CHAPTER XVII: MINISTRY OF STEEL

KIOCL Limited

17.1 Injudicious expenditure on Pig Casting Machine in Blast Furnace Unit

Kudremukh Iron and Steel Company Limited (KISCO), Bangalore, a joint venture company promoted by KIOCL Limited, MECON Limited and MSTC Limited, was established with the objective of producing low sulphur low phosphorous pig iron and to convert a part of it into ductile iron spun pipes (DISP).

KISCO was incurring continuous losses from the very first year of its operations (2001-02). It became (June 2006) wholly owned subsidiary of KIOCL and was finally merged with KIOCL w.e.f. 1 April 2007 becoming a unit of KIOCL, i.e., Blast Furnace Unit (BFU). Even after merger, BFU continued to incur losses and was shut down from 5 August 2009.

In the meanwhile, KIOCL decided (August 2008) to set up a third Pig Casting Machine (PCM) a downstream equipment for BFU. This was in addition to the existing two PCMs. The decision on the third PCM was on the advice of MECON Limited (October 2007) to attend to the breakdowns of existing machines without exposing workers to the hazards and also improve productivity by continuously running the BFU. KIOCL placed (September 2009) a work order for design, manufacture, supply, construction, erection, testing and commissioning and performance guarantee tests of PCM at a cost of ₹ 3.89 crore. KIOCL incurred ₹ 4.20 crore towards procurement and installation of PCM.

Examination in Audit revealed that:

(i) Though the Board decided (July 2009) to stop production at BFU from August 2009, KIOCL issued (September 2009) work order for third PCM which was not commissioned (March 2013).

(ii) The existing two PCMs were operating below 65 *per cent* of their capacity in 6 years and about 75 *per cent* in rest of the years.

(iii) The Board decided (March 2010) to keep the operations of BFU suspended till integration of both backward (Coke Oven Plant) and forward operations (DISP Plant). DISP Plant was to get its input from PCMs and was proposed (October 2011) to be set up in partnership through a Special Purpose Vehicle (SPV). The gestation period for setting up a DISP project was to be 24 months from the issue of Letter of Intent. As of March 2013, KIOCL was yet to identify the partner for implementation of DISP project. In this scenario, the third PCM which was already idle for 26 months from January 2011 would remain idle for a minimum period of another 24 months until the DISP project was completed.

The Company stated (July 2013) it had, at the time of taking decision to install a third PCM, examined all aspects viz. increase of productivity, safety of workforce, easy maintenance etc. However, due to recession in the market for pig iron, which was beyond its control, operations of BFU had to be suspended and it was making all efforts to restart the operations of BFU. With the operation of two PCMs, continuity in production at BFU was getting affected, besides leading to overlooking of safety aspects. Further, there were technological improvements in the design of third PCM and metal handling system. The new PCM had much improved technological aspects.

The reply is not acceptable in view of the following:

- The financial consultant, in his appraisal note on KISCO (June 2000), had opined that pig iron operation is not viable on a standalone basis. CMD of KIOCL also noted (August 2008) that there was no ready market for pig iron already manufactured and it was lying in stock. Disposal of stock was also cited as the reason for shutdown of BFU in the first instance. The closing stock of pig iron for the year 2006-07, 2007-08 and 2008-09 was 20348 MT, 5845 MT and 43462 MT respectively. In this scenario, with the stock lying unsold, procurement of additional machinery to increase productivity lacked justification. The Company could not succeed in setting up SPV for DISP making the utility of PCM doubtful.

- Continuity in BFU production was not a viable reason for installation of third PCM as it was noticed that BFU was also shut down during 2008-09 owing to clearance of pig iron stocks. Technological improvements needed to be viewed in the background of time elapsed between decision to install the third PCM in 2009 and the time that would be needed to actually put it to use.

Ministry in its reply (September 2013) reiterated the views of the Company and stated that BFU was still shutdown and the Company was pursuing the establishment of DISP Plant and Coke Oven Plant, which were yet to materialise.

Hence, despite knowing that BFU was not viable on standalone basis and having closed its operations, KIOCL ordered for setting up a third PCM which has been idle for the past 26 months and would remain idle for a minimum of another 24 months from the issue of letter of intent, which has also not been issued so far (September 2013). This has resulted in idling of funds and injudicious expenditure of ₹ 4.20 crore.

MSTC Limited

17.2 Loss due to non recovery of dues

Financing of import of scrap when market price was falling, coupled with unrealistic increase of exposure limit and imprudent action of return of documents resulted in loss of ₹ 60.56 crore

MSTC Limited (the Company) acted as a facilitator to its customer Sesa International Limited (Sesa) and financed its imports. As per the terms of the agreement (November 2006) the Company would endorse the purchase order as facilitator for imports as per the

indent of Sesa. The Company would also open Letter of Credit (L/C) with the bank. The materials so imported were to be pledged with the Company and to be lifted by Sesa on 'cash and carry' basis.

In March 2008, Sesa approached the Company to facilitate import of 5000 MT shredded scrap of UK origin valuing ₹ 10.25 crore. The proposal was accepted and L/C was opened by the Company in March 2008 through Indian Overseas Bank (IOB). The original shipment date of April 2008 was subsequently extended to September 2008 by Sesa. Out of the total consignment of 4718 MT, Sesa accepted (September 2008) only the first two consignments of 2632 MT and refused to accept the remaining 2086 MT (October 2008) of scrap on the plea of non-compliance of the related documents with the revised terms of L/C.

Thereafter, Sesa again approached (August 2008) the Company to finance import of 22000 MT steel scrap valuing ₹ 56.45 crore against eight contracts. Though scrap from previous proposal remained unlifted and price of ferrous shredded scrap started falling in the international market since August 2008, the Company enhanced (August 2008) the existing exposure limit of ₹ 60 crore to ₹ 100 crore for accommodating the current proposal. However, between October 2008 and December 2008, Sesa again refused to accept 16398 MT of scrap on similar grounds of non-compliance of the related documents with Ls/C.

Examination in audit revealed that even while the Company discussed the minor nature of the discrepancy, it acceded to the request of Sesa and returned the documents to IOB with whom Ls/C were opened. Ultimately, IOB had to pay (April 2009) ₹ 52.71 crore to two suppliers as per order of the High Court in London through their negotiating banks[1] and recovered (between April 2009 and February 2010) the same (₹52.71 crore) from the Company alongwith interest and legal charges of ₹ 0.61 crore and ₹ 8.57 crore respectively. The Company, in turn, preferred a claim (March 2010) on Sesa for ₹ 57.08 crore excluding interest @ 12.5 *per cent* on the said amount from March 2010. Sesa, however, refused to entertain such claim stating that they had returned the documents to the Company for necessary action and did not receive the materials.

Kolkata Port Trust auctioned the steel scrap not accepted by Sesa that lay at Haldia Dock Complex and sent (September 2010) an amount of ₹ 2.23 crore to the Company. Further, sale proceeds for balance material amounting to ₹1.02 crore was kept with the receiver as fixed deposit as per Court order. Due to the unrealistic increase of exposure limit as well as the imprudent action of return of documents based on admittedly minor discrepancy, the Company had to suffer a loss of ₹ 60.56[2] crore (December 2013) due to non-recovery of dues.

The Company stated (December 2012) that exposure limits of Sesa were increased based on long business relationship. It was also stated that the Ls/C were opened when the price of scrap was increasing in the international market. The reply admits that exposure limit was enhanced not on the basis of commercial justification. Further, the exposure limit was enhanced in August 2008 (from ₹ 60 crore to ₹ 100 crore) though, the prices of scrap

[1] ***Standard Chartered Bank of Dubai and Fortis Bank of London***

[2] ***₹62.79 crore - ₹2.23 crore***

had started falling in international market. The Company further contended that discrepancies in documents pointed out by Sesa should have been pointed out by the banker at the time of rejection of such documents. The Company has, however, failed to protect its financial interests while dealing with discrepancies in documents presented with the terms and conditions of L/C.

The matter was reported to the Ministry in September 2013; their reply was awaited (March 2014).

17.3 Loss due to failure to safeguard financial interests

The Company suffered a loss of ₹ 55.48 crore due to failure in safeguarding its financial interests while financing the procurements on behalf of Tirupati Fuels Private Limited

MSTC Limited (the Company) acts as a facilitator to its customers for import/procurement of materials. The Company financed procurement of coking coal by Tirupati Fuels Private Limited (TFPL) since 2007-08 without entering into any formal agreement or fixing any exposure limit. Further, the Company did not assess the performance of TFPL nor did it obtain any credit rating of TFPL from the external agencies. During the period, 2007-08 to 2008-09, the Company financed procurement of 91116.28 MT of coal but TFPL lifted only 43634.78 MT. The Company further approved (February 2010) additional financing of ₹ 33.61 crore to TFPL for procurement of coal though coal valuing ₹ 136.56 crore procured earlier was lying unlifted which increased the total financing to ₹ 170.17 crore. TFPL lifted only 49 *per cent* of materials procured till 2009-10 leaving unlifted stock valuing ₹ 91.26 crore. The Company, however, fixed (10 June 2010) an exposure limit of ₹ 200 crore for TFPL for 2010-11. The Company entered (18 June 2010) into a formal agreement with TFPL on import/procurement of LAM Coke and Coking Coal from indigenous and international sources. The agreement was valid for a year. The exposure limit for 2011-12 was fixed on 13 May 2011 at ₹ 175 crore.

The Company continued to finance TFPL for procurement of coking coal on various occasions (till November 2011) though materials remained unlifted. TFPL registered itself with the BIFR[♠] in November 2012 for determination of its sickness where it did not acknowledge dues to the Company. BIFR, however, dismissed the reference of TFPL in December 2013. The Company also tried to e-auctiojn unlifted materials on two occasions (March 2013) but failed to attract any participant in such sale. In the meanwhile, the Company received (March 2013) an order from the High Court of Calcutta stating that no coercive action should be taken by the Company against TFPL without the consent of BIFR. As on February 2014, ₹ 65.64 crore remained unrecovered from TFPL against which security deposit of only ₹ 10.16 crore was available.

The Company stated (December 2012 and February 2014) that efforts were being made to realize the dues and further acknowledged (February 2014) that it filed an application before the High Court for recalling of the latter's order and approached BIFR for sale of

[♠] ***Board for Industrial and Financial Reconstruction***

materials. The Company was, however, unable to sell unlifted ageing stock of TFPL and recover its outstanding dues, realization of which amounting to ₹ 55.48 crore[1], appears remote. Thus, the Company failed to safeguard its financial interests and thereby suffered loss of ₹ 55.48 crore due to additional financing to TFPL without evaluating its performance.

The matter was reported to the Ministry in September 2013; their reply was awaited (March 2014).

17.4 Non-recovery due to unrealistic financing of imports

Financing imports for a customer with unsatisfactory financial performance leading to non-recovery of ₹ 28.73 crore.

MSTC Limited (the Company) acts as a facilitator to its customers for importing materials. On being approached (June 2008) by MeherKiran Enterprises Limited (MKEL) the Company, despite being aware of the fact that MKEL had liabilities of ₹ 28.62 crore as against own fund of ₹ 11.72 crore as on 31 March 2008, decided (August 2008) to finance procurement of imported coal valuing ₹ 55 crore without signing any agreement which was in violation of the provisions of its Marketing Manual. The Company financed (August 2008) ₹ 60 crore being the value of coal (27500 MT) imported by MKEL which, however, lifted only 1825 MT of coal valuing ₹ 4.15 crore and did not lift the balance quantity on the plea of drastic fall in the market price of coal.

The Company subsequently entered (July 2009) into a Memorandum of Agreement (MoA) with MKEL for further financing of import of coal as well as to regularize financing of coal imported earlier (August 2008). The basic objective of the MoA was to reduce the average price of the high value imported coal procured in August 2008 and conversion of such coal into coke at an agreed conversion charges of ₹ 2000 per MT payable by the Company to MKEL. The entire sale proceeds of such converted coke were to be received by the Company in order to liquidate the outstanding dues.

The Company financed procurement of 50448 MT coal valuing ₹ 57.22 crore between November 2009 and November 2010. Though the entire quantity of coal procured in August 2008 and 47052.26 MT[2] procured subsequently was lifted and converted into coke, the sale proceeds of the same were not adequate to realize the entire dues from MKEL. Further, the Company had paid ₹ 4.54 crore towards payment of conversion charges to MKEL (September 2012).

The Company further financed procurement of 23666 MT of coal valuing ₹ 26.18 crore by MKEL during the period, August 2012 to February 2013, out of which 15842 MT was lying unlifted as on January 2014. Total outstanding dues of MKEL stood at ₹ 56.59 crore (January 2014). The Company had pledged coal[3] of ₹ 13.91 crore in addition to security deposit of ₹ 11.95 crore furnished by MKEL and mortgage of land valuing ₹ 2 crore (approximately) as collateral security. Thus, the Company stares at a

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[1] ***₹ 65.64 crore - ₹ 10.16 crore***
[2] ***50448MT - 3395.74 MT lying unlifted***
[3] ***₹ 12.91 crore for coal and ₹ 1 crore for coke***

financial loss of ₹ 28.73[1] crore (January 2014) as prospect of realisation of dues from MKEL are remote.

The contention of the Company (December 2012) that there was no financial loss as coal had remained pledged with the Company is not acceptable as the value of coal lying at the customer's premises was not sufficient to recover the total outstanding dues from MKEL. Thus, unrealistic financing of the imports of MKEL despite being aware of its unsatisfactory financial performance, has led to non-recovery of ₹ 28.73 crore.

The matter was reported to the Ministry in September 2013; their reply was awaited (March 2014).

Steel Authority of India Limited

17.5 Avoidable freight expenditure

Due to delay in completing the required documentation to avail concessional Class 180 rate for transportation of iron ore from captive mines to ISP Burnpur, the Company had to incur avoidable higher freight of ₹ 10.74 crore.

Railway Board notified the Rate Circular (RC) no. 36 of 2009 stipulating Class 180 rate for train load movement of iron ore meant for domestic consumption in the manufacture of Iron and Steel. It also stipulated that the distance based charge on the traffic would not be levied, if the following conditions were fulfilled:

(i) One time submission of documents[2]

(ii) Submission of certified copies of the relevant Monthly Excise Returns on a quarterly basis.

IISCO Steel Plant, Burnpur (ISP) of Steel Authority of India Limited (SAIL or the Company) uses the services of Indian Railways to transport iron ore from captive mines for consumption in steel plants. ISP should have fulfilled the above conditions to avail the benefits of Class 180 rate effective from 6 June 2009.

Examination in Audit revealed that ISP did not fulfill these conditions despite repeated reminders from Indian Railways in March 2011, June 2011 and July 2011. Indian Railways finally de-notified ISP from Class-180 from 18 September 2011 and charged higher freight rate applicable on exports resulting in ISP incurring avoidable expenditure

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[1] ***₹ 56.59 crore – (₹ 12.91 + ₹ 1.00 +₹ 11.95 + ₹ 2.00) crore***

[2] ***including Industrial Entrepreneur Memorandum (IEM) or certificate from Joint Plant Committee under Ministry of Steel indicating the licensed capacity of the plant or copy of MoU between the PSU and the associated Ministry; Consent for operation from Pollution Control Board for the current year; Factory license for the current financial year; Certificate of registration under Contract Labor Act; Central Excise Registration Certificate; Monthly Excise Return for the month prior to the current month; Affidavit on non-judicial stamp paper in prescribed format certifying that only iron ore for domestic consumption will be received in their siding; and a stamped indemnity note to indemnify the Railways against mis-declaration of export iron ore as domestic iron ore or any other misuse of rules prescribed by the Railways from time to time, etc.***

of ₹ 10.74 crore between from 18 September 2011 and 22 October 2011. Indian Railways allowed Class 180 rate to ISP vide message dated 21 October 2011 after ISP management completed formalities required under RC-36.

Management stated (December 2013) that it did not take action to submit the required documents during June 2009 to March 2011 as RC-36/2009 was a modified circular of RC-24/2008; documents/returns required to be submitted as per RC-36/2009 were the same as those required as per RC-24/2008; need for re-submission of the documents was not mentioned in the revised RC; appropriate action was taken on each correspondence received from Indian Railways during March-July 2011; and it had claimed for refund of the excess deduction made. Ministry reiterated (February 2014) the views of the Management.

It is evident from the reply that the ISP/Company did not take prompt action to comply with the conditions as stipulated in circular dated 1 June 2009. Belated action of ISP also was not complete. Affidavit and Indemnity Bond submitted to the Railways on 26 July 2011 were returned by the latter on 4 August 2011 as the documents were not in the prescribed form. Request of ISP for refund of the excess freight deducted had not yet been accepted by the Railways (December 2013).

Thus, due to delay in completing the required documentation to avail concessional Class 180 rate for transportation of iron ore from captive mines to ISP, Burnpur, the Company had to incur avoidable higher freight of ₹ 10.74 crore.

17.6 Delay in commissioning of Reheating Furnace at VISP/SAIL

Deficiencies in planning and technical due diligence in deciding the scope of work delayed commissioning of new RHF by over 58 months. Visualized savings of ₹ 28.36 crore from new RHF on account of lower scale loss and furnace oil consumption were not achieved even after incurring an expenditure of ₹ 9.85 crore.

Visvesvaraya Iron and Steel Plant (VISP), Bhadravati, Karnataka, of Steel Authority of India Limited (SAIL) has two re-heating furnaces (RHFs), each having a rated capacity of 15 tonne per hour (TPH) to cater to reheating and rolling requirements of primary mill. These RHFs installed in 1965-66 had outlived their life; had inherent design limitations leading to abnormal generation of scale (more than 2.5 *per cent*); and were consuming furnace oil of more than 75 litre/tonne of the output as compared to about 50 litre/tonne consumed by modern furnaces.

Centre for Engineering and Technology (CET), an in-house consultancy wing of SAIL prepared a feasibility report and recommended (January 2006) replacement of two RHFs with a new RHF of 30 TPH capacity which would be more energy efficient consuming 53 litre furnace oil per tonne besides increasing overall yield of primary mill by 1 *per cent* due to decrease in scale loss. CET estimated capital investment of ₹ 8.79 crore and total savings that would accrue to VISP from the project at ₹ 9 crore per year.

VISP placed an order (March 2008) on M/s. Wesman Engineering Co. Pvt. Ltd., Kolkata (the contractor) for design, supply, erection, testing and commissioning of the RHF at a

firm contract price of ₹ 10 crore (net of CENVAT). The contractor was to commission the facilities in twelve months i.e. by 28 February 2009. The new RHF, however, was not commissioned as of 31 January 2014, even after lapse of 58 months.

Examination in Audit revealed delay of 22 months in finalisation of drawings, 16 months in rectification of defects noted in the first hot trial, and 8 months to rectify defects noted in the second hot trial. Further scrutiny of the records revealed that CET feasibility report and provisions of the contract had provided four months for submission and approval of detailed design, engineering and drawings documents. VISP, however, took three and half months just to hold the kick-off meeting to finalise the protocol for submission of drawings and approval. As a result, VISP continued to incur higher scale losses and furnace oil consumption.

Management attributed (January 2014) delay in submission/approval of drawings and commissioning of the project to inefficient project management of the contractor and modification and changes in the design after preliminary acceptance and hot trial.

Reply does not deny the fact that there was inordinate delay in completing the project which deprived VISP of the benefit of energy efficient RHF. Faulty planning and lack of technical due diligence on part of CET in concluding the scope of work necessitated modification and changes in the design after preliminary acceptance.

Thus lack of proper planning, technical due diligence and coordination between contractor and VISP resulted in non-commissioning of RHF within the stipulated time. As a result, visualized saving of ₹ 28.36 crore from new RHF on account of lower scale loss and furnace oil consumption was not achieved despite incurring expenditure of ₹ 9.85 crore.

The matter was reported to the Ministry in February 2014; their reply was awaited (March 2014).