

Chapter III : Financial Operations

Audit Objective: To assess whether the financial operations of the CSD are carried out in accordance with the financial and accounting rules and principles as applicable to Government Organisations.

3.1 Turnover and Profitability

The trends in the turnover and profitability according to the CSD proforma accounts during the six years under review were as follows:

Table 1: Financial Results of CSD
(Rs. in crore)

	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Sale	4480.99	4749.42	4163.21	4791.72	5614.69	6955.11
Purchase	3850.90	4033.26	3525.71	4087.69	4898.52	6185.57
Trading Exp	308.48	380.47	329.53	331.98	320.25	392.42
Q D Provision	140.27	148.87	137.49	152.08	175.00	216.50
Staff Expense	38.03	45.51	43.25	46.28	48.10	72.98
Operating Exp	10.14	11.17	10.81	11.50	13.90	14.39
Gross Profit	243.90	208.42	196.58	242.50	234.15	282.34
Net Profit	196.73	154.76	146.23	183.65	168.88	203.69
Closing Stock	362.58	384.17	410.33	432.93	446.17	567.91

But for the year 2005-06, the CSD Sales had increased consistently during the last six years. The dip in sales in 2005-06 was mainly due to reduced price advantage as a result of imposition of VAT in many states, which was later withdrawn or reduced in case of many commodities.

Despite significant increase in sales from Rs.4481 crore in 2003-04 to Rs. 6955 crore in 2008-09 registering an increase of 55 *per cent* the gross and net profit had not been commensurate with the increase. This was mainly due to increase in cost of purchase of goods for sale as also steady increase in the closing stock. The closing stock had increased by 57 *per cent* during the last six years.

While CSD had been able to keep Trading and Operating Expenses under control, the increase in Quantitative Discount had also contributed to lower

profits. The issue of Quantitative Discount has been discussed in detail in Paragraph 3.6 of this report.

3.2 Financial Reporting

CSD prepares Annual Accounts consisting of Trading and Profit & Loss Accounts and the Balance Sheet for each financial year. These accounts though purporting to follow broad commercial principles like double entry system and accrual basis do not follow the generally accepted regimen of financial reporting. There is no statement indicating the significant accounting policies followed nor are there proper explanatory notes regarding departure from such principles. There is also some ambiguity regarding the stewardship of accounts and the external auditor's certificate. It would be desirable to adopt the generally accepted set of accounting policies with the standard regimen of disclosure and certification akin to those adopted by organisations having commercial operations.

An internal audit report is attached to these accounts, which is signed by the official who is also the Controller of Defence Accounts and the Internal Financial Advisor. Internal audit of the organisation by the official who is also responsible for treasury control and financial advice compromises the independence of the internal audit function.

Recommendation 2

CSD and URCs should adopt a set of accounting policies with disclosure requirements akin to those adopted by Organisations having commercial operations.

3.3 Accounting of CSD Profits

Roughly 50 *per cent* of profits generated from operations of CSD are taken as CSD profits in the Demand for Grants for disbursement to various beneficiaries. In other words, even though the amount disbursed reflects half of the profits made in the CSD operations, the disbursement is made out of the Consolidated Fund of India.

In the 56th meeting of the BOCCS held in March 1986 it was decided that 50 *per cent* of the net trade surplus of CSD for a particular year would be distributed as 'Grants-in Aid' in the subsequent year from Consolidated Fund of India. The amount was distributed both as Regular grant and Ad hoc grant. Regular grants are given to a few organisations on a regular basis every year. In addition, in a given year, BOCCS provides grants to other organisations on an ad hoc basis. After distribution of these grants, the remaining part of the available budget was distributed amongst the Services in the ratio of Army 0.85, Air Force 0.10 and Navy 0.05. Till 2004-05, Ministry of Defence in their Demands for Grants reflected these disbursements as "Grants-in-Aid". From the year 2005-06, a new object head "Contribution"

was introduced. Provision and booking of this expenditure under the object head 'Contribution' was incorrect as the nature of payment remained that of grants from the Consolidated Fund. It also diluted financial controls over utilisation of these amounts as under the General Financial Rules, utilisation certificates could be insisted only for Grants-in-Aid.

Such a significant change in the accounting policy was made without consultation with the Comptroller and Auditor General of India as required under the Constitution of India. It seriously diluted accountability of such disbursements. It was particularly significant as such disbursements percolated to the Units/formations and formed a part of the unit's Regimental Fund. The Grants-in-Aid were credited to Regimental Fund by the Services and treated as Non Public Fund in the hands of the recipients.

The change of accounting treatment of such disbursements from grants-in-aid to Contributions takes away the audit jurisdiction of the Comptroller and Auditor General of India on utilisation of such amounts by the recipients.

3.4 Transfer of money from Consolidated Fund of India (CFI) to Non Public Fund as grants to Services

During 2002-03 to 2008-09, a sum of Rs.601.88 crore was appropriated from the CFI, being 50 *per cent* of the net trade surplus. Out of this, Rs. 63.05 crore was distributed to various beneficiaries. The balance amount of Rs. 538.83 crore was shared by Services which were transferred to the Non Public Fund. Such Non-Public Funds i.e. Regimental Funds are maintained by Armed Forces authorities for welfare activities of service personnel and their families. Despite substantial amount of Government Funds being transferred to these Non-Public Funds, access continues to be denied to audit and therefore, we are unable to provide assurance on the proper utilisation of these funds.

3.5 Regular and Ad hoc Grants-in-Aid/ Contributions to organisations

From examination of the papers relating to sanction of Grants-in-Aid available with the BOCCS, it was observed that in several cases, provisions of General Financial Rules were violated. The findings of audit are discussed in the subsequent paragraphs.

3.5.1 BOCCS and CSD sanctioned grants to themselves in violation of GFR

As per Rule 206 of General Financial Rules (GFR), Grants-in-Aid could be sanctioned to personnel or a public body or an institution having a distinct legal entity. CSD, a department in Government and BOCCS, a standing committee with fixed membership sanctioned grants to themselves, in

violation of the proviso regarding distinct legal entity. Grants-in-Aid amounting to Rs. 7.85 crore were sanctioned to DDG (Canteen Services) in Delhi who acted as Secretariat to BOCCS and CSD HO during the period 2002-03 to 2008-09 as shown below.

Table 2: Grants-in-Aid to BOCCS and CSD

Year	Sectt of BOCCS		CSD HO Mumbai		(Rupees in lakh)	
	Regular	Ad hoc	Regular	Ad hoc	Regular	Ad hoc
2002-03	0.97	1.00	65.79	10.00	66.76	11.00
2003-04	1.27	5.00	86.38	10.00	87.65	15.00
2004-05	1.00	2.00	67.95	10.00	68.95	12.00
2005-06	1.46	3.00	64.34	40.00	65.80	43.00
2006-07	1.84	5.00	80.81	160.00	82.65	165.00
2007-08	1.69	0.00	74.31	0.00	76.00	0.00
2008-09	2.04	0.00	89.62	0.00	91.66	0.00
Total	10.27	16.00	529.20	230.00	539.47	246.00
Grand Total					785.47	

3.5.2 Grants-in-aid were sanctioned without adequate details as required under GFR

As per Rule 209 (1) of GFR, any Institution or Organisation seeking Grants-in-Aid would be required to submit an application which includes all relevant information such as Article of Association, bye laws, audited statement of accounts, sources and pattern of income & expenditure etc. to enable the sanctioning authority to assess the suitability of the Institution or Organisation seeking grant. The application should clearly spell out the need for seeking grant and should be submitted in such form as may be prescribed by the sanctioning authority. The Institution seeking Grants-in-Aid should also certify that it had not obtained or applied for grants for the same purpose or activity from any other Ministry or Department of the Government of India or State Government.

It was observed in audit that that no such application was prescribed by the BOCCS. During 2002-03 to 2006-07, regular and ad hoc Grants-in-Aid were sanctioned to 67 beneficiaries out of whom ad hoc beneficiaries were 38. Out of these, seven beneficiaries, mostly organisations related to Ministry of Defence, and which included RM Discretionary Fund, Ministry of Defence, Ministry of Defence (Finance) and Kendriya Sainik Board were recommended for ad hoc grant amounting to Rs. 1.85 crore by the Executive Committee and sanctioned by Ministry of Defence even though there was no demand from them, which was a pre-requisite for sanctioning the grants-in-aid.

3.5.3 Grants-in-aid sanctioned without utilisation certificate for previous grants

As per Rule 212 (1) of GFR, fresh grants were not to be sanctioned to institutions who failed to submit utilisation certificates. Confirmation was sought for from BOCCS by Audit that all the grants were sanctioned against demands from the organisation concerned and institutions who had failed to submit the utilisation certificate were not considered again for distribution of Grants-in-Aid. It was not provided to audit. However, BOCCS in February 2010 confirmed that for before sanction of grants for 2008-09 the utilization certificate in respect of the grants (contribution) for 2007-08 were being obtained.

3.5.4 Receipt of utilisation certificates and audited accounts of grants not monitored

As per Rule 212 (1) of GFR, in respect of grants to an Institution or Organisation, a certificate of actual utilisation of the grant received for the purpose for which it was sanctioned in the prescribed Form, should be insisted upon. The utilisation certificate should also disclose whether the specified quantified and qualitative targets had been reached against the amount utilised, and if not, the reasons therefor. The utilisation certificate should be submitted within twelve months of the closure of the financial year. Rules provided that receipt of such certificate should be scrutinized by the Ministry or Department concerned. Organisations/ Institutions who failed to submit the certificates along with other requisite details were not to be considered for allotment of grants for subsequent years.

At BOCCS, it was observed that receipt of utilisation certificates was not being watched up to 2007-08, as required under Rule 212(1) of GFR. No utilisation certificate was ever insisted from Army, Navy or Air Force for their share of grants. In 13 cases of other grants amounting to Rs. 31.95 crore, information for which was made available to audit, it was observed that utilisation certificates received were single line certificates stating that the grant allotted had been utilized. One such beneficiary was CSD HO itself. In four other cases, utilisation certificates were called for from the beneficiaries after a decade, only when the same were asked for by Audit.

It was observed that the beneficiaries were not submitting the audited statement of accounts with the utilisation certificates as per Rule 210 of the GFR up to 2007-08.

3.5.5 Grants were given without specific details or for doubtful purposes

Rule 209 (3) of GFR stipulated that award of grants should be considered only on the basis of viable and specific schemes drawn up in sufficient detail by the Institutions or Organisations. The budget for such schemes should

disclose, *inter alia*, the specific quantified targets likely to be attained against the outlay. As demands for the ad hoc grants were not supported by detailed proposals from the recipient institutions, which was contrary to the provision, the method of sanction of grants did not reflect adherence to any systematic procedure. As the minutes of the meetings of BOCCS were silent on this issue, it could not be ascertained on what basis ad hoc grants were allocated. Several such cases came to the notice of Audit.

- (i) Grants-in-Aid aggregating Rs. 16.20 crore were allotted to Defence Service Officers Welfare Fund (DSOWF) from 2003-04 to 2006-07. The amount was utilized in a staggered manner up to May 2007. In the meanwhile, the amount was kept in fixed deposit for various periods which earned interest of Rs. 73.16 lakh. The interest earned was not disclosed in the utilisation certificate rendered to the sanctioning authority.
- (ii) It was observed that an amount of Rs. 75 lakh was sanctioned to Headquarters, Southern Command Military World Games Secretariat to meet unforeseen expenditure during the Military World Games. Details of the expenditure could not be produced to audit.
- (iii) During 2002-03 to 2006-07, an amount of Rs. 1 crore was allocated to the Services Golf course. Though the Grants-in-Aid were allocated to the Services Golf course, the utilisation certificate was furnished by the Army Environmental Park and Training Area. It was also observed that the 'Receipt and Payment' accounts of the grantee for that year did not account for the grants-in-aid received.
- (iv) During 2003-04, CSD HO received an amount of Rs. 96.38 lakh as Grants-in-Aid. However, the utilisation certificate was for Rs. 86.38 lakh while the amount actually transferred to non public fund was Rs. 124.03 lakh. Similarly, for 2004-05 and 2005-06, the amounts of Grants-in-Aid received were Rs. 77.94 lakh and Rs. 104.34 lakh, respectively, whereas the amounts credited to non-public fund were Rs. 94.90 lakh and Rs. 105.77 lakh, respectively. CSD HO stated that the amounts disbursed include loans and financial assistance given to the staff for various welfare activities. It further stated that these amounts were later recovered in installments and as a result, over a period of time such grants got accumulated and again utilized. From the reply it became apparent that CSD HO has created a fund from which loans are disbursed but interest earned on these loans had not been disclosed while seeking fresh grants.

Recommendation 3

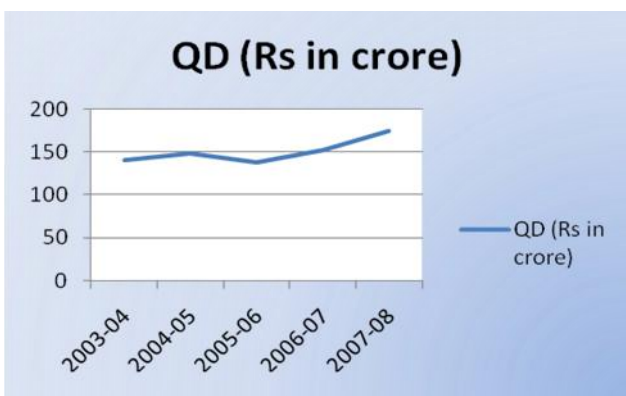
The Chief Accounting Authority should ensure that no change in the accounting policy is made without prior consultation with the Comptroller and Auditor General of India as required under Article 150 of Constitution of India. The disbursement of profit to eligible organisation should be made as grants-in-aid within the ambit of General Financial Rules and further use of the object head “Contribution” should be discontinued forthwith.

Recommendation 4

The regular and ad hoc Grants-in-Aid should be sanctioned in a transparent manner on the basis of detailed proposals and these grants should be used only for welfare of service personnel as is set out as CSD’s objectives. Ministry should issue suitable instructions in this regard to ensure compliance with the provisions of GFR.

3.6 Transfer to Non Public Fund through Quantitative Discount (QD)

CSD provides Quantitative Discount (QD) in the form of free stores to all the



URCs. It is disbursed through the budgetary grant of the Ministry of Defence. QD is calculated at 4.5 per cent in respect of goods on which CSD loads a profit margin of six per cent and 3.5 per cent in respect of goods on

which CSD loads a profit of five per cent. The amount so calculated is included in the subsequent year’s budget under the head “Supplies and Materials”.

CSD operates a Government funded monopoly selling in a closed market with pre determined prices with captive consumers having monetary ceiling on purchases. It was noted in audit that benefit of such QDs was not passed to the customers and added to the profits of URCs. The incentive in the form of QD, therefore, could not be viewed as a trade discount as reflected in the CSD proforma accounts. It was in fact transfer from CFI to non-public fund without conforming to the provisions of the General Financial Rules. During the six years from 2002-2003 to 2007-2008, Rs. 883.46 crore was transferred in the form of QD.

Such transfer in the form of trade discount also affected adversely the profitability of the CSD and resultantly, Government revenues. Since 50 per

cent of the CSD profit should accrue to the Government, treating QD as a charge to the trade understated the profit and thereby deprived Government of India of revenue. The table below indicates the revenue loss to Government.

Table 3: Loss of revenue on account of Quantitative Discount in 2002-08

(Rupees in crore)						
Year	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
QD Paid	131.74	139.21	148.18	137.37	152.01	174.95
Net Profit	149.81	196.73	154.76	146.23	183.65	168.88
Actual profit	281.55	335.94	302.94	283.60	335.66	343.83
Share of Govt	140.78	167.97	151.47	141.80	167.83	171.92
Share deposited	74.91	98.37	77.38	73.12	91.83	84.44
Loss of Revenue to Govt	65.87	69.60	74.09	68.68	76.00	87.48
Total Shortfall to Govt						441.73

Recommendation 5

Quantitative Discount should not be an instrument to transfer funds from public fund to non-public fund without accountability. Such transfers should be carried out in a transparent manner within the ambit of General Financial Rules.

3.7 Banking Arrangements: Delay in credit of funds to CSD Accounts.

3.7.1 Delay in transfer of surplus funds from Depot Bank Accounts to CSD HO Account

Cheques received from URCs on account of sales are deposited into Area Depot Public Fund Account in the respective branches of the Banks. As per CSD instructions, Banks have to afford credit in the Area Depot Accounts within four days in case of local cheques and within 14 days in case of outstation cheques. In case of delay, penal interest is leviable on the Bank at the Savings Account rate plus two *per cent*. Further, the Banks are required to transfer the funds in excess of Rs. 5000 standing at the credit of the Area Depot Account to CSD Head Office (HO) Public Account Main on a day-to-day basis through telegraphic transfer (TT).

The Cash Statements and Bank Statements at five Area Depots for the year 2007-08 were scrutinized. It was observed that amounts in excess of Rs. 5000 were not transferred to CSD HO Account through TT on a regular basis. Details are reflected in the table.

Table 4: Average bank balance in the Area Depot Account
(in Rupees)

Depot	Average balance in Bank Account in 2007-08	
	Monthly Average Balance	Average Interest for one year
Kolkata	12236484	978919
Agra	34988256	2799060
Jaipur	32769291	2621543
Kirkee	63635604	5090848
Secunderabad	26678389	2134271
Total penal interest foregone		13624641

On non transmittal of Area Depot amount to CSD HO account, CSD stated that these amounts represented uncleared cheques. However, the Depots did not have the details of date of clearance of cheques, in the absence of which they were unable to exercise control over timely clearance of cheques by the bank. Under the circumstances, the correctness of the penal interest charged for late clearance of the cheques could not be verified also. CSD stated that efforts were on to ascertain the cleared/uncleared balances in the Depot bank accounts.

3.7.2 Delay in crediting Area Depot Accounts surplus to CSD HO Account

There were also delays ranging from 1 to 440 days in affording credit by the banks (Punjab National Bank and State Bank of India) to the CSD HO Account after the Area Depot Banks had transferred the amount through TT. We calculated that as a result of such delay during the period 2003-04 to 2007-08, the banks held CSD funds of Rs. 31.00 crore for the entire period without payment of interest. Interestingly, while penal interest could be claimed from the Banks for delayed credit of cheques of URCs to Area Depot Accounts, no such provision existed for delay in affording credit of the amount telegraphically transferred to CSD HO Account. It was estimated in audit that interest at the rate of eight *per cent* in respect of delay beyond three days in affording credit in such cases during the period 2003-04 to 2007-08 worked out to Rs. 2.48 crore.

CSD stated that delay had mainly occurred in the Eastern and Northern regions due to difficult working environment and poor connectivity in these areas. However, it was observed that delay had occurred in Western and Southern regions also. Delays of up to 440 days in according credit indicate poor monitoring and lack of control by CSD in the management of funds.

3.7.3 Penal interest not treated as Government Revenue

During the period 2003-04 to 2008-09, CSD received Rs. 1.81 crore on account of penal interest for delayed credit of URC cheques by Banks. This was accounted for as 'Other Receipts' in the Profit & Loss Account. As the said interest was levied due to late remittance of money to the Consolidated Fund of India (CFI), penal interest arising from such late credit should rightly have been treated as the revenue of the Government of India. As such, its credit to Profit & Loss Account and further distribution as profit had occasioned a loss of Rs. 0.90 crore to the Government. CSD stated that the case would be referred to Ministry of Defence/Controller General of Defence Accounts for clarification based on which the procedure would be modified in future.

Recommendation 6

CSD needs to closely monitor the timely credit of funds into its account. It should pursue with the Banks for payment of interest for delay in crediting amount telegraphically transferred by Area Depots' Banks and for indicating credit balances with details of cleared and uncleared cheques.

Recommendation 7

The accounting policies may be reviewed so that the income from non trading activities is correctly accounted for.

3.8 Outstanding Creditors and Debtors

3.8.1 Outstanding Creditors

CSD was to settle the accounts of creditors pertaining to the period 2003-04 to 2007-08 amounting to Rs. 22.18 crore as of March 2009. There was a substantial reduction in the outstanding creditors during the year 2004-05 due to provision of additional funds for clearance of the suppliers' bills. The details as of 31st March for each year are given in the following table.

Table 5: Outstanding Creditors
(Rupees in crore)

Year	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Total Purchases	3850.90	4033.26	3525.71	4087.69	4898.52	6185.57
Less AFD Purchases	780.04	831.62	498.25	668.79	800.24	1034.63
Net Purchases	3070.86	3201.64	3027.46	3418.90	4098.28	5150.94
Creditors as on 31st March.	938.87	233.44	296.93	444.38	640.22	1155.60
Percentage of creditors to Purchases	30.57	7.29	9.81	13.00	15.62	22.43

The percentage of creditors to purchases which was 30.57 *per cent* in 2003-04 came down to 7.29 *per cent* in 2004-05 due to provision of additional funds for payment to creditors. However, creditors were on an increasing trend since

then which indicated that CSD had been unable to manage its purchases within the allotment of funds under the head 'Supplies and Materials'.

CSD stated that bills pertaining to the period 2003-04 to 2007-08 could not be cleared due to certain observations by CDA and payment of bills earlier to 2003-04 was made only after processing the case on file. As the availability of records relating to such old transactions was itself doubtful, in such cases the liability needed to be written back to the Profit and Loss Account in accordance with the commercial accounting principles.

3.8.2 Outstanding Debits

As of 31 March 2009, 11964 Debit Notes amounting to Rs. 11.21 crore were outstanding for recovery from various suppliers, of which 1460 Debit Notes valuing Rs2.54 crore pertained to the period prior to 2004-05.

Inability to recover debts due for more than five years implied that such recoveries were doubtful. The debtors prior to 2002 were also not covered with proper Bank Guarantee (BG). Hence possibility of recovery was remote.

Recommendation 8

CSD should take immediate action to clear the old outstanding credit and debit items. The cases where records relating to purchases are not available and creditors are not demanding payment should be written back to the profit in accordance with the commercial accounting principles.

Recommendation 9

CSD needs to take expeditious action to recover the amounts outstanding for more than five years or write off the same as per laid down procedure.