MCMS).

The Naval Staff Qualitative Requirements (NSQRs) for the MCMS Suite were formulated in February 2004 and the equipment was prioritised as operational and immediate. Despite that, the contract for procurement of the MCMs could, however, be finalised in January 2008, by which time, mid life upgradation of three ships out of four was completed. While the bid for MCMs were received in November 2004, Technical and Field Evaluation could be completed only by March 2006. The Cost Negotiation Committee conducted its proceedings only from November 2006 and approval of RM was obtained in September 2007.

The contract for supply of four MCM suites was concluded finally, with M/s Thales, in January 2008 at a cost of Euros 30.50 million (Rs 170 crore)

⁸ Mine Counter Measure System Suite consists of a package of three equipment viz. a Mine Hunting Sonar (MHS) to detect the mines, a MCM Command and Control System (MCM C2 System) as the nerve centre for the MCM operations and the expendable Mine Identification and Disposal System (MIDS) meant to identify and destroy the mines.

with delivery schedule between November 2009 and April 2011. Thus, Navy took almost four years i.e 48 months (February 2004 to January 2008) against the time frame of 29 months provided in multi-vendor cases in Defence Procurement Procedure 2006, for completion of different procurement activities.

Navy, while submitting their proposal for the MLU (December 2003), had clarified that the commencement of the MLU would coincide with the Normal Refit (NR) / Medium Refit (MR) of these ships. Due to inordinate delay in acquisition process of the MCM suite, Navy was forced to reschedule the NR/MLU of the ships as shown in the table:

Name of the ship	Planned/ Original date of commencement	Actual period of NR/MLU	Expected date of delivery of MCM suite
Cannanore	December 2004	March 2006 to November 2006	April 2010
Konkan	November 2005	December 2006 to September 2007	October 2010
Kozhikode	December 2006	May 2007 to January 2008	April 2011
Cuddalore	October 2008	October 2009* to July 2010 (likely)	November 2009

** The NR / MLU was postponed to coincide with delivery of the MCM suite.*

Despite the rescheduling, the MLU was completed on the first three ships without the MCM equipment. Navy, was, therefore, forced (October 2007) to de-link the scope of fitment of the MCM suite on the first three ships from the MLU and planned to install it during the next extended Short Refit (ESR). Navy also would be forced to incur an estimated extra expenditure of Rs 20.40 crore on installation of MCM equipment on the ships due to delay. By this time, in the case of the first three ships, at least two years out of the extended life of eight / ten years would be over.

Apart from the MCMs, sanction for the MLU provided Rs 65 crore for equipment / weaponry for each ship which were to constitute the core of the upgradation programme and were critical to the role the ship plays. Out of 38

equipment required to be fitted on each ships, only 23, 25 and 25 equipments were actually fitted on the three ships whose MLU was completed while six, five and five equipment were fitted subsequent to the MLU. Again, the AK 630 Gun Mounts and Operational Director System, sanctioned at a cost of Rs 8.60 crore per ship were delinked from the MLU package as the guns were not supplied in time. In the case of the IGLA Surface to Air missile, although Rs 3 crore was provided, even the Request for Proposal has not been issued.

Thus, major weapons / equipment constituting 50 per cent of the total cost have not been installed. Audit also noted that the reduction in scope of the MLU work was done without the approval of Competent Financial Authority even though, critical capabilities were not added during the MLU. The delay in fitment of the envisaged equipment will not only adversely affect their operational capabilities but also significantly reduce the benefits to be reaped from extension of their service life by eight to ten years.

Accepting the facts, Ministry stated in November 2009 that as per DPP time taken to finalise the CNC report is 24-1/2 months. The time taken was on account of resolution of various issues raised during processing of the case.

4.5 Loss in procurement of petroleum products

Flaws in the rate contract coupled with lackadaisical approach in clearing the bills of IOC resulted in loss of Rs 136.39 crore to Indian Navy.

Indian Navy (IN) uses eight types of primary fuels for running various ships, machinery and equipments and has been procuring these petroleum products from Indian Oil Corporation Limited (IOC) since 1992-93 through Rate Contract. Of the eight types of primary fuels, Low Sulphur High Flash High Speed Diesel (LSHFHSD) accounts for more than three fourths of the total petroleum products consumed by IN. Navy has an estimated annual financial out go of approximately Rs 760 crore on purchases of petroleum products.

The Administered Price Mechanism (APM) for petroleum products was deregulated over a period of four/five years commencing from 1998. In the APM deregulated era, IN entered into rate contracts with IOC in 2000 and

2005. In terms of the conditions of the rate contract for the period 2005-2008, IN was entitled to claim 'prompt payment discount' ranging from Rs 10 per KL/MT to Rs 20 per KL/MT. Audit noticed that, IN failed to claim 'prompt payment discount' to the full extent due to delays in processing then bills/making payments to IOC timely. Resultantly, IN failed to realize Rs 0.79 crore on this account from IOC.

Audit further observed that the rate contracts concluded by Indian Railways with IOC between 2004 -05 and 2008-09 contained a provision for discount in the cost of High Speed Diesel (HSD) for the 'volume sales'. However, the rate contracts concluded by IN with IOC did not provide for this condition. Resultantly, IN lost an opportunity to realise Rs 135.60 crore from IOC on the purchases of LSHFHSD made between 2004-05 and 2008-09.

Accepting the facts, the Ministry intimated, in December 2009 that it has not always possible to avail 'prompt payment discount' due to the limitations or the operational requirements of the system. Ministry further confirmed that the Price Negotiation Committee of the Ministry has been able to extract a commitment from IOC, for giving discount equivalent to 35 *per cent* of the discount offered by them to Indian Railways, on the volume sales of LSHFHSD and HSD commencing from the next rate contract.

Miscellaneous

4.6 Delay in fruition of Online Examination System of Navy

Faulty drafting of tender documents, first time in 2004 and again in 2007, for award of a contract to develop the Indian Navy Online Examination System led to delay in computerising the examination system prevailing in the IN. Despite an expenditure of Rs 97.92 lakh, the IN will not be able to conduct all 12 examinations online even by 2013.

The Directorate of Naval Education (DNE) is the nodal agency of the Indian Navy (IN) for conducting a number of examinations for recruitment / promotion purposes. Indian Navy in 2004, decided to migrate from the

existing system to an online computer-based examination system. After procedural delays resulting in the re-tendering of the contract twice, Integrated Headquarters (IHQ), (Navy) could conclude a contract only in February 2007, with M/s Sankhaya Infotech Ltd., Secunderabad, at a total cost of Rs 1.26 crore⁹, for development of the Indian Navy Online Examination System (INOES). While the contract was to be completed by August 2007, the firm was able to deliver the INOES by July 2008 only.

The system was to be implemented at 18 locations across length and breadth of India at Designated Examination Centres (DEC). After delivery and acceptance testing of the software in July 2008, six mock examinations were conducted between September 2008 and June 2009. During these mock examinations, the system exhibited a number of problems. The software problems were primarily attributable to large number of candidates and large size of files. By October 2008, the system was non-operational and found to be unreliable as the DECs had been giving repeated defect lists. Nonetheless, the last payment milestone @ 60 per cent of the cost of software contracted, valuing Rs 24.45 lakh, was released to the firm in the same month. To remedy the problem, each time a problem arose, the firm provided software patch to be installed/updated in the main software. It was seen that this approach resulted in more problems¹⁰.

Audit noted that the delay in delivery of the software was also due to lapse on the part of DNE to inform the vendor of a particular condition regarding hosting of all IN systems on NIC¹¹ servers to ensure IT¹² related security and robustness. Despite being aware of this clear requirement, the same was not clarified in the Request for Proposal (April 2006). Subsequently, during System Requirement Study Acceptance, in May 2007 the vendor was told to provide software that could be uploaded on NIC servers. As per NIC

⁹ Inclusive of Rs 28.12 lakh for Annual Maintenance for three years, to be paid later.

¹⁰ More problems relating to – (a) Download/upload of files through dial up mode (b) Problems in the registration modules at the INOES website thus denying candidate. Opportunity to Register for an exam (C) Difficulty in feeding mathematical/scientific

Questions in the Question paper and (d) Source code of software

¹¹ National Informatics Centre, a government body

¹² Information Technology

requirements the software was to be subjected to a third party 'external audit' to ensure stringent technical audit prior to hosting the portal. This resulted in a delay of seven months.

The firm was thus, ultimately able to deliver a modified software in August 2009, more than one year after the formal acceptance and delivery of the initial INOES software. However, the INOES could be put to use for the first Pilot Examination only by January 2010. Audit noted that despite the fact that the original goal was to switch over to an online system for 12 different examinations, the same has not been achieved since the Pilot Examination was held for only one subject. As on date (April 2010), a second subject / examination is scheduled to go online in October 2010, five other examinations during 2011 and 2012 while the remaining examinations are proposed to go online at an indefinite date after 2013.

The Ministry explained (January 2010) that the registration and conduct of examination were two different processes and that no problems were noticed with the registration. Ministry further stated that hosting the website on a server owned by the NIC required an 'external audit'. Dependence on an external agency for conduct of audit was, thus, the primary cause of delay. Ministry clarified that Mock Examinations have been helpful in training the users, administrators and fine tuning of online examination SOPs, etc. Ministry added that the delays and rectifications have been cost neutral.

The Ministry's reply does not take into cognizance the fact that the tender action initially initiated in 2004 was flawed as the Tender Enquiry did not contain all the relevant clauses necessary for successful execution of the project. The Chairman NLC¹³ accepted this fact in November 2006 and emphasised the need for preparation of tender documents in complete detail and thereafter incorporation of all relevant/necessary clauses in the contract documents. However, IN again erred in this respect in the fresh tender and the contract concluded.

¹³ Naval Logistics Committee, empowered to negotiate the terms and conditions of contract with a vendor

Audit appreciates Ministry's view that registration and conduct of examinations are two different processes. However, as the size of files for an on-line system would determine the technical specifications in terms of bandwidth required, speed of transfer etc, it is felt that greater due diligence in evaluating requirements and testing the system would have helped in curtailing the delay and increasing confidence levels in migrating to an on-line system. Incidentally, the original warranty of the system expired in July 2009. Though the system was delivered in 2008, all 12 examinations will not be online even by 2013

To sum, although the need for a modern online computerised system for 12 examinations was felt in 2004, as on date, even after an expenditure of Rs 97.92 lakh Indian Navy has been able to utilise the INOES (April 2010) for only one Pilot Examination.

4.7 Lack of due care in passing claims of vendors

Naval officials did not exercise required care in passing claims of vendors or in availing the benefit of exemption from excise duty. As a result, Indian Navy incurred an expenditure of Rs 1.61 crore, out of which Rs 1.40 crore could be recovered at the instance of Audit.

Effective handling of procurement cases requires knowledge of applicable taxes, duties, etc and exemptions from the said taxes, duties, etc. Similarly, monitoring of claims raised against contractual payments requires thorough familiarity with relevant terms and conditions. Test check of the tendering process and bills raised at various naval establishments revealed that concerned officials did not perform their duties as expected leading to avoidable expenditure of Rs1.61 crore. Two cases illustrating the same are narrated below:

Case I: Avoidable payment of management fee amounting to Rs 1.40 crore

In January 2004, Ministry of Defence issued a work order on Cochin Shipyard Limited for the design, development and pre-production activities of the Air Defence Ship (ADS). The work order stipulated that cost of design and other

related additional work in accordance with the scope of work would be reimbursed on the basis of actual expenditure plus a 5 *per cent* management fee. However, it also clarified that with respect to taxes, duties and levies, if payable, reimbursement would be limited to actual expenditure. Audit scrutiny of the bills submitted by the shipyard for the construction of ADS revealed that the shipyard was charging management fee @ 5 *per cent* on income tax, service tax and bank charges for the design work executed under three separate contracts concluded with two foreign firms. Despite the clear-cut contractual clause governing payment of management fee, the Warship Overseeing Team (WOT) admitted claims amounting to Rs 1.40 crore made by the shipyard during the period March 2006 to November 2008, which were later cleared for payment by the Controller of Defence Accounts disclosing inadequate concern for internal control both at the level of the WOT and the accounting authorities.

As a follow up to audit observation, WOT on the directives of IHQ (MOD) (N)/DND, recovered in August 2009 an amount of Rs 1.40 crore towards excess management fee paid on external design contracts, from the adjustment voucher/ bills submitted by the shipyard.

Ministry accepted the facts in May 2010.

Case II: Incorrect treatment of Excise Duty resulting into avoidable payments

In May 2007, Controller of Procurement, Mumbai (CPRO, MB) floated tenders to nine firms on Limited Tender Enquiry basis for procurement of copper ingot, zinc ingot, aluminium ingot and ingot antimony. The quote, for supply of copper ingot, by M/s Mehta Tubes Limited @ Rs 450 per Kg (exclusive of ED), was considered as lowest.

Audit scrutiny of the evaluation of bids received for procurement of copper ingots revealed the following flaws:

- M/s Mehta Tubes Ltd. had not included ED in their quoted price. They had categorically specified that the ED would be applicable as extra. Another vendor M/s Hind Metal Syndicate Pvt. Ltd. had quoted for

copper ingots @ Rs 487 per Kg (inclusive of MODVAT¹⁴). The quote of M/s Hind Metal Syndicate Pvt. Ltd., works out to Rs 429¹⁵ per Kg excluding ED. However, this quote was not declared as the lowest since the rates quoted i.e Rs 487 per Kg were assumed by CPRO to be exclusive of ED.

- CPRO MB also failed to take cognizance of the fact that the excise duty exemption was available to the Indian Navy since 1995. CPRO, thus, made the payment to the firm i.e M/s Mehta Tubes Ltd. @ Rs 535.48 per Kg (inclusive of ED @ 14 *per cent*, Educational cess, Secondary and Higher Education cess and Central Sales Tax @ 4 *per cent*).
- Rejection of the lowest quote of M/s Hind Metal Syndicate Pvt. Ltd. resulted in undue benefit to M/s Mehta Tubes Ltd. of Rs 15.17 lakh in procurement of 16,982 Kg copper ingots.

Accepting the facts, Ministry stated, in May 2010, that the error was due to oversight and without any malafide intention. It further added that the total loss was Rs 3.57 lakh and not Rs 15.17 lakh as worked out by audit in respect of copper ingots as the rates for taxes like VAT and ED are same for all vendors. Ministry's reply is not tenable as Ministry has not taken into account the payment of ED at the time of calculation of loss for which Navy was exempted since 1995. Audit contention is further strengthened as Ministry itself admitted that excise authorities are being approached for refund of ED paid.

Additionally, audit noticed that there was a similar error in determining the lowest quote for procurement of zinc ingots and aluminium ingots. The procurement was made from M/s Max Steel, even though, M/s Hind Metal Syndicate Pvt. Ltd. had quoted the lowest. This resulted in an extra expenditure of Rs 5.65 lakh in procurement of zinc and aluminium ingots.

In sum, an avoidable expenditure of Rs 20.82 lakh was incurred owing to incorrect treatment of ED.

¹⁴ MODVAT stands for Modified Value Added Tax. It is a scheme for allowing relief to the final manufacturer on excise duty borne by their suppliers in respect of goods manufactured by them.

¹⁵ Rate quoted by M/s Hind Metal Syndicate Pvt. Ltd. : Rs 487 per Kg (inclusive of MODVAT Rs 58). Effective quote without MODVAT Rs 429 per Kg

4.8 Recovery/saving at the instance of Audit

An amount of Rs 90.07 lakh was recovered / saved in two cases after having been pointed out by Audit.

During the course of audit, several instances of financial irregularities and lapses were noticed in different units and establishments. Acting upon the advice of audit, the auditee initiated necessary action resulting in recovery/saving of Rs 90.07 lakh to the exchequer in two cases. Each case is discussed below:

Case I: Amendment in the total cost of supply order

Material Organisation (MO), Mumbai, in August 2008, placed two orders on M/s BHEL for supply of the same item, namely Cam Roller, for different quantities (10 and 50 numbers). Audit, in January 2009, pointed out that there was a wide variation in the per unit price in the two orders, i.e. Rs 4,801 and Rs 38,263, respectively. Accordingly, MO took up the matter with M/s BHEL and amended the total cost of the order in April 2009, which resulted in a saving of Rs 16.74 lakh.

The Ministry accepted the facts in December 2009.

Case II: Excess payment

Ministry of Defence accorded sanction for the acquisition of three Landing Ship Tanks (LST) for the Indian Navy through indigenous design and construction at Garden Reach Shipbuilding and Engineering, Kolkata (GRSE) at a total cost of Rs 699.60 crore inclusive of Base & Depot¹⁶ spares (Rs 63.60 crore). As per the Letter of Indent (LOI), payment in respect of B&D spares was to be made in four stages. Audit scrutiny of relevant documents revealed that an amount of Rs 73.33 lakh was paid in excess to GRSE during the second and third stage payment for the supply of B&D spares due to erroneous

¹⁶ B&D spares constitute the spare equipment and spare parts estimated as required to maintain a ship during the first five years of commission.

calculation. On this being pointed out in audit, Warship Overseeing Team, Kolkata recovered the excess amount from the subsequent bills of GRSE.

The Ministry accepted the facts in November 2009.