CHAPTER II

PERFORMANCE REVIEWS RELATING TO GOVERNMENT COMPANIES

2.1 Felling and Conversion of trees by Himachal Pradesh State Forest Corporation Limited

Highlights

The Company failed to initiate steps for undertaking work departmentally to eliminate the agency of contractors in a phased manner thereby defeating the very purpose of formation of the Company.

(Paragraph 2.1.7)

The Company did not prepare annual budget plans in advance of the financial years as done by all Government departments and actual achievements did not commensurate with the budgeted estimates.

(Paragraph 2.1.8)

There was delay in receipt of marking lists, taking over and working of lots resulting in loss of Rs.1.88 crore due to payment of extension fee, interest and less extraction of timber.

(Paragraphs 2.1.13 and 2.1.15)

Submission of incorrect data to the Pricing Committee resulted in fixation of higher royalty rates and consequent avoidable payment of royalty of Rs.2.36 crore to the Forest Department.

(Paragraph 2.1.12)

Fixation of higher royalty rates by assuming obtainable yield at a higher rate resulted in a loss of Rs.1.74 crore.

(Paragraph 2.1.25)

Failure of the Company to review requirement of manpower resulted in payment of salary and wages of Rs.8.75 crore to surplus manpower during the period June 2003 to March 2007.

(Paragraph 2.1.31)

Management information system and internal control mechanism were deficient. The data/returns received from the field were not used for creating a data bank for use in decision making to improve the working of the Company.

(Paragraphs 2.1.34 and 2.1.35)

Introduction

2.1.1 The Himachal Pradesh State Forest Corporation Limited (Company) was incorporated (March 1974) under the Companies Act, 1956, with a view to undertake proper and scientific exploitation of forest resources in the State by nationalising operation of extraction of timber to eliminate the agency of contractors.

The affairs of the Company are managed by the Board of Directors consisting of not less than two and not more than twelve Directors including the Chairman, Vice Chairman and the Managing Director. The Managing Director is the Chief Executive of the Company and he is assisted by the Executive Director, the Financial Advisor, Company Secretary and four Directors. The Company has 14 Forest Working Divisions, five Himkasth Sale Depots which are managed by the Divisional/Depot Managers and two Rosin and Turpentine factories managed by the General Managers. The organisational chart of the Company is given in **Annexure-IX**.

Scope of audit

2.1.2 A review on the working of the Company was included in the Report of the Comptroller and Auditor General of India (Commercial)-Government of Himachal Pradesh for 1995-96. The review was discussed by the Committee on Public Sector Undertakings (COPU) in November 2000. The recommendations of COPU and action taken notes thereon were received in March 2001 and March 2003 respectively. There were no recommendations of COPU relevant to the subject under present performance audit. Four Forest Working Divisions from each of the two Directorates (North and South) were selected for audit based on marked volume of trees taken over for exploitation during 2002-03 to 2006-07 which was 10.08 lakh cum as against the total volume of trees of 14.98 lakh cum. The present Performance review, conducted from January to April 2007, is based on scrutiny of records maintained at the Head office, all the three Directorates and eight* out of 14 Forest Working Divisions selected on simple random sampling method without replacement. It covers the activity of exploitation of forests *i.e.* taking over of lots of trees marked by the Forest Department, felling and conversion of taken over trees and transportation of extracted timber to road side and sales depots during the last five years ended March 2007.

Audit objectives

2.1.3 The audit objectives of the Performance review were to ascertain whether:

- the Company succeeded in eliminating contractors from the extraction activities;

* *Shimla, Sawra, Rampur, Chopal, Mandi, Kullu, Dharmshala and Chamba*

- the Company prepared annual working plan well in advance in consultation with the Forest Department and planned its activities prudently;
- the forest/trees allotted to the Company by the Forest department and forests/trees on private land bought by the Company were taken over immediately after joint inspection of marking of forests/trees;
- the payment of royalty, sales tax, *etc*. to the Government and payment to private forest/tree owners was made as per the rules prescribed by the State Government;
- the felling of trees, extraction of timber and its transportation to the sales depots was done in an efficient, economical and effective manner; and
- there was effective management information and internal control system and evaluation mechanism in the Company.

Audit criteria

2.1.4 The audit criteria adopted for assessing the achievement of audit objectives were:

- action plan and guidelines issued by the Company;
- rules relating to taking over of forest/trees and awarding of work for felling and extraction of timber;
- manual of procedure and instructions for the timber extraction and working of Himkasth Sales Depot(Manual);
- orders of the State Government/Company relating to payment of royalty and sales tax to the Government and extraction and transportation charges to the contractors;
- provisions of the Himachal Pradesh Forest Produce (Regulation of Trade) Act, 1982; and
- provisions in the Accounting System Manual.

Audit methodology

2.1.5 The methodology adopted for achieving the audit objectives with reference to the audit criteria was examination of:

- agenda papers and minutes of the meetings of the Board of Directors and sub-committees, if any;
- working plan and guidelines issued by the Company along with annual budget *vis-a-vis* actual achievement;
- records relating to marking list, taking over of lots, allotment of works, execution of work and payments to Labour Supply Mates, payment of royalty, extension fee and interest, *etc*;

- management information and internal control system and evaluation mechanism along with Internal Audit Reports and Certified Annual Accounts; and
- issue of audit enquiries and interaction with the Management.

Audit findings

2.1.6 Audit findings, arising from the performance review on Felling and Conversion of trees by the Company were issued (June 2007) to the Government/Company and were discussed (7 August 2007) in the meeting of the Audit Review Committee for State Public Sector Enterprises (ARCPSE). The Principal Secretary (Forests), Government of Himachal Pradesh and the Managing Director of the Company attended the meeting. The views expressed by the members have been taken into consideration while finalising the review.

Audit findings are discussed in the succeeding paragraphs.

Timber Extraction Works

Failure to eliminate contractors from timber extraction works

2.1.7 The State Government, exploits forests departmentally, as well as by engaging private contractual agencies for other forest operations and regulating timber trade. The Company was specifically set up with the objective of extraction of timber from forest area so as to eliminate the agency of contractors from this activity. The work relating to forests exploitation was entrusted to the Company in a phased manner from 1974-75 and was completely handed over to it in 1982-83. The price and the terms and conditions for handing over standing trees and other forest produce by the Forest Department to the Company are to be determined on yearly basis by a Committee known as 'Pricing Committee' constituted by the State Government.

The Company failed to eliminate the agency of contractors from timber extraction works defeating the very purpose of setting up the Company.

The Company has not evolved a mechanism for undertaking timber extraction works departmentally to eliminate the agency of contractors in a phased manner over a prescribed period. This resulted in complete dependence on contractors and defeated the very purpose of nationalisation of timber extraction works as well as fulfilling the purpose of setting up the Company.

The Management stated (July 2007) that there is complete ban on green marking and in view of salvage and scattered markings, it was not possible to use modern machine tools for exploitation works. Due to lack of infrastructural facilities and skilled manpower, the departmental working of lot was not possible. The reply is not tenable as the Company failed to initiate steps for promotion of departmental working to eliminate the agency of contractors in a phased manner thereby defeating the very purpose of formation of the Company.

Deficient budgetary control

2.1.8 Budget is a quantitative, financial expression of a programme of measures planned for a year. The budget is drawn up with a view to plan future operations, allotment of funds and determined expenditure and returns of expenditure and to make *ex-post facto* checks on the results obtained. Timely preparation of budget and analysis of the variations noticed during execution serve the purpose of internal control. The budgets indicate the health of an organisation. The following deficiencies were noticed in the preparation and use of budget as a tool of internal control:

- The Company did not prepare annual budget plans well before the commencement of the financial years. There were delays in preparation and submission of budgets by the divisions, its consolidation at Directorate level and finalisation at head office. The annual budgets for 2002-03 to 2006-07 were approved by the Board of Directors (BODs) after five to eight months from the commencement of the financial year, indicating the casual state of affairs/no link between expenditure and income and total lack of financial control and management.
- There was no system of reviewing/reporting the actual performance periodically with reference to targets with a view to analyse the reasons for shortfall, if any and take remedial measures. Fact is, with delayed passing of budget, review and reporting was of little consequence.
- Delay in finalisation of budget also means that the Company had less time to spend money and during the first few months of financial year, there were constraints of expenditure.
- Delayed budget also led to delay in finalisation of annual accounts.

The table below indicates the budgeted and actual income, expenditure and profit/loss of the Company for the last five years ending March 2007:

(Rupees in lakh)

	2002-03	**2003-04***	**2004-05***	**2005-06***	**2006-07***
Budgeted					
Income	14,945.30	13,720. 00	13,823.00	15,316.25	14,827.07
Expenditure	14,935.00	15,033.00	14,243.00	15,186.75	14,741.41
Profit (+)/Loss (-)	(+)10.30	(-)1,313.00	(-)420.00	(+)129.50	(+)85.66
Actual					
Income	12,769.86	13,359.57	13,675.04	14,184.60	13,580.97
Expenditure	14,760.20	14,504.20	13,804.05	14,272.52	14,075.51
Profit (+)/Loss (-)	(-)1,990.34	(-)1,144.63	(-)129.01	(-)87.92	(-)494.54
Variation					
Income	(-)2,175.44	(-)360.43	(-)147.96	(-)1,131.65	(-)1,246.10
Expenditure	(-)174.80	(-)528.80	(-)438.95	(-)914.23	(-)665.90
Profit (+)/Loss (-)	(-)2,000.64	(+)168.37	(+)290.99	(-)217.42	(-)580.20

Source: Annual accounts of the Company.

* *The figures of actual income and expenditure for the years 2004-2007 are provisional*

Huge variations both in budget allocation and expenditure indicated that the budgeted figures were not based on any scientific analysis of performance during earlier years or any database maintained at the Head office.

The Management stated (July 2007) that efforts to streamline the system for preparation of budget in time were being taken. The Principal Secretary (Forests) during ARCPSE meeting (August 2007) also emphasized the need for analysing the variations and taking effective measures to minimise them.

Working results

The Company incurred loss of Rs.55.82 crore in timber extraction works during 2002-06 as the cost of extraction of timber was higher then the sale value.

2.1.9 The working results of timber extraction works for the five years ended March 2006 are given in **Annexure-X.** It would be seen from the details in the Annexure that the Company incurred loss in timber extraction works in each year during the period of review and total loss incurred during the five years amounted to Rs.55.82 crore. The cost of production of timber during the last five years was 5.10, 24.96, 15.39, 1.38 and 8.90 *per cent* higher than the sale value.

As against the loss of Rs.55.82 crore in timber extraction works of the Company during 2001-06*, the over all net loss of the Company during the same period was Rs.33.31 crore thereby indicating that profit of Rs.22.51 crore generated by other activities was absorbed by losses in timber extraction works.

In view of recurring losses, the State Government, on the recommendation of the BODs, constituted (July 2005) a committee of seven members under the chairmanship of Vice Chairman of the Company for investigating the reasons for losses in working of timber and also to study the working of adjoining hill states to make suitable recommendations to reduce/eliminate the losses. The Committee was required to submit its report within three months. The report had, however, not been submitted so far (August 2007).

The reasons for losses as analysed in audit were as under:

- delay in working of lots resulting in deterioration of timber and payment of extension fee;
- huge losses in the working of private lots on royalty basis;
- total dependence of the Company on contractors for extraction/auction/sale of timber despite having surplus manpower; and
- payment of interest on delayed payment of royalty.

The Management confirmed (July 2007) the working results and the reasons for the losses as analysed by Audit. Effective steps need to be taken to minimise the losses.

* *Accounts of 2006-07 not finalised*

Timber extraction works

2.1.10 The table below indicates the volume of trees marked, royalty and sales tax payable and timber obtained during the last five years ended 2006-07:

Year	Volume marked/taken over (cubic meters in lakh)	Royalty payable (Rupees in crore)	Sales tax payable (Rupees in crore)	Converted Timber obtained (cubic meters in lakh)
2002-03	3.32	33.98	10.20	2.15
2003-04	2.33	22.08	6.62	1.90
2004-05	3.21	28.67	8.60	1.71
2005-06	3.76	43.92	5.49*	1.87
2006-07	2.36	26.35	3.29	2.02
Total	**14.98**	**155.00**	**34.20**	**9.65**

Source: Compiled from the relevant records of the Company.

The above details shows that royalty of Rs.155 crore and sales tax/value added tax of Rs.34.20 crore was payable for the volume marked/taken over during the last five years ending March 2007. As against this, royalty of Rs.124.76 crore and sales tax/value added tax of Rs.30.39 crore was due for payment up to March 2007. Out of above, only Rs.21.09 crore was outstanding (June 2007) and the remaining amount had already been paid to the State Government. The amount of Rs.21.09 crore comprised of Rs.15.05 crore pertaining to 2002-03 (Rs.8.67 crore due in March 2003) and 2005-06 (Rs.6.38 crore due in March 2006) and the balance amount of Rs.6.04 crore pertained to 2006-07 (due in February 2007). The amount was pending reconciliation by various Forest Working Divisions of the Company with the respective Divisional Forest Officers. Delay in reconciliation and subsequent delay in payment of royalty results in payment of interest for the period of delay as pointed out in paragraph 2.1.13 *infra*.

The Management attributed (July 2007) the delay in making timely payment of royalty to reasons like paucity of funds, disputes with the Forest Department, non-fixation of final royalty rate in advance, *etc*. due to which payment of interest was stated to be unavoidable. The reply is not tenable as being a commercial organisation, the Company should manage its affairs efficiently and economically and co-ordinate its activities with the Forest Department at highest level for timely fixation of royalty rates. The reconciliation should have been completed in time to avoid unnecessary payment of interest.

* *Sales tax was payable @ 30 per cent up to 2004-05, but the same has been substituted by VAT @ 12.5 per cent from 1 April 2005*

Delay in receipt of marking lists, taking over of lots and non-preparation of plan by the Divisional Managers

2.1.11 As per rules, the marking lists for *khair, chil*, fuel wood, coppice and bamboo *etc*. are to be received by the Company from the Forest Department by 15 September of the year in which the lots are to be worked and for fir, spruce, *deodar, kail etc*. by 15 December of the preceding year during which the lots are to be worked. No marking lists should be received either by the Directors or the Divisional Managers from the Forest Department without the approval of the Managing Director (MD) after 15 September and 15 December respectively. The lots are to be taken over under proper receipt after inspection by the field staff of the Company within one month from the receipt of marking lists. A plan of operation for exploitation of the lots has to be drawn by the Divisional Managers of Forest Working Divisions of the Company in relation to the time schedule so as to complete the exploitation within the working period of lots.

It was observed (April 2007) that out of 292 lots marked for felling during 2003-06 in five[*] Forest Working Divisions, marking lists of 74 lots were received after 15 December, that too without the approval of the MD. Further, 166 lots were taken over after the scheduled period of one month. A plan of operation was also not drawn up the Divisional Managers of eight[**] Forest Working Divisions selected for scrutiny. Delay in receipt of marking lists/taking over of lots and non-preparation of plan by the Divisional Managers delayed the completion of timber extraction work resulting in payment of extension fee of Rs.57.56 lakh to the Forest Department and less extraction of timber valuing Rs.38.80 lakh as brought out in paragraphs 2.1.13 and 2.1.15 *infra* respectively.

The Management assured (July 2007) to look into the matter. The Principal Secretary (Forests) also assured (August 2007) during ARCPSE meeting that the instructions would be issued to the field units for not accepting the lots after the scheduled date without the approval of the Managing Director.

Excess payment of royalty and value added tax

2.1.12 The royalty rates are fixed by the State Government on the recommendations of the Pricing Committee constituted by it on advalorem basis as a percentage of weighted average sale rates as worked out by the Company based on rates obtained in auctions during the preceding year.

The Company paid royalty for 2005-06 lots at the rates fixed by the Pricing Committee on the basis of weighted average sale rates of 2004-05 as furnished (July 2005) by the Company. As the rates furnished by the Company for 2004-05 were abnormally high, the MD got the matter investigated by the Director (Marketing) and the revised weighted average sale rates were forwarded (December 2006) to the Principal Chief Conservator of Forests for

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[*] *Shimla, Chamba, Chopal, Sawra and Rampur*

[**] *Shimla, Chopal, Rampur, Sawra, Dharamsala, Chamba, Kullu and Mandi*

Intimation of incorrect input resulted in fixation of higher royalty rates and consequential excess payment of royalty (Rs.2.10 crore) and value added tax (Rs.26.29 lakh).

rectification of royalty rates by the Pricing Committee. The Pricing Committee directed (February 2007) the Principal Secretary (Forests) to take stock of the correct position and recommend the action to be taken in the next Pricing Committee meeting. Final outcome was still awaited (August 2007). The Company did not take action against the officials responsible for furnishing incorrect information relating to rates of 2004-05. Intimation of incorrect weighted average sale rates of 2004-05 resulted in fixation of higher royalty rates and consequential excess payment (June 2006) of Rs.2.36 crore (royalty: Rs.2.10 crore and value added tax: Rs.26.29 lakh) which is yet to be received back from the State Government.

The Management admitted (July 2007) the facts. The Principal Secretary (Forests) stated (August 2007) during ARCPSE meeting that the revised data furnished by the Company would be examined and final outcome intimated to Audit in due course.

Avoidable excess payment of interest and extension fee

Non-payment of royalty on due dates resulted in payment of interest of Rs.52.76 lakh on royalty during 2003-07.

2.1.13 Royalty for trees taken over by the Company from Forest Department is required to be paid to the Department in two to ten installments depending upon the working period of lots. Delay in payment of installments of royalty attracts interest at the rate of 9 *per cent per annum* payable to the Forest Department with effect from April 2004 (prior to this, the rate of interest was 11.5 *per cent per annum* applicable with effect from 1 April 2001). The Company did not pay the installments of royalty on the due dates and thus had to pay Rs.52.76 lakh to Forest Department as interest on royalty during 2003-07.

Further, as per the standard terms and conditions of agreement with the Forest Department, the Company is required to complete the work of lots within the working period allowed by the Forest Department for completing the extraction work of lot in the forest. The Company can seek extension in working period on payment of extension fee for the extended period. As per decision of the Pricing Committee (August 2001) of the State Government**,** the Company is liable to pay extension fee as under:

- If royalty has been paid, at the rate of 0.2 *per cent* per month for first extension and at the rate of 0.3 *per cen* thereafter (2.4 to 3.6 *per cent per annum*).
- If royalty has not been paid, at the rate of 1.5 *per cent* per month (18 *per cent per annum*) for first extension and at the rate of 2 *per cent* per month (24 *per cent per annum*) thereafter.

In this regard, it was observed (April 2007) as under:

- Test check of records in five* Forest Working Divisions revealed (April 2007) that out of 292 lots taken over during 2003-06, the work of 288 lots was awarded to the Labour Supply Mates (LSMs) after delay of one to 17 months from the start of the working period.

* *Shimla, Rampur, Chopal, Chamba and Sawra*

The delay in allotment and completion of work resulted in avoidable expenditure of Rs.57.56 lakh.

- The delay in awarding the work was mainly on account of snow bound forests, cancellation of tenders due to higher rates received in tenders, non-participation of LSMs in tender, *etc*. The delay in allotment and completion of work resulted in payment of extension fee of Rs 77.49 lakh to the Forest Department in respect of 115 lots in these five FWDs during 2000-01 to 2004-05 against which Rs.19.93 lakh only was recovered from the LSMs under the provisions of the agreement for delay of one to 14 months in execution of work. This resulted in avoidable expenditure of Rs.57.56 lakh. So far (August 2007), the Company has not devised mechanism for awarding work immediately after taking over lots, avoiding delay in execution and recovery of entire amount of extension fee from the LSMs for delay in completion of work.
- The financial prudence demands that to avoid payment of extension fee at higher rates, royalty should be paid in time on scheduled dates. Scrutiny of lot files revealed that the four* Forest Working Divisions of the Company either did not pay or made part payment of royalty relating to lots of 2002-03 though royalty for ensuing year's lots was paid as per schedule. This resulted in avoidable payment of extension fee of Rs.49.03 lakh at the rate of 18 *per cent per annum* for 2002-03 lots. Had the Company paid royalty for lots of 2002-03 before making payment for 2003-04 lots, the payment of extension fee could have been reduced to Rs.9.81 lakh thereby resulting in saving of Rs.39.22 lakh.

The Management stated (July 2007) that the royalty could not be paid in time due to financial constraints and availing of cash credit from the banks was not advantageous as the bank interest rate was higher than the rate of interest being charged by the Forest Department. It was further stated that payment of extension fee was unavoidable due to delay in taking over of lots, allotment of work to LSMs and execution of timber extraction works and evolving of any other mechanism was not possible. The reply is not tenable as the non-payment of royalty in time and non-working of lots within lease period made the Company liable to pay interest and extension fee respectively at the rate, which was much higher than the interest rate of 11.75 to 10.25 *per cent per annum* being charged by banks on cash credit during the period 2002-03 to 2006-07. Besides, the reasons put forth for payment of extension fee were controllable and the payment could have been minimised by better co-ordination with the Forest Department and managing the affairs of the Company economically and efficiently.

Loss due to faulty taking over of lots

2.1.14 On the recommendations of the Pricing Committee, the State Government decided (December 1999) that the Company would take over the lots handed over to it after due date by the Forest Department for working and

* *Rampur, Chamba, Sawra and Chopal*

these would be treated as received in the next year. On such lots, the Company would pay royalty and sales tax to the Forest Department as per the rates applicable for the next year's lots. During test check of records in five* Forest Working Divisions, it was noticed (April 2007) that the marking lists of 11 lots due for exploitation during 2002-03 and 28 lots due for exploitation during 2003-04 were received by the Company in January and February 2002 and February to June and October 2003 respectively with a delay of one to 11 months. Thus, these lots were required to be considered for the subsequent years *i.e.* 2003-04 and 2004-05 respectively. The royalty rates were reduced in the subsequent years. The concerned Divisional Managers, however, did not consider these lots for the subsequent years resulting in excess payment of royalty of Rs.42.76 lakh including sales tax.

Loss due to delay in working of lots by Labour Supply Mates (LSMs)

2.1.15 The work of felling, conversion and carriage of timber up to road side depots of four lots** was awarded between July 1997 and July 2001 to LSMs which was scheduled to be completed between June 1999 and June 2003**.** The work was not completed by the concerned LSMs within the stipulated period. As per clause 12(a) of the agreement with LSMs, the work was cancelled and the Company got these works completed through other LSMs at the risk and cost of first LSMs. The delayed working of the lots resulted in loss of Rs.38.80 lakh on account of less extraction of timber/timber found rotten/extension fee paid to the Forest Department. The cases filed (October 2004 and May 2006) by the FWD, Chopal with the Arbitrator (Director South of the Company) against the first LSMs for recovery of loss in respect of first two lots were still (August 2007) pending for decision. The Company did not take action against the first LSMs in accordance with the clause 12(a) of the agreement in respect of remaining two lots.

The Management admitted (July 2007) during ARCPSE meeting that two cases were pending with the Arbitrator for decision. It assured that the necessary action in remaining two cases would also be initiated.

Wasteful expenditure on purchase of timber tools

2.1.16 Revised terms and conditions of tender (condition No. 16) circulated (July 2000) by the Company for implementation during timber extraction works, *inter alia*, provided that successful tenderers would arrange labour, tools, godown and accommodation at their own cost and the Company would have nothing to do with such arrangements.

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* *Chopal, Rampur, Sawra, Chamba and Kullu*

** *{No.10/2001-03 (Dhartasuli: Rs.10.79 lakh), No. 6/97-99 (Kanda uni:Rs.20.95 lakh), No 4/2001-02 (Chamba: Rs.4.56 lakh) and No. 17/2001-02 (Churah:Rs.2.50 lakh)}*

Test check of records (April 2007) revealed that three[1] Forest Working Divisions purchased timber tools valuing Rs.21.28 lakh during 2001-2007 for supply to the LSMs. In view of revised terms and conditions, purchase of timber tools worth Rs.21.28 lakh lacked justification and their distribution to the LSMs amounted to undue favour to them.

The Management stated (July 2007) that the matter was being looked into.

Excess payment due to incorrect accountal of wet lead [2]

2.1.17 As per practice in vogue, normal wet lead is taken as half of the measured distance. It was, however, noticed (April 2007) that in respect of 15 lots pertaining to 2002-03 and 2003-04, normal wet lead was not reduced to half for calculating the total manual carriage lead while preparing economics/upset price, based on which timber extraction works were awarded to the LSMs. This resulted in allowing higher rate for manual carriage of timber and consequent excess payment of Rs.12.16 lakh to the LSMs in three[3] Forest Working Divisions.

The Management in ARCPSE meeting stated (August 2007) that the cases mentioned in the para would be looked into and uniform system for accountal of normal lead would be followed in future.

Loss due to payment for inflated lead

2.1.18 As per rules,[4] leads for manual and mechanised carriage etc. have to be measured, fixed during planning and mentioned while inviting tenders or allotting the work.

The work of '*khad*'[5] floating was awarded (November 1999) for Rs.67.68 lakh to a LSM by FWD, Sawra on lowest rate of Rs.1,490.05 per cum against schedule rate of Rs.1,753 per cum. The work was started in December 1999 and completed in March 2001.

During currency of work, a dispute arose regarding lead (distance of river up to Mohri Khatal) and after re-measurement (October 2000) by the DM of FWD, Sawra, the lead was found 35 KM as against 52 KM taken for working out the schedule of rate while calling for tenders. Accordingly, the re-worked contract value of Rs.44.57 lakh was released (June 2001) after withholding Rs.22.11 lakh.

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1 *Dharamsala, Chamba and Mandi*

2 *Wet lead is the distance of marked forest from one end to another for carriage of timber*

3 *Shimla, Mandi and Chamba*

4 *Para 1.3 of Procedure and Instructions for the timber extraction works and working of Himkasth Sale Depots*

5 L*ot No. 5/96-97 {(Chinon) from Foot-Odor (Dodra Kawar) to Mohri Khatal (UP)}*

Aggrieved by the action, the LSM filed (April 2002) a case in the Hon'ble High Court which referred the matter to the Arbitrator. The Director (South) was appointed (December 2002) as Arbitrator. During the pendency of the case, the Company, on the initiative of the LSM, settled the matter and paid (September 2005) him Rs.20 lakh on the apprehension of losing the case due to its failure to mention the distance of lead in the tendered document/allotment letter. Thus, non-adherence to the prescribed procedure resulted in a loss of Rs.20 lakh.

The Management admitted (July 2007) that this happened due to a system failure and that the lead was now being taken as 35 KMs. The reply is not tenable as the Corporation had not yet (August 2007) introduced the system of mentioning lead in tender documents and agreement deeds to make the system more transparent and reliable.

Non-adjustment of royalty and sales tax of rotten trees

2.1.19 As per the decision (October 1999) of the Pricing Committee, royalty and sales tax is not payable for rotten and hollow trees where the volume of such rotten/hollow trees is more than 5 *per cent* of the marked volume. In order to ascertain the quantum of the rotten/hollow trees, joint inspection has to be conducted by the officers of the Company and the Forest Department on the request of the Company within two months of felling of trees. Rotten/hollow trees are those which have 25 *per cent* or more rottage or hollowness at the stump cross section.

Failure to follow the laid down procedure resulted in non-adjustment of royalty and sales tax of Rs.85.95 lakh paid in respect of rotten trees.

It was observed (April 2007) that in seven lots of four* Forest Working Divisions, the joint inspection of lots was not got conducted within the stipulated period of two months and no efforts were made at highest level to ensure the presence of officials of Forest Department to verify the rotten volume of 13,684 cum. This volume was more than five *per cent* of the marked volume in each lot. As a result, royalty and sales tax of Rs.85.95 lakh paid on these rotten trees to the Forest Department could not be got adjusted and resulted in loss to the Company.

In ARCPSE meeting, the Management stated (August 2007) that the matter was under consideration of the Pricing Committee and it would be settled as per their decision.

Loss due to non-working of lots

2.1.20 As per rules, the trees standing on very steep and rocky portions, likely to be damaged during felling or conversion, should not ordinarily be marked and if marked, should not be taken over.

* *Kullu, Chamba, Sawra and Chopal*

Taking over of trees in contravention of the procedure and instructions resulted in loss of Rs.70.95 lakh.

It was noticed (April 2007) that standing volume of 4,454 cum and felled volume of 2,716 cum in Shimla and Kullu Forest Working Divisions was taken over for exploitation during 1992 to 1998. These were not worked by the Company as the trees were on very steep and rocky portions and were being shown as work-in-progress and stock suspense till date (August 2007). Taking over of these lots in contravention of the procedure and instructions resulted in loss of Rs.70.95 lakh.

The Management stated (July 2007) that a committee had been constituted to look into the matter and recommend action to be taken.

Delay in realisation of dues for supply made to tribal areas

Non-streamlining of procedure for recovery of dues from the Forest Department on account of supply of fuelwood and timber to tribal areas resulted in non-recovery of Rs. 6 crore and loss of interest of Rs.50.30 lakh.

2.1.21 The Company supplies fuelwood, charcoal and timber to tribal areas of the State through the Forest Department. The sale proceeds are also received through the Forest Department. As on 31 March 2005, Rs.39.68 lakh, being the cost of 155 cum timber, was recoverable from the Forest Department. During 2005-07, the Company further supplied 140.192 cum timber and 1,05,894 quintals of fuelwood valued at Rs.3.21 crore, recovery of which was awaited (August 2007). In addition transportation charges of Rs.2.39 crore were also recoverable (31 March 2007) from the Forest Department for the supplies made during 2002-07. Thus, total recoverable amount from the Forest Department as on March 2007 amounted to Rs. 6 crore. It is pertinent to mention here that for delay in payment of royalty, the Company is paying interest at the rate of 9 *per cent* to the Forest Department whereas no interest is paid by the Forest Department/Government to the Company for delay in payment of dues for supplies made to tribal areas. As the Company arranged funds for meeting its day to day working capital requirement by obtaining cash credit facility from different banks at interest rates ranging from 11.75 to 10.25 *per cent* during 2002-03 to 2006-07, non-reimbursement of dues by the Forest Department/Government for a long period resulted in loss of interest of Rs.50.30 lakh to the Company.

The Principal Secretary (Forests) in the ARCPSE meeting stated (August 2007) that the system was being streamlined for timely realisation of dues of the Company.

Irregular writing off shortages/driage

2.1.22 As per rules, the physical verification of timber, fuelwood and pulpwood lying in retail sale depots is required to be conducted at the end of each financial year so as to see that stocks as per books of accounts are physically in existence and also to work out the normal wastage on account of driage and action taken for abnormal wastages/shortages.

The Forest Working Division, Kullu did not work out normal and abnormal shortages of pulp and fuelwood in its retail sale depots on regular basis. During 2002-03, it worked out shortage of 1,799.067 cum pulp (315.068 cum) and fuelwood (1,483.999 cum) based on the difference between timber as per books and stocks physically verified. Shortages were attributed to driage/wastage in handling which were not worked out/allowed to the depots earlier. These shortages valued at Rs.22.45 lakh were written off (January 2004) by the Divisional Manager of the Forest Working Division though he had no authority to do so. The Company neither investigated the reason for non-conducting of physical verification prior to 2002-03 nor taken action against the Divisional Manager for exceeding his power to write off the shortages.

The Management admitted (July 2007) the lapse on the part of concerned Divisional Manager in acting beyond the delegated powers. It was assured that the matter would be placed before the Board of Directors for further action.

Failure to investigate the cases under stock suspense

2.1.23 The cases of loss of timber due to floods, fire, *ghall*[*] theft, shortage in transportation, *etc*. are shown under the head stock suspense pending enquiries/recoveries/settlement/write-off, *etc*. by the appropriate authority. At the end of 2000-01, the stock suspense amounted to Rs.4.79 crore. The Company further transferred Rs.3.66 crore to suspense head during 2001-02 to 2005-06. After recovery of Rs.1.41 crore and writing off Rs.27.53 lakh during the above period, Rs.6.76 crore (insured stock Rs. 1.83 crore and Rs. 4.93 crore uninsured) appeared in the accounts under this head as on 31 March 2006.

Analysis of cases involving Rs.4.31 crore appearing under this head in Kullu and Sawara FWDs revealed that the cases pertained to 1982-2005. The Company did not review the cases periodically to identify the administrative action to be taken in each case. Though, the Chairman of the Company also emphasised (February 2004) the need to clear the items under this head, the Company did not make any serious effort to investigate the cases and clear the suspense head (July 2007).

The Management stated (July 2007) that a committee has been constituted to look into these cases.

Exploitation of private timber

2.1.24 Sale of private timber was nationalised in the State in January 1983. Accordingly, the Company was entrusted with the exploitation of private trees and sale of timber obtained. The purchase and sale of private timber is regulated by the H.P. Forest Produce (Regulation of Trade) Act, 1982. The price to be paid to the tree owners is notified by the State Government under Section 7 of the *ibid* Act. During 2001-03, the price (royalty) of standing trees was paid to the owners at the rates fixed by the State Government and the timber extracted was sold by the Company as its own. From 2003-04

[*] *Ghall is a process of transportation of timber through river from forest to road side depots*

onwards, another system of sale linked price for working of private lots was introduced by the State Government. Under this system, the sale proceeds are paid to the owners after deducting actual direct expenses incurred by the Company with interest and 15 *per cent* handling charges. The owners of trees are required to exercise option for either of the two methods. An option once exercised was to be final and irrevocable.

The standing volume of trees taken over from the private tree owners and payment made thereagainst during 2002-03 to 2006-07 was as under:

Year	**Standard Volume (in cubic meter)**	**Price of trees (Rs.in lakh)**	**Price per cubic meter (in Rupees)**
2002-03	42,013	847.00	2,016.04
2003-04	49,750	639.75	1,285.93
2004-05	44,110	687.46	1,558.51
2005-06	41,859	554.09	1,323.71
2006-07	52,399	628.79	1,200.00

Source: Compiled from the relevant records of the Company.

In this regard, the following points were noticed.

Loss due to fixation of higher royalty rates for exploitation of private trees

Fixation of higher royalty rates for exploitation of private trees resulted in loss of Rs.1.74 crore on exploitation of 67 lots during 2001-03.

2.1.25 Scrutiny of records revealed that the Company incurred loss of Rs.8.82 crore during 2001-02 and 2002-03 on exploitation of private timber (Rs.3.40 crore in 2001-02 in six[1] Forest Working Divisions and Rs.5.42 crore in 2002-03 in nine[2] Forest Working Divisions). Test check of records relating to exploitation of private trees for 2001-03 in Shimla Forest Working Division revealed that out of 87 private lots exploited on royalty basis, the division was not able to recover even the direct costs incurred on exploitation of 67 lots and thus, sustained a loss of Rs.1.74 crore. It was observed that the main reason for loss was fixation of higher royalty rates by assuming obtainable yield at a higher rate. Though, the MD is one of the members of the Pricing Committee, yet he failed to furnish the realistic data of assumed yield to the Pricing Committee so that the royalty rates could have been fixed on realistic basis and financial loss to the Company would have been avoided.

The Management admitted (July 2007) the facts and stated that the system was changed from 2003-04 and the Company did not incur further losses.

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[1] *Shimla, Nahan, Solan, Mandi, Hamirpur and Una*
[2] *Shimla, Nahan, Chopal, Nerwa, Solan, Fatehpur, Kullu, Hamirpur and Una*

Excess payment to private tree owners

2.1.26 As per final economics (December 2004) of a private lot (Kotgarh), an amount of Rs.31.99 lakh was payable to the Special Power of Attorney[*] (SPA) after deducting felling, conversion, transportation and handling charges on the actual yield. An amount of Rs.48.43 lakh was, however, paid (October 1998 to November 1999) in three instalments to the SPA based on approved tentative economics of Rs.69.06 lakh.

After completion of felling and conversion of trees, the Company obtained 662.952 cum timber during the above period, which was 179.050 cum less than the expected yield. The Company did not take less yield into account while releasing second and third installment of royalty to safeguard its interest, though the actual yield was known to the Company at that time. The final sale proceeds (December 2004) amounted to Rs.63.94 lakh and only Rs.31.99 lakh was payable to the SPA, however, the Company had already paid Rs.48.43 lakh to the SPA thereby resulting in excess payment of Rs.16.44 lakh. The Company filed (November 2005) a case for recovery of the same in the High Court against the SPA and tree owners. Final outcome was awaited (July 2007). The present situation arose due to failure to exercise internal checks (releasing of second and third instalment without taking into account less yield) during currency of the work.

The Management admitted (July 2007) the lapse of the then Divisional Manager, Rampur while releasing second and third instalments of royalty, who had since retired from service. The fact, however, remains that the Management failed to take action against the Divisional Manager concerned in time.

Transportation of timber

2.1.27 The table below indicates the volume of timber obtained after extraction of felled trees taken over from the Forest Department and the timber transported to sale depots during the last five years ended 2006-07:

Year	Timber obtained[#] (cubic meters in lakh)	Timber transported to sale depots. (cubic meters in lakh)	Percentage of timber transported to timber obtained
2002-03	2.15	1.32	61.40
2003-04	1.90	1.19	62.63
2004-05	1.71	1.02	59.65
2005-06	1.87	0.98	52.41
2006-07	2.02	0.97	48.02

Source: Compiled from the relevant records of the Company.

[*] *SPA: A person authorised by the tree owners for dealing with the Company on their behalf*

[#] *Also includes timber not transported during the last year*

It would be seen from the above that percentage of timber transported to the sale depots ranged between 48.02 and 62.63 during 2002-07. The percentage of timber transported had reduced from 62.63 in 2003-04 to 48.02 in 2006-07. There were no reasons on record for decrease in transportation of extracted timber

Downgrading of timber

2.1.28 When timber is received at the HSDs, it is categorised according to quality as Smuda, B and C class, rotten, broken pieces, etc. The table below gives the details of total timber sold, timber graded/sold as C class and the percentage of C class timber to total timber sold during the last five years ended 31 March 2007:

Year	Total timber sold (cum)	Timber graded as C class (cum)	Percentage of C Class timber to total timber sold
2002-03	1,17,795	24,346	20.67
2003-04	1,33,309	23,593	17.70
2004-05	95,124	14,893	15.66
2005-06	1,04,179	2,810*	2.70
2006-07	1,01,820	142*	0.14
Total	**5,52,227**	**65,784**	

Source: Compiled from the relevant records of the Company.

Delay in transportation of timber to sale depot resulted in deterioration of quality and consequent less realisation of revenue of Rs.31.77 crore on its sale.

It is evident from the above details that out of 5,52,227 cum timber sold during 2002-07, 65,784 cum was sold as C class at the rates which were lower than the average sale rates of B class timber by Rs.4,418 to Rs.5,899 per cum. The extraction of C class timber is not permissible under Clause 9 of Schedule 'A' annexed to the agreement executed with the LSMs. The Company is not having any mechanism to check the quality of timber extracted in the Forests and as such there are possibilities that the C grade timber was being extracted by LSMs and yet the payment was being made to them. In the absence of records to show the quality of timber extracted in the forest, it is presumed that the quality of timber deteriorated during long transit period due to exposure to vagaries of weather resulting in its classification as C class and consequent less realisation of revenue of Rs.31.77 crore.

The Principal Secretary (Forests) stated (August 2007) in the ARCPSE meeting that the procedure of grading the timber had been modified and there had been considerable decrease in the quantity of C Class timber in 2005-06.

* *This is due to change in system of classification of timber in HSDs effective from September 2005*

It is a fact that due to modifications of the procedure of grading of timber, the quality of C grade has considerably reduced but at the same time the weighted average sale rate of B grade has come down substantially to Rs. 6641 per cum in 2005-06 and Rs.7,338 per cum in 2006-07 from Rs. 8663 per cum in 2004-05. It is thus indicative of the fact that the modified procedure had not served its purpose.

Loss due to non-deduction of service tax

2.1.29 GOI amended (December 2004) the Service Tax Rules, 1994 with effect from 1st January 2005. The amended Rules provide that where consignors or consignees are falling under the specific categories provided in the Service Tax Rules, service tax is required to be paid by them instead of goods transport agency. As the Company falls under the specified category, service tax at the prescribed rate was required to be paid by it after deduction from the freight paid to the transporters for transportation of timber. The Company, however, did not issue instructions to its Forest Working Divisions for deducting service tax from the transporters till March 2006.

It was noticed (April 2007) that 14 FWDs* did not recover service tax of Rs.16.08 lakh from the transporters during the period January 2005 to March 2006 though the same was deposited (March 2006) by the Company resulting in undue benefit to the transporters and loss to the Company to that extent.

The Management admitted (July 2007) the lapse and informed that an amount of Rs.4.13 lakh had been recovered from the transporters and efforts were being made to recover the remaining amount.

Arbitration cases

2.1.30 In terms of Clause 27 of the standard agreement deed executed with the LSMs, disputes of less yield, shortages, losses on account of *ghall*, flood and fire, recovery of extension fee, *etc*. are referred by the MD to the Arbitrator appointed by the Company. It was noticed (April 2007) that in almost all cases, the Arbitrators were officers of the Company. The Arbitration Act, 1940 provide for giving award within four months, yet 26 cases involving recovery of Rs.6.16 crore from the LSMs referred to the Arbitrators during August 1997 to November 2006 were pending for decision as on 31 March 2007 as detailed below:

Year	No. of cases pending	Amount (Rupees in lakh)
1997-98	1	174.04
2000-01	2	109.61
2003-04	3	54.83
2004-05	7	92.64
2005-06	9	153.34
2006-07	4	31.94

Source: Compiled from the relevant records of the Company.

* *Dharamsala, Mandi, Sundernagar, Kullu, Chamba, Fatehpur, Una, Hamirpur, Shimla, Sawra, Chopal, Rampur, Solan, and Nahan*

It would be seen from the above details that the pending arbitration cases were five months to nine years old.

The Management stated (July 2007) that the Arbitrators were to perform quasi-judicial function and they could not be forced to decide the matter without following complete procedure. The reply is not tenable as the time limit prescribed in the Arbitration Act for deciding cases should have been adhered to.

Manpower management

Surplus manpower

The Company failed to reduce the surplus manpower. Salary and wages paid to surplus manpower during June 2003 to March 2007 amounted to Rs.8.75 crore.

2.1.31 The Company did not review the requirement of manpower till March 2003 though the marked standing volume fell from 6.87 lakh cum in 1990-91 to 3.32 cum in 2002-03. On the directions (April 2003) of the State Government, the Company assessed (May 2003) the position of staff and 75 regular and 978 daily waged employees were declared surplus. As on March 2007, the number of surplus employees was 1,008 (2 regular and 1,006 daily waged) and wages paid to them during June 2003 to March 2007 amounted to Rs.8.75 crore (Regular: Rs.11.84 lakh and Daily waged: Rs.8.63 crore). Though the matter for deployment of surplus manpower in other organisations was being pursued with the State Government, the surplus staff was still (August 2007) on the roll of the Company.

The Principal Secretary (Forests) in the ARCPSE meeting informed (August 2007) that the Government had decided to absorb the excess manpower of the Company in the Government Departments. The actual deployment of the surplus manpower in other departments was, however, awaited (August 2007).

Payment of salary and wages to officials not working with the Company

2.1.32 Two Stenographers being shown as working at the Head Office and FWD, Shimla were actually working in the State Government Secretariat since January 1996 and April 2001 respectively. Orders of the competent authority for allowing them to work in the State Government Secretariat were not on record. From January 1996 to 31 March 2007, the Company incurred an expenditure of Rs.23.49 lakh on their pay and allowances without taking any work from them resulting in payment of idle wages. It is also pertinent to mention here that Forest Working Division Kullu, Mandi, Nahan, Sawra, Rampur and HSD Baddi were working without stenographers.

The Principal Secretary (Forests) in ARCPSE meeting stated (August 2007) that efforts would be made to send these officials to the State Government on deputation basis.

Corporate governance

2.1.33 Corporate governance is the system by which Companies are directed and controlled by the Management in the best interest of the shareholders and other stake holders ensuring greater transparency and better and timely financial reporting. The Companies are governed through the BODs.

As per the Memorandum and Articles of Association, the BODs should consist of minimum two and maximum 12 Directors. As on 31 March 2007, the BODs had 12 Directors (four officials and eight non-official including the Chairman and Vice Chairman).

In this regard, the following deficiencies were noticed:

- None of the 20 meetings of the BODs held during 2002-2003 to 2006-07 had full presence of the members of the BODs.
- Nominee of the Finance Department (Financial Commissioner Cum Secretary/Principal Secretary (Finance) did not attend 15 meetings.
- One of the non-official Directors was engaged in timber extraction works as a LSM in Forest Working Division, Chamba without any disclosure/declaration of his interest as required under section 299 of the Companies Act, 1956.
- After admitting (March 2005) that lack of professional management was also one of the contributory factors to the losses of Public Sector Undertakings (PSUs), the State Government stressed (March 2005) the need of recasting the BODs of PSUs by inducting at least two independent and professionally qualified Directors for giving valuable support to the senior management to run the PSUs along professional lines and instructed (March 2005) the Forest Department for taking appropriate action. Audit, however, noticed that neither the Forest Department nor the Company had taken requisite action so far (August 2007).

The Management stated (July 2007) that the State Government had to take action regarding appointment of professional directors. Regarding diversification of activities, it was stated that action had been taken in the field of eco-tourism and as regards medicinal plants, project report had been prepared and expected recoveries were being worked out.

Internal control and internal audit

Internal control

2.1.34 Internal control is an integral part of the process designed and effected by the Management of an organisation to achieve its specified objects ethically, economically and efficiently. It helps in creating reliable MIS for effective decision making. Internal Control System is most effective when it is built into the entity's infrastructure and is an integral part of the essence of the organisation. In order to exercise internal control upon the activities, the organisation should have functional and internal audit manuals.

In this regard, Audit observed as under:

- The present functional manual (viz. Procedure and instructions for timber extraction work and working of Himkashth Sales Depot) was prepared long back in 1988. The same has not been updated to include important instructions issued from time to time in regard to working of the Company.

- The procedure laid down in the revised Accounting System Manual regarding maintenance of cash book *i.e*. crediting/debiting the cash book with cash received, other receipts, cash withdrawn from the banks and payment of expenses, daily closure of cash book, daily working of balances, counting of cash in hand, and signing of cash book daily by the cashier and the supervisory officer was not followed by Forest Working Division, Sawra. Taking advantage of the lapse, an official of the division suspectedly misappropriated Rs.4.88 lakh during 2005-07. After being pointed out by Audit, the Management started (May 2007) looking into the matter. Final action was awaited (August 2007).

- The Company did not have an effective MIS. The Head Office of the Company obtained voluminous technical, financial and non-financial information from the Directorates and Forest Working Divisions through various periodical returns or one time collection of information. Such returns, received by various sections of the Company, are not put to use for development of master data base. Due to lack of consolidation and analysis of data, the top Management was not able to utilise it for effective monitoring and decision making.

- Accounting System Manual prepared (March 2004) by a firm of Chartered Accountants at an expenditure of Rs.2.47 lakh was only partly implemented by the Management.

The Management stated (July 2007) that there was always a scope for improvement, which was a gradual process. The Principal Secretary (Forests), however, agreed in ARCPSE meeting (August 2007) that there was dire need to strengthen the MIS with the help of computerisation and efforts would be made in this regard. He further stated that in future, system reports would be prepared in house instead of getting these prepared from out side agencies.

Internal audit

2.1.35 Internal audit is an integral part of internal control system of an organisation. It is an important tool in the hands of the Management which helps in promoting accuracy and reliability in an organisation's accounting data.

Internal audit of some of the units was being got conducted from the firms of Chartered Accountants. Some other units were being audited by an internal audit cell of the Company. Audit observed the following deficiencies in the internal audit system:

- The Company has not prepared internal audit manual for guidance of the Internal Auditors.
- The staff in the internal audit cell was being posted temporarily from different units as a stop gap arrangement without proper training.
- The reports of internal auditors were dealt with at the level of Financial Advisor/Executive Director and not submitted to the MD/BODs.
- The Company did not maintain year-wise detail of outstanding observations of internal auditors or observations which were repeated year after year for taking remedial/preventive action.

Absence of evaluation mechanism

2.1.36 Evaluation mechanism of different activities at different stages of operation was not in place in the Company. There was no system of comparing the actual financial results with the budgeted estimates of the Company as a whole and sale proceeds of each lot with the tentative economics prepared in the beginning. Neither there was system of grading the timber in the field in the manner in which it was being sold in the sale depots. In the absence of evaluation mechanism, the Management was not in a position to assess the impact of its actions on the working of the Company for taking necessary remedial actions.

The Management stated (July 2007) that the system of evaluation of activities was being introduced and the system of preparation of final economics of lots after sale of entire timber had been introduced for 2005-06 lots.

Acknowledgement

2.1.37 Audit acknowledges the co-operation and assistance extended by the Company and officers of the State Government at various stages of conducting the performance audit.

The matter was reported to the Government in June 2007; reply is awaited (September 2007).

Conclusion

The Company failed to eliminate the private contractors from timber extraction works. It did not prepare annual budgets well before the commencement of financial years. Actual achievements were also not

compared with the budgeted estimates. There was delay in receipt of marking lists, taking over of lots and extraction and transportation of timber. The Company suffered losses due to avoidable payment of royalty, obtaining of less yield, avoidable payment of extension fee, payment of royalty and sales tax for rotten trees, deterioration of timber during transit and excess manpower. Management information and internal control system were deficient and evaluation mechanism was non-existent.

Recommendations

- **Action plans/annual budgets should be prepared well before the commencement of the financial years and compared with actual achievements.**
- **The working through private contractors should be reduced gradually by promoting departmental extraction of timber.**
- **Delays in receipt of marking list, taking over of lots, execution of works and payment of royalty should be avoided.**
- **Action should be taken to eliminate surplus manpower.**
- **System of management information and internal control should be strengthened and evaluation mechanism put in place.**

2.2 Performance review on the Working of Himachal Pradesh Agro Industries Corporation Limited

Highlights

There was no practice of preparing annual plan well before the commencement of financial year in consultation with the State Government Departments which were the main buyers of the Company's products.

(Paragraph 2.2.7)

The financial position of the Company deteriorated as its accumulated loss of Rs.4.61 crore (31 March 2003) increased to Rs.9.25 crore (31 March 2007) which had partially eroded the paid-up capital of Rs.11.80 crore as on that date.

(Paragraph 2.2.11)

Out of five production units, three units were incurring losses continuously on account of low capacity utilisation due to lack of adequate demand from the State Government Departments and inability of the Company to market its products in the open market.

(Paragraphs 2.2.15 to 2.2.21)

The Company purchased major portion of food grains for manufacturing cattle feed during off season resulting in incurring of avoidable extra expenditure of Rs.54.35 lakh.

(Paragraphs 2.2.22)

Out of 20 trading units and one petrol pump, 10 units were continuously incurring losses and loss suffered by these units during five years up to 2006-07 amounted to Rs.1.59 crore due to inaction of the Management to improve their working.

(Paragraph 2.2.24)

The Government/Company failed to reduce the surplus manpower. Salary and wages paid to surplus manpower during the period 2003-2007 amounted to Rs.1.10 crore.

(Paragraph 2.2.26)

Management information and internal control systems were deficient and the system of appraisal of performance was non-existent.

(Paragraph 2.2.32)

Introduction

2.2.1 Himachal Pradesh Agro Industries Corporation Limited (Company) was incorporated (September 1970) with a view to promote agro based industries in the State. The main objectives of the Company are to:

- accelerate and increase agricultural production;
- contribute to the production of subsidiary and supplementary foods;
- increase the availability of supplies of food; and
- contribute to the development of agro industries in the State.

In pursuance of its objectives, the Company was operating five production units, one each for manufacturing pesticides and insecticides, agricultural implements, honey processing and one each for cattle and poultry feed. The Company was also running 20 trading units and one petrol pump in the cities and towns of the State. The trading units deal in items such as cement, iron and steel, bitumen, tyres and tubes, batteries, *etc*.

The Management of the Company is vested in the Board of Directors (BODs) consisting of 15 Directors including the Chairman and the Managing Director (MD), who is the Chief Executive. He is assisted by a General Manager, three Deputy General Managers, a Chief Accounts Officer and a Production Manager (Commercial/Pesticides) at the Head Office. Operational/trading activities in the field units are being looked after by two Deputy General Managers and the field units are headed by branch in-charges. Organisational chart is annexed as **Annexure-XI.**

Scope of audit

2.2.2 The working of the Company was last reviewed in the Report of the Comptroller and Auditor General of India (Commercial) for the year 1999-2000. The review was discussed by the Committee on Public Sector Undertakings (COPU) in July 2007. The recommendations of COPU are awaited (August 2007).

The present Performance review on the working of the Company conducted during April and May 2007 covers scrutiny of records for the last five years ended 31 March 2007 maintained at the Head Office, all the five production units and 10 out of 21 units (20 trading units and one petrol pump) selected on random sampling basis without replacement.

Audit objectives

2.2.3 The audit objectives of the Performance review were to ascertain whether:

- the Company succeeded in achieving the objectives for which it was incorporated;
- the Company utilised the installed capacity of its manufacturing units to the optimum level;
- the activities were carried out effectively, efficiently, economically and ethically;
- the Company utilised its manpower effectively and efficiently;
- effective internal control procedure was in vogue and adequate monitoring (management information system) and follow up was in place; and
- internal audit was used as a tool to make internal control effective.

Audit criteria

2.2.4 The audit criteria used for assessing the achievement of audit objectives were:

- instructions/guidelines issued by the State Government and Government of India (GOI) from time to time in regard to working of the Company;
- agenda and minutes of the meetings of the BODs;
- targets fixed for manufacturing and trading activities;
- purchase, sales and marketing procedures/policies;
- provision in the Accounts Manual; and
- human resource policies.

Audit methodology

2.2.5 The methodology adopted for attaining the audit objectives with reference to audit criteria was examination of:

- instructions and guidelines of the State Government and GOI issued from time to time;
- agenda and minutes of the meetings of the BODs and Committees constituted by the BODs;

- records relating to indents, production registers, tender and purchase order files, sales registers, sales invoices, stock registers, *etc.;*
- management information and internal control system; and
- interaction with the Management and issue of audit queries.

Audit findings

2.2.6 Audit findings, arising from the performance review on the working of the Company were issued (July 2007) to the Government/Company and were discussed (16 August 2007) in the meeting of the Audit Review Committee for State Public Sector Enterprises (ARCPSE). The Joint Secretary (Horticulture), Government of Himachal Pradesh and the Managing Director of the Company attended the meeting. The views expressed by the members have been taken into consideration while finalising the review.

Audit findings are discussed in the succeeding paragraphs.

Planning and budgetary control

2.2.7 Advance planning based on database maintained and market survey conducted from time to time is very vital for running an organisation efficiently, economically and effectively. Preparation of annual budget which is a quantitative financial expression of a programme of measure planned for a given period, forms an integral part of planning. The budget is drawn up with a view to plan activities for future and to make *ex-post-facto* checks on the results obtained. Timely planning/preparation of budget and analysis of the variations noticed during actual execution serve the purpose of internal control also.

In this regard, the following deficiencies were noticed:

- The Company did not plan its annual activities in consultation with the different departments (Horticulture, Agriculture, Forest and Public Works) of the State Government despite its dependence on them for sale of its products.
- The Annual Business Plan and Resources Forecast (BPRF) were not being prepared before commencement of the financial year. Hence, Audit was unable to determine the growth which the Company wanted to achieve during the year and whether the Company was able to sustain the same. Annual Budgets and targets were prepared (April-July) on the basis of performance during the previous years.
- The Company neither maintained data base nor conducted field/market survey to see market trends.

The targets fixed and actual achievements thereagainst during the last five years ended 31 March 2007 were as under:

(Rupees in crore)

Particulars	**2002-03**	**2003-04**	**2004-05**	**2005-06**	**2006-07** **(Provisional)**
Manufacturing units					
Target of sales	11.16	11.16	11.16	6.48	4.25
Achievement	7.31	5.50	4.53	3.53	3.31
Shortfall (-) Excess (+)	(-) 3.85	(-) 5.66	(-) 6.63	(-) 2.95	(-) 0.94
Percentage shortfall	34.50	50.72	59.41	45.52	22.12
Trading Units					
Target of sales	16.49	16.52	18.30	19.61	25.66
Achievement	11.80	12.24	12.05	17.54	21.82
Shortfall (-) Excess (+)	(-) 4.69	(-) 4.28	(-) 6.25	(-) 2.07	(-)3.84
Percentage shortfall	28.44	25.91	34.15	10.56	14.96

Source: Compiled from the relevant records of the Company.

It may be observed from the above details that:

- The Company was not able to sustain the targets fixed for sales in manufacturing and trading units in all the years.
- The shortfall in manufacturing units ranged between 22.12 and 59.41 *per cent* during 2002-03 to 2006-07.
- Instead of taking remedial actions to increase the sales of manufactured items, the Company reduced the target by 41.94 *per cent* in 2005-06 and 61.92 *per cent* in 2006-07 as compared to the targets of 2004-05, indicating a negative growth. Even the reduced targets were not achieved.
- Similarly, the Company could not achieve the sale target of trading items in all the years. Thus, there was negative growth on both sides.

The Government stated (September 2007) that the Company planned its activities well in advance in consultation with different departments and annual targets were fixed on the basis of data base and survey of market. The reply is not tenable as the Management did not produce record relating to meetings held with different departments, data base maintained and conducting of market survey.

Capital structure

2.2.8 The authorised capital of the Company was Rs.15 crore consisting of 15 lakh shares of Rs.100 each. As against this, the paid-up capital of the Company as on 31 March 2007 was Rs.11.80 crore, subscribed by the Government of Himachal Pradesh (Rs.9.84 crore) and GOI (Rs.1.96 crore).

Failure to avail benefit of disinvestment scheme of Government of India

2.2.9 In accordance with the scheme for disinvestment, the GOI communicated (March 1994) to the State Government that it would pass on its shares (Rs.1.96 crore) for a token consideration (Rs.1,000) to the State Government in case the Company had negative net worth. In case of positive net worth on the basis of latest available accounts, it was to offer its shares at a price 25 *per cent* less than the book value. As the net worth of the Company was negative during 1993-94 and 1994-95, the BOD approved (June 1994) the disinvestment proposal of the GOI. As no follow up action was taken to avail the benefit under the scheme, the State Government was deprived of the benefit of acquiring share capital of Rs.1.96 crore for a token consideration of Rs.1,000. This lapse was pointed out in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000. The State Government informed (September 2003) the COPU that Rs.1,000 sent to the GOI were received back (May 2003) and the Company was asked (May 2003) to submit statement of realisable assets and liabilities along with value. The State Government further informed the COPU that the detail of expenditure involved for valuation of realisable assets and liabilities were being analysed (September 2003) by the Engineering Cell of the Company. Audit observed that no further action has been taken in the matter so far (September 2007).

The Government replied (September 2007) that the Company was not interested to get the benefit of receipt of equity of the GOI by paying Rs.50 lakh in cash because the Company would have incurred a loss of Rs.50 lakh without getting any tangible cash transfer of Rs.1.96 crore which would have been only on paper. The reply is not tenable as the Company had negative net worth during 1993-95 and it was required to pay only Rs.1,000 and not Rs. 50 lakh. The State Government would have acquired equity of Rs.1.96 crore at a cost of Rs.1,000 only.

Borrowings

2.2.10 Long-term and short-term loans of Rs.1.11 crore and Rs.1.60 crore along with interest of Rs.1.40 crore and Rs.1.63 crore were overdue for payment to the State Government since 1983-84 and 1990-91 respectively at the end of March 2007. Besides, a sum of Rs.76.68 lakh (including interest of Rs.36.68 lakh) borrowed from the Ministry of Food Processing Industries, GOI was also outstanding as on 31 March 2007. The Company was not able to repay the loans due to its poor financial health.

Financial position

The accumulated loss of Rs.4.61 crore as on 31 March 2003 increased to Rs.9.25 crore as on 31 March 2007, which had partially eroded the paid-up capital of Rs.11.80 crore as on that date.

2.2.11 The financial position of the Company for the last five years ended 31 March 2007 is given in **Annexure-XII.**

Annexure-XII shows that accumulated loss of Rs.4.61 crore (31 March 2003) increased to Rs.9.25 crore (31 March 2007). The accumulated loss of Rs.9.25 crore had partially eroded the paid-up capital of the Company of Rs.11.80 crore as on 31 March 2007. So far, the Company has not drawn any long term growth or economy plan to reduce the accumulated loss.

Un-utilised grant

2.2.12 The Company had not utilised grant of Rs.9.97 lakh received (1991-92) from the State Government for Poultry Development Scheme. In reply to the review on the working of the Company incorporated in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000, the Government informed (September 2003) the COPU that the Company proposed to utilise/refund the grant in future, but no further action has been taken so far (August 2007) to utilise the grant or refund the amount.

The Government stated (September 2007) that the grant would be utilised whenever up-gradation of machinery in the Feed Unit would take place. The reply is not tenable as the Company had given a similar reply to the COPU in September 2003 and the grant was still (September 2007) lying unutilised since its receipt (1991-92).

Diversion of funds

The grant of Rs. 50 lakh received from the State Government was diverted for other than the intended purpose.

2.2.13 The Company received (July 1997) Rs.50 lakh from the State Government to procure potatoes between 7 to 23 July 1997 under the Potato Support Scheme to provide remunerative prices to agriculturists. The Company neither procured potatoes nor refunded the amount. It diverted the amount for payment of salary and wages (Rs.2.42 lakh) and discharge of liabilities (Rs.47.58 lakh). The Director of Agriculture had been demanding (October 1999) the return of the amount along with interest @ 18 *per cent per annum* which worked out to Rs.90 lakh (July 2007). The fact of diversion of funds was also pointed out in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000. The State Government replied (September 2003) to the COPU that the Company had submitted a proposal for adjusting the amount against Rs.1.28 crore recoverable from the Agriculture Department on account of expenses incurred by the Company in running workshop of the Department at Bhangarotu and the matter was under correspondence. Audit, however, noticed (May 2007) that the State Government had refused (November 2006) to accept the proposal and the Company was liable to pay the amount of Rs.50 lakh along with interest of Rs.90 lakh up to July 2007 to the Agriculture Department.

The Government stated (September 2007) that in case, the Agriculture Department does not agree to pay Rs.1.28 crore to the Company, the Company would approach the State Government for conversion of Rs.50 lakh into equity. The reply is not tenable as the State Government has already refused to adjust the amount against the amount being shown as recoverable from the Agriculture Department.

Working results

2.2.14 The working results of the Company for the last five years ended 31 March 2007 are given in **Annexure-XIII**. It would be seen from the Annexure that the Company had been continuously incurring losses year after year and it incurred loss of Rs.5.33 crore during the last five years which was due to the following reasons:

- Under utilisation of installed capacity of plants (paragraphs 2.2.15, 2.2.17, 2.2.19 and 2.2.21 *infra*);
- Non-closure of trading units continuously running in losses (paragraph 2.2.24 *infra*);
- Payment of idle wages (paragraph 2.2.26 *infra*).

The Government stated (September 2007) that the operational loss had been reduced from Rs. 1.95 crore in 2005-06 to Rs.1.26 crore in 2006-07 and it further projected to reduce it to Rs.18.37 lakh in 2007-08. The reply is not tenable as the Company has not formulated any concrete plan so far (September 2007) to reduce the operational loss to Rs.18.37 lakh in 2007-08.

Manufacturing activities

Pesticides Formulation Plant

Productions and sales performance

2.2.15 The Company set up a Pesticides Formulation Plant at Parwanoo at a cost of Rs.70.40 lakh. It obtained (February 1983 to August 1998) registration from the GOI for manufacturing 39 products of insecticides and pesticides under the Insecticides Act, 1968.

The licensed capacity of the plant and utilisation there against during the last five years ended 31 March 2007 was as under:

Year	**2002-03**	**2003-04**	**2004-05**	**2005-06**	**2006-07**
Licenced Capacity					
Liquid (KL)	250	250	250	250	250
Dust and wettable dry powder (WDP) (MT)	1,150	1,150	1,150	1,150	1,150
Actual Production					
Liquid (KL)	28.18	-	-	-	-
Dust and wettable dry powder (WDP) (MT	70.5	97.3	163.5	95.7	47.1
Percentage utilisation					
Liquid	11.27	-	-	-	-
Dust and wettable dry powder (WDP	6.13	8.46	14.22	8.32	4.10
Sales					
Targets (Rs. in crore)	2.50	2.50	2.50	2.50	0.92
Achievement (Rs. in crore)	1.08	0.29	1.87	0.95	0.43
Percentage achievement	43.20	11.60	74.80	38.00	46.74

Source: Compiled from the relevant records of the Company.

From the details in the above table and scrutiny of other connected records of production and sale of pesticides revealed as under:

- Capacity utilisation of the plant in respect of liquid formulation was 11.27 *per cent* during 2002-03. There was no production thereafter as neither Hindustan Antibiotics Limited placed purchase orders on the Company nor there was demand for the same from the State Government Departments. It was noticed that the State Government Departments were purchasing their requirement of liquid formulation from private firms.

- The capacity utilisation in respect of WDP ranged between 4.10 and 14.22 *per cent.*

- Low capacity utilisation resulted in payment of idle wages of Rs.5.80 lakh as the plant remained idle for 578 days during the last five years ended 31 March 2007.

- Besides, the Company also incurred an avoidable expenditure of Rs.5.20 lakh on account of fixed charges of electricity over and above the contract demand actually utilised by the plant.

Against the targeted loss of Rs.17.71 lakh, the Pesticides Formulation Plant incurred loss of Rs.75.72 lakh during 2003-07.

- Against the targeted loss of Rs.17.71 lakh, the plant incurred loss of Rs 75.72 lakh during the last five years ended 31 March 2007.
- The Production Manager of the plant was heading the Pesticides Division at the Head Office since June 2003. He had been looking after the activities relating to marketing of bio-fertilizers and bio-pesticides also. The in charge of quality control was looking after the production in the plant. The posting of the Production Manager at the Head Office mainly to look after marketing of bio-fertilizers/bio-pesticides, the work which should have been done by one of the Marketing Officers, deprived the Company of the benefit of his supervision in the plant on a sustained basis.

2.2.16 The low capacity utilisation was mainly due to poor marketing and lack of patronage by the State Government. Even though the four products[&] of the Company got tested (2003-04) by the Agriculture and Horticulture Departments of the State Government from Himachal Pradesh University of Horticulture and Forestry, Solan and Himachal Pradesh University of Agriculture, Palampur for bio-efficiency were found to be of standard quality, the Agriculture and Horticulture Departments of the State Government procured only 70.02 MT of pesticides/insecticides valuing Rs.1.43 crore from the Company against their total procurement of 120.11 MT and 536.56 MT of pesticides/insecticides valuing Rs.2.64 crore and Rs.10.17 crore respectively during the last five years ended 31 March 2007. The quantity procured by these departments from the Company was only 10.66 *per cent* of their requirement of pesticides/insecticides. The rest of the material was purchased by these departments from private parties who were on rate contract with the State Government (429.05 MT valued at Rs.7.51 crore) and from the producers who supplied the material under their brand names (157.60 MT valued at Rs.3.87 crore). This resulted in supply of the material to the consumers at higher cost of Rs.1.39 crore as the rate contract material was supplied after adding five *per cent* commission (Rs.45.30 lakh) to be shared equally by the department concerned and the Company and the material purchased under the brand names was costlier (Rs.94 lakh) in comparison to the rate at which the Company could have supplied after formulating the same in its plant. This was despite the fact that the Company and the private firms use the same technical material purchased from the same source and repack the same after processing as per the requirement under the Insecticides Act, 1968. Thus, the Company could have supplied the entire quantity without compromising the quality. But the Company failed to convince the Agriculture and Horticulture Departments and the consumers about the quality and cheaper cost of its products. The Company remained dependent on the Government Departments for orders and did not formulate any market strategy to sell its products in the open market through its 20 trading units located within the State.

[&] *Mencozeb 75% Wettable powder (WP), Carbendazim 50% WP, Dodine 65 % WP and Copperoxychioride 50 % WP*

The Government stated (September 2007) that the Company had established (April/May 2007) contact with Hindustan Antibiotics Limited (HAL) and buyers in Rajasthan. They hoped to break even or make nominal profit in 2007-08.

Cattle and Poultry Feed Plants

Production performance

2.2.17 The Company set up two Cattle and Poultry Feed plants at Parwanoo and Jachh at a cost of Rs.3.84 lakh and Rs.9.85 lakh respectively**.** The details of installed capacity, actual utilisation there against and percentage utilisation of capacity during the last five years ended 31 March 2007 are as under:

Particulars	**2002-03**	**2003-04**	**2004-05**	**2005-06**	**2006-07**
Parwanoo					
Installed capacity (single shift) (MT)	4,800	4,800	4,800	4,800	4,800
Actual production (MT)	3,839	4,379	3,548	3,568	3,119
Percentage utilisation	79.98	91.23	73.92	74.33	64.98
Jachh					
Installed capacity (single shift) (MT)	2,400	2,400	2,400	2,400	2,400
Actual production (MT)	73	1,559	1,754	887	1,043
Percentage utilisation	3.04	64.96	73.08	36.96	43.46

Source: Compiled from the relevant records of the Company.

Scrutiny of details in the above table and other connected records in respect of production and sale of cattle and poultry feed revealed as under:

- The percentage of capacity utilisation at Parwanoo plant during 2002-03 to 2006-07 ranged between 64.98 and 79.98, except in 2003-04 when it increased to 91.23 due to receipt of maximum orders for cattle feed from the Department of Animal Husbandry under drought relief scheme.
- The percentage of capacity utilisation at Jachh plant ranged between 36.96 and 73.08 during 2003-04 to 2006-07 and it was only 3.04 in 2002-03 due to closure of the plant for six months for renovation.
- The Company depended mainly on orders from the State Government for sale of cattle and poultry feed. The percentage of sales in the open market to total sales in respect of Parwanoo and Jachh plants ranged between 32.65 and 55.80 and 1.13 and 13 respectively during the period 2002-03 to 2006-07.

- The low capacity utilisation resulted in payment of idle wages of Rs.5.11 lakh and avoidable extra expenditure of Rs.4.64 lakh on account of fixed charges for contract demand of electricity over and above the actually availed contract demand.

The Government stated (September 2007) that the sales could increase only if the Company had working capital to purchase the raw material and establish retail distribution network. It further stated that it was not possible to stop payment of wages and incurring of other fixed expenditure. The reply is not tenable as there was nothing on record to show that the Company had made efforts to generate working capital. So far as establishing of retail distribution network is concerned, the Company is already having 20 trading units in the entire State and the same could have been used for retail distribution.

Non-production of fish feed

The Company was not producing fish feed though it modernised its plant at Jachh at a cost of Rs.17.29 lakh.

2.2.18 The annual requirement of fish feed in the State was 65 to 70 MT. The Fisheries Department of the State provided (2002-03) Rs.15 lakh to the Company for modernising its existing feed plant at Jachh for production of trout fish feed. The Company was required to supply the trout fish feed to the Fisheries Department as well as to the fish farmers of Kullu and Mandi districts through its sale outlets. Audit observed (May 2007) that after modernising (September 2002 to May 2003) the plant at a cost of Rs.17.29 lakh at Jachh by keeping it closed for eight months, the Company was still not producing trout fish feed (August 2007).

The Government stated (September 2007) that the Company was ready to manufacture and sell fish feed through its branches provided confirmed orders were received from the Fisheries Department. The reply is not tenable, as per commercial practices for marketing its products the Company itself should enquire about the requirement of fish feed from the Fisheries Department/fish farmers of the State and supply accordingly. This way the Company could have also reduced its losses by increasing the capacity utilisation of its plant at Jachh and using the idle manpower. Further, the Fisheries Department had requested (September 2006 and June 2007) the Company to start regular production of trout fish feed and make the same available through its sale outlets. The Department had conveyed (June 2007) its annual requirement of trout fish feed to the extent of 20-25 tonnes.

Production performance of Implements Factory

2.2.19 The implements factory set up in October 1982 at a cost of Rs.67.83 lakh caters to the demand for agricultural implements from the State Government Departments and private consumers. The installed capacity, actual production there against, percentage utilisation of installed capacity, targeted and actual sales during the last five years ended 31 March 2007 is given in **Annexure-XIV.**

Scrutiny of the details revealed as under:

The capacity utilisation of Implements Factory decreased from 32.21 *per cent* in 2002-03 to 7.13 *per cent* in 2006-07 due to lack of demand for its implements.

- The percentage utilisation of capacity decreased from 32.21 in 2002-03 to 7.13 in 2006-07.
- The shortfall in achievement of sales increased from Rs.36.03 lakh in 2002-03 to Rs.71.19 lakh in 2005-06. Instead of making efforts to increase the sales, the Company decreased the target of sales from Rs.90 lakh to Rs.50 lakh in 2006-07 but in this year also there was shortfall of Rs.23.36 lakh in sales.
- The losses suffered by the unit increased from Rs.16.45 lakh in 2002-03 to Rs.35.29 lakh in 2006-07. The total loss suffered by the unit during these five years amounted to Rs.1.51 crore.

2.2.20 Scrutiny of records revealed (May 2007) that the high incidence of loss was on account of low capacity utilisation due to dependence on the Government Departments for sale of implements, poor marketability, high operating cost, competition from private parties and avoidable extra expenditure of Rs.2.41 lakh on account of fixed charges for contract demand of electricity over and above the actually availed contract demand. The same state of affairs was pointed out in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000. The State Government in their reply to COPU stated (September 2003) that efforts were made to transfer the factory to Himachal Road Transport Corporation (HRTC) but the HRTC did not agree and the Company was exploring other alternatives. It was, however, observed that the Company had not explored other alternatives so far (May 2007). Further, though the State Government had assured (June 1995) to procure 50 *per cent* requirement of the Government Departments from the Company, there was nothing on record to show that the Company was meeting their requirement to that extent.

The Government stated (September 2007) that the Company had approached the State Government for revival of the plant. The decision of the Government is, however, awaited (September 2007).

Honey Processing Plant

Production performance

2.2.21 Reference is invited to paragraph 2A.8.1 (iv) (a) and (b) of the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000 wherein performance and purchase of honey processing plant at Kandrori was commented upon. It was stated in the para that against the projected profit of Rs.0.61 crore, the plant had incurred loss of Rs.0.46 crore during the last four years ended 31 March 2000. The loss was mainly due to inadequate marketing arrangements. The Government stated (September 2003) to COPU that the Company had made arrangements for sale through Bajaj Sevashram Limited, Udaipur and sold 8,784.40 Kgs honey during 2000-01 and 22,464 Kgs during 2001-02. The Company was also exploring marketing of honey through other dealers.

Scrutiny of records revealed (May 2007) that during the last five years ended 31 March 2007, the plant incurred loss of Rs.46.34 lakh against the sale of Rs.15.16 lakh made during this period. The Company had projected loss of Rs.58.89 lakh against the projected sale of Rs.1.01 crore. The details are given in **Annexure-XV**. The capacity utilisation ranged only between 1.63 and 6.76 *per cent* as against the projected 80 *per cent* capacity utilisation in the revised (March 1997) Techno Economic Feasibility Report. As analysed in audit, low capacity utilisation was mainly on account of inadequate working capital and consequent non-procurement of raw honey, low storage capacity of 35 MT against the requirement of 90 MT to reach at break even, non-availability of cold storage to keep Hidroxge Methyl Furfural of raw honey at acceptable temperature level and inadequate marketing. The Company also did not explore marketing of honey through other dealers as promised to COPU.

Keeping in view the ground realities, the BODs decided (September 2003) to close down or to lease out the plant. The State Government, however, decided (December 2003) to revive the plant and the services of Vice Chancellor, Himachal Pradesh University (an expert in bee keeping) were sought for this purpose. The Vice Chancellor submitted (January 2005) his report and suggested ways and means to revive the plant. His suggestions had not been implemented so far (September 2007).

The Government stated (September 2007) that various market strategies were being adopted for sale through different agencies and interested parties. A proposal had been sent to the GOI for 50 *per cent* subsidy on total project cost of Rs. 55 lakh required for up-gradation of the plant and a 100 MT capacity cold storage would be established. The reply is only an after thought as during the last five years under review, the Management had not made such efforts.

Avoidable extra expenditure

The purchase of raw material in off season resulted in incurring of an avoidable extra expenditure of Rs.54.35 lakh.

2.2.22 Maize, de-oil rice bran (DRB), rice polish, soya flaks, wheat-bran and de-oil mustard oil cake (DMOC) are the main foodgrain ingredients for manufacture of cattle feed. These foodgrains are available at cheap rates in the market in two seasons of the year *i.e.* April to June and September to November.

Test check of records of cattle and poultry plant at Parwanoo revealed that during the last five years ended 31 March 2007, the Company purchased (through open tenders) major portion of foodgrains during off season when the rates were higher as compared to the rates during the season as indicated below:

		Quantity purchased					
Sr No	**Food grains ingredient (MT)**	**During season (MT)**	**Off season (MT)**	**Total (MT)**	**Percentage of quantity purchased during off season to total purchase**	**Per MT higher rates paid during off season as compared to rates in season (Rupees)**	**Avoidable extra expenditure (Rs in lakh)**
1	Maize	428.14	1,798.97	2,227.11	80.78	542.53	9.76
2	Rice Polish	242.00	458.72	700.72	65.46	688.87	3.16
3	De-oil Rice Bran (DRB)	1,868.41	7,067.34	8,935.75	79.09	636.73	45.00
4	Soya Flaks	290.71	378.07	668.78	56.53	1,917.63	7.25
5	Wheat Bran	149.66	118.08	267.74	44.10	813.00	0.96
6	De-Oil Mustard oil cake (DMOC)	912.30	1,963.52	2,875.82	68.28	697.22	13.69
	Total	**3,891.22**	**11,784.70**	**15,675.92**	**75.18**		**79.82**

Source: Compiled from the relevant records of the Company.

It would be seen from the above that the Company purchased 75.18 *per cent* of its total requirement of foodgrains during off season resulting in incurring of avoidable extra expenditure of Rs 79.82 lakh. For the purchase of 11,784.70 MT foodgrains during off season, the Company required Rs.4.62 crore at the rates prevailing during the season. Even if, the Company had arranged the above amount by availing overdraft from the banks for nine months, the Company could have saved Rs.54.35 lakh after adjustment of interest of Rs.25.47 lakh payable to the banks.

The Government stated (September 2007) that there was no loss on account of procurement of raw material during off season as the Company was recovering full cost of feed. The Company neither had funds to built up stock of raw material nor intended to built such inventory due to short shelf life of raw material. The reply is not tenable as purchase of raw material during season at cheaper rates would have increased the profit of the Company. The contention of the Management that the raw material had short shelf life is also not tenable, as the suppliers from whom the Company purchases raw material during off season purchase the same during season and store the same for sale in off season.

Trading activity

Trading in items not covered in the Memorandum and Articles of Association

2.2.23 As stated in paragraph 2.2.1 *supra*, the Company was running 20 trading units and one petrol pump through out the State which deal in sale of trading items such as cement, iron and steel, bitumen, tyres and tubes,

The sale of items not covered in the objectives increased from 33 *per cent* in 2002-03 to 71 *per cent* in 2006-07.

batteries, petrol and diesel**,** *etc*. which are, however, not covered in its objectives as included in the Memorandum and Articles of Association (MAA) of the Company. The sale of items not covered in the objectives accounted for 33, 36, 42, 62 and 71 *per cent* of the total sales during the last five years ended 31 March 2007. The Company was concentrating more on trading of items not covered in its objectives resulting in lack of overall focus in achievement of main objectives. Though the trading activities not covered in the objectives were approved (June 1995) by the BODs, formal amendment in the MAA was yet to be carried out (September 2007). This was also pointed out in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000. The Government stated (September 2003) to the COPU that the proposed amendments to be incorporated in the MAA of the Company were being examined. No further action had, however, been taken so far (September 2007), which was indicative of an indifferent attitude of the Management.

The Government stated (September 2007) that the above mentioned items except bitumen are incidental and ancillary to the attainment of main objects and hence there was no need to carry out amendment in the MAA. The reply is not tenable as the items which are traded are not incidental or ancillary to the attainment of the main objectives of the Company.

Performance of trading units

Ten trading units were continuously incurring losses and loss suffered during the period 2002-07 by these units amounted to Rs.1.59 crore but the Management did not take any action to improve their working or to close these units.

2.2.24 Scrutiny of records (May 2007) relating to the trading units revealed as under:

- Out of 20 trading units and one petrol pump, only two units (Shimla and Chamba) earned profit of Rs.40.83 lakh during the last five years ended 31 March 2007.
- Nine[*] units earned profit of Rs.40.01 lakh and loss of Rs.76.32 lakh in different years during 2002-07.
- Remaining 10[$] units were continuously incurring losses. Their loss during the last five years ended 31 March 2007 amounted to Rs.1.59 crore.
- Out of above 10 units, six[**] units were under the direct supervision of a Deputy General Manager stationed at Dharamshala. Their loss during the last five years amounted to Rs.1.04 crore.
- The Management did not take action to improve the working of the trading units or to close these units.

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[*] *Jachh, Parwanoo, Rampur, Morinda, Mandi, Kullu, Bilaspur, Solan and Nalagarh*

[$] *Kumarsain, Rohru, Nagrota, Paonta Sahib, Dharamsshala, R.O. Morinda, Jawalamukhi, Amb, Una and Hamirpur*

[**] *Dharamshala, R.O. Morinda, Jawalamukhi, Amb, Una and Hamirpur*

Sundry debtors

2.2.25 As per credit policy of the Company, credit sale to the Government Departments was permissible subject to the condition that amount was recovered in the same financial year. For credit sale to private parties, officers allowing such credit were to be held responsible for recovery of the dues.

Position of debtors as on 31 March 1999 was commented upon in the Report of the Comptroller and Auditor General of India (Commercial) for the year ended 31 March 2000. The Government stated (September 2003) to COPU that the position of debtors was being monitored on monthly basis and efforts were being made to reduce the outstanding position to the bare minimum. Despite above assurance to the COPU, the Management did not make efforts to recover the old debts and as a result the debts increased from Rs.2.21 crore (March 1999) to Rs.4.28 crore (31 March 2007).

Age-wise position of the outstanding debts of Rs.4.28 crore as on 31 March 2007 was as under:

Outstanding for	**(Rupees in lakh)**
Less than one year	359.74
More than one and less than three years	14.19
More than three years	54.30
Total	**428.23**
(Government Departments: Rs.403.40 lakh, Private: Rs.24.83 lakh)	

Source: Compiled from the relevant records of the Company.

Scrutiny of records relating to sundry debtors revealed as under:

- Debts of Rs.3.41 crore as on 31 March 2002 increased to Rs.4.28 crore as on 31 March 2007.
- Debts of Rs. 8.13 lakh pertaining to private parties were outstanding for recovery for more than three years.
- Debts of Rs.32.34 lakh pertaining to the Government Departments were outstanding for over 3 to 15 years. The reasons for debts remaining outstanding for such a long period were not analysed/brought to the notice of BODs.
- Recovery of debts of Rs.37.68 lakh (Government:Rs.23.85 lakh and private parties: Rs.13.83 lakh) were considered doubtful of recovery by the Management. Debts of Rs.13.83 lakh pertaining to private parties were under litigation as on 31 March 2007.
- There was no practice of receiving confirmation of outstanding balances from the debtors before preparation of annual financial statement each year.

- The responsibility for not recovering the amount of credit sale to private parties was not fixed on the officers concerned as per the credit sale policy of the Company.

The Government stated (September 2007) that special drive was being launched to recover the outstanding debts and action would also be initiated against those who fail to recover private debts within the stipulated time. The reply is not tenable as the effectiveness of measures being taken would be known in due course and the Company failed to honour the commitment made to COPU in September 2003 regarding efforts to reduce the debts to bare minimum.

Manpower

Manpower management

2.2.26 The Company has not fixed norms for deployment of staff with reference to actual work load in the field units and at the Head office.

During 2003-07, the Company paid Rs. 1.10 crore to 21 employees who were in excess of the requirement.

The Management assessed (2001-02) 80 employees as surplus in the Company. As against this, the Company was able to reduce the strength of surplus manpower to 21 as on May 2007 through absorption in other Government departments/voluntary retirement scheme. During 2003-07, the Company paid Rs.1.10 crore to above 21 surplus employees.

The Government stated (September 2007) that the number and salary of excess employees was notional as the list of surplus employees was prepared in view of critical financial position of the Company. The reply is not tenable as the list of surplus employees furnished to the State Government could not be treated as notional and the Company was able to reduce the strength of surplus employees from 80 in 2001-02 to 21 up to May 2007.

Undue benefit to daily wage workers

2.2.27 As per instructions of the State Government (April 2000), daily wage workers of all Government Departments/Undertakings having completed eight years of continuous service as on 31 March 2000 were eligible for regularisation. It was observed (May 2007) that the Managing Director of the Company regularised (March 2003) eleven daily wage workers who had completed only two to four years of continuous services as on 31 March 2000 in violation of the State Government instructions. This resulted in extension of undue benefit of increase in salary and wages by Rs.12.98 lakh to these workers.

The Government stated (September 2007) that the BODs was a competent authority which works like Government for employees of the Company. The reply is not tenable as the MD of the Company took the decision and even BODs cannot go beyond the instructions of the State Government.

Irregular promotions

2.2.28 The BODs decided (June 1996) that for promotion of officers of Class A category in future, the Departmental Promotion Committee (DPC) would consist of Commissioner-cum-Secretary (Horticulture), MD and General Manager of the Company. It was noticed (May 2007) that the MD filled (May 2002 and May 2004) four Category 'A' posts without the approval of the DPC resulting in non-compliance of the decision of the BODs.

The Government stated (September 2007) that the decision (June 1996) of the BODs remained inoperative and the promotion was made as per notified R&P Rules. The reply is not tenable as during April 1997, the promotions of some other officials were made by the DPC as per decision (1996) of the BODs.

2.2.29 The MD changed (September 2006) the initial cadre of a Laboratory Assistant appointed (December 1981) as Clerk with retrospective effect and allowed him promotions up to the level of Marketing Assistant (June 2004). The promoted official had neither the required experience of seven years as Senior Clerk nor he had qualified the Departmental Promotion Test as provided in the Recruitment and Promotion Rules of the Company. As per instructions (January 2003) of the State Government, such matters were required to be referred to the Committee consisting of Finance Secretary, Administrative Secretary, Secretary-*cum*-Director Institutional Finance (DIF) and MD and thereafter approval of the BODs was required. This resulted in violation of the State Government instructions and undue favour of Rs.8.08 lakh to the employee on account of increase in salary and wages up to March 2007.

The Government stated (September 2007) that as per R&P Rules, the MD. was fully competent to change the cadre. Government was silent whether this could be done retrospectively for duties not performed as clerk. The reply is not tenable as the same is at variance with the instructions of the State Government and the concerned employee was not having the required experience.

Marketing

2.2.30 Marketing is the backbone of an organisation. Production also corelates with the marketing efforts to avoid locking up of funds in inventory. There were eight Marketing Officers (MOs) and six Marketing Assistants (MAs) in the Company who were posted in different branches/units. Scrutiny of records revealed that the Company had not framed any marketing policy for selling its products. It never held any seminar of prospective consumers with a view to educating them about the suitability and benefit of buying the Company's products. The Management also did not fix any targets of sale to be achieved by the above MOs and MAs. Though, the annual incidence of their salary and wages worked out to Rs.45.65 lakh, there was nothing on record to show that they procured any orders for sale of Company's products.

Besides, two MOs and two MAs were deployed (between November 1991 and April 2007) in other Government Departments on deputation basis and they could be repatriated to the Company at any time by the borrowing departments. The Company has not established any distribution/dealership retail net work for sale of its products and its trading units are located only in cities and towns.

The Government stated (September 2007) that the Marketing Assistants were not MBAs experienced in marketing. They were from cadre of Clerks. The reply is not tenable as it was for the Company to recruit suitable MOs and MAs or to give training to the MAs who are from the cadre of Clerks.

Corporate governance

2.2.31 Corporate governance is the system by which companies are directed and controlled by the Management in the best interest of the shareholders and others stake holders ensuring greater transparency and better and timely financial reporting. The BODs is responsible for governance in the Company.

In this regard, Audit observed the following:

- As against four meetings of the BODs to be held in a year under Section 285 of the Companies Act, 1956, the Company held three meeting each during 2002-03, 2004-05 and 2005-06.
- The Financial Commission-*cum*-Secretary (Finance) did not attend any meeting held during 2003-04 and 2005-06.
- One non-official Director did not attend any meeting during 2002-03 and 2005-06. Similarly, two other non-official Directors during 2003-04 and 2004-05 and three non-official Directors during 2006-07 did not attend any meeting.
- The budget proposals prepared by the Company were not submitted to the BODs for consideration.
- The BODs did not discuss measures to increase production and sale. Thus, there was lack of policy initiative relating to production, marketing and improvement in working.

The Government stated (September 2007) that the audit view point had been noted and being advisory in nature, the same would be placed before the BODs for information.

Internal control

2.2.32 Internal control is an integral part of the process designed and effected by the Management of an organization to achieve its specified objectives ethically, economically and efficiently. It helps in creating a reliable financial and management information system (MIS) besides facilitating effective decision making. Internal control system is most effective when it is built into the entity's infrastructure and is an integral part of the essence of the organisation. Internal audit is an important part of the internal control system. In order to streamline the working procedure and exercise effective internal control upon its activities, the organisation should have functional and internal audit manuals.

Audit noticed (May 2007) the following deficiencies in the internal control system:

- The Company did not have a well defined MIS. It did not maintain a centralised database. Information source and information use centers were also not identified to effectively channelise the flow of information for decision making.
- The information and statistics available in regard to periodical progress in manufacturing and trading activities *vis-à-vis* laid down performance targets were inadequate and insufficient to identify the areas of deficiency for suggesting remedial measures.
- The Company had no system of performance appraisal of activities with a view to assessing the extent to which it was able to promote and achieve its main objectives.
- The Company also did not have a system of periodical reporting through monthly/quarterly/six monthly returns to the top management indicating factual position of working and recommendations/follow-up required.
- The Company had not prepared functional and internal audit manuals so far (September 2007). Non-preparation of manuals even after more than three decades of its existence was indicative of lackadaisical approach of the Management towards developing an efficient and effective working procedure and internal control system.
- The internal audit was being got conducted year after year from a firm of Chartered Accountants at a fee ranging between Rs.0.60 lakh and Rs.0.70 lakh per year. The report is submitted yearly. Though, the reports were generally submitted to the MD, there was no system to monitor the follow-up action on the reports. The Company did not maintain a consolidated record to show the number of observations settled as a result of follow-up and those remaining outstanding for want of action.
- Though, the duties of the internal auditors, *inter alia*, contain review of policies, procedures and internal control system of the Company yet their reports never contained any observation in this regard.

The Government stated (September 2007) that the Company had maintained centralised database and different matters were regularly reported to the BODs. A system of monthly reporting on performance of units was in vogue and reports and suggestions of internal auditors were considered appropriately.

The reply is not tenable as during the currency of review as well as in the meeting of ARCPSE, the Management did not produce to Audit any database for scrutiny. The actions proposed to be taken to improve the working were also not placed before the BODs. The Company could not produce detail of observations made by the internal auditors during the period of review and which were outstanding for compliance as on 31 March 2007.

Acknowledgement

2.2.33 Audit acknowledges the co-operation and assistance extended by the Company and officers of the State Government at various stages of conducting the performance audit.

Conclusion

The Company did not draw any long-term plan for achievement of its main objective of promoting agro-based industries in the State. It did not plan annual activities well before the commencement of financial year in consultation with State Government Departments, which were the main buyers of Company's products. Out of five production units, three units were incurring losses continuously on account of low capacity utilisation due to lack of adequate demand from the State Government Departments and inability of the Company to market its products in the open market. Un-economic operation of trading units and surplus manpower also contributed to losses of the Company. Management information and internal control systems were deficient and the system of appraisal of performance was non-existent.

Recommendations

- **The Company should focus on its main objectives. It needs to plan annual activities well before the commencement of financial year in consultation with State Government Departments, which are the main buyers of Company's products.**
- **Capacity utilisation of production units should be increased and concerted efforts should be made to sell its products in the open market.**
- **The working of loss making trading units should either be improved or these should be closed without further delay.**
- **Management information and internal control system needs to be strengthened and the system of appraisal of performance put in place.**
- **It should formulate an aggressive production and marketing policy.**

2.3 Information Technology Review of Computerised Reservation of Hotel Rooms in Himachal Pradesh Tourism Development Corporation Limited

Highlights

The Company introduced (1993) software computerised Central Hotel Reservation System for Hotel reservation facility at Central Reservation Office, Shimla. The software was got modified (September 2000) as web enabled software from National Informatics Centre.

Some of the important findings as a result of audit are mentioned below:

No policies relating to computerisation have been framed by the Company.

(Paragraphs 2.3.8)

There was delay in adopting various changes made by the Company from time to time in the rent rates, *etc*. in the computerised system resulting in faulty reports.

(Paragraphs 2.3.11 and 2.3.13)

The Company failed to recover cancellation charges of Rs.2.42 crore from the customers who reserved the rooms in the hotels at nil advances due to defect in the System.

(Paragraph 2.3.18)

The Company completed (March 2007) Local Area Network (LAN) in three units at a cost of Rs.10.88 lakh but as the System had no provision to upload the data from the online hotel reservation system; the basic purpose of LAN was defeated.

(Paragraph 2.3.20)

Introduction

2.3.1 The Himachal Pradesh Tourism Development Corporation Limited (Company) was incorporated in September 1972 as a wholly owned Government Company with a view to providing a complete package of tourism services including accommodation, catering, transport facilities and sports activities.

The Company introduced (1993) computerised 'Central Hotel Reservation System' (CHORES) for hotel reservation facility only at Central Reservation Office (CRO), Shimla. The CRO reserved the hotel rooms on the basis of requests obtained from various marketing offices/hotels/tourist information offices/general sales agents/travel agents and sent the daily reservation charts of reservation for each hotel at least three days in advance using Company's vehicles, public transport system, fax, telephones, *etc.* To overcome various shortcomings of the existing software, the Company got the CHORES modified (September 2000) as web enabled software from National Informatics Centre (NIC).

As on 31 March 2007, the Company had 55 hotels (Hotels, *Yatri Niwas*, Cottages/Log huts) having 1006 rooms and 10 marketing offices for hotel reservation.

Organisational set-up

2.3.2 The management of the Company vests in the Board of Directors consisting of 12 Directors including the Chairman (Chief Minister is the ex-officio Chairman) and Managing Director (MD) who is the Chief Executive. The MD is assisted in his day to day activities by the General Manager. The management of marketing offices/hotels/cafes is under the charge of Deputy General Managers/Assistant General Managers/Senior Managers/Managers and Assistant Managers.

Senior Accounts Officer (IT) is the overall in charge of computerisaion in the Company.

Objectives of computerised reservation

2.3.3 The main objectives of switching over to computerised reservation (Internet) from central reservation office are to:

- decentralise the hotel reservation from the centralised booking;
- provide easy access to the customers/tourists to know about the availability position of accommodation in the Company's hotels;
- make the reservation process easier at marketing offices/hotels within and outside the State;
- keep proper track of reservation and cancellation made by the customers and to help them;
- reduce the gap of communication between the customers and the Company's hotels where the customers actually check in;
- increase occupancy in Company's hotels; and
- provide facility to the customers to know about the various tourist spots and Company's properties in the State web site of the Company.

Scope of audit

2.3.4 The IT Audit of records relating to reservation of hotel rooms of five[1] out of 10 marketing offices and 12[2] out of 55 hotels/*yatri niwas*/log huts in the State was conducted during March - May 2007.

Audit objectives

2.3.5 Objectives of the IT Audit were to evaluate:

- reliability, integrity and authenticity of the data;
- availability of the data;
- safety and security of data; and
- IT environment in various booking centers and availability of related documentation.

Audit criteria

2.3.6 The audit criteria used for the IT audit were:

- The IT best practices; and
- The business rules for the charging of fares.

Audit methodology

2.3.7 The methodology adopted for attaining audit objectives with reference to audit criteria was as under:

- Review of agenda and minutes of meeting of the Board of Directors (BODs) and Committee constituted by the BODs.
- Study of the computerised system.
- Before commencing audit, the audit objectives, criteria and scope were discussed (March 2007) with the General Manager (HPTDC) in an entry conference. The audit findings were discussed (May 2007) with the Managing Director (HPTDC) in an exit conference.

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[1] *Marketing Offices: Chandigarh, Delhi, Kullu, Manali and Shimla*

[2] *Hotels: Holiday Home, Shivalik, Peterhoff, Kunzum, Manalsu, Log huts, Hadimba huts, Beas, Sarvari, Silvermoon, Castle Naggar and Himachal Bhawan*

Audit findings

General

There was no password, backup and Business Continuity Plan policy to ensure security of the System and data.

2.3.8 Though the company decided to go for computerisation in 1993, it has not yet framed any policies relating to computerisation. Some of the important policies which have not been formed include the 'Password policy', 'The Backup Policy', 'The Business Continuity Plan' and above all the company's IT strategy.

Test check of 17 units revealed that trained staff was deployed only in five units for handling advance reservation. In remaining 12 units, either the staff was not trained or computers were not available for online reservation. In the absence of adequate on the job training, users were not able to handle different modules.

The Management accepted (May 2007) the audit observations and stated that efforts would be made to provide in-house training to the officials.

Non-conducting of post implementation review

2.3.9 Post implementation review is necessary to evaluate as to whether the System meets the envisaged requirements. Audit noticed (May 2007) that the Company had not conducted post implementation review on the working of the software.

System shortcomings

Lack of accounting module in the system

The System had no module for accounting purpose.

2.3.10 The System had no accounting module. The System was being utilised for electronic blocking of rooms, confirmed reservation of rooms *vis-à-vis* the availability position of accommodation which was electronically processed by the System. The System also did not produce daily/monthly returns for inter-unit adjustment of reservation amount and calculation of commission of General Sales Agents or Travel Agents. This was being done manually by the accounts officials.

The Management stated (May 2007) that the matter regarding providing of accounting module was under consideration and the needful would be done in the next phase.

System did not show effective rates

2.3.11 Though, the customers can view discount offers, the System gives actual tariff instead of the discounted rates when he enters the reservation menu and selects for reservation in hotel where discounted tariff is applicable.

It was noticed in audit that:

- the System did not display the room rent with European Plan (EP)[3] and Continental Plan (CP)[4] distinctly;
- in six[5] hotels, the System failed to ensure the collection of Modified American Plan (MAP)[6] charges during May and June 2006 as the System did not display the MAP based tariff of rooms. It only reflected room rent on EP or CP basis which was fed in the System;
- the Company decided (November 2005) to allow 30 *per cent* discount on room rent to senior citizens in all hotels during season and additional 10 *per cent* over and above the discount announced in off season. Similarly, the privilege card holders were entitled to 20 *per cent* discount on the charges for accommodation, food and beverages in addition to the discount announced by the Company from time to time subject to a maximum of 50 *per cent*. During test check of computerised system for reservation of rooms in hotels, it was noticed that the System did not contain the facility of providing discount on reservation of rooms in hotels to senior citizens and privilege card holders at the time of on line reservation.

The Management stated (May 2007) that the Company offered various discounts from time to time and the same were shown under a separate icon “Special Offer” and that the matter would be considered for rectification during up-gradation of the System.

Excess deduction of commission

2.3.12 The Company started (May 2006) on-line advance reservation of hotel rooms (through credit card) through HDFC bank at 5 *per cent* commission from May 2006 and 3.5 *per cent* from January 2007 which is deducted by the bank itself.

During audit of computerised reservation system in Marketing Office, Shimla, Audit noticed that the System did not display the discounted rates of rooms rent for monsoon and winter seasons with the result the customers made payment as per actual rent through credit card and commission was deducted by the HDFC on the actual rent instead of on discounted rent received by the Company in its hotel. This resulted in excess deduction of commission of Rs.0.15 lakh by HDFC bank on discount of Rs.3.22 lakh (allowed between May 2006 and March 2007) and resulted in loss to the Company to that extent.

The Management stated (May 2007) that online advance reservation was started from May 2006 through HDFC bank whereas the System was developed in September 2000. It was further stated that the matter would be considered for rectification during up- gradation of the System.

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[3] *European Plan means tariff of room*

[4] *Continental Plan means tariff of room includes breakfast*

[5] *Silvermoon, Sarvari, Beas, Rohtang Manalsu, Kunzum and Holiday Home.*

[6] *Modified American Plan means tariff of room includes breakfast and lunch or dinner*

Generation of faulty reports

The reports generated through the System were incorrect and misleading.

2.3.13 Test check of reports extracted from the System for 1 April 2005 for occupancy of all hotels revealed that the percentage of occupancy of some hotels was shown as negative.

Various reports extracted from the System revealed that the booking office-wise business reports reflected Rs.158.08 crore as net amount of advance reservation for 2005-06 whereas the final accounts of the Company reflected the total room rent income including booking through the System for the same year as Rs.15.84 crore only. Thus, the reports generated through the System were incorrect and misleading.

The Management stated (May 2007) that the error had been brought to the notice of the NIC and the same would be corrected in the software of hotel reservation system.

Faulty generation of customer Identification number (ID)

2.3.14 The System generates unique customer ID for each customer at the time of reservation. The test check of data, however, revealed that the System generated 58 duplicate customer IDs. Such situations may create problem to the Company as well as to the customers. If two customers have the same customer ID and one of them approaches for cancellation of reservation, the System may cancel the reservation of other customer too who has the same customer ID.

Test check of the data revealed that the System had not generated 1,089 customer ID numbers during September 2000 to March 2007. The missing customer IDs might have posed problem to the Management as well as to the customers at the time of check in.

The Management stated (May 2007) that such mistakes happened sometimes due to technical snag in web server.

Change Management

Less realisation of advance room rent

2.3.15 The Company revises tariff of hotel rooms from time to time after analysing the occupancy or after providing extra facilities in the accommodation. The Company generally revises tariff from 1 April each year.

During test check of reservation of rooms through computer System in three[7] hotels, it was noticed that the tariff of rooms in the System was not linked with the date from which the tariff was effective and changed tariff simply over wrote the existing rates. This resulted in less realisation of advance room rent

[7] *Beas, Kunzum and Sarvari*

of Rs.0.06 lakh during 2007-08 for reservation made up to March 2007. It deprived the Company of the benefit of enhanced advance room rent to the above extent.

The Management stated (May 2007) that the difference of room rent was collected by the concerned unit at check out time and that the matter would, however, be considered for rectification during up-gradation of the software.

Failure to club different category of rooms through the System

2.3.16 There are different categories of rooms in Company's hotels. The Company changes the category of rooms from time to time after providing extra facilities.

During test check of the System of online hotels reservation, it was noticed that after deletion of one category of rooms from the System and merger of the same with other category, the rooms of earlier category remained in the data file though they were shown as merged with the other category in the master file as the System updates the added category of rooms. Thus, the deleted category of rooms is available in the merged category for further reservation.

To cope with the problems, the booking officials first extracted the reservation chart of that hotel and after merging/deleting the one category of rooms and again confirmed this reservation in the System in the merged category at nil advances manually. This should have been done through the System to avoid clerical mistakes.

Other points of interest

Non-releasing of unoccupied reservation from the System

The System does not release unoccupied reserved rooms. Thus, the Company fail to reserve such rooms even though the same are not occupied.

2.3.17 As per Company's policy, 100 *per cent* of the room rent for the first day and 50 *per cent* for subsequent days are to be received for advance reservation of rooms in Company's hotels.

Test check of arrival charts extracted from the System of different hotels for 2006-07 revealed that confirmed reservations were made at nil advances for regular/ selected customers but the customers failed to check in the hotels on the scheduled dates. The concerned hotels failed to cancel the reservations from the System where such reservations were made for more than two days. Due to non-releasing of such reserved rooms from the System, the Company could not reserve these rooms for other customers.

The table below indicates the position of reservations made against nil advances during 2002-07 and consequences thereof:

Particulars	2002-03	2003-04	2004-05	2005-06	2006-07
Total transaction reserved	19,051	23,579	26,426	29,638	35,903
Total transaction cancelled	3,692	4,155	2,366	2,568	4,199
Transaction cancelled out of reservation made against nil advances	2,928	3,460	2,219	2,441	2,910
Transaction cancelled out of reservation made as per applicable rates	764	695	147	127	1,289
Percentage of cancellation out of reservation made against nil advances to total cancellation	79.31	83.27	93.79	95.05	69.30
Percentage of cancellation against reservation made as per applicable rates to total cancellation	20.69	16.73	6.21	4.95	30.70

The percentage of cancellation of reservations made against nil advances to total cancellation ranged between 69.30 and 95.05 which was very high in comparison to percentage of cancellation against reservation made as per applicable rates to total cancellation. It indicated that the persons who were allowed to reserve rooms against nil advances took undue advantage of the facility and cancelled the reservation at will without keeping in mind the loss to the Company.

Loss of cancellation charges

2.3.18 As per Company's policy for cancellation of reservation, 80 *per cent* of the advance is refunded in case request for cancellation is received before seven clear days or more before the scheduled date of check in. If the request for cancellation is received between four to six days before the date of check in, 50 *per cent* of advance is refunded. No refund is given if the request for cancellation is received less than four days before the date of arrival.

Due to reservation of rooms at nil advances, the Company could not recover cancellation charges of Rs.2.42 crore.

Audit noticed (May 2007) that in case of those customers who reserved the rooms in hotels at nil advances but cancelled their reservation prior to the scheduled date of checking in the hotel, the Company could not recover the cancellation charges of Rs.2.42 crore at the minimum rate of 20 *per cent* from the customers due to reservation made at nil advances as detailed below:

Particulars	2002-03	2003-04	2004-05	2005-06	2006-07	Total
Reservation amount of internet booking (in lakh)	369.53	438.67	519.33	598.88	754.12	2,680.53
Number of units (rooms) reserved	36,137	44,156	46,850	52,669	64,835	244.647
Reservation amount per unit (Average) (rupees)	1,023	993	1,109	1,137	1,163	5,425
Units cancelled of nil advance (numbers)	7,553	12,467	24,041	28,111	36,211	1,08,383
Reservation amount to be taken (in lakh)	77.27	123.80	266.61	319.62	421.13	1,208.43
Minimum reservation amount to be cancelled at the rate of 20 per cent (in lakh)	15.45	24.76	53.32	63.92	84.23	241.68

It was noticed that the cancellation of reservation was being done manually instead of through the System. The System should have automatically calculated the refund admissible and released the reservation. Audit further noticed that though the booking officials cancelled the reservation from the System, the amount refunded was not entered in the System in most of the cases. Thus, the reports generated for analysing the booking office-wise business for the specific period did not reflect the correct reservation (net) amount and defeated the very purpose of generation and analysis of various reports.

Test check of expected arrival chart of customers of seven[8] hotels/huts for March 2007 also revealed that the booking officials of various marketing offices/hotels/tourist information centres reserved the rooms through the System at nil advances. The customers neither cancelled the reservation nor checked in the hotels on the scheduled date resulting in loss of cancellation charges of Rs.3.81 lakh.

Failure to use transport reservation system software

2.3.19 The web site of the Company shows the accessibility to the particular place and also the transport facility available in Company's vehicles but the reservation in the Company's vehicles is not available online. The Company also got developed (March 2002) a transport reservation software at a cost of Rs.0.75 lakh from National Informatics Centre Services Inc.

[8] *Holiday Home, Peterhoff, Kunzum, Hadimba Cottage, Rohtang Manalsu, Log Huts and Beas*

(A Government of India Enterprise under NIC) for advance booking in Company's vehicles to increase the occupancy.

The transport reservation software developed at a cost of Rs.0.75 lakh was not being used.

During test check of records of transport reservation system, it was noticed that advance booking of Company's vehicles was being done manually even after lapse of five years of the development of software for reservation resulting in wasteful expenditure of Rs.0.75 lakh. The Head Office of the Company had issued (July 2003) three computers to transport wings for transport reservation but the same were being utilised by the transport wings for typing and accounts works.

The Management stated (May 2007) that as the booking of passengers in contract carriages during off season was less than the seating capacity of the buses and it had to ply light vehicles instead of Company's buses, the System could not be implemented. The reply is not acceptable as the Company was aware of this situation prior to development of the software.

Non-inter-linking of the local area network with online hotel reservation system

2.3.20 The Company completed Local Area Network (LAN) in three[9] units up to March 2007 at a cost of Rs.10.88 lakh and work of LAN in two[10] units was in progress.

Audit noticed (May 2007) that the System had no provision to upload the data from the online hotel reservation system. The inter unit adjustment of advance rent of reservation was also being fed manually by the accounts section in the System. Thus, the basic purpose of LAN to make the work easy, reducing manual intervention was defeated.

The matter was reported to the Company/Government in July 2007; their replies are awaited (September 2007).

Conclusion

Though, the Company had done a tremendous job of creating web site and providing facility of online reservation in its hotels, there were various defects in the System such as overwriting of existing tariff on revision of tariff, non-linking of tariff to date, packages like various discounts and MAP, AP and New Year tariff. The System also did not generate the desired reports *viz*. permits issued to customers, daily cash statement, linking with hotel LAN system, *etc*. which were necessary for effective management information system and internal control.

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9 *Hotel Holiday Home, Head Office and Hotel Peterhoff*
10 *Himachal Bhawan, Chandigarh and Hotel Pinewood, Barog*

Recommendations

- **The Company should connect each hotel with one another and also with the Corporate Office for effective monitoring and internal control.**

- **The Company should review the System with a view to incorporate all the business rules for tariff charging of hotel rooms. This would avoid loss to the Company on account of non-realisation of advance room rent.**

- **The Company should incorporate accounting module in the System to facilitate generation of reports for inter unit adjustment of reservation amount and calculation of commission of General Sales Agents and travel agents.**