CHAPTER IX: MINISTRY OF SHIPPING

Cochin Shipyard Limited

9.1 Improper estimate in quoting prices for construction of double-ended Ro-Ro Ferry vessels

Cochin Shipyard Limited incurred a loss of ₹7.83 crore due to fixing of low contract price for the Ro-Ro Ferry vessels built for Kochi Municipal Corporation.

Kochi Municipal Corporation (KMC) invited (9 December 2014) a Detailed Project Report (DPR) from Cochin Shipyard Limited (CSL) for the construction of two Double Ended Ro-Ro[1] Ferry vessels required for operation between Fort Kochi and Vypeen Island. CSL submitted (18 December 2014) the DPR along with its offer for construction of vessels at a price of ₹7.60 crore (₹3.80 crore each) on non-profit basis. The offer was accepted by KMC and a contract was entered between KMC and CSL on 2 March 2015. Construction of both the vessels was completed (January 2017 & February 2017) after a delay of 169 days & 109 days respectively from the contractual date of delivery (July 2016 & October 2016). The vessels were delivered on 27 April 2018.

Audit observed that against the estimated cost and contract price of ₹7.60 crore, CSL incurred a total cost of ₹15.43 crore for construction of both the vessels whereas it recovered only ₹7.60 crore as against the total cost. No claim was preferred by CSL to recover the balance amount of ₹7.83 crore. Thus, wrong estimate had resulted in loss of revenue of ₹7.83 crore.

The Management replied (September 2018) that during the progress of the project, some additional features were made for improving the overall quality/reliability of the vessels. The contract price was fixed considering KMC's limited financial resources and the additional expenditure was made as a social commitment. The Ministry endorsed (January 2019) the views of CSL.

However, the fact was that KMC did not request any additional feature or quality improvement in the vessels. Had the same been required, it should have been brought to the notice of KMC by CSL and demand for increased cost price raised. The reply of CSL supports audit observation that CSL could not claim for increase in cost for additional features or quality improvement done in the vessels, which were not provided in the contract. Moreover, KMC did not request for any price concession due to its financial difficulties and CSL being a commercial undertaking was expected to follow commercial prudence while accepting and implementing contracts and client's payment ability should not have been a factor for determining cost price. Thus, fixation of unrealistic low contract price in the estimate had resulted in avoidable loss of ₹7.83 crore to CSL.

[1] ***RORO/Roll-on Roll-off: These ships are vessels designed to carry wheeled cargo, such as cars, trucks, semi-trailer trucks, trailers, and railroad cars, that are driven on and off the ship on their own wheels or using a platform vehicle, such as a self-propelled modular transporter.***

The Shipping Corporation of India Limited

9.2 Payment of Performance Related Pay in violation of DPE Guidelines

As per DPE guidelines, profits from only the core business activities of the CPSEs were to be considered for distribution of Performance Related Pay (PRP) to employees but the Shipping Corporation of India considered non-core profits also, for distributing PRP.

The Department of Public Enterprises (DPE), Ministry of Heavy Industries and Public Enterprises approved (November 2008) payment of Performance Related Pay (PRP) for Board level and below Board level executives and non-unionized supervisors of Central Public Sector Enterprises (CPSEs). The CPSEs were required to follow a 'Bell Curve' approach in grading the officers so that not more than 10 *per cent* to 15 *per cent* are graded outstanding and 10 *per cent* are to be graded below par who are not to be paid any PRP[2]. Further, DPE clarified[3] that PRP should be distributed based on profits accruing only from core business activities of the CPSEs.

The Board of Directors of the Shipping Corporation of India Limited (SCI) approved (February 2011) a PRP Scheme for its employees but since SCI reported losses during 2011-12 to 2013-14, PRP was not payable. During 2014-15, SCI reported profit before tax (PBT) amounting to ₹276.13 crore and PRP of ₹11.03 crore was paid to employees, as per approval (November 2016) of Board of Directors.

Audit observed:

- The Management did not deduct non-core profits such as profit on sale of fixed assets including ships (₹122.42 crore), interest on employees loan (₹0.64 crore), Interest on loan given to joint venture (JV) (₹ 28.67 crore), dividend from mutual funds (₹6.72 crore) and interest income on rescinding of ship building contracts (₹ 124 crore) aggregating to ₹ 282.45 crore from PBT, while calculating profit available for distribution of PRP. If such profits are excluded, being non-core profits, there was no profit[4] arising from core business activity during the year 2014-15 which would entail payment of PRP.

- SCI categorized the below par employees into two categories *viz*. 'Opportunity for development (OFD)' consisting of 9.84 *per cent* of total employees and 'Do not meet expectation (DNME)' consisting of 1.48 *per cent* of total employees. The OFD category employees were paid PRP amounting to ₹38.46 lakh while DNME employees were not paid any PRP. This means that PRP was paid to major section of below par employees also in violation of DPE guidelines.

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[2] *As per DPE clarification dated 6 July 2011.*

[3] *18 September 2013 and 02 September 2014*

[4] *PBT (₹ 276.13 crore) less inadmissible non-core activity income (₹2 82.45 crore) resulting in (-)₹6.32 crore*

The Ministry replied (4 December 2018) that:

- The objects for which SCI was established were defined in its Memorandum of Association (MoA) and purchase and sale of vessels was mentioned therein, indicating that profit arising from sale of ships was an income from core activity.

- SCI's investment in JVs was in line with its MoA and the loans given by SCI to its JVs was part of its core business and accordingly the earnings from this investment constitute core business activity of SCI.

- The placing of orders and consequent rescindment of ship building contracts was in line with the core business activities and hence any associated income was also core business income for SCI.

The reply is to be viewed against the following:

- SCI's core activity was marine logistics and incomes relating to the core activity such as freight, charter hire, demurrage etc. were booked under the head "Revenue from Operations" in the Annual Financial Statements. Though the Management has stated that income earned from profit on sale of fixed assets including ships, interest income etc. amounting to ₹ 282.45 crore was also from core activities, as per the audited financial statements of SCI for 2014-15, these incomes fall under "Other Income'.

- A business enterprise cannot carry out any activity unless it is permitted by its MoA. However, mention of an activity in the MoA alone does not mean that it is a core activity.

- The Remuneration Committee, while deliberating on payment of PRP to employees, did not distinguish profit from core activities from other profits. Hence the Management's stand that all activities are core activities is not a conscious decision but an argument put forth after audit raised the issue.

Thus, the payment of ₹11.03 crore to its employees by SCI as "Performance related pay", was not in compliance with DPE guidelines.