

## CHAPTER II: MINISTRY OF MINES

### Hindustan Copper Limited

#### **2.1 IT Audit on implementation of Oracle e-Business Suite (EBS)**

Hindustan Copper Limited (HCL) implemented Oracle E-Business Suite (EBS) in October 2008 to standardise the Process and for uniform codification throughout HCL and also to centralise the processing and to minimise the time and cost for Hardware Maintenance at remote places. HCL has implemented Oracle E-Business Suite R12 ERP system to carry out all the business functions of the Company from various locations. The company incurred ` 4.52 crore towards cost of software and ` 8.70 crore for hardware cost. The following issues were observed during audit of Oracle EBS application:

##### **2.1.1 IT related issues**

Following issues were observed in audit:

##### **IT policies**

The Company has not formulated any Information Security Policy stating user classification for profile creation, password policy, number of failed login attempts, etc. exposing the system to threats of unauthorized usage and loss of data. The management replied (April 2014) that they were in the process of preparation of IT security policy.

##### **Logical access control**

##### **(i) Seeded application user account protection**

In terms of Secure Configuration Guide for Oracle E-Business Suite, the passwords for seeded application accounts should be changed or disabled. However, it was observed that several application user accounts\* were kept with their default password against the recommendation of Secure Configuration Guide for Oracle E Business Suite, Release 12 of Oracle Corporation – Version 1.1.1. This indicated potential exposure to the risk of unauthorised access. While accepting (April 2014) the fact, the management assured to take appropriate steps.

##### **(ii) Unauthorised login activity**

Scrutiny of user login records, on sample basis, revealed the following:

- \* User ids of few users were logged in when the original user was absent or on leave indicating the possibility of the user id being shared.

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\* *OP\_CUST\_CARE\_ADMIN, OP\_SYSADMIN, MOBILEADM, etc.*

- \* In terms of Secure Configuration Guide for Oracle E-Business Suite, the maximum number of failed login attempts per day was to be configured as five. But it was observed that unsuccessful logins were not being monitored as significant number of failed login attempts were noticed under various user ids.

The management accepted (April 2014) the finding and was in the process of taking appropriate measures.

**2.1.2 Quality of Master Data:** Master data files are meant for integrity, consistency, completeness and accuracy of master data records. Master data is of vital importance as information stored in master data files are usually critical to the processing and reporting of financial and operational data. Accuracy of master data files can affect many related transactions and must therefore be adequately protected.

- (i) **Material Master:** The material master contains various data—identification number, description, unit of measurement of materials required by the Company. It was, however, observed:

- \* That multiple ids (33716 ids out of 749944 ids) were created for same materials indicating lack of supervision in maintenance and updation of master records. Management had stated (April 2014) that based on use and transaction, material codes are assigned to multiple inventory organisations across all the units.

- (ii) **Vendor Master:** Analysis of the Vendor Master (other than employees) revealed that:

- \* No party name was attached for several vendor ids and address field was also not captured for several vendors indicating incomplete data.
- \* Creation of two different vendor ids for several suppliers, though Permanent Account Number (PAN) was same for each of such two different ids. Existence of duplicate vendor ids in the master indicated lack of validation control which led to placement of purchase order to the same vendor under different vendor ids.

While accepting (April 2014) the fact, the management had agreed to take necessary action.

- (iii) **Wrong definition of unit of measurement:** There are materials with unit of measurement (UoM) “NO”. For such items quantity in stock should be in whole numbers. However, scrutiny revealed some instances where quantity in stock were in fractions though the UoM was “NO”, thereby indicating deficiency in customization. The management offered (April 2014) no comment as no item code reference was provided to them. The reply of the management was not acceptable as related information was available in their ERP system.

### **2.1.3 Depreciation of fixed assets:**

Schedule XIV of the Companies Act, 1956 requires that any asset valuing ` 5000 or less is to be depreciated fully in the year of addition. In 630 cases it was seen that assets

valuing ` 5000 or below were not depreciated fully and an amount of ` 1.04 lakh needed to be depreciated. Management stated (July 2014) that necessary rectification has been carried out and accounted for. Further checks, however, revealed that some such instances still existed in the system without rectification which indicated that the system of accounting for depreciation is still prone to errors.

The Company could not map the depreciation rates allowed by the Companies Act, 1956 and charged depreciation at rates other than the prescribed rates. It was observed that there was 83 asset items valuing ` 859.79 lakh (out of total 21309 asset items valuing ` 22386.13 lakh) which were charged depreciation at rates other than rates of depreciation prescribed the Companies Act. Management stated (July 2014) that these are the assets which are in use since long i.e. before the introduction of Schedule XIV to the Companies Act and that the rates of depreciation which are being charged at the derived rates based on the estimated life of the asset. The contention of the Management is not correct as all assets are required to be depreciated as per Schedule XIV to the Companies Act. In case of 1 asset valuing ` 35.08 lakh, depreciation flag was kept at “yes”, however, no depreciation rate was attached. Management stated (July 2014) that necessary rectification has been carried out at the instance of Audit. However, no such action was undertaken.

#### ***2.1.4 Manual intervention in financial records***

##### ***\* Tracking of customer credit balance for sales***

In terms of marketing policy of the company, 100 *per cent* payment should be made by the party before lifting materials from the company. However, scrutiny revealed that delivery of materials valuing ` 182.55 lakh was made to three customers though no actual advance payment was received from the same. Thus, non-existence of monitoring system for verification of real-time customer payment led to allowance of soft credit facilities to parties who were not eligible for the same. The management had stated (April 2014) to take necessary action in this regard.

***2.1.5 Valuation of Stock items:*** As per accounting policy of the Company, the raw materials are valued at the lower of the net realizable value and weighted average cost. Scrutiny of valuation of stock items in the system revealed that:

- \* Instances where quantity of closing stock of materials was zero but total value was captured as more than zero.***
- \* Items in the stock valued at “NIL” though quantity was available.***
- \* Same items of stock at stores which were valued at different rates. This indicated lack of inventory management through the system and against the prudent accounting principles. Moreover, existence of same materials with different quantity may lead to improper inventory control. In respect of point no. (1), the management had accepted (April 2014) the audit observation that for zero material quantity, stock value will also be zero. For point no. (2), the management had stated (April 2014) that for materials having stock quantity less than one unit and for non-moving items item cost (item rate) was zero. The reply of the***

management was not acceptable that in the list there were some items, quantity of which were more than one unit and none of the materials were separately marked as non-moving item. In respect of point no. (3), the management had stated (April 2014) those items for which item cost were updated on day to day basis, different rate may exist for same item. The reply of the management was not acceptable as different rate for same item of material should not exist as per prudent inventory management.

### ***2.1.6 Delay implementation of Payroll Module***

The payroll module was one of the modules of Oracle EBS package procured in 2008. This payroll module was, however, implemented in all the units alongwith legacy payroll system only in 2011-12, indicating delay in implementation and intended benefits of the same.

The matter was reported to the Ministry in February 2015; their reply was awaited (March 2015).

### ***2.2 Fraudulent accounting activities***

**Benefits were extended to customers by forging, manipulating the documents as well as by passing fictitious entries in the system to camouflage the accounts of the company.**

As per the procedure followed by Hindustan Copper Limited (the Company), the customer has to deposit money in advance in form of RTGS, pay order, cheque or demand draft (DD) for purchase of copper product. Thus, before issuing delivery order, receipt of payment/availability of sufficient credit balance in the customers' account was to be ensured.

The Company had introduced Oracle E-Business Suite as its Enterprise Resource Planning (ERP) system since 01 October 2008. The Accounts Receivable Module (ARM) of the ERP system is used to record receipt of payments for sale of copper products while the Marketing Module (MM) is used for recording of sales transactions. When a customer makes payment for lifting materials, money receipt entry is recorded in the ERP which is applied to generate delivery order to allow the customer to lift materials.

Scrutiny of customer files, delivery orders, bank statements, data from ERP system and analysis of the same through IDEA package disclosed that fictitious entries were made both in ARM and MM at Regional Sales Office (East) (RSOE), Kolkata to extend pecuniary gains to some customers. However, the files of the customers as provided to audit by the management were incomplete and did not contain all the papers relating to the business carried out with those customers.

It was noted that money receipts and bank statements were fabricated for issue of delivery orders in favour of customers. During the period covered in audit (2010-11 to 2013-14), the company transacted with 48 customers in the RSOE, Kolkata, out of which 3 cases of irregular/unauthorized transactions were noticed during test check. It was found that

₹ 282.44 lakh was shown as fraudulent receipts against which delivery orders of ₹ 182.55 lakh were issued (**Annexure-I**). Such fraudulent receipts were subsequently reversed.

Audit examination further revealed that there were instances of transfer of customer refunds to other customers or unjustified customer refunds. The ERP system captured such refunds as invoice issued to the customer. Out of 73 customer refund cases, 28 refunds were routed through a particular account code viz. “25418–Bank Transfer” which was used as an intermediary account to park the above refunds and later the same was transferred to the accounts of other customers and shown as receipts from such customers. This was done either to enable such unduly benefitted customers to lift materials or to adjust their outstanding dues. Through this mechanism, credit balances of ₹ 241.81 lakh in respect of 34 customers (due as on 1 October 2008 – date of go live of ERP) were fraudulently transferred to the account of 13 customers which accounted for about 42 *per cent* of the total amount (₹ 578 lakh) due to customers as on 1 October 2008 (**Annexure-II**).

Audit also observed that out of six number of bank guarantees (BGs) valuing ₹ 200 lakh furnished by M/s. Almetal Industries Private Limited (AIPL), five BGs valuing ₹ 150 lakh were not encashed and allowed to expire by September 2011, even though at that point of time the customer had outstanding dues of ₹ 257.73 lakh. Scrutiny of this customer ledger account also revealed that a cheque of ₹ 50 lakh received from the customer was not encashed and reversed subsequently and AIPL was extended undue benefit of ₹ 8, 69,800 by passing a wrong credit memo on account of interest. It was further observed that undue advantage was extended to two customers viz. AIPL valuing ₹ 91.78 lakh and M/s. Shree Bajrang Bali Ashok Construction Private Limited valuing ₹ 38.16 lakh by way of unauthorized fake balance transfer from other customers’ account.

We also noticed following deficiencies in the internal control system of the Company:

- \* Basic control of matching receipt numbers, financial instrument numbers and dates with the physical documents was not exercised.
- \* There was no system of recording of receipt of cheques from the customers. As a result, control over cheques being encashed was lacking.
- \* The system of monitoring the Bank Guarantees was not ensured as no bank guarantee register was maintained.
- \* Internal control through the ERP system was lacking as the vouchers, credit memos/ debit memos, rectification or reversal of entries were created and updated by using the same user id which is against the basic IT security norms.
- \* The laid down policy of the company regarding delegation of powers was not followed properly for issue of credit notes and allowing refunds to the customers.
- \* On the basis of instruction of the audit committee of the company, though all manuals including internal audit manuals were submitted (1 February 2011) by State Productivity Council – West Bengal, yet those manuals were not adopted (August 2014).

- \* Internal audit reports were not discussed at length in the audit committee meetings. As such, it could not be concluded whether the audit committee was regularly monitoring the internal audit findings.
- \* There was no system of periodical confirmation of balances of debtors and there was no comprehensive fraud policy.

While scrutinising the ERP records of all the above transactions, it was noticed that most of the transactions were executed using a user id viz. "RSOE\_FIN\_1". It was found that a permanent employee of the company used this id till August 2011. Thereafter, the same id was used by a contract employee till the completion of contract tenure (March 2013). Audit observed that there was lack of justification towards allowing a contract employee to use this id of the Finance section of the company. Further, this id was utilised not only to create the document but also to validate/approve the same. Further, it was noticed that another id viz. "FIN\_CORE\_1" was used by Advisor (Finance). It was also found that in January 2012 a new employee in the Marketing (Finance) was recruited to take over the duties from the contract employee and to replace the contract employee after a gap of six months. But the same was not done; rather, the new employee was shifted (July 2012) to another section, thereby allowing the contract employee to continue with the job upto 31 March 2013, during which period most of these irregularities took place. It would appear that the continuance of the contract employee even when a regular employee had been recruited would suggest complicity.

Management accepted (January 2015) all the above audit observations. However, despite such serious irregularities, management has neither fixed responsibility nor initiated any legal action.

The matter was reported to the Ministry in February 2015; their reply was awaited (March 2015).