CHAPTER - III

Transaction Audit Observations

Important audit findings noticed as a result of test check of transactions of the State Government Companies are included in this Chapter.

Tamil Nadu Newsprint and Papers Limited

3.1 Undue benefit to a private handling agent

The Company extended an unintended benefit of ₹6.08 crore as differential Railway freight to a private handling agent in contravention of tender/work order conditions.

Tamil Nadu Newsprint and Papers Limited (Company) invited (November 2009) global tenders for the import of coal and the tender documents *inter alia,* stipulated that the contract would be split into two parts *viz*., Purchase Order (PO) on the overseas principal for coal on Cost & Freight (C&F) Tuticorin basis and a Work Order (WO) on their Indian counterpart for stevedoring, handling and loading operations @ ₹66.41/MT. The tender further stipulated that though it was for C&F Tuticorin basis, the supplier was permitted to perform the shipment through Tuticorin or any other port depending upon his convenience and that in such a case the charges for stevedoring, handling, loading operations would be restricted to ₹66.41/MT and the Railway freight (which was to be borne by the Company as per the tender) would also be restricted to the freight amount applicable (₹333.72/MT) for movement from Tuticorin to Pugalur and the excess freight was to be borne by the supplier. These stipulations were included in the PO issued (December 2009) to the successful tenderer for supply of 2.40 lakh MTs of Indonesian coal @ US$ 68.80/MT (C&F Tuticorin). The WO was issued to their Indian handling agent for handling the coal consignment at Tuticorin port @ ₹66.41/MT. The first shipment against the above PO was effected through Tuticorin port. The Company paid the foreign supplier and their Indian handling agent at the agreed rates and the freight from Tuticorin to Pugalur (319 KMs) @ ₹333.72/MT was also paid by the Company.

From the subsequent shipment onwards, the supplier routed the coal through Karaikal port. After making payments to the foreign supplier and their Indian handling agent at the agreed rates and the Railway freight from Karaikal to Pugalur (229 KMs) @ ₹253.51/MT, Senior Manager (Transport) in a *suo moto* note stated (June to October 2010) that as per the PO clause, the Railway freight had to be considered as ₹333.72/MT even for shipments through Karaikal port and the difference between the freight charges payable for Tuticorin to Pugalur @ ₹333.72/MT (₹4.01 crore) and the freight charges paid by the Company for Karaikal to Pugalur @ ₹253.51/MT (₹3.04 crore) had to be paid to the handling agent as differential Railway freight. The proposal was approved by the General Manager (M&L) and a sum of ₹0.97 crore was paid to the handling agent as differential Railway freight.

The Company issued four more POs (July 2010 to May 2011) for the import of coal. All the shipments against these POs were routed through Karaikal

port. Besides making payments to the coal suppliers and their handling agents, the Company paid ₹5.11 crore to the handling agents as the differential Railway freight. Thus, the Company paid ₹6.08 crore as differential Railway freight against these five POs.

As the tenders clearly stipulated that in case of shipment through other than Tuticorin port, the freight charges would be restricted to freight charges applicable from Tuticorin to Pugalur and that the Railway freight would be borne by the Company, the payment of differential Railway freight to the handling agents is irregular and resulted in an unintended benefit of ₹6.08 crore to them.

The Government replied (September 2012) that in all the tenders as well as purchase orders, it was clearly stated that the Railway freight was payable as applicable to Tuticorin port and that when coal supply was on C&F Tuticorin basis and the delivery was to be made by wagons to Pugalur sidings, all expenses like port dues, stevedoring, handling, loading, freight, *etc*., were to be reckoned for movement from Tuticorin to Pugalur.

The reply is not tenable as the tender stipulated that stevedoring, handling and loading were the responsibilities of the handling agents and expenses for these at Tuticorin or any port were payable at ₹66.41 per MT. The tender also stipulated that Railway freight would be borne by the Company. Therefore, payment of differential Railway freight to the supplier lacked justification and resulted in an undue benefit of ₹6.08 crore.

Tamil Nadu State Transport Corporations

3.2 Loss of interest

Four Tamil Nadu State Transport Corporations (STCs) suffered loss of interest of ₹2.53 crore due to investment of provident fund contributions in a company known to be loss making.

The State Government had formed an exclusive trust for Provident Fund (PF) and gratuity along with formation of respective State Transport Corporations (STCs). As per the rules governing the PF trust, the STCs shall transfer their own contributions and that of their employees on a monthly basis to the fund which shall be invested in banks or in approved Government securities as prescribed by the Government of India from time to time.

As a part of regular investment, the PF trusts of four STCs at Villupuram, Salem, Kumbakonam and Coimbatore had invested (between July 1999 and February 2002) a sum of ₹4.29 crore in redeemable non-cumulative bonds issued by Pradeshiya Industrial Investment Corporation of Uttar Pradesh Limited (PIICUP), Lucknow (guaranteed by the Government of Uttar Pradesh), with an interest rate varying between 13 to 13.75 *per cent per annum*.

In October 2003, PIICUP informed the STCs that it had reduced the interest rate on bonds to 10 *per cent per annum* with effect from 14 August 2003,

citing continuous downward trend of interest. PIICUP had paid interest amounting to ₹1.71 crore to the STCs for the period up to November 2003 and stopped payment of interest thereafter. PIICUP expressed (August 2004) to the STCs its inability to service their debts and its willingness to repay the principal amount as a final settlement. The STCs considered various options like filing Writ Petition against PIICUP and invoking the guarantee. In the meanwhile, PIICUP informed (January 2009) the STCs to give concurrence to accept the principal amount only without interest before 31 March 2009 and if they fail to do so, PIICUP would consider offering only 75 *per cent* of the principal amount due to its continuing adverse financial health and severe liquidity crunch. The STCs received back the principal amount from PIICUP between March 2009 and February 2010. No interest was paid on this amount.

We observed that:

- The decision to invest PF funds in the bonds of a loss making Company was *ab initio*, injudicious as PIICUP was incurring losses continuously from 1996-97 and its paid-up capital of ₹110.58 crore was eroded by March 1999 itself.
- Even after knowing the financial sickness of PIICUP from its own letter (August 2004), the STCs never attempted to withdraw their investment till February 2009, despite PIICUP's readiness to liquidate the principal amount.
- Though the repayment of these investments along with interest was guaranteed by the Government of Uttar Pradesh, the STCs did not exercise the option to invoke the same and get back the principal with interest, the reasons for which were not on record.
- As the STCs were responsible for reimbursing the shortfall in the PF trust, the loss of interest suffered by the PF trust would be to the account of STCs.

Thus, injudicious decision to invest the PF trust accumulation in a company known to be making loss with subsequent delays in withdrawing the amount led to avoidable loss of ₹2.53 crore.

The Government while accepting the loss of interest stated (November 2012) that the STCs had taken all efforts to recover the dues of both principal and interest from PIICUP. But due to reasons beyond their control, there was no alternative except to accept the principal only.

The reply is not tenable as the STCs failed to take note of the fact that the financial position of PIICUP was dismal at the time of investment. Even after knowing the financial sickness of PIICUP (August 2004), the STCs inordinately delayed in taking back the principal amount till February 2009. Responsibility needs to be fixed on the officers/trustees who authorised such investment which led to the loss. This case also reflects on the lack of internal controls and vigilance mechanism to check such misdemeanor.

Tamil Nadu State Transport Corporation (Villupuram) Limited

3.3 Loss due to injudicious financial projection

The Company's acceptance to operate Hop-on Hop-off sightseeing services in Chennai city based on injudicious financial projection resulted in a loss of ₹71.17 lakh.

Based on the suggestion (November 2006) of the Commissioner of Tourism, Government of Tamil Nadu to consider introduction of Hop-on Hop-off[43] sightseeing tours in Chennai for the benefit of tourists, Government asked Tamil Nadu State Transport Corporation (Villupuram) Limited (Company) to prepare a project proposal for the same. The Company sent a proposal (December 2006) to the Government, which *inter alia*, envisaged that with a 20 seat capacity coach with an occupancy of 60, 80 and 100 *per cent* in the first three years, the project would earn a profit of ₹20 lakh per coach in the fifth year assuming exemption from the payment of road tax. The fare assumed was ₹250 per head.

The Board of Directors of the Company accorded approval (June 2007) for introduction of these services and for the purchase of four 18 seat luxury coaches for this purpose. The Government issued (October 2007) orders for the operation of the above scheme and also exempted the coaches from the payment of road tax for five years from the date of introduction. The Company purchased (January 2009) four 18 seat luxury coaches at a total cost of ₹68.42 lakh and introduced the services from February 2009.

As the Company incurred cash losses (₹22.17 lakh till September 2011) in the operation of the above services mainly due to abnormally low occupancy (24 and 21 *per cent* in the first two years), it discontinued (September 2011) these services with the approval of its Board and transferred (September 2011) the four coaches to Metropolitan Transport Corporation Limited, Chennai (MTC) at their book value. During the operation of these services (February 2009 to September 2011), the Company suffered a total loss of ₹71.17 lakh (cash losses: ₹22.17 lakh and depreciation: ₹49 lakh).

In this connection, we observed as follows:

(i) The Company's core business was to link the various towns/villages in the district of its operation and it did not have any experience in the operation of such services. Hence, *ab initio,* the Company should not have taken up these operations.

(ii) While sending the proposal to Government in December 2006, the Company assumed an occupancy ratio of 100 *per cent* from third year onwards despite the fact that the Company was aware that occupancy ratio of such projects in other cities such as Bangalore was not encouraging.

[43] In the Hop-on Hop-off tour, coaches go on round trips through a fixed route at a regular frequency to enable tourists to get in and get down at any place of tourists interest covered by the service.

(iii) The Company informed (March 2011) the Board that the routes covered by Hop-on Hop-off sightseeing coaches were in the operational jurisdiction of MTC and that a large number of MTC buses were touching the tourist places at frequent intervals with cheaper fares and the tourists preferred to avail of these services. This fact was known to the Company even at the time of sending the proposal to the Government in December 2006. The Company, however, ignored this fact and assumed 100 *per cent* occupancy from third year onwards and concluded that the project would earn a profit of ₹20 lakh per coach in the first five years.

Thus, the Company's injudicious projection of viability of the Hop-on Hop-off sightseeing tours and its acceptance to operate the same though it was not in the geographical scope of its activities resulted in avoidable loss of ₹71.17 lakh.

The Government replied (November 2012) that based on the projection made, the sightseeing tour services were operated and after analysis of outcome and cost benefit analysis and other factors, the Company discontinued the operation as it was not found to be profitable. The reply is not tenable as the project was entrusted to the Company based on its projection in December 2006. This was *ab initio,* a flawed projection.

Tamil Nadu Minerals Limited

3.4 Revenue loss

Company suffered a revenue loss of ₹1.12 crore in the supply of color granite cut slabs to a private construction firm.

Tamil Nadu Minerals Limited (Company) is engaged in the commercial exploitation and export of granite and production and sale of other minerals. Based on the offers received against the global tenders, the selling price of raw granite blocks are fixed by a Committee constituted by the Board.

M/s East Coast Constructions & Industries Limited (ECCI), who were the contractors for the construction of new Tamil Nadu Legislative Assembly building in Chennai requested (September 2009) the Company to offer the Company's rates for the supply and laying of approximately 30,000 M^2 Kashmir white/pink granite cut slabs in that building. The Company expressed its inability to undertake laying work and offered (September 2009) to supply the cut color granite slabs @ ₹181/₹182 per square feet (sq.ft.) for Kashmir white/pink slabs. After negotiations, the Company reduced its rates to ₹177/₹178 per sq.ft, which included cost of raw granite blocks, cost of processing them into cut slabs, transportation, loading/unloading and taxes. Accordingly, ECCI placed (September 2009) orders on the Company for supply of 33,700 M^2 of Kashmir pink and 7,300 M^2 of Kashmir white granite slabs of the size 4' X 2' X 25 mm for a value of ₹7.86 crore.

While quoting for the above supply of color granite cut slabs, the Company adopted the cost of raw granite slabs as ₹8,000 per M^3 being the amount payable to the raising agents for production of raw blocks and did not include the cost of raw blocks. Based on the recovery rate adopted by the Company

viz., 1 M^3 = 172 sq.ft., the raw material cost included in the end price of ₹177/178 per Sq. ft. worked out to ₹46.50 per Sq.ft.

The Company produced the raw granite blocks through raising agents and outsourced the work of processing the same into cut slabs and supplied 3, 66,528 sq.ft. (34,051.29 M^2) of Kashmir pink granite cut slabs and 1,13,752 sq.ft .of Kashmir white granite cut slabs (10,567.82 M^2) to ECCI during the period November 2009 to September 2010.

In this connection, we observed as follows:

As the Company's selling prices for various sizes and types of raw granite slabs are fixed by its Board, it should have taken the price fixed by the Board as material cost while quoting for the above supply. In September 2009, the minimum selling price for raw white and pink granite blocks as approved by the Board for the size required by ECCI was ₹12,000 per M^3, which worked out to ₹69.75 per sq.ft.. As against this, the Company reckoned the cost of raw granite blocks as ₹46.50 per sq.ft. for both Kashmir pink and Kashmir white raw blocks. This incorrect adoption of material cost while quoting for the supply of granite cut colour slabs had resulted in a minimum revenue loss of ₹1.12 crore to the Company in the supply of Kashmir pink and white cut slabs {3,66,528 + 1,13,752 X (₹69.75 – ₹46.50)}.

The matter was reported to the Company/Government in August 2012; their reply was awaited (December 2012).

TIDEL Park Coimbatore Limited

3.5 Avoidable extra expenditure

Company's failure to obtain competitive rates for its term loan requirement resulted in an avoidable extra expenditure of ₹1.05 crore.

The Board of Directors of TIDEL Park Coimbatore Limited (Company) approved (October 2007) the construction of Information Technology (IT) Park at Coimbatore (project) at an estimated cost of ₹300 crore and authorised the Company to approach State Bank of India (SBI) and Indian Bank for term loans. The Company informed (October 2007) the Board that in response to the sealed quotation procedure seeking term loan of ₹135 crore for the project, two offers were received *viz.*, SBI and Indian Bank @ 10.4 *per cent* and @ 10.5 *per cent* interest rate respectively. After detailed discussion, the Board authorised the Chairman of the Company to approach SBI, Coimbatore and Indian Bank, Chennai for a term loan of ₹100 crore each as they were the shareholders and lenders of TIDEL Park Limited, Chennai.

Based on the request of the Company in March 2008, Indian Bank (June 2008) and SBI (July 2008) sanctioned a term loan of ₹100 crore each at 11 *per cent per annum* and 11.25 *per cent per annum* respectively. They charged one *per cent* and 0.50 *per cent* of the loan amount as processing fee. The Board authorised (August 2008) the Chairman and Managing Director of the Company to negotiate with these banks for adopting a uniform interest rate of 11 *per cent* and processing fee of 0.5 *per cent* as processing fee. The Company signed all the documents and accepted the terms and conditions of lending banks in toto and while sending the acceptance letter, the Company

requested (September 2008) Indian Bank to take up with the authorities concerned for charging processing fee at 0.50 *per cent* of the loan amount. SBI and Indian Bank released the first instalment of term loan after deducting the processing fee of ₹50 lakh and ₹ one crore respectively.

Due to an unforeseen delay in the implementation of the project, the Company requested both SBI and Indian Bank for rephasement of the loan by postponing the commencement of repayment by one year and this was agreed to by them. Indian Bank charged ₹55.15 lakh as processing fee for the rephasement of the loan (at 50 *per cent* of the original processing fee plus service tax of ₹5.15 lakh) as against ₹40,000 charged by SBI for the same purpose. Thus, the Company totally paid ₹1.55 crore to Indian Bank towards processing fee and rephasement charges, while it paid only ₹50.40 lakh to SBI for the same purpose.

In this connection, we observed as follows:

(i) Considering the huge quantum of loan involved, the Company should have obtained offers from various banks to get the most competitive rates and other terms and conditions. It is pertinent to mention that in TIDEL Park, Chennai, besides SBI and Indian Bank, three more banks, *viz*., Central Bank of India, Canara Bank and Indian Overseas Bank were also share holders.

(ii) While putting up the subject to the Board, the third offer received (July 2007) from Central Bank of India to lend at 10.5 *per cent* was not informed to the Board.

Thus, failure of the Company to get offers for the term loan from more banks and its failure to take up the issue of higher processing fee effectively with Indian Bank before signing the loan documents resulted in an avoidable extra expenditure of ₹1.05crore (₹1.55 crore – ₹50.40 lakh).

The Company replied (March 2012) that the proposal for reduction of processing fee on par with SBI was under the consideration of Indian Bank. The reply is not tenable in view of the fact that Indian Bank had not even replied to the Company's request till date (September 2012).

The matter was reported to the Government in September 2012; their reply was awaited (December 2012).

Tamil Nadu Police Housing Corporation Limited

3.6 Construction of houses without administrative approval

Construction of flats under 'own your house' scheme for police personnel without the administrative approval of the State Government led to blocking up of ₹90.25 lakh and consequential interest loss of ₹20.45 lakh.

Tamil Nadu Police Housing Corporation Limited (Company) is engaged in construction of houses/flats for allotment to police personnel (a) as quarters and (b) under 'Own Your House Scheme'. Under (b), the Company constructs houses/flats on land provided to it by the State Government and the required funds for construction are also provided by the Government in the form of house building advance of the allottees. The difference between the total cost and the eligible House Building Advance (HBA) is collected as deposit from

the allottees.

Based on the Company's request, the State Government permitted (August 2000) the Company to receive land measuring one acre and 17 cents in Tirumullaivoil, a suburb of Chennai, as a gift from a philanthropist for construction of quarters for police personnel. The Board of Directors of the Company accorded (September 2006) financial sanction for ₹102.50 lakh for construction of four high income group and 10 middle income group flats under 'own your house scheme' and for executing the works after getting administrative approval from the State Government.

Accordingly, the Company requested (November 2006) the State Government to accord administrative approval for the above scheme to be implemented by utilising the funds released by the State Government every year under HBA allocation to the police department.

Without following the normal procedure for the construction of houses under 'own your house' scheme like getting the administrative approval from the State Government, selecting the beneficiaries and collecting the deposit, the Company started implementing the above scheme in January 2007 and completed the same in September 2009 at a total cost of ₹90.25 lakh. The flats have not been allotted till date (September 2012) for want of administrative approval from the State Government. The Government directed (June 2011) the Company to fix responsibility for the lapse and to initiate disciplinary proceedings against the officials involved.

In this connection, we observed as follows:

(i) In contravention of the State Government directive to use the gifted land for construction of quarters for police personnel, the Company put up proposal to the Board for construction of flats under 'own your house' scheme.

(ii) Without waiting for the State Government's administrative approval, the Company completed the construction in all respects by September 2009.

Thus, construction of flats under 'own your house' scheme for police personnel in contravention of the State Government directive had resulted in blocking up of ₹90.25 lakh for more than three years and consequential interest loss of ₹20.45 lakh[44], defeating the very purpose for which the land was gifted to the Company *i.e.*, construction of quarters for police personnel.

The Company replied (March 2012) that the construction activities were initiated as a welfare measure with the hope of getting the State Government's approval.

The reply is not tenable as the construction has *ab initio* been undertaken without proper approval and the flats constructed are remaining unallocated leading to blockade of funds to the tune of ₹90.25 lakh.

The matter was reported to the Government in August 2012; their reply was awaited (December 2012).

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[44] Calculated at 8 *per cent* on ₹90.25 lakh for 34 months.

3.7 Avoidable payment/liability of interest on Income Tax

Claim of ineligible deduction on profits earned led to short payment of Income tax and resulted in an avoidable payment/liability of interest - ₹66.21 lakh

Tamil Nadu Police Housing Corporation Limited (Company) is engaged in construction of houses/flats for allotment to Police personnel (a) as quarters and (b) under Own Your House Scheme. The Company receives supervision charges for all the above works. In other words, the Company is executing these construction works on behalf of the State Government.

During the three financial years 2007-08 to 2009-10, the Company earned profits and therefore became liable to pay Income Tax under the provisions of Income Tax Act, 1961 (Act).

Section 80 IB (10) of the Act dealing with deductions in respect of profits and gains of the companies engaged in developing and building housing projects stipulates that the amount of deduction in case of such undertakings would be 100 *per cent*. However, under explanation to the above Section it is clearly stated that such deduction shall not be admissible to any undertaking which executes the housing projects as a works contract awarded by any person including State or Central Government.

As per the provisions of Sections 208 and 209 of the Act, failure to pay quarterly advance tax and 90 *per cent* of the assessed tax before the end of the financial year would attract interest payment under Section 234 C and 234 B of the Act, respectively.

While paying the advance tax and the Income Tax for the three financial years from 2007-08 to 2009-10, the Company presumed that it would be eligible for 100 *per cent* deduction of its profits under Section 80 IB (10) of the Act and declared 'Nil' income. Accordingly, the Company paid Minimum Alternate Tax as per the provisions of Section 115 JB of the Act at 15 *per cent* of the book profits, while the normal rate of Income Tax is 30 *per cent* of the taxable income. While filing the Income Tax Returns for these three years, the Company claimed similar deductions.

Income Tax Department (Department), while assessing the returns filed by the Company for the years 2007-08 (December 2010) and 2008-09 (December 2011) disallowed the deductions claimed by the Company under Section 80 IB (10) for these two years on the ground that it was executing the construction projects as works contract for the State Government and was not eligible for the deductions in view of the explanation given under that Section. Accordingly, the Department demanded additional tax of ₹58.42 lakh and ₹ Nil and interest of ₹20.77 lakh and ₹4.43 lakh respectively for these two years.

The Company did not contest this disallowance and paid the tax (₹58.42 lakh) and interest (₹20.77 lakh) in March 2011 and the interest of ₹4.43 lakh was adjusted (December 2011) by the Department against the refund due.

For the financial year 2009-10, the Company is liable to pay ₹2.44 crore as income tax and interest of ₹41.01 lakh (up to June 2012) under Section 234 B

and 234 C.

In this connection, we observed that despite the clear cut provision in the Act that the deduction under Section 80 IB (10) is not available to an undertaking which executes housing projects on behalf of Central or State Governments, the Company failed to comply with the provisions of the Act resulting in an avoidable expenditure on interest of ₹66.21 lakh (₹25.20 lakh paid and liability ₹41.01 lakh).

The Company replied (February 2012) that the process of getting expert's opinion regarding the applicability of Section 80 IB is under process. The reply is not acceptable as the Company had neither contested the disallowance under Section 80 IB nor has the tax been paid under protest.

The matter was reported to the Government in June 2012; their reply was awaited (December 2012).

Tamil Nadu Generation and Distribution Corporation Limited

3.8 Undue benefit to a private power producer

Payment of cost of naptha used as a fuel in power generation on derived basis instead of restricting the same to actual consumption as per the Power Purchase Agreement led to an undue benefit of ₹331.54 crore to a private power producer.

Tamil Nadu Generation and Distribution Corporation Limited (Company), formerly known as Tamil Nadu Electricity Board entered (January 1997) into a Power Purchase Agreement (PPA) with PPN Power Generating Company Limited (PPN) to purchase power generated in its power plant to be set up near Nagapattinam. The term of the PPA was 30 years from April 2001. PPN was to use natural gas as fuel and naptha as alternate fuel.

The two part tariff for purchase of electricity from PPN comprised recovery of annual fixed charges (interest, depreciation, taxes, *etc*..) and variable charges (energy charges covering mainly the fuel cost). The PPA *inter alia*, provided that PPN shall submit monthly invoices for all amounts accrued in the preceding months for the estimated fixed and variable cost and the Company has to settle the same within 30 days. The PPA also provided that after the end of each financial year, PPN shall submit to the Company an annual invoice setting forth all amounts due under the tariff and a reconciliation of the actual amounts receivable from the Company for the previous financial year against the sum of monthly estimated payments made by the Company. If such invoice shows net payment due to PPN by the Company or net payment due to the Company by PPN, such amount shall be paid within 30 days after the invoice is rendered. The time limit for raising disputes over annual invoices shall be one year from the due date for payment of such invoice.

PPN started commercial operation in April 2001. It rendered monthly invoices to the Company, containing charges for fuel consumption based on

the actual consumption of natural gas and derived[45] consumption of naptha and the Company paid these amounts as claimed by PPN.

PPN rendered annual invoices for the years 2001-02 to 2009-10 in July 2011 and for 2010-11 in September 2011. No reconciliation of derived quantity of naptha against the actual quantity was carried out and the earlier claim revised.

In this connection, we observed as follows:

(i) The very objective of rendering annual invoice at the end of each year and reconciliation of actual amounts receivable for the power exported is to make necessary adjustments for the amounts claimed on estimated basis against the amounts payable on the basis of actual quantities. The Company did not raise the issue of non-reconciliation of derived naptha consumption against actual consumption in the annual invoices with PPN within one year as prescribed in the PPA for raising disputes.

(ii) The actual consumption of naptha for power generation during the five years from 2006-07 to 2010-11 was 11,20,634 MTs. Against this, the Company had paid for 12,01,569 MTs being the derived consumption of naptha during the same period resulting in excess payment for 80,935 MTs of naptha valued at ₹331.54 crore to PPN.

Thus, the payment for Variable Fuel Cost based on derived consumption of naptha instead of restricting it to actual consumption had resulted in an undue benefit of ₹331.54 crore to PPN.

The Company replied (March 2012) that the prevailing practice in the power sector is that Station Heat Rate is fixed on a normative basis unless agreed to otherwise and the savings between normative and actual are not passed on to the buyer by the generating company.

The reply is not acceptable in view of the fact that in the instant PPA, the very inclusion of clause relating to annual invoices requiring reconciliation of all the payments that were made on estimated basis with the actuals was to adjust the excess/short payments.

The matter was reported to the Government in August 2012; their reply was awaited (December 2012).

3.9 Short realisation of revenue

Assessment of Defence production units under HT Tariff-II A instead of HT Tariff-I A resulted in short realisation of revenue to the extent of ₹21.26 crore.

The four Defence Production Units (Units) in Tamil Nadu, *viz*., Heavy Vehicles Factory (HVF), Ordnance Factory (OF), Heavy Alloy Penetrator Project (HAPP) and Cordite Factory (CF) avail of High Tension (HT) service connections from Tamil Nadu Generation and Distribution Corporation Limited (Company), formerly Tamil Nadu Electricity Board. These units

[45] Naptha consumption was derived by deducting the heat generated by natural gas (quantity of natural gas consumed multiplied by its calorific value) from the total heat generated (Station Heat Rate multiplied by total power delivered to the Company) and dividing the resultant figure by calorific value of naptha.

avail bulk HT supply at single point and use the same predominantly for industrial purposes and partly for distribution to their residential colonies. Till 16 March 2003, the entire HT consumption (including the residential consumption) was billed under HT Tariff-I A applicable to industrial establishments. These units have separate energy meters for recording the consumption of power by the residential colonies.

Para 7.11 of the Tariff Order issued by Tamil Nadu Electricity Regulatory Commission (TNERC) effective from 16 March 2003, dealt with the problem faced by consumers taking HT bulk supply at single point *viz*., their residential consumers were paying at HT tariff which was much higher than the domestic tariff. Taking this into consideration, TNERC ordered as follows:

(a) Those consumers who avail HT supply for predominantly domestic loads and supply within their area shall be billed under the existing HT Tariff-II A instead of HT Tariff-III.

(b) In respect of consumers who avail HT supply for industrial purpose and also extend LT supply to their residential areas, the HT supply comes under Tariff-I A. The domestic bulk consumption under such HT categories shall henceforth be charged under the newly introduced LT Tariff-I C.

In view of this provision, the four Defence Production Units in the State, which come under category (b) above, should have been billed under HT Tariff-I A for their industrial power consumption and under LT Tariff-I C for their residential power consumption from 16 March 2003. Instead, the Company billed these units under HT Tariff-II A, applicable to those establishments, which avail HT supply predominantly for domestic load (category (a) above). This has resulted in short realisation of revenue to the extent of ₹21.26 crore for the period 16 March 2003 to April 2012. The short realisation is still continuing (September 2012).

The Government replied (August 2012) that TNERC had classified the Ministry of Defence establishments under HT Tariff-II A in its tariff order of March 2003.

The reply is not acceptable as HT Tariff-II A is meant for those consumers who avail HT supply for predominantly domestic loads. As Defence Production Units draw power mainly for industrial purpose and distribute a part of the same to their residential colonies, their industrial consumption should have been billed under HT Tariff-IA and the residential consumption under LT Tariff-IC.

3.10 Undue benefit to a power trader

Injudicious deletion of compensation clause for failure to supply the contracted quantum of power resulted in extension of undue benefit to the tune of ₹14.86 crore to a power trader.

Tamil Nadu Generation and Distribution Corporation Limited (Company), formerly Tamil Nadu Electricity Board floated (May 2009) a tender to purchase power from approved traders to meet the deficit. Clause-11 of the Annexure to the tender provided for payment of compensation charges for failure to supply 80 *per cent* of the contracted quantum of power in a month.

While responding to the tender, PTC India Limited (PTC) had stated that the compensation clause shall be applicable on 'individual plant basis'.

The Company issued (July 2009) a Letter of Acceptance (LOA) and also signed an agreement (October 2009) for purchase of power during the period July 2009 to May 2010. The compensation clause as furnished by PTC in its offer was enclosed to LOA along with other terms and conditions.

PTC started supplying power to the Company from July 2009. In all the months from July 2009 to February 2010, there was shortfall in power supply with reference to 'individual plant basis'. The total power supplied by PTC, however, was more than 80 *per cent* of the contracted quantum during July, August, October and November 2009 but less than 80 *per cent* in September 2009 and December 2009 to February 2010. PTC, therefore, became liable to pay compensation of ₹31.81 crore to the Company for the period July 2009 to February 2010 ('individual plant basis') and ₹14.86 crore for the months September 2009 and December 2009 to February 2010 (total contracted quantum basis).

In January 2010, PTC requested the Company to delete that portion of the compensation clause on 'individual plant basis' on the plea of operational/technical problems in some of the power plants. Subsequently, PTC changed its stance and requested (February 2010) the Company to amend Clause-11 relating to compensation with prospective effect as the agreement was non-performable. This, in effect, meant that PTC wanted deletion of the entire compensation clause retrospectively.

The Board of Directors of the Company discussed (March 2010) the request of PTC and approved the deletion of compensation clause of the agreement retrospectively, as it could not be implemented and decided to include the same clause with prospective effect from March 2010.

As the compensation clause for failure to supply 80 *per cent* of the total contracted quantum of power in a month was included in the tender itself, the Company's acceptance of PTC's request to delete this Clause retrospectively amounted to post tender modification of the agreement terms and resulted in undue benefit of ₹14.86 crore to PTC being the compensation payable by it to the Company for the months September 2009 and December 2009 to February 2010 (total contracted quantum basis).

The Company replied (April 2012) that any contract to do an act, which after the contract is made becomes impossible by reason of some event which the promisor could not prevent, becomes void and therefore it took the decision to consider the request of PTC to delete the compensation Clause with retrospective effect.

The reply is not tenable as the retrospective deletion amounted to post tender modification. Further, the very same clause with the provision relating to levy of compensation charges on total contracted quantum basis was made applicable for the remaining three months of the contract *viz.*, March to May 2010 and a sum of ₹5.16 crore was recovered (October 2010) from PTC as compensation charges for its failure to supply 80 *per cent* of the total contracted quantum during these months.

The matter was reported to the Government in June 2012; their reply was

awaited (December 2012).

3.11 Excess payment of performance incentive

Company's failure to restrict the performance incentive for supply of coal as per the Fuel Supply Agreement led to excess payment of ₹2.17 crore

Tamil Nadu Generation and Distribution Corporation Limited (Company) formerly Tamil Nadu Electricity Board entered (November 2008) into a Fuel Supply Agreement (FSA) with Mahanadi Coal Fields Limited (MCL) for the supply of 110.80 lakh MT of coal *per annum* to the four thermal power stations of the Company at Ennore, North Chennai, Mettur and Tuticorin. The FSA, *inter alia,* contained a clause (3.12.1) for payment of performance incentive (PI) by the buyer to the supplier for supply of coal in excess of 90 *per cent* of annual contracted quantity (ACQ).

The quantum of PI was to be computed by multiplying the quantity eligible for PI by a factor (0.15 for supply between 90 and 95 *per cent* of the contracted quantity and 0.30 for supply more than 95 *per cent* of the contracted quantity) and the simple average of the Base Prices of "E" and "F" Grades of coal. The above FSA was effective for five years from 1 December 2008.

During the period December 2008 to March 2009, MCL supplied 43.66 lakh MT of coal (42.22 lakh MT of 'F' grade coal and 1.44 lakh MT of 'D' grade coal) against the 90 *per cent* of *pro rata* ACQ of 36.23 lakh MT for this period and therefore became eligible for payment of PI as per FSA clause. Though 'D' grade coal was not mentioned in the FSA, TNEB accepted the supply of this costlier coal (₹840 per MT).

MCL raised (August and October 2009) a claim for ₹8.47 crore being the PI payable for 7.43 lakh MT (43.66 – 36.23) of coal supplied over and above 90 *per cent* of ACQ for the period December 2008 to March 2009 and the Company paid the amount in October 2009. In this claim, the simple average base price of 'F' grade coal was adopted (₹440 per MT).

Subsequently, MCL raised (April 2010) an additional claim for ₹3.96 crore stating that the simple average base prices of 'D' and 'F' grades of coal worked out to ₹640 per MT {(₹440 +₹840)/2} against ₹440 per MT adopted earlier.

On receipt of this additional claim, the Company should have pointed out to MCL that as per FSA clause for computing PI, simple average base price of 'E' and 'F' grades of coal only should be considered (₹440 per MT) and that the base price of grade 'D' (₹840 per MT) which was not mentioned in the FSA should not be considered. Instead, it paid (June 2010) the additional amount claimed by MCL under protest. It then requested (June 2010) MCL to consider calculation of PI based on weighted average prices of grades 'F' and 'D'. MCL turned down this request on the ground that the application of weighted average base price for calculation of PI was not envisaged in the instant FSA. The Company totally paid an amount of ₹12.58 crore as PI for the period December 2008 to March 2009. The Company failed to effectively take up with MCL that as the quantity of 'D' grade coal (not envisaged in FSA) supplied was just 3 *per cent* of the total supply, incentive for that quantity alone could be claimed at its base price of ₹840 per MT.

Thus, the Company's failure to restrict the PI for supply of coal as per FSA resulted in an excess payment of ₹2.17 crore to MCL being the difference between the PI paid (₹12.58 crore) and the PI payable as per FSA (₹10.41 crore).

The Company replied (July 2012) that if it had refused to receive 'D' grade coal, MCL might have restricted the supply of 'E'/'F' grade coal also.

The reply is not relevant as the audit observation was not on the acceptance of 'D' grade coal or payment of higher price for the same. The audit observation was that the computation of PI was not in accordance with the provisions of FSA and resulted in excess payment.

The matter was reported to the Government in June 2012; their reply was awaited (December 2012).

3.12 Revenue loss

Failure to collect demand/start up power charges as per the provisions of the Power Purchase Agreement with Bio-Mass based power generator resulted in a revenue loss of ₹1.17 crore.

Tamil Nadu Generation and Distribution Corporation Limited (Company) formerly Tamil Nadu Electricity Board entered (June 2002) into a Power Purchase Agreement (PPA) with Raghurama Renewable Energy Limited (RREL) for the purchase of entire surplus energy generated by them in the 18 MW Bio-Mass based power plant in Ramanathapuram District. Besides prescribing the rate at which the power exported to the Company would be paid, the PPA included clauses prescribing Tariff for power drawn by RREL from the Company's grid for start up operations.

Clause 10 (a) (i) of the PPA stipulated that start-up power drawn by RREL from the Company's grid shall be charged at Company's High Tension Tariff-I rate applicable for industrial consumers and that the maximum demand charges shall be charged based on sanctioned or recorded demand whichever was higher. Clause 13 of PPA provided that the Company shall have the right to vary the tariff and the terms and conditions from time to time.

Tamil Nadu Electricity Regulatory Commission (TNERC) in its Tariff Order effective from 16 March 2003 had fixed Tariff-I for industrial consumers at ₹3.50 per unit as energy charges and ₹300 per KVA as demand charges. RREL requested the Company (February and March 2004) to exempt renewable energy based Independent Power Producers (IPPs) like them from payment of demand charges on startup power as they would be using such power for a very limited duration only. The Company, in turn, requested (August 2004) TNERC to approve a flat rate of ₹4.47 per unit for startup power consumed by generators using Bio-Mass fuels. TNERC did not reply.

The Company extended a service connection to RREL (September 2004) with a contracted demand of 2,000 KVA for startup power in its power generation plant and the plant started generation from October 2004.

The Company decided (November 2004) to collect only energy charges for startup power drawn by RREL. It did not collect any demand charges from RREL for the startup power from November 2004 to April 2006.

TNERC in its subsequent Tariff Order issued in May 2006 stipulated that import power drawn for startup purpose shall be billed at the flat rate of ₹6.2181 per unit. The Company, however, continued to collect from RREL @ ₹3.50 per unit only till RREL relinquished its status as Bio-Mass plant and switched over to coal based generation in March 2009. The Board terminated (March 2009) the PPA entered into with RREL.

Thus, the failure of the Company to collect demand charges from RREL during the period from November 2004 to April 2006 and collection of ₹3.50 per unit as energy charges against the flat rate of ₹6.2181 per unit for start up power during the period from May 2006 to March 2009 has resulted in a revenue loss of ₹1.47 crore. Out of this, a sum of ₹30.14 lakh being the short collection of flat energy charges for the period from December 2007 to March 2009 was recovered from RREL based on an observation of the Internal Audit Wing of the Company. A sum of ₹1.17 crore still remains to be recovered from RREL.

The matter was reported to the Company/Government in August 2012; their reply was awaited (December 2012).

3.13 Excess payment of customs duty

Incorrect computation of assessable value for payment of Customs Duty on imported coal led to excess payment of Customs Duty to the tune of ₹0.84 crore.

The Company imports coal to meet the short fall in supply of indigenous coal through Minerals and Metals Trading Corporation (MMTC), Metal Scrap Trading Corporation (MSTC), Tamil Nadu Newsprint and Papers Limited (TNPL), *etc*., on High Sea Sales (HSS) basis. In addition to Cost, Insurance and Freight (CIF) price payable to the overseas supplier, HSS commission is payable to the agency through which such imports are channelised.

Till May 2004, the assessable value for Customs Duty for goods imported on HSS basis was computed by adding to the CIF price, HSS commission on notional basis @ two *per cent* of the CIF value or the actual HSS commission paid if more than two *per cent*.

Central Board of Excise and Customs (CBEC) after detailed examination of the issue of inclusion of HSS commission to assess the value for payment of Customs Duty, clarified (May 2004) that the actual HSS contract price paid by the buyer would constitute the transaction value and inclusion of HSS Commission on notional basis may not be appropriate. This meant that instead of adding two *percent* of CIF value as HSS commission to compute the assessable value, the actual HSS commission paid by the buyer was to be added to CIF value.

We observed that for the coal imported by the Company on HSS basis during the period February 2010 to August 2011, through the above agencies, the Company computed the assessable value by adding to the CIF value HSS commission at two *per cent* (about ₹120 per MT) though it paid only ₹33 per MT as HSS commission. This resulted in excess payment of customs duty to the tune of ₹2.68 crore during this period.

On being pointed out by Audit, the Company started (April 2012) paying Customs Duty based on actual HSS commission paid. The Company accepted (May 2012) the excess Customs Duty payment of ₹2.68 crore and stated that out of this, refunds from Customs authorities could not be obtained for ₹0.50 crore as the time limit of one year prescribed for refund claims had elapsed. The Company further stated that it had recovered this amount from the payments due to MMTC, the agency through which coal was imported. The Company further stated (July 2012) that it had preferred refund claims for an amount of ₹1.01 crore and that the refund application for the balance amount of ₹1.17 crore would be filed shortly.

We further observed that as per the purchase order terms, the payment of Customs Duty was the responsibility of the Company and hence the recovery of ₹0.50 crore from the payments due to MMTC was not in line with the purchase order terms. It is pertinent to mention that in another instance of such unilateral recovery made (January 2012) by the Company from the bills of MMTC, it had categorically rejected such unilateral deductions as they were not in line with the purchase order terms. Therefore, the Company is liable to refund this amount to MMTC. In respect of refund claims preferred by the Company for ₹1.01 crore, claims pertaining to ₹0.34 crore had since become time barred as more than one year had lapsed from the date of payment of customs duty.

Thus, the Company's incorrect computation of assessable value for payment of Customs Duty had resulted in excess payment of Customs Duty to the tune of ₹0.84 crore (₹0.50 crore + ₹0.34 crore).

The matter was reported to the Company/Government in September 2012; their reply was awaited (December 2012).

General

3.14 Follow-up action on Audit Reports

Explanatory notes outstanding

3.14.1 The Audit Reports of the CAG represent the culmination of the process of scrutiny starting with initial inspection of Accounts and records maintained in the various Government Companies and Statutory Corporations. It is, therefore, necessary that they elicit appropriate and timely response from the Executive. Finance Department, Government of Tamil Nadu had issued instructions (January 1991) to all Administrative Departments to submit explanatory notes indicating a corrective/remedial action taken or proposed to be taken on the Paragraphs and Performance Audit Reports included in the Audit Reports within two months of their presentation to the Legislature, without waiting for any notice or call from the Committee on Public Undertakings (COPU).

The Audit Reports for the years 2008-09 and 2009-10 were presented to the State Legislature in May 2010 and September 2011, respectively. Eleven out of 13 Departments, which were commented upon, had not submitted explanatory notes on 35 out of 43 Paragraphs/Performance Audit Reports, as of 31 October 2012, as indicated below:

Year of Audit Report (Commercial)	Total number of Paragraphs/Performance Audit Report in the Audit Report	Number of Paragraphs/Performance Audit Reports for which explanatory notes were not received[46]
2008-09	24	16
2009-10	19	19
TOTAL	**43**	**35**

Department-wise analysis is given in the **Annexure-15**. The Energy Department is responsible for non-submission of large number of explanatory notes.

Compliance with the Reports of Committee on Public Undertakings (COPU)

3.14.2 The Action Taken Notes (ATNs) to the paragraphs included in the Report of the COPU are to be furnished by the concerned Departments within six months from the date of presentation of these reports to the State Legislature. Replies to 129 paragraphs pertaining to 25 Reports of COPU presented to the State Legislature between January 2003 and April 2012 had not been received as of 31 October 2012 as indicated below:

Year of COPU Report	Total number of Reports involved	Number of paragraphs in respect of which replies were not received
2002-03	5	5
2003-04	3	5
2004-05	2	3
2006-07	2	5
2009-10	7	47
2010-11	3	40
2011-12	3	24
TOTAL	**25**	**129**

Response to Inspection Reports, Draft Paragraphs and Performance Audit reports

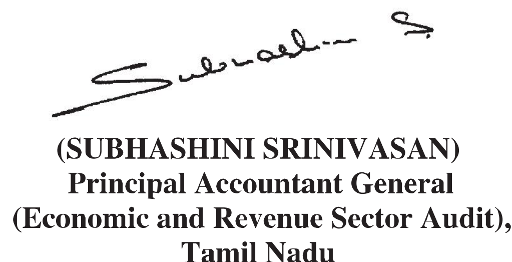
3.14.3 Audit observations noticed during audit and not settled on the spot are communicated to the heads of the Public Sector Undertakings (PSUs) and departments of the State Government through Inspection Reports. The heads of PSUs are required to furnish replies to the Inspection Reports through the respective heads of Departments within a period of six weeks. Inspection Reports issued up to March 2012 pertaining to 66 PSUs disclosed that 3,121 paragraphs relating to 750 Inspection Reports remained outstanding at the end of October 2012; of these, 174 Inspection Reports containing 605 paragraphs had not been replied to for more than two years. Department-wise break-up of

[46] Paragraphs/performance audit reports for which no explanatory notes were received but discussed by COPU are excluded.

Inspection Reports and audit observations outstanding as on 31 October 2012 are given in **Annexure-16.**

Similarly, Draft Paragraphs and Performance Audit Reports on the working of PSUs are forwarded to the Principal Secretary/Secretary of the Administrative Department concerned demi-officially seeking confirmation of facts and figures and their comments thereon within a period of six weeks. However, nine Draft Paragraphs and one Performance Audit Report forwarded to the various Departments during the period from June to October 2012, as detailed in **Annexure-17**, had not been replied so far (December 2012).

It is recommended that the Government should ensure that (a) procedure exists for action against the officials who fail to send replies to Inspection Reports/Draft Paragraphs/Performance Audit Reports/ATNs on the recommendations of COPU as per the prescribed time schedule, (b) action to recover loss/outstanding advances/overpayments is taken within prescribed time and (c) the system of responding to audit observations is revamped.



Chennai
The 25 Feb 2013

(SUBHASHINI SRINIVASAN)
Principal Accountant General
(Economic and Revenue Sector Audit),
Tamil Nadu

Countersigned

New Delhi
The 26 Feb 2013

(VINOD RAI)
Comptroller and Auditor General of India