PREFACE

This Report of the Comptroller and Auditor General of India contains the results of the performance audit of the management of vessels by the Shipping Corporation of India during the period from April 2005 to March 2010 and is based on the test audit of records of the Company.

Executive Summary

The Shipping Corporation of India Limited (Company), a Navratna PSU under the Ministry of Shipping, GOI, is the country's largest shipping Company, and owns around one third of the Gross Tonnage of Indian fleet. The fleet strength of the Company came down from 83 in 2005-06 to 76 in 2009-10 and the tonnage capacity remained almost static at around 50 lakh tonnes. The turnover of the Company also remained almost static while the profits declined sharply from ₹ 1042 crore to ₹ 377 crore over the years 2005-06 to 2009-10.

Performance Audit was undertaken to examine the activities relating to acquisition, management and operations of vessels by the Company during the last five years from 2005-06 to 2009-10. Significant audit findings are discussed below:

The share of Indian ships in the carriage of country's overseas trade had gradually declined from 14 per cent in 2005-06 to 8 per cent in 2008-09, though the country's overseas trade had increased by 34 per cent in the corresponding period. Non-availability of required tonnage was one of the reasons for decline in share of Indian trade. Though there was appreciation of the direct and indirect taxation problems being faced by the Indian Shipping Industry from all the stakeholders, the Government is yet to resolve the vital concerns of the shipping industry. The Government policy initiatives like tonnage taxation introduced in April 2004 were not adequate to create level playing field for the Indian shipping lines over their counterparts carrying country's cargo.

Acquisition of vessels

The Company planned to acquire 39 vessels during 10th Five Year Plan (2002-07) and 62 vessels during the 11th Five Year Plan period (2007-12) but could acquire only 14 vessels and 25 vessels respectively during the above period (upto 2009-10). Even after considering the orders placed for vessels during 2010-11 there would still be a shortfall of 26 vessels in the achievement of target set by the Company for the 11th Five Year Plan period.

The Company did not make use of its delegated powers for acquiring vessels resulting in delay in placement of orders with the shipyards. The delay (time taken 14 to 34 months) in getting the approval from the GOI resulted in escalation in the cost of vessels by approximately ₹ 2,100 crore as compared to the indicative price as reported by international agencies besides loss of business opportunity.

Due to shortfall in acquisition of vessels, the average age of Company's vessels was 15.63 years as against 11 years of their immediate competitor in the private sector. Out of 76 vessels available with the Company, 20 vessels had already outlived their economic life and 16 other vessels were on the verge of completing their economic life. The age of the Company's fleet did not compare well either with their nearest competitor or with the average age of the country's fleet.

Thus, the Company could not modernize and enhance its fleet capacity which in turn, adversely impacted its business growth especially when the country's seaborne trade was growing at a pace of 8.5 per cent annually and world fleet also registered a growth of 23 per cent.

Operation of Vessels

The bulk segment made sizeable contributions to the revenue earnings and profitability of the Company. The profit from this segment, however, declined from ₹ 980.11 crore during 2008-09 to ₹ 484.93 crore during 2009-10. The liner segment which earned a profit of ₹ 100.29 crore in 2005-06 has been incurring losses since 2006-07 that reached a level of ₹ 225.09 crore during 2009-10. The Company commenced and closed down liner services in quick succession putting at risk its credibility as a reliable service provider.

Audit also observed that there were no clear policy guidelines for placement /employment of vessels on short term or long term. Therefore, in the evolving situation of ships waiting for employment, the Company had to agree for charter hire rate below the market rate as the fixtures were concluded based on the discovery of price through the spot market. Further, as the proceedings of the negotiations with the brokers were not documented, audit could not get any assurance on the fairness and transparency of the process.

The Company could not find suitable employment for vessels resultantly the idle days were 4.46 and 3.25 per cent in 2008-09 and 2009-10 respectively as against 1.33 per cent in 2007-08 and a consequent loss of ₹ 134.04 crore towards standing charges. There was no system in place for analysing the reasons for idling for taking corrective action.

For operation of its Very Large Crude Carriers (VLCCs) Company could not get any business from Indian Oil Corporation Limited during the period 2007-08 to 2009-10, despite the fact that IOC imported 92 million metric tonnes of crude oil through other VLCCs. The Company has no system of analysing reasons for not encashing such enormous business opportunity available within the country especially when earlier, most of the oil imports were being done through the Company.

To conclude, the country's total import of crude oil during 2009-10 was 159 million tonnes, of which Company's share was only 9 per cent. The Company, therefore, needs to be aggressive in capturing the market share of import of crude oil and accordingly evolve a strategy for meeting customers' requirement for securing long term contracts.

In the absence of any norms, the repairs and maintenance cost of the Company ranged between 13 to 16 per cent as against 9-10 per cent as compared with that of Great Eastern Shipping Company Limited, the nearest Indian competitor.

Oversight mechanism

Though the Company failed to achieve the annual targets set by them in three out of the five year period, with the scaled down MOU targets with the GOI, the Company was given full weightage on the key performance parameter of tonnage acquisition in all the years. Thus, the underlying principle of an MOU to motivate the Company to strive for further growth was defeated

The MIS was also weak and needed upgradation to meet the business needs of the Company.

Conclusion

With the removal of trade barriers and globalisation, the shipping industry's fortunes are driven by the growth of seaborne trade and supply of vessels. Non-existence of level playing field in the matter of taxation impacted the competitiveness of the Indian shipping industry especially in the context of increased competition from the foreign shipping companies.

The Company did not pursue an ambitious acquisition policy to augment and modernise its fleet. The Company was not adhering to its annual fleet acquisition targets and there were significant slippages resulting in cost overrun and also affecting its operational efficiency. The Company in the absence of policy guidelines on the engagement of vessels on long term and spot market rates, deployed majority of the vessels on fixtures at a charter hire rate determined by the spot market. The idle days when the ships were not earning any income but incurring cost increased indicating the need for closer monitoring.

Based on the Audit findings the following significant recommendations are made:

- *As the linkages between the development of the economy and growth of shipping industry are strong, the Government may address the concerns faced by the Industry to facilitate a strong national core fleet.*

- *The Company needs to frame and implement a time bound acquisition policy for fleet growth and modernisation to face the global competition.*

- *The Company should ensure that vessels are employed gainfully and avoid idling of vessels. Also, the Company needs to be aggressive in getting business from its major customers, particularly the Oil Majors.*

- *The Company needs to have a system of reviewing loss making operations at regular intervals for taking remedial measure in time.*

- *The Company should formulate a policy for having an optimum mix of owned and inchartered vessels in the liner segment to bring down the high incidence of inchartered costs.*

The Ministry while accepting the last three recommendations stated that the action on the first two recommendations has already been initiated / taken.

Chapter

1 Introduction

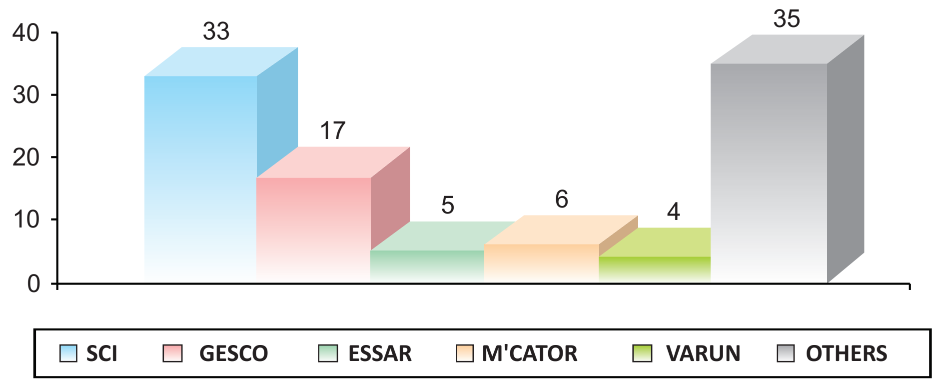
1.1 Shipping Industry

The shipping industry being global in nature, its prospects are linked to the growth of trade and services of the countries. India has a long coastline of 7517 kilometres with 12 major and 200 minor ports and about 95 per cent of India's international trade by volume or approximately 70 per cent by value is seaborne (March 2009). The performance of the shipping industry assumes great significance in the Indian economy as it contributes 2.5 to 3 per cent of GDP. A study conducted (2006) by the Working Group on Shipping and Inland Water Transport constituted by Planning Commission emphasized the need for increased national tonnage , as out of the total freight bill of ₹ 73,300 crore of the country an amount of ₹63,900 crore was paid to foreign flagged vessels towards freight.

Around 65 per cent of the total Indian fleet of 9.61 million Gross Tonnage[1] (March 2010) was owned by five big companies, viz. the Shipping Corporation of India Limited (33 per cent), Great Eastern Shipping Company Limited (17 per cent), Mercator Lines Limited (6 per cent), Essar Shipping and Logistics Limited (5 per cent, Varun Shipping Limited (4 per cent) and balance by other smaller companies as depicted in the graph below.

GRAPH-1

Share of Fleet by Companies in India



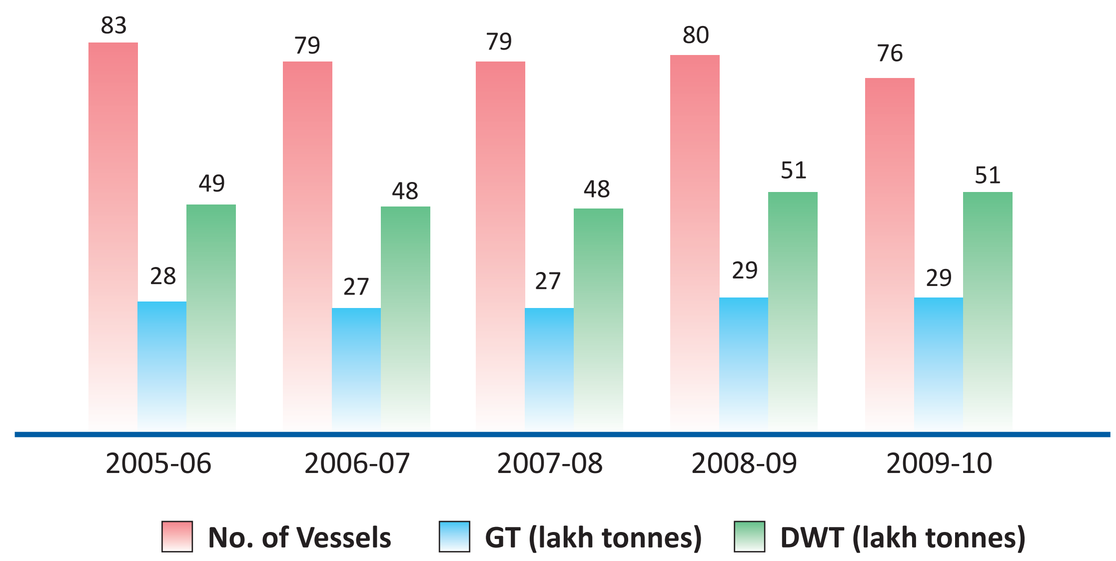
[1] *Gross Tonnage (GT) or Gross Registered Tonnage (GRT) is a notified measure of ship capacity calculated from the total volume of all enclosed spaces measured in cubic meters, using a standard formula.*

1.2 Company profile

The Shipping Corporation of India Limited (Company) was formed in October 1961 by amalgamating Eastern Shipping Corporation and Western Shipping Corporation. Since August 2008, the Company is enjoying Navratna status. Being the country's largest shipping company, it owns and operates around one third of the Indian tonnage and provides various kinds of marine trade services such as tanker, break bulk, liner services, etc. Besides, it also mans and manages number of vessels on behalf of various Government departments and organizations.

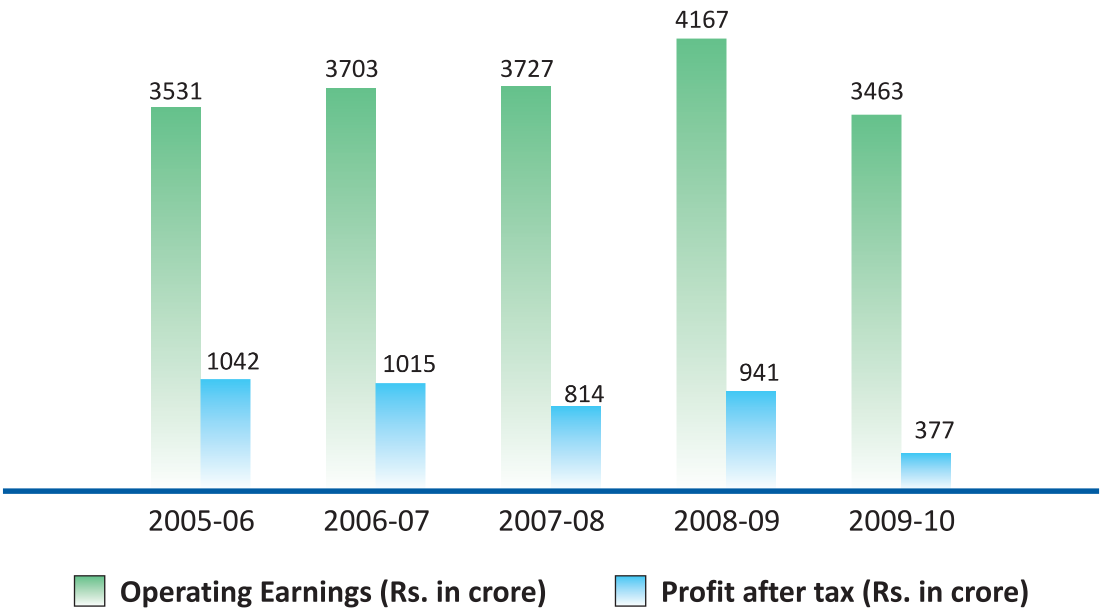
The fleet represents the assets of the shipping company and the growth of the operating revenue is linked to its fleet strength. The key parameters of the Company like fleet strength, Dead Weight Tonnage (DWT)[2], Gross Tonnage (GT), Operating Earnings and Profit after tax for the five years ending 31 March 2010 are briefed in the following graphs:

GRAPH-2



[2] *Dead Weight Tonnage (DWT) is the displacement of any loaded condition minus the lightship weight. It includes the crew, passengers, cargo, fuel, water and stores.*

GRAPH-3



As may be seen from the above graphs, the fleet strength of the Company reduced from 83 in 2005-06 to 76 in 2009-10 and there was only marginal increase in the Gross Tonnage during this period. Consequently, the growth of the Company in terms of earnings and profit remained dismal over the period of five years from 2005-06 to 2009-10 in general and in particular in 2009-10; which was one of the main reasons for undertaking the present study.

Chapter

2 Audit Framework

2.1 Scope of Audit

This performance audit covers the activities relating to acquisition, management and operations of vessels undertaken by the Company during the last five years from 2005-06 to 2009-10 with main thrust on the Bulk and Liner Segments, which put together account for almost 95 per cent of the total earnings of the Company. In addition, Government's policies on maritime trade and its impact on the shipping industry were also examined.

2.2 Audit Objectives

The performance audit was conducted to assess and evaluate whether:

- Government's maritime policies were conducive to the growth of the industry in general and public sector in particular;
- Company's Plans were directed towards sustainable business performance, maintaining market share and steady growth;
- Systems and procedures for vessel acquisition were robust, efficient, transparent and competitive;
- The operations of the Company were carried out in an efficient and economic manner and
- Maintenance of old vessels was as per statutory requirements and industry norms.

2.3 Audit Criteria

The performance of the Company was assessed against the following criteria:

- Merchant Shipping Act 1958.
- Targets fixed by the Government and Company for various activities.
- Minutes of meetings of the Board of Directors and Management Committees;
- Contract Agreements;
- Best Practices adopted by the industry.

2.4 Audit Methodology

Audit commenced with an entry conference with the Management on 21 April 2010 wherein the scope, audit objectives and sample were discussed and the audit criteria were agreed upon. Audit examined the relevant records of the Company which included electronic data supplemented by questionnaires and memoranda. The records of Ministry of Shipping and Director General (Shipping) relating to framing/revision of Government policies were also examined. In addition, data relating to crude oil imports by oil majors (IOCL, HPCL and BPCL) was collected, analysed and incorporated in the report, wherever found necessary. Based on the examination, draft Performance Audit Report was issued to the Management and an exit conference was held on 13 November 2010 to discuss the audit findings. Replies / explanations furnished by the Management and Ministry (April 2011) have been considered while drawing audit conclusions which are discussed in the subsequent chapters.

2.5 Acknowledgement

Audit acknowledges the co-operation extended by Ministry of Shipping, Managements of the Shipping Corporation of India Limited and Oil sector Public Sector Undertakings in furnishing of records, information and clarifications to audit teams.

2.6 Audit Findings

Audit findings are discussed in the following chapters:

Chapter 3: highlights government policies and their impact on the growth of shipping industry.

Chapter 4 : flags issues relating to the acquisition of fleet

Chapter 5 : dwells on issues relating to the operation and maintenance of vessels.

Chapter 6: discusses issues of inadequacies in oversight mechanism.

Chapter 7: Conclusions and Recommendations.

Chapter

3 Government Policies: Impact on Shipping Industry

3.1 Government Support

Prior to November 2001, the Government of India (GOI) supported the country's flag vessels and Indian shipping lines through the right of first refusal[3] and all Public Sector Undertakings (PSUs) /Government departments were required to finalise the import and export contracts on Free on Board (FOB)[4] and Cost and Freight[5] basis respectively. The Shipping wing of the Ministry of Shipping, GOI called Transchart was making shipping arrangement in the above cases. As a part of this arrangement, the bids were invited by Transchart and even though the lowest bid was from a foreign flag owner, Indian flag owners were given a chance to match the price. In November 2001, GOI while deciding to continue with the restriction in respect of imports, allowed the PSUs/Government departments to finalise export contracts on FOB basis.

Subsequently, in April 2005, the GOI allowed, Indian Oil Corporation Limited (IOC) and in March 2007, Hindustan Petroleum Corporation Limited (HPCL) and Bharat Petroleum Corporation Limited (BPCL) to make their own shipping arrangements for import of crude oil on cost considerations, though these Oil PSUs still had to obtain permission from Director General (Shipping), Ministry of Shipping, GOI for inchartering foreign flag vessels. As a result, the crude oil import which accounted for 71 per cent (47.16 million MTs) of the shipping arrangements made by Transchart in 2004 came down to only 39 per cent (10.97 million MTs) during 2010.

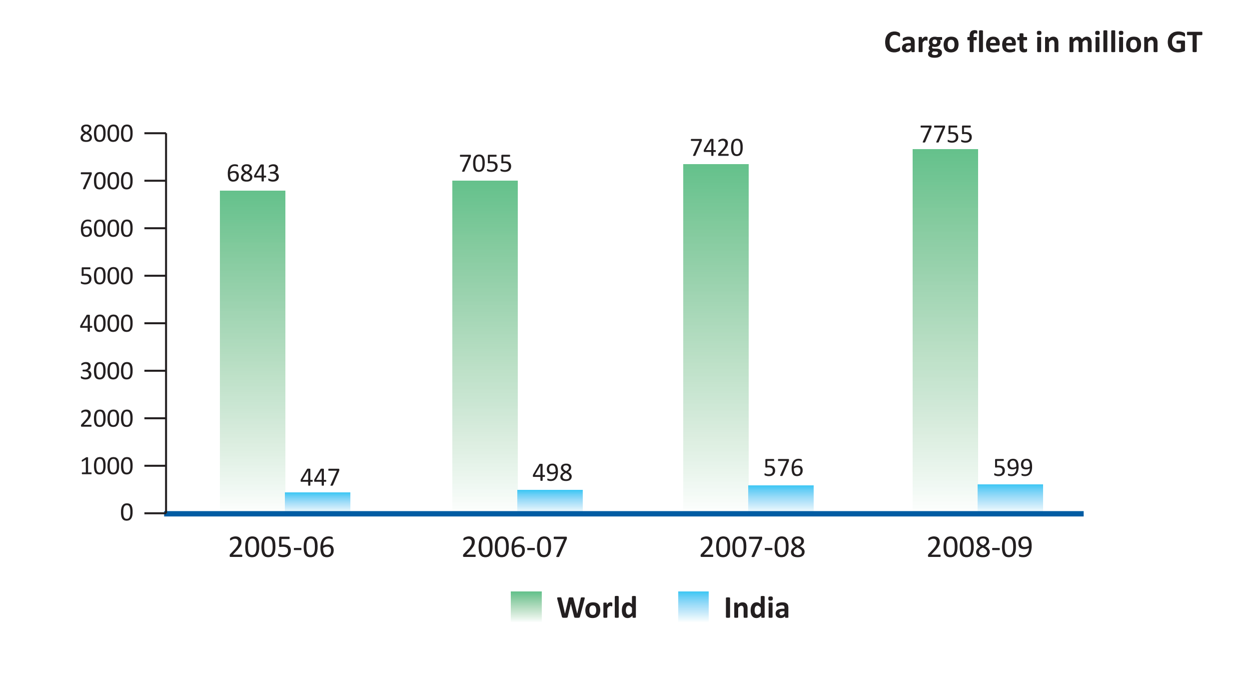
Further, as is evident from the table/graphs below, the share of Indian vessels in India's overseas trade decreased from 61 million tonnes (14 per cent) in 2005-06 to 50 million tonnes (8 per cent) during 2008-09 while the percentage of Indian fleet to world fleet remained static at 1.17 during the same period.

[3] *Right to match the rates quoted by foreign lines*
[4] *Buyer has to arrange and pay for shipment of the cargo*
[5] *Seller has to arrange and pay for shipment of the cargo*

Table - 1

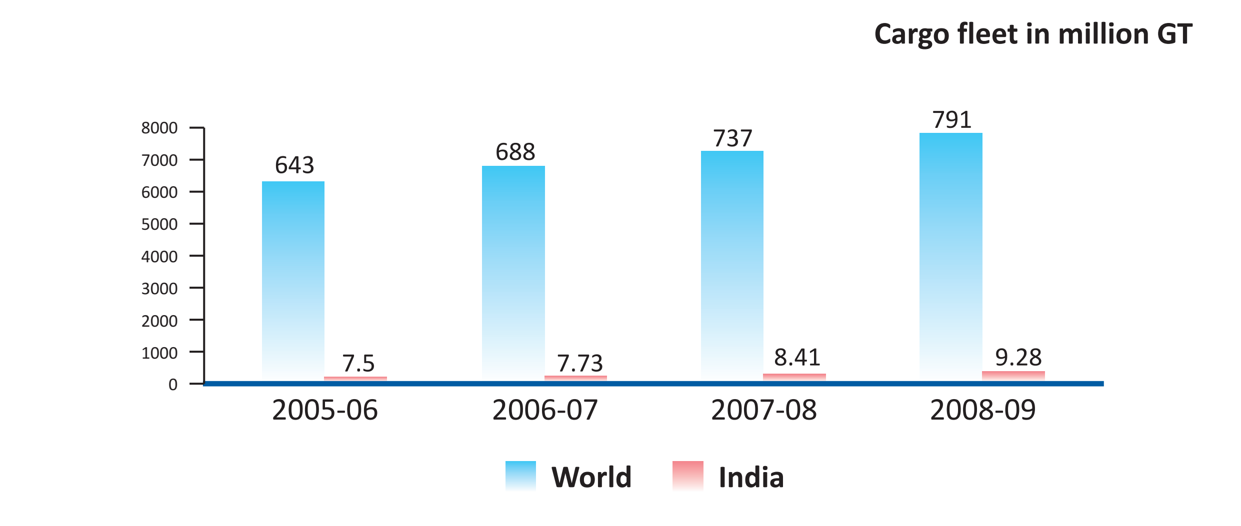
Growth (2005 to 1.1.2009)	World	India
Seaborne trade	13 per cent Increased from 6843 to 7755 million tonnes	33.90 per cent Increased from 447.14 to 598.70 million tonnes.
Cargo fleet	23 per cent Increased from 643 to 791 million GT	24 per cent Increased from 7.50 to 9.28 million GT
Indian vessels in overseas trade	Not applicable	Decreased from 13.7 to 8.4 per cent From 61 to 50 million tonnes
Share per cent of Indian fleet	Not applicable	Remained 1.17 during the period

GRAPH-4



Similarly, the graph below indicates the growth of world cargo fleet and Indian fleet during 2005-06 to 2008-09:

GRAPH-5



The Ministry endorsed the Audit view that non-availability of required tonnage was one of the reasons for the decline in share of Indian tonnage in carriage of Government/Indian dry bulk cargoes.

After the restrictions were relaxed, the share of Indian ships in the carriage of country's overseas trade had gradually declined from 14 per cent in 2005-06 to 8 per cent in 2008-09, though the country's overseas trade had increased by 34 per cent in the corresponding period.

3.2 Need for increased national tonnage

The need to strengthen the Indian shipping industry assumes great significance in view of the various recommendations made by several entities.

a) The Working Group on Shipping and Inland Water Transport constituted (2006) by Planning Commission had emphasized the need for increased national tonnage on the following grounds:

- Overall Indian freight bill was US $ 16.3 billion (₹ 73,300 crore) and out of this, over $ 14.2 billion (₹63,900 crore) was paid to foreign flag vessels as the mercantile fleet under the Indian flag was only 1.17 per cent.

- The shipping sector contributed 2.5 to 3 per cent of GDP.
- Negotiating power to control freight costs and to guard against undue freight charges by cartels and monopolies as it was essential to have a certain percentage of tonnage in every cargo sector;
- Maintaining the supply lines for essential cargo like crude on national energy security concerns was essential as proved during the Iraq war as all the crude imported from the Middle East through Indian ships.

b) 'Working Paper on Policy for India's Services Sector prepared (March 2010) by Department of Economic Affairs, GOI also highlighted the need to strengthen Indian fleet in view of the positive contribution from the Indian shipping industry to the GDP of the country.

The Ministry stated (April 2011) that the Government was aware of the urgent need for enhancement of national tonnage and with the positive steps taken by the Government including introduction of tonnage tax regime to reduce the tax burden of Indian Shipping companies and permitting 100 per cent foreign direct investment in the shipping sector, the Indian tonnage for the first time crossed 10 million GT mark and stood at 10.38 million GT as on 28 February 2011.

While audit acknowledges the recent growth in the tonnage, the fact remains that this growth is not commensurate with the country's increasing growth in seaborne trade and therefore, needs to be stepped up.

3.3 Government's indecision on vital issues

Though there was appreciation of the problems being faced by the Indian Shipping Industry from all the stakeholders, the Government did not act promptly to resolve these vital issues which impacted adversely the growth of the Industry, as is evident from the issues discussed below.

(i) Restrictive Tax Regime for Indian shipping

In order to enable Indian shipping to compete globally in a level playing field, the Government of India introduced tonnage tax regime[6] for the industry with effect from April 2004. The Indian shipping companies, even otherwise were in a disadvantageous position, as they were exposed to a variety of other direct/indirect taxes as detailed in Annexure I, which were not applicable to the Shipping Industry in other countries. Incidence of these taxes for Indian shipping Companies was 4 - 5 per cent higher than its international counterparts, as assessed by CARE, a renowned Government Research Agency[7].

[6] *Tonnage tax is a special scheme of taxation for shipping companies. As per the scheme , tax is levied on the basis of aggregate of tonnage income (its capacity) of ship.*
[7] *Report on Shipping Industry 2010 by CARE Research, a Division of Credit Analysis & Research Limited.*

This being a major concern hampering the growth of Indian shipping industry, recommendations were made at various forums at different points of time for abolition of the additional tax burden as indicated below:

- The industry through Indian National Shipowners' Association (INSA)[8] took up (since November 2005) the issue of burdening the industry with higher incidence of taxes, which was against the spirit of competitive level playing field.
- A Group constituted by the Government of India under the chairmanship of Joint Secretary, Department of Shipping, Ministry of Shipping , Road Transport and Highways in October 2005 recommended (December 2006) for exemption from these taxes.

The Working Paper for Policy for India's Services Sector of the Department of Economic Affairs (March 2010), GOI also favored extending tax benefits for building a strong Indian fleet.

(ii) Other pending issues

The decisions on the following issues raised by INSA since November 2005, were also still pending (December 2010) with the GOI:

- Grant of infrastructure status to the shipping industry;
- Access to cheaper funding of the acquisition of new vessels;
- Transchart to be empowered to fix percentage of cargo to be moved by Indian flag vessels;
- Long term chartering agreement by PSUs for critical energy cargoes of crude oil, petroleum products and gas to be negotiated and concluded exclusively with Indian ship owners for Indian flag vessels.

The Ministry stated (April 2011) that the above issues were taken up with Ministry of Finance, GOI and further added that it had asked Ministry of Petroleum to impress upon the Public Sector Oil marketing companies to indicate their long term tanker requirement so that adequate Indian tonnage is built up for the purpose and that for cargo reservation for Indian flag vessels, policy decision was to be taken by the Government.

In sum, there is a need to expedite action on the above concerns to provide Indian shipping players a level playing field to facilitate them to compete effectively with the global players.

[8] *Indian National Shipowners Association – a collective forum of shipowners with 36 members (34 in the private sector and two in the public sector viz. the Shipping Corporation of India Limited and Poompuhar Shipping Corporation Limited, Chennai).*

Chapter

4 Acquistion of Fleet

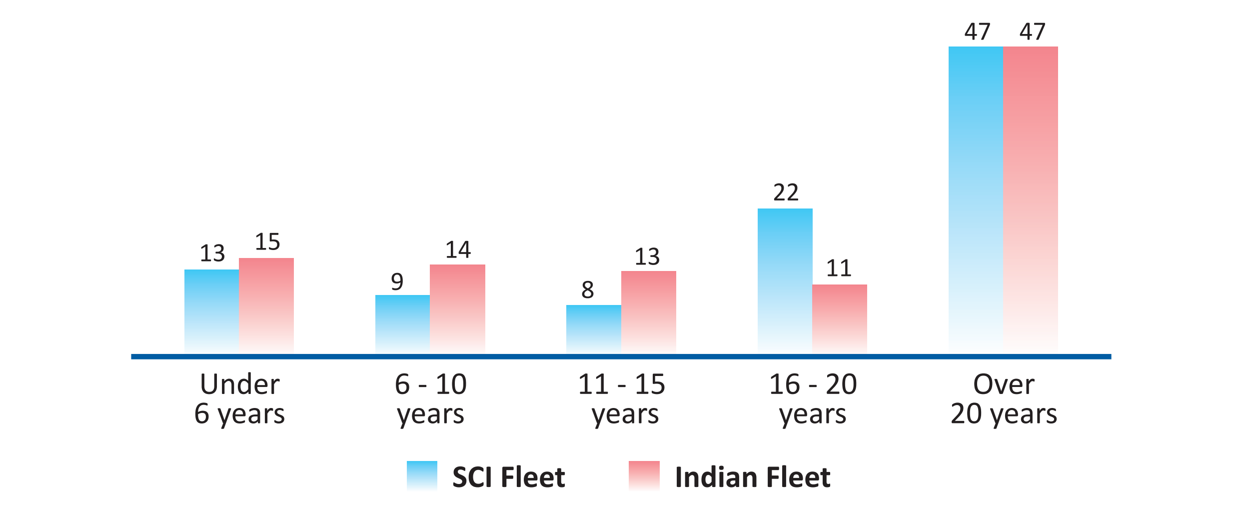
4.1 Fleet profile

The Company has a total of 76 vessels with 29.26 lakh Gross Tonnage, with the average age of 18 years. The age of the vessel plays a crucial role in the earning as well as in the cost of operation especially in the global competitive environment where the clients prefer younger vessels. Audit observed that as against the Company's average age of 18 years, average age of fleet of Great Eastern, its immediate competitor in the domestic market was 11 years.

A comparative position of stratified age profile of the Company's fleet and the Indian fleet as on 31 March 2010 is detailed below:

GRAPH - 6

Age profile of SCI fleet and Indian fleet (in percentage)



Audit analysis revealed that average age of the Company's fleet did not compare well either with their nearest competitor or the country's average age especially in the age group of 16-20 years.

Table - 2 Economic age of the various categories of vessel

In years

Category	Prescribed economic life	Age 0 -10	Age 11 -20	Age > 20	Total
Crude oil tankers	20	7	7	8	22
Product tankers	20	3	5	2	10
Very Large Crude Carriers	20	4	-	-	4
Chemical carriers	20	-	3	-	3
Gas carriers	30	-	2	-	2
Bulk Carriers	25	1	3	14	18
Container vessels	25	2	3	-	5
Offshore supply vessels	20	-	-	10	10
Passenger vessels	30	-	-	2	2
Total		**17**	**23**	**36**	**76**

It may be seen that out of a total of 76 vessels available with the Company, 20 vessels had already outlived their economic life and 16 other vessels were on the verge of completing their economic life prescribed by the Government. In fact, out of 36 ageing vessels, 24 vessels were tankers and bulk carriers which were critical for the operations of the Company. This adversely impacted the Company's competitiveness in the overseas trade and restricted the business opportunities.

The Ministry stated (April 2011) that the Government norms on economic life are only for guidance and more particularly for acquisition of second hand vessels and it is not mandatory to phase out the existing vessels in Indian fleet after the economic life norms indicated by the Government. It further stated that with the induction of new vessels and phasing out of older vessels during 2010-11, average age of SCI fleet has now improved to 15.63 years.

The fact remains that higher age of fleet has implications in form of greater operating expenses and lower charter rates.

4.2 Acquisition plans

The Company has been drawing up its own five yearly tonnage acquisition plans to synchronise with the respective national Five Year Plans. These are broken into annual acquisition plans. The target and achievement of acquisition plans during 10th (2002-07) and 11th (2007-12) Five Year Plans are given below:

GRAPH - 7

Shortfall in Acquisition

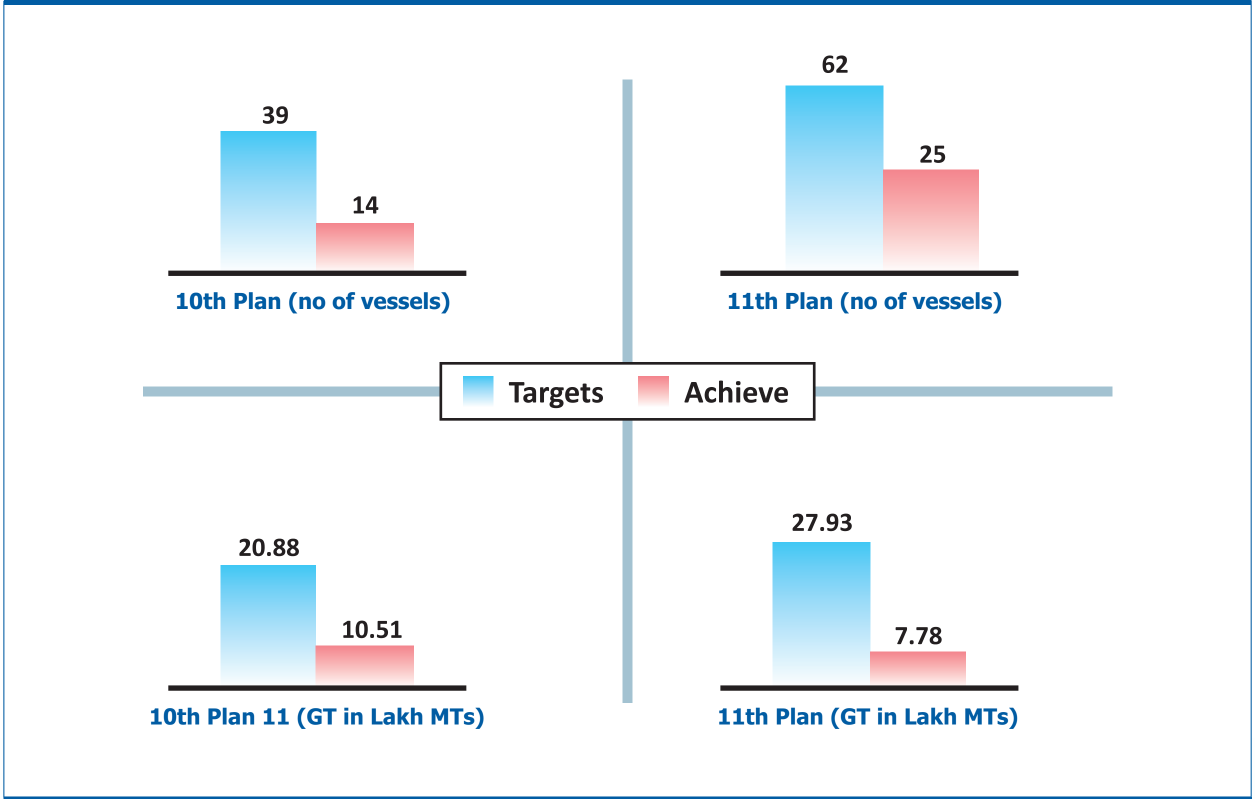


Table - 3

Particulars	10th Five Year Plan		11th Five Year Plan	
	No of vessels	GT in lakh MTs	No of vessels	GT in lakh MTs
Target	39	20.88	62	27.93
Achievement	14	10.51	25	7.78
Percentage of achievement	36	50	58	28

An analysis in audit revealed that the Company failed in achieving the acquisition targets set in 10th Five Year Plan and could not even reach half way mark. Similarly, based on the past trend, making good the shortfall of 37 vessels (20.15 GT) during the 11th Plan period appears to be an uphill task in the remaining period of two years.

The Ministry attributed (April 2011) the 10th Five Year Plan period shortfall to the restrictions imposed by Government (March 2002 to January 2004) on long term financial commitment in view of the proposed disinvestment in the Company. The shortfall during 11th Five Year Plan period was attributed to the global meltdown. It further stated that SCI had ordered 11 vessels during 2010-11 and as such, the backlog at present was only 26 vessels and some more proposals were already under process.

The fact, however, remained that the Company could not modernize and enhance its fleet capacity which in turn, adversely impacted its business growth especially when the country's seaborne trade was growing at a pace of 8.5 per cent annually and world fleet also registered a growth of 23 per cent.

4.2.1 Impact of delay in acquisition of vessels :

(a) Cost Escalation

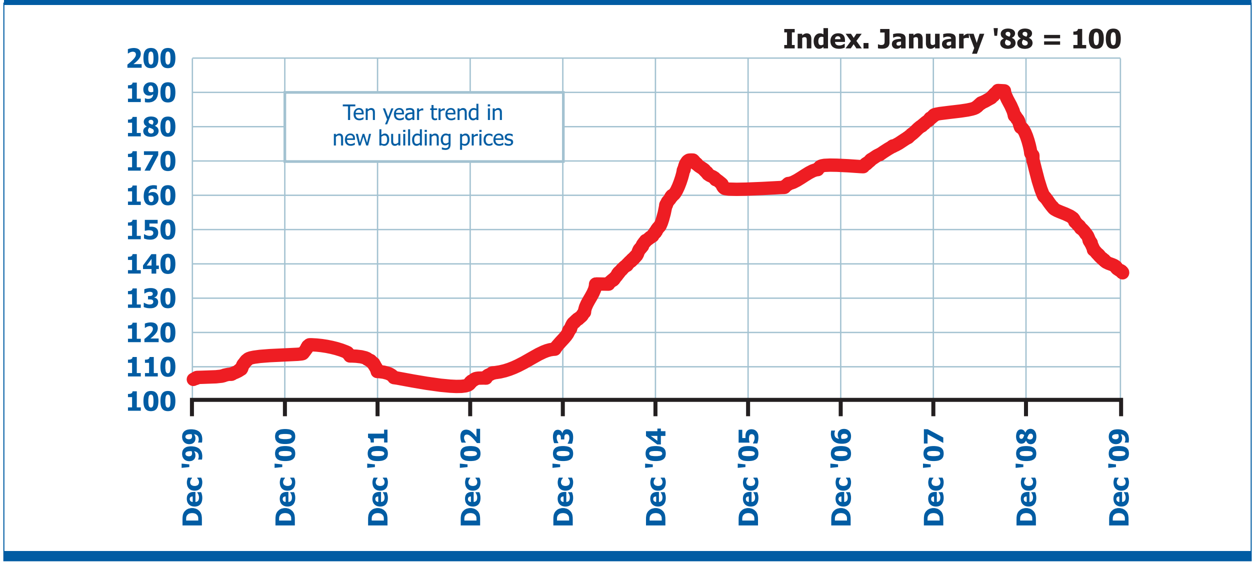
The Corporate Plan 2005 of the Company outlined the broad strategies for vessel acquisition. As per the Plan, vessel acquisition was to be done to rejuvenate the fleet periodically and within the delegated powers of the Company. Till August 2008, the Company was enjoying the status of 'Mini Ratna' with financial powers up to `500 crore for capital expenditure and thereafter, it was conferred 'Navratna' status and was empowered to decide on investment without any financial limits. During the period April 2005 to August 2008, when the Company was a 'Mini Ratna', audit noticed that the Company exercised their delegated financial powers only for six out of 32 vessels ordered and the remaining 26 vessels were clubbed into seven projects which exceeded the financial powers necessitating clearance by Public Investment Board and approval by Cabinet Committee on Economic Affairs.

Though the Company took parallel action to invite technical bids, it could not place orders as the Government's approval was awaited. The Company finally invited commercial offers during May 2005 to July 2008, at a time when the prices of new building vessels were on the rise, as may be seen from the following graph[9]:

[9] *Clarkson Shipping Intelligence Weekly, publication of Clarkson Research Services Limited, UK*

GRAPH - 8

Ten year trend in new building prices



Audit further observed that despite the commitment by the Ministry to clear/submit the investment proposal to CCEA within 14 weeks as provided in the MOU for the year 2007-08, it took 14 to 34 months to accord approval in respect of seven projects for acquisition of vessels.

As seen from the table below, there were undue delays at various stages in according approval, which ultimately resulted in acquiring vessels at higher cost besides loss of business opportunity.

Table - 4

Delay in umber of months)

Sl No.	Project	Time taken for Govt. approval #	Holding of PIB Meeting	Queries from appraising agencies	Re-tender	Delay on Company's part
1.	2 Very Large Crude Carriers	14	6	5	Nil	Nil
2.	2 Container Vessels	21	10	2	11	2
3.	6 Long Range 1 Crude Tankers	21	10	6	Nil	1
4.	4 Aframax Crude Tankers	17	3	9	7	Nil
5.	2 Long Range II Crude Tankers	17	Nil	9	7	Nil
6.	6 Handymax Bulk Carriers	34	10	8	14	1
7.	4 Panamax Bulk Carriers	30	10	8	12	2

 # based on the date of submission of proposal and date of approval by the Government

The delay in getting the approval from the Government resulted in steep rise in prices of 26 vessels by ₹2105.81 crore (Annexure-II) when compared with the indicative prices as reported by international agencies and indicated to the Government in the acquisition proposals.

The Ministry without furnishing justification for delay in according approval for the acquisition of vessels by the company stated (April 2011) that:

- Taking the indicative price for cost overrun was not appropriate as the actual cost depended on technical specifications, demand and supply situation, availability of steel, main engines and other major equipments, delivery schedule, payment terms, etc.
- As a going concern, it would not be possible for SCI to place orders for all the vessels at one point in time and the acquisitions have to be staggered.
- Timing all the acquisitions at the bottom of the cycle would be impossible for any organisation.

The reply has to be viewed in the light of the following facts:

- The Company adopted the same criteria i.e. published indicative price for assessing the reasonableness of the contracted price and for initiating negotiations with the suppliers.
- As a result of delay, commercial offers for 12 out of 26 vessels were invited in April – May 2007 when the prices were on the upswing. The bunching could have been avoided if there were regular acquisitions.
- Though it may not be possible to time all the acquisitions at the bottom of the cycle, periodic acquisitions would have helped the management in taking advantage of the lower prices.

However, the fact remains that the timing of asset acquisition is critical to the success of any shipping venture. On comparison, audit noticed that Companies like Great Eastern have been able to take advantage largely because of following such a strategy.

In essence, due to non-achievement of targets, the Company's fleet strength remained more or less static. The Company acquired eight vessels but it disposed off 15 vessels over a period of five years. Therefore, the net addition was only 2.51 lakh GT (9 per cent) against the country's fleet growth of 12.24 lakh GT (14 per cent). Further, 30 vessels (10.05 lakh GT) on order as on 31 March 2010 would not add substantially to the tonnage capacity as 24 vessels (7.55 lakh GT) would have to be replaced due to old age in the near future.

(b) Loss of business opportunity:

Audit noticed that delay in getting Government approval resulted in loss of opportunity earnings to the extent of ₹358 crore , considering the estimated charter hire rates assumed by the Company for these seven projects.

Audit further observed that post 'Navratna' status (August 2008), the Company took less than six months (in three projects comprising 5 vessels) in ordering vessels.

Ministry stated (April 2011) that such calculation of opportunity cost is not correct as the time taken by Government agencies to evaluate and appraise the proposals and grant final approval would only defer the project by that much period and as such cash flows (both cash inflows and cash outflows) would be shifted ahead. It further stated that operating life of the vessels was assumed as 25 years and time taken in getting approvals does not result in any shortening of economic operating life of the vessel.

The fact, however, remains that delay in acquisition of vessels besides impacting the present cash flows of the Company also impact the market share of the Company which gets captured by other competitors.

Chapter

5 Operation of Vessels

5.1 Operation of Vessels

The Company's operations are divided into two major segments viz.

(i) **Bulk segment** which includes dry bulk, crude and product tankers, gas carriers and chemical carriers etc and,

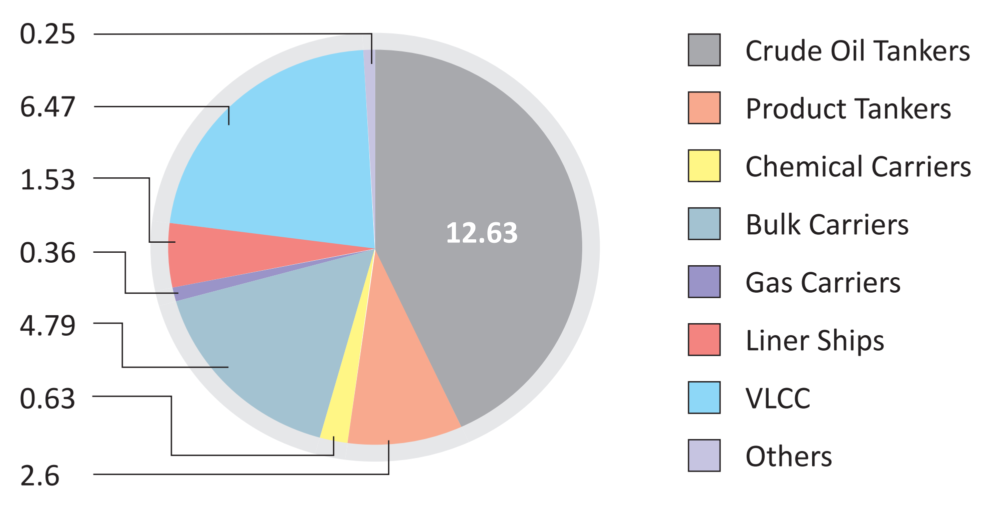
(ii) **Liner segment**, which includes break-bulk and container transport.

These two segments put together constitute about 95 per cent of the total operating earnings of the Company.

As is evident from the graph below, the major share belonged to crude oil tankers which was 43 per cent of the total capacity of 29.26 lakh GT as on 31 March 2010:

GRAPH - 9

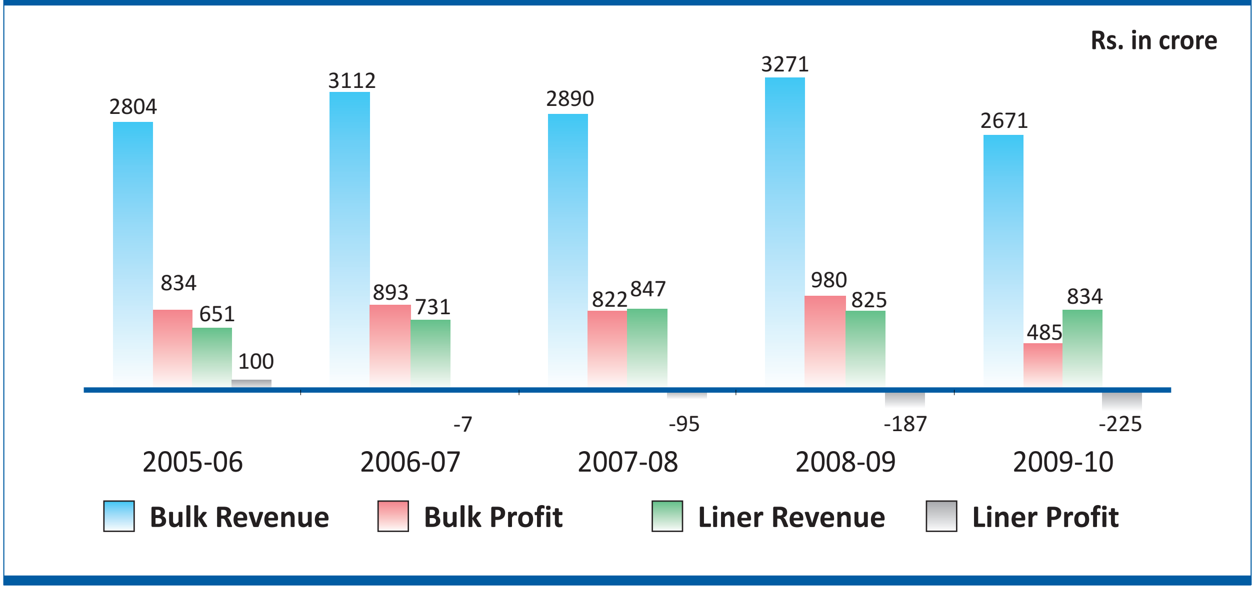
Gross Tonnage



The break up of the profitability of the Bulk and Liner segments during the period 2005-06 to 2009-10 is indicated below:

GRAPH - 10

Profitability of Bulk and Liner Segments



It may be seen from the table that though the bulk segment made sizeable contributions to the revenue earnings and profitability of the Company, the profit from this segment declined from `980.11 crore during 2008-09 to ₹ 484.93 crore during 2009-10. The liner segment which earned a profit of ₹100.29 crore in 2005-06 has been incurring losses since 2006-07 which is increasing gradually and has reached a level of ₹ 225.09 crore during 2009-10.

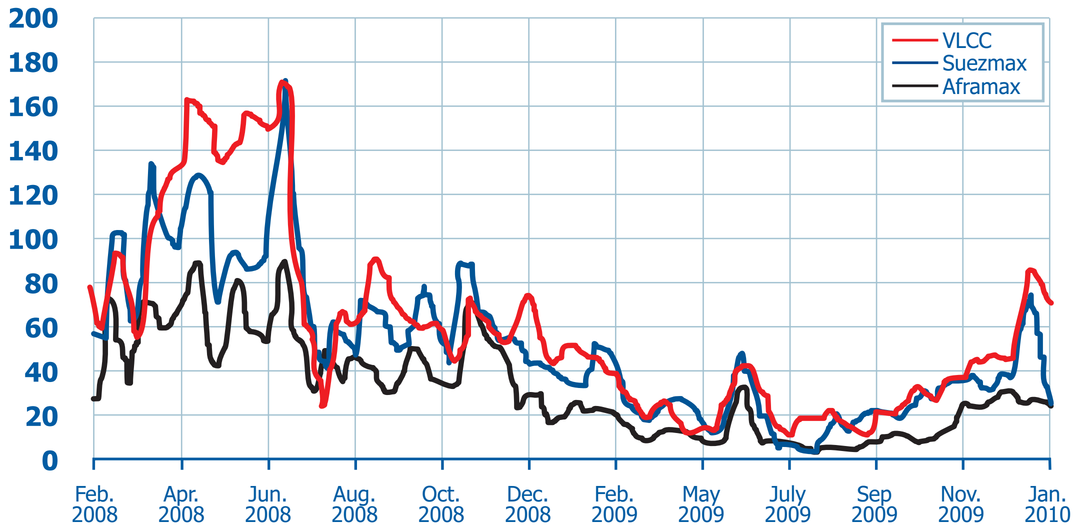
The Ministry stated (April 2011) that the reason for poor profit in 2009-10 was not stagnation of SCI fleet, but mainly the market conditions post global economic meltdown at the end of 2008, which affected the shipping markets severely. It further stated that shipping is a cyclic industry and slowdown would follow a period of boom. Accordingly, a shipping company cannot be expected to show growing profits over a longer period as it is affected by global demand and supply forces.

The reply does not address the core issue of growth of tonnage, which is not associated with the cyclical nature of the industry. In a span of 14 years as of 31 March 2010, the tonnage had actually reduced to 51 lakh DWT (76 vessels) from 54 lakh DWT (122 vessels).

Audit further analysed that fall in the charter hire rate of crude oil tankers was one of the reasons for decline in the profitability during 2009-10. The index for charter hire rate of crude oil tankers for the period February 2008 to January 2010 showed volatility and fell by about 88 per cent as could be seen from the following graph as reported in the Clarkson Intelligence Weekly:

GRAPH - 11

Crude Tanker Spot Earnings ($, 000's/day)



The other reasons, as observed by audit, which contributed to fall in operating income and profitability, are discussed below:

5.1.1 Deployment of vessels

Deployment of vessels was made by the Company either on time charter[10], or voyage charter[11], called fixture[12] or these were deployed to fulfil commitment under Contract of Affreightment (COA).

Audit noticed that vessels were deployed through brokers for which the Company as on 31 March 2010, was having a panel of 24 brokers (18 Indian and 6 foreign). A weekly meeting was held with the empanelled brokers to obtain quotes and the responses received were evaluated followed by negotiations for concluding the terms and conditions of the fixture.

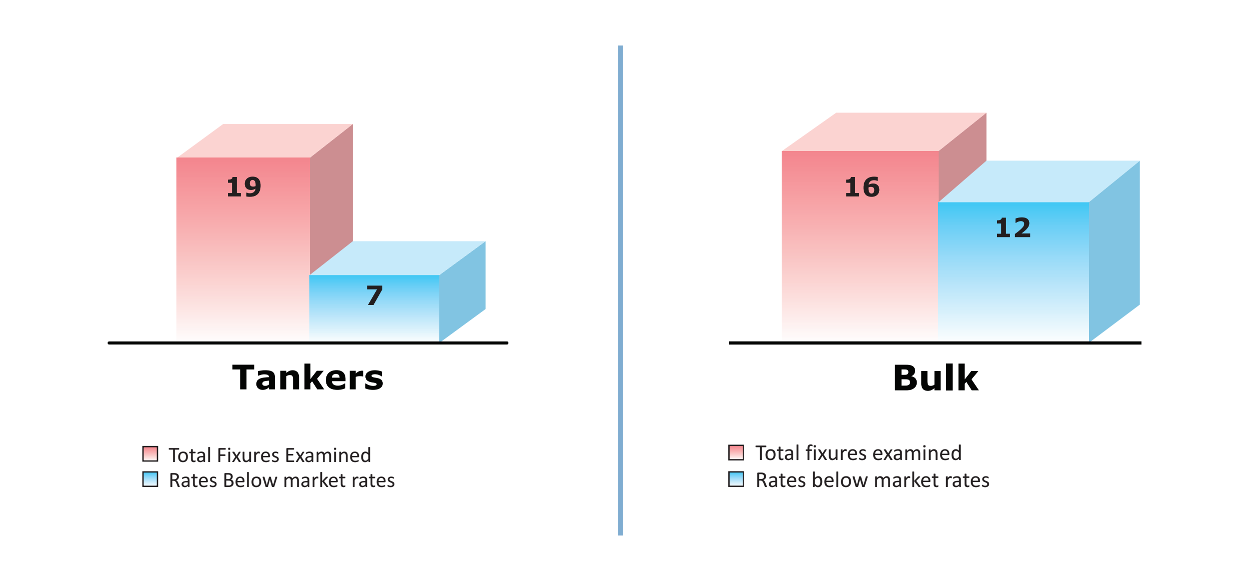
Audit examined a random sample of 35 fixtures out of a total of 546 fixtures concluded during 2007-08 to 2009-10, to ascertain the effectiveness of the system. The table and graphs below indicate the number of responses received for deployment of tankers and bulk carriers and the rates received as compared to the market rates:

[10] *Hiring of a vessel for a specific period of time.*
[11] *Hiring of a vessel and crew for a voyage between a load port and a discharge port.*
[12] *Conclusion of the contract with the charterer.*

Table - 5

No of brokers responded	Tankers	Bulk	Total
1	8	5	13
2	6	6	12
3	0	2	2
4	4	1	5
5	1	2	3
Total	**19**	**16**	**35**
Rate at par or above market rate	12	4	16
Rate below market rate	**7**	**12**	**19**

GRAPH - 12



It may be seen from the table and graphs that in 25 out of 35 cases, only one or two quotes were received and in 19 out of 35 cases, the rates received were below the prevailing market rates as published in the Clarkson Shipping Intelligence Weekly.

Audit also observed that there were no clear policy guidelines for placement /employment of vessels on short term or long term. Therefore, in the evolving situation of ships waiting for employment, the Company had to agree for charter hire rate below the market rate as the fixtures were concluded based on the discovery of price through the spot market. Further, as the proceedings of the negotiations with the brokers were not documented, audit could not get any assurance on the fairness and transparency of the process.

The Ministry stated (April 2011) that the negotiations which were done by the concerned Chartering Officers based on the exchange of negotiations normally through the brokers, either via mail or telephone, were captured by the broker and documented later which were made available to the Company. It further stated that this was the worldwide practice followed by all shipping companies.

Audit observed that IOC had voice recording system of tracking the entire negotiation process for chartering vessels. The Company was yet to follow the best practices to bring transparency in the system.

5.1.2 Idling of vessels

Idling of vessel necessarily involves incurring of standing charges besides revenue loss. During the last three years ending 2009-10; the Company lost 1978 revenue operating days incurring standing charges of ₹134.04 crore. The percentage of idle days to revenue operating days which was 1.33 only in 2007-08 had gone up to 4.46 and 3.25 in 2008-09 and 2009-10 respectively.

Though idle days were being reported monthly, there was no system in place for analysing the reasons for idling for taking corrective actions.

The Management attributed (December 2010) the idling days to the non-availability of cargo on vessel dates.

The idling of vessels when the global and national trade was growing at a faster pace is a cause of concern and therefore needed attention.

Noting the Audit concern, the Ministry agreed (April 2011) that the idling period needs to be analysed.

5.1.3 Operation of Very Large Crude Carriers

(a) The Company acquired two Very Large Crude Carriers (VLCCs) in January 2005 and August 2005 and two in October 2008 and June 2009 mainly to gain a share in the growing business of transportation of imported crude in the country.

Audit observed that Company could not get any business from Indian Oil Corporation Limited (IOC) during the period 2007-08 to 2009-10, despite the fact that IOC imported 92 million metric tonnes of crude oil through other VLCCs. The Company has no system of analysing reasons for not encashing such enormous business opportunity available within the country especially when earlier, most of the oil imports were being done through the Company.

The Management stated (December 2010) that the maintenance of database had no archival value as each fixture was specific in its context. The Ministry stated (April 2011) that price was the prime customer need and maintenance of database of customer needs may not help to secure orders.

To conclude, the country's total import of crude oil during 2009-10 was 159 million tonnes, of which SCI's share was only 9 per cent. The Company, therefore, needs to be aggressive in capturing the market share of import of crude oil and accordingly evolve a strategy for meeting customers' requirement for securing long term contracts.

(b) Audit examination revealed that the VLCCs owned by the Company were, however, engaged in cross trade.

Table below indicates the earnings and profitability of VLCCs during 2007-08 to 2009-10.

Table - 6

₹ in crore

Year	Earnings	Profit
2007-08	195.52	57.63
2008-09	269.11	123.97
2009-10	306.62	87.55

Though the Company made profits in the cross trade of VLCCs, audit observed that out of a total of 19 fixtures made during 2007-10, 13 were concluded through single broker of which four fixtures were with the charter rates below the prevailing market rates (Details in Annexure III).

While ignoring the fact of over dependence on a single broker for employment of VLCCs, the Ministry justified (April 2011) the difference in the rates obtained on the grounds of the possible continuation of existing fixture, fixtures of longer duration, better technical specifications of vessels and deployment of vessels on maiden voyage by the competitors.

The reply of the Ministry is to be viewed in the following context:

(a) The Company is predominantly depending on one broker only for fixing VLCCs.

(b) The comparable market rates quoted by Audit were based on rates published in the Clarkson Shipping Intelligence Weekly which indicated the then prevailing global market trends.

In sum, the Company needs to diversify the base of its brokers to ensure better market price for deployment of its vessels.

5.1.4 Non- fulfilment of commitment with Oil PSUs

The Company has been entering into yearly Contract of Affreightment (COAs) with Oil PSUs like BPCL and HPCL for transportation of crude.

A review of the COAs entered during the three years ending March 2010 revealed that the Company failed to fulfil the quantity commitments due to inadequate tonnage available with it as discussed below:

GRAPH - 13

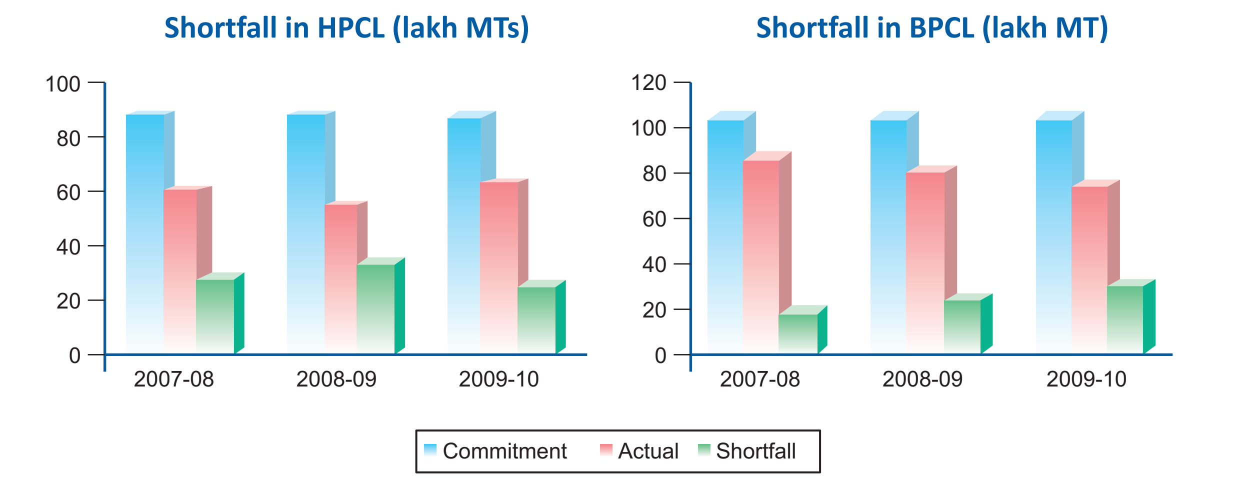


Table - 7

In lakh MTs

Particulars	2007 - 08		2008-09		2009-10	
	BPCL	HPCL	BPCL	HPCL	BPCL	HPCL
Commitment	83.50	110.00	83.50	110.00	83.50	110.00*
Actual	57.15	91.08	52.09	84.89	59.76	78.17
Shortfall	26.35	18.92	31.41	25.11	23.74	31.83
Percentage of shortfall	32	17	38	23	28	29

*(*excluding transported through inchartered vessels)*

Audit observed that despite the fact that the Company was having an assured business in this segment from the oil PSUs; it failed to fulfil its commitment due to non availability of vessels. Audit noticed that while in case of HPCL, the Company had to incharter vessels at 105 times (112.04 lakh MTs of crude oil) at a cost of ₹ 448.40 crore for transporting oil; whereas for BPCL, as there was no such provision in the COA, the latter made their own shipping arrangements.

The Management stated (December 2010) that shortfall in lifting was due to mismatch in the dates of availability of vessel and the loading dates offered by BPCL/HPCL.

The Ministry stated (April 2011) that SCI's fleet of crude oil tankers was just enough to fulfil the COA commitments, provided the cargo lifting dates were given on vessels availability dates. However, the loading dates mainly depend upon HPCL/BPCL refinery requirements, congestion/waiting at load and discharge port and availability of product at load port, etc. Ministry further added that it was incorrect to state that the Company could not take advantage of the assured business as the company's crude tankers were gainfully employed under COA voyages with minimum idling between two voyages. Induction of any additional units, exclusively to perform COA voyages, would have only increased the idling days.

The fact remains that due to inadequate planning and coordination, the Company could not take advantage of the assured business. Ministry's contention of induction of additional tonnage resulting in idling days has to be seen in the backdrop of Company's meagre share of mere 9 per cent in the import of crude oil by the country.

5.2 Liner Container Services

Liner container services offer regular scheduled transport on specified and fixed routes. Containerisation permits the same cargo to be transported not only by ship, but also loaded onto a truck or rail car before or after the ocean transportation. Globally, 90 per cent of non-bulk cargo moved by containers is stacked on ships.

The Company acquired three container vessels of 1868 TEUs[13] (two in December 1993 and one in January 1994). After a gap of 14 years, the Company acquired two more container vessels of 4400 TEUs each in October 2008. As on 31 March 2010, the total capacity of the container vessels was 14407 TEUs, which was just 0.11 per cent of the world fleet.

Audit observed that though the container traffic handled at major ports in India grew from 22.66 lakh TEUs in 2005-06 to 65.86 lakh TEUs in 2008-09 (growth of 191 per cent), the Company could increase their share from 1.57 lakh TEUs to 2.82 lakh TEUs (growth of 80 per cent).

With its own and inchartered container vessels, the Company operated a total of seven container services during 2005-06 to 2009-10, as detailed below.

[13] *Twenty feet Equivalent Unit*

Table - 8

(Profit/Loss (-) in ₹ in crore)

Particulars	2005-06	2006-07	2007-08	2008-09	2000-10	Remarks
India US East Coast Service (IDX)	NA	NA	NA	NA	NA	Commenced - May 2006, closed - March 2008
Far East to Middle East (Hyper Galex)	NA	NA	NA	NA	NA	Commenced – November 2006 closed - April 2008
India Red Sea	NA	NA	NA	NA	NA	Commenced – Feb 2009 closed - Sept 2009
India Subcontinent Europe Service	8.92	8.92	8.92	8.92	8.92	Commenced in 1994
India Far East Cellular Service (INDFEX 1)	43.64	43.64	43.64	43.64	43.64	Commenced in June 2001
India Far East Cellular Service (INDFEX 2)	18.85	18.85	18.85	18.85	18.85	Commenced in June 2002
SCI Middle East India Liner Express (SMILE)	0.00	0.00	0.00	0.00	0.00	Commenced in March 2008
Total	**61.16**	**-23.15**	**-58.54**	**-150.06**	**-206.15**	

The Company incurred continuous losses on this segment since 2006-07, which had accumulated to ₹438 crore as on 31 March 2010. In fact, first three services commenced and closed within a span of less than two years. In view of the losses, the management in October 2009, reviewed the operations of this segment and assessed that exiting from the services would cost ₹782 crore.

The management attributed (December 2010) the losses to the operation of India - US Service during the year 2005-06 till 2008-09. Management further argued that exiting from this business would also not be in the national interest as SCI was the only Indian company in this business.

Audit is of the view that compromising on the commercial viability would not be financially prudent and the national interest would be better served only if the operations are self sustaining.

While agreeing with Audit that commercial considerations were important , the Ministry stated (April,2011) that as a long term player in the Liner Business, there would be periods of profits and losses, but overall, the Liner Business was beneficial to SCI. It further stated that SCI was mainly focusing on energy transportation business and in the Container Sector; it was mainly in the niche market, catering to India – Europe Trade and Far East – India Trade. **It added that the size of SCI's operations was very small as it was not having enough hardware and depended on the inchartered tonnage for its operations. SCI was affected by the vagaries of charter market, very adversely.** The container sector had, however, turned around during 2010-11, as it posted a profit of Rs.80 crore upto 31 December 2010.

Though the Company made a profit of Rs.80 crore during 2010-11, the fact remains that it made a cumulative loss of ₹ 438 crore upto 2009-10 and there is a need for continuous review of liner business to avoid any major losses in the future. There is also an urgent need to build up tonnage in the liner segment to protect the Company from the vagaries of charter market.

Audit examination revealed the following inadequacies:

(a) Loss on India- USA East Coast Service (IDX)

The Company, with four consortium members operated the India- US East Coast (INDAMEX) Service from March 2000 onwards. When the consortium partners put (March 2004) in higher capacity vessels the Company was not in a position to place a vessel of that capacity and thus decided (January 2005) to exit from the service. During the period of operation, the Company incurred a loss of ₹ 25.13 crore mainly due to low capacity utilisation. In addition, the Company was also expected to meet the estimated liability of ₹ 9 to ₹ 11.50 crore towards New York Long Shoreman pension fund due to withdrawal of service.

In February 2006, the Company decided to recommence the service as India -USA East Coast Service (IDX) on the same route with a minimum profit projection of ₹ 2.78 crore per annum. The Company inchartered two vessels for a period of 35/37 months and commenced the service from May 2006 in consortium with other partners. As the Service incurred heavy losses and the other partners pulled out from the service, the Company also closed down (March 2008) the service after incurring a loss of ₹ 107.63 crore.Audit observed that:

- The service was recommenced in May 2006 mainly to avoid the estimated pension liability of ₹ 9 to 11.50 crore, necessitated due to closure of the earlier service which ultimately increased to ₹ 17.67 crore.

- Company failed to place vessels as per requirement of the service and had to pay blank off charges of ₹ 12.74 crore (net) to other consortium partners as per the terms of consortium agreement.

- The capacity utilization in the service was far below the assumptions. It could achieve only 61 per cent in 2006-07 and 74 per cent in 2007-08 on the west bound journeys against 85 per cent assumed. Similarly, on the east bound journey, it could achieve 33 per cent in 2006-07 and 61 per cent in 2007-08 against 50 per cent assumed.

- The cost of inchartered vessel was higher i.e. US $ 22,000 each per day instead of US $ 20,000 each per day assumed.

While accepting the fact that SCI had to exit the earlier service due to inability to provide suitable vessel, the Ministry stated (April 2011) that the second service was withdrawn by all the partners mainly due to steep drop in freight rates as a result of recessionary trends in US Trade. It further stated that SCI had always been striving to have dedicated container services on India–USA sector, since USA was an important trade partner of India.

The closure and commencement of service in quick succession indicated that the Company did not have a well considered strategy. This also put at stake its own image as a reliable operator.

(b) Higher cost due to inchartering of vessels

During the period under review, the Company inchartered six vessels for periods ranging from 806 days to 1616 days involving a pay out of US $ 165.83 million (₹746.22 crore) as detailed in the Annexure IV.

Audit examination of one inchartered vessel, SCI Vijay (capacity 2800 TEU), revealed that the vessel was inchartered (October 2005) for five years at the rate of USD 30,000 per day and USD 48.45 million was paid till March 2010 as charter hire charges. Standing charges incurred by the Company for similar owned container vessels inducted (October 2008) was US $ 19,000 per day. Considering the standing charges for owned vessel, the additional cost incurred for this vessel worked out to US $ 17.78 million (₹83.55 crore) for 1616 days. Audit further observed that though the Company planned acquisition of three 3500 TEU container vessels at an indicative price of USD 43 million per vessel during 10th Five Year Plan period, the option of buying a new vessel was not evaluated while inchartering the vessel.

The Management as well as Ministry accepted (December 2010 and April 2011 respectively) the need for owned vessels for liner services and added that action for acquiring additional container vessels had been initiated.

5.3 Repair and maintenance of vessels

Repairs and maintenance of the fleet constitutes one of the major items of expenses and includes expenditure on repairs of deck and engine, consumption of stores and spares, chipping and painting and surveys.

In the absence of any norms, the performance of the Company with regard to repairs and maintenance was compared with that of Great Eastern Shipping Company Limited, the nearest Indian competitor and audit observed that the expenditure incurred by the Company was comparatively higher as indicated below:

Table - 9 Repairs and maintenance expenditure (including consumption of stores) as percentage of operating earnings

Company	2007-08	2008-09	2009-10
SCI	15	13	16
Great Eastern Shipping Company	9	10	10

The Management stated (December 2010) that it was not practical to draw benchmark or norms to evaluate performance. It added that the expenditure on repairs and maintenance was to be incurred constantly to maintain the vessels in seaworthy condition and to comply with statutory requirements, irrespective of the commercial use of the vessel.

The Ministry stated (April 2011) that there were no benchmarks or norms on repairs and maintenance expenditure fixed by the Company or by the industry and it would depend upon the type, age, condition of the vessel and trading pattern. It further added that comparison of overall repairs and maintenance cost of SCI vessels vis-a-vis Great Eastern vessels was unjustified as Great Eastern has lesser number of vessels, lower age profile thereby reducing the repair and maintenance expenditure.

The reply of the Management/Ministry is to be viewed in light of the fact that significant higher repair and maintenance cost reflects the operational inefficiencies of the vessels which have a cascading impact on its business opportunities and therefore, needs to be addressed for corrective action.

5.4 Dry-docking of vessels

For assessing the seaworthiness of the vessels, as per the statutory requirement of Indian Register of Shipping[14], the vessels are required to undergo major repairs called dry docking in an interval of two years and twice within a cycle of five years. The dry docking forms a significant part of the total repair and maintenance expenditure.

During 2007-08 to 2009-10, the Bulk Segment of the Company dry-docked 67 vessels at a total cost of ₹ 408.19 crore.

[14] *Classification Society for registration of vessels in India.*

Audit randomly selected nine vessels (contracts) out of 67 vessels dry-docked during 2007-08 to 2009-10 for examination. Details of vessels selected for examination are given in Annexure V.

Audit observed the following deficiencies in awarding, execution and payments:

- The Company received poor response from the ship yards for dry-docking and concluded contracts with reference to the limited quotes received. The maximum response received in all the cases test checked was only three.

- The bills received from yards for dry docking were 10 to 39 per cent inflated as compared to the settled amount. Further, the scope of work as envisaged originally and executed finally was not supported with any variance analysis.

- The inflation of the bills by the yards was not considered by the Company while evaluating their performance for awarding subsequent works.

- The supervising officers of the Company certifying the work were not made accountable for the large scale variations in the bills.

The Management stated (December 2010) that minimum number of quotations received during 2010-11 had improved to four.

The Ministry accepted (April 2011) the fact that the present manual system has limitation to analyze the variation in the scope of work during actual implementation and stated that SCI was implementing an IT project to address the issue. It further stated that SCI was finalizing a formula / process by which the yard performance rating would also take into account the inflation of bills.

Chapter

6 Oversight Mechanism

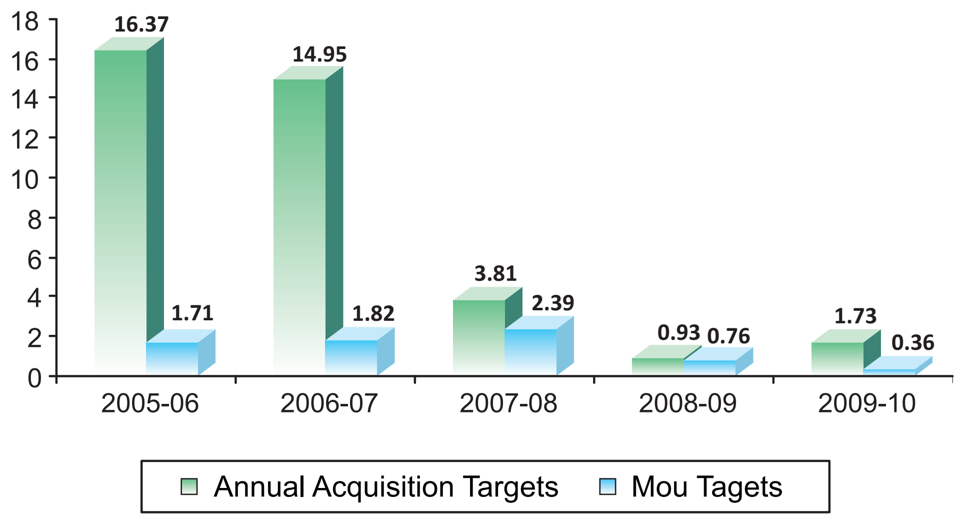
6.1 Monitoring by the Ministry of Shipping

The Government monitors the performance of the Company through Memorandum Of Understandings (MOUs) and during the period under review, the Company achieved "excellent" ratings in all the years[15].

Audit, however, noticed that the targets for tonnage acquisition which is one of the key performance parameter, as per MOUs, were far below the annual acquisition plans targets as discussed below:

GRAPH - 14

Comparison between annual acquisition targets with MOU targets



[15] *Rating for 2009-10 is based on results reported by the Company to the Ministry*

Table - 10 Gross Tonnage in Lakh MTs

Year	Annual Acquisition Plan (GT)	MOUI Target (GT)	Actual (GT)	Percentage of actual with reference to Annual Acquisition Plan	Percentage of actual with reference to MOU Target
2005-06	16.37	1.71	3.20	19.55	187.13
2006-07	14.95	1.82	3.86	25.82	212.09
2007-08	3.81	3.39	5.64	148.03	166.37
2008-09	0.93	0.76	1.72	184.95	226.32
2009-10	1.73	0.36	0.38	21.97	105.56

As could be seen from the above table, the Company was rated 'excellent' despite their lacklustre performance with reference to their own target set in the annual plan in three out of five years.

The Ministry stated (April 2011) that due to extreme uncertainty regarding how much tonnage would be approved for ordering (by Government), the MOU targets were kept lower than the Annual Plans. It further stated that the actual achievements in tonnage acquisition were considerably higher than the MOU targets which indicated high level of motivation to achieve the highest possible performance.

The above reply is not tenable as tonnage acquisition i. e. capacity building, is a critical component of a shipping company and therefore, needs closer monitoring at different levels. The MOU with the Government is in fact one instrument through which this activity could be given a momentum. Downsizing the target in MOU would only hamper the long term acquisition plans of the company. Further, the fact remains that there cannot be two sets of targets, one for rating purpose and other for business requirement.

Though the Company failed to achieve the annual targets set by them in three out of the five year period but the fact remains that with the scaled down MOU targets with the GOI, the Company was given full weightage on the key performance parameter of tonnage acquisition in all the years. Thus, the underlying principle of an MOU to motivate the Company to strive for further growth was defeated.

6.2 Monitoring by Management

Management Information System (MIS) is a vital tool with the management to monitor various activities and to take business decisions. Audit observed structural deficiencies in the MIS such as:

- mismatches in various information- generated through MIS and as appearing in the annual accounts of the Company regarding sector-wise profitability,

- MIS was not able to work out the trip wise profitability of vessels chartered out on time charter basis,
- data relating to debit note raised in terms of charter party agreements / COAs available in the system was not integrated with financial accounting system and thereby was exposed to manual intervention and
- the database lacked proper validation as out of a sample of 875 entries for the year 2009-10 checked in Audit, 66 entries for an amount of ₹117.77 crore were found without voyage numbers which is a crucial data,

Though these deficiencies were encountered while preparing the Corporate Plans of 2000 and 2005, these were still persisting (March 2010). Thus, the fact is that the management was taking important decisions based on the data which was not adequate and reliable.

The Ministry while noting the audit observations stated (April 2011) that with the implementation of new ERP system and linkage of all the business activities into the new system, it would be possible to generate precise MIS reports for guidance of the Management.

Chapter

7 Conclusion and Recommendations

7.1 Conclusion

With the removal of trade barriers and globalisation, the shipping industry's fortunes are driven by the growth of seaborne trade and supply of vessels. Though the Indian fleet has grown by 24 per cent during 2005-06 to 2008-09, it did not match the growth of trade during that period and the share of Indian shipping industry in the country's trade declined from 14 per cent to 8 per cent during this period. Non-existence of level playing field especially on taxation impacted the competitiveness of the Indian shipping industry in the backdrop of increased competition from the foreign shipping companies.

The Company did not pursue an ambitious acquisition policy to augment and modernise its fleet and the tonnage capacity remained almost static during the period 2005-06 to 2009-10. The Company was not adhering to their annual fleet acquisition targets and there were slippages resulting in cost overrun thereby impacting their operational efficiencies. The Company in the absence of policy guidelines on the engagement of vessels on long term and spot market rates, deployed majority of the vessels on fixtures at a charter hire rate determined by the spot market. The idle days when the ships were not earning any income but incurring cost were on the rise indicating an urgent need for closer monitoring. Frequent commencement and closure of liner services within a short duration resulted not only in financial loss to the Company but also affected their credibility as a reliable service provider.

The Management Information System was not effective and there were conflicting data on various parameters of operational efficiency. The Management needs to look into all the above critical issues and streamline its operations so as to achieve its Mission of a global player in overseas trade.

7.2 Recommendations

Based on the Audit findings discussed in the foregoing chapters, the following recommendations are made:

1. As the linkages between the development of the economy and growth of shipping industry are strong, the Government may address the concerns faced by the Industry to facilitate a strong national core fleet.

2 The Company needs to frame and implement a time bound acquisition policy for fleet growth and modernisation to face the global competition.

3 The Company should ensure that vessels are employed gainfully and avoid idling of vessels. Also, the Company needs to be aggressive in getting business from its major customers, particularly the Oil Majors.

4. The Company needs to have a system of reviewing loss making operations at regular intervals for taking remedial measure in time.

5. The Company should formulate a policy for having an optimum mix of owned and inchartered vessels in the liner segment to bring down the high incidence of inchartered costs.

The Ministry while accepting last three recommendations stated that action on first two recommendations has already been initiated/ taken.

(Arvind K. Awasthi)
Deputy Comptroller and Auditor General
and Chairman, Audit Board

New Delhi
Dated : 24 June, 2011

Countersigned

(VINOD RAI)
Comptroller and Auditor General of India

New Delhi
Dated : 24 June, 2011

ANNEXURE - 1

Details of tax on Indian Shipping Lines
Chapter 3 - Para No. 3.1.1 (i)

Sl. No.	Type of taxes	Tax effect (per cent) FY 2009-10	Tax effect (per cent) FY 2009-10	Exemption in other Countries
1	**Corporate Income Tax on other income**	33.99	33.22	United Kingdom, Singapore and Germany
2	**Minimum Alternate Tax on profit/loss on sale of assets**	17.00	19.93	United Kingdom, Singapore, Germany and Ireland
3	**Dividend Distribution Tax**	17.00	16.61	United Kingdom, Singapore, Ireland, Netherlands, Germany and Australia
4	**Fringe Benefit Tax**			Since withdrawn
5	**Withholding tax liability on interest paid to foreign lenders**	10.00	10.00	Netherlands and Germany
6	**Withholding tax liability on charter hire charges paid to foreign ship owners**	10.00	10.00	Singapore and Netherlands
7	**Seafarers' taxation**	0-34	0-34	Singapore
8	**Wealth tax**	Applicable Slab Rates	Applicable slab rates	United Kingdom, Netherlands and Germany
9	**Sales tax/Value Added Tax on ship supplies**	4-12.5	4-12.5	Germany and Netherlands
10	**Lease tax on charter hire charges**	4-12.5	4-12.5	Germany and Netherlands
11	**Customs duty on stores, spares and bunkers**	30-40	30-40	United Kingdom
12	**Service tax**	10.30	10.30	United Kingdom, Ireland, Singapore and Australia

ANNEXURE - 2

Detailed working of increase in cost of ₹ 2105.81 crore Referred to in Chapter 4, Para 4.2.1 (a)

Name of the Project	Original proposal		Final proposal		Overrun at estimated cost	
	Date of Board Approval	Amount*	Date of Contract	Amount**	In months	Amount
2 Very Large Crude Carriers	27.07.04	791.00	28.10.05	1196.79	15.27	405.79 (51.30%)
2 Container Vessels	31.01.05	477.00	14.11.06	568.02	21.73	91.02 (19.08%)
6 Long Range I Tankers	31.01.05	972.00	27.10.06	1705.68	21.13	733.68 (75.48%)
4 Aframax Tankers	30.07.05	1091.20	10.08.07	1168.42	24.70	77.22 (7.08%)
2 Long Range II Tankers	27.01.06	528.00	10.08.07	594.26	18.67	66.26 (12.55)
6 Handymax Bulk Carriers	31.01.05	702.00	04.12.07	1105.35	34.57	403.35 (57.45)
4 Panamax Bulk Carriers	30.07.05	633.60	13.08.08	962.09	37.00	328.49 (51.84%)
Total		**5194.8**		**7300.61**		**2105.81**

Note : * calculated at the exchange rate on the date of Board Approval
** calculated at the exchange rate on the date of contract signed

ANNEXURE - 3

Details of charter hire rates for VLCCs (Referred to in para 5.1.3(b))

Name of the VLCC	Date of entering the market	Period*	Charter hire rate fixed (US$ per day)	Market rate (as reported by Clarkson)	Ministry's reply	Further remarks of audit
Desh Vishal (June 2009 built)	24.02.09	For 3 months 9 months 3 months 3 months	33600 34350 35750 36750	Report dated 27.03.2009 One double hull 2007 built VLCC was fixed for one year at US $ 60000 per day on 5 February 2009.	The vessel was fixed for US $ 60000 per day in continuation of the existing fixture. The vessel was entered in the market in February 2009 although the vessel was scheduled for delivery in June 2009. Charter hire rates fixed for some fixtures during April – May 2009 ranged from US $ 35000 to US $ 37500 per day and fixtures were for storage purpose also.	The fixture reported by audit was based on the Clarkson Shipping Intelligence Weekly and the context in which the vessels fixed was not indicated therein. Apart from the fixtures indicated, there were other fixtures as detailed below (i) One more double hull 2006 built VLCC was fixed for six months at US $ 57000 per day. (ii) Another double hull 1999 built VLCC was fixed for six months at US $ 62000 per day.
Desh Virat (October 2008 built)	11.08.09	For 6 months 3 months 3 months	33750 34750 35750	Report dated 28.08.2009 One double hull 2009 built VLCC was fixed for 6 – 12 months at US $ 36000 per day on 5 August 2009	The fixture at US $ 36200 was for three years and SCI was not in the market for long term fixtures as the market was on the downslide.	m.t. Desh Vaibhav was entered in the market by the Company on 8 September 2009 and fixed for three years. Hence, the contention that the company was not in the market for long term fixture was not correct. Further, another double hull 2000 built VLCC was fixed for three years at US $ 36200 per day on 23 July 2009.
Desh Vaibhav (August 2005 built)	08.09.09	For three years from 02.12.09 onwards.	30000 / 32250 / 34500 for 12 months each	-do-	The fixture reported at US $ 36000 was for a new built vessel for utilisation as gas oil storage. Crude oil tankers can carry gas oil only during their maiden voyage and once a dirty crude oil was loaded the vessel was no longer suitable for loading gas oil.	As stated above a double hull 2000 built VLCC was fixed for three years at US $ 36200 per day on 23 July 2009.
Desh Ujala (January 2005 built)	06.10.09	For two years from 05.02.10 onwards.	30000 for 12 months and 32000 for 12 months	Report dated 4.12.09 One double hull 2001 built VLCC was fixed for 2 years at a charter hire rate of US $ 40000 per day on 29 September. 2009.	The vessel reported by audit was capable of carrying nearly 2 million barrels without requirement of lightening, navigation and cargo systems designed with redundancy i.e. the vessel has two independent systems for propulsion, navigation and cargo such that if one fails the other can take over. With such advanced design the vessel presumably must have been very expensive	Apart from the one case reported by audit there were two more fixtures as detailed below. (i) One double hull VLCC was fixed for three years at a charter hire rate of US $ 34000 per day. (ii) Another double hull 2006 built VLCC was fixed for six months at a charter hire rate of US $ 37500 per day.

(*In all the cases, the charter has the option to continue with the agreed rates after the primary period is over)

ANNEXURE - 4

Details of inchartered vessels
Chapter 5-Para No.5.2)

Name of the vessel	Period from	Period to	Total duration of hire (days)	Character hire rate (US $ per day)	Total charter hire paid (in lakh US $)
SCI Vijay	27 October 2005	31 March 2010	1616	30000	484.80
SCI Trust	7 July 2006	7 January 2010	1280	22250	284.80
SCI Diya	1 October 2006	18 December 2008	809	26000	210.34
SCI Kiran	27 November 2006	10 February 2009	806	22000	177.32
SCI Jyoti	20 December 2006	5 October 2009	1020	22000	224.40
SCI Mahima	14 August 2004	31 August 2007	1112	24875	276.61
Total					**1658.27**

(₹746.22 crore @ exchange rate of US$ 45)

ANNEXURE - 5

Statement showing details of vessels selected for audit (Referred to in Para No.5.4)

(₹ in crore)

Vessel Name	Year of dry dock	No. of yard short-listed	No. of offers received	Lowest Bidder/ Name of the Ship Yard Place	Quoted days	Actual Days	Difference in Days	Budget Cost	Quoted Cost	Billed Cost	Settled Cost	% of reduction
M V Ganga Sagar	2007-08	5	2	**M/s Yiulian Shipyard, China**	30	63	33	7.4	6.18	9.72	7.19	26.03
MV Lok Prakash	2007-08	8	3	**M/s Yiulian Shipyard, China**	28	60	32	6.2	6.16	10.08	6.11	39.38
MT Guru Govind Singh	2007-08	6	3	**M/s Dubai Drydock Ltd., Dubai.**	26	30	4	9	8.99	9.75	8.74	10.36
MT R N Tagore	2008-09	7	2	**M/s Colombo Dockyard PLC, Colombo**	25	36	11	6.5	5.97	8.57	6.36	25.86
MT Motilal Nehru	2008-09	7	1	**M/s Colombo Dockyard PLC, Colombo**	26	33	7	7.5	7.49	12.32	8.25	33.06
MT B C CHaterjee	2008-09	7	2	**M/s Colombo Dockyard PLC, Colombo**	24	30	6	6	5.94	8.42	5.94	29.45
MT Bharatidasan	2009-10	7	3	**M/s Colombo Dockyard PLC, Colombo**	30	43	13	12.45	12.24	16.03	13.59	15.22
MT Desh Shakti	2009-10	4	2	**M/s Arab Shipbuilding and Repair, Bahrain**	25	48	23	7.3	6.84	6.02	4.74	21.26
MT Maharshi Karve	2009-10	7	1	**M/s Colombo Dockyard PLC, Colombo**	30	50	20	11.2	10.79	14.17	10.78	23.92
Total					**244**	**393**	**149**	**73.55**	**70.60**	**95.08**	**71.70**	**24.59**