

Chapter IV

Contract management

BOT-Toll and BOT-Annuity agreements.

In BOT-Toll agreement, the Concessionaire recovers the investment along with return from the tolling rights for a predetermined concession period. The grant which is given to fill the viability gap of the project is released periodically in proportion to the equity brought in by the Concessionaire. To keep track of the grant released, Concessionaire's funding and the revenue collected, escrow accounts are required to be opened under all BOT-Toll agreements. Under the BOT-Annuity agreement, investment is recovered through the predetermined annuity payments made by the Authority. The annuity payment commences after a predetermined date which is the stipulated date of completion of the project. In the event of delay in completion of the project, penalty is levied on the Concessionaire if the delay is attributable to the Concessionaire but the annuity commences from the predetermined date despite the delay. As these agreements are different from the traditional EPC contracts, framing of terms and conditions of the concession agreements and inclusion of relevant clauses to safeguard the financial interests of the Authority viz. sharing of surplus/profit in BOT-Toll agreements, recovery of savings in project cost due to deletion of items of work after the award of contract, operation of escrow account, penalty for delay in completion of the project attributable to the Concessionaire, etc., assume greater significance. Further, in respect of BOT-Annuity projects where the Authority collects the toll revenue, it has to ensure that there are no avoidable delays in the commencement of toll collection after completion of the projects.

4.1 Monitoring of project financing

The Authority should have an effective monitoring mechanism to ensure that the funds released for a particular project have actually been utilised for that project. This is achieved through the operation of escrow account by the Concessionaire. The other mechanism with the Authority is to appoint at its cost, another firm of Chartered Accountants as independent auditor to audit and verify the project finance. Audit noticed deficiencies in implementing the monitoring mechanism as discussed below.

4.1.1 Escrow account

As per the concession agreements for BOT-Toll projects, the Concessionaires were required to open an escrow account (EA) with a bank and all receipts and payments in respect of the project were to be routed through this account. The Concessionaires were required to forward monthly EA report within five days of the end of each month to the Authority. The terms and conditions of operation of the EA also required the bank to forward a copy of the account each to the Concessionaire, the Authority and the lenders. A review of such statements would provide insight into the utilisation of funds. Of the four BOT-Toll projects, Audit found that in respect of three projects, viz. Jaipur-Kishangarh, Satara-Kagal and Delhi-Gurgaon (BOT-Toll projects), the copies of the EAs were neither forwarded nor the Authority demanded the same. The urgency of periodic review of the EA statements was

illustrated by the report of the Financial expert, who was engaged by the Independent Consultant to scrutinise the accounts of Delhi-Gurgaon project, which pointed out (February 2005) that the assessment of efficient utilisation of project funds was hampered due to the following deficiencies in the operation of the EA:

- equity infusion of Rs.100 crore was not routed through EA.
- operations in the EA were not in line with the approved quarterly/ annual budgets.
- the actual expenditure pattern did not conform to the cash flow priority laid down in the escrow agreement.
- disbursal program under escrow arrangement was not in conformity with the drawal schedule of the loan agreement.

The Authority which initially stated that it had directed the Satara-Kagal Concessionaire to maintain EA in line with the agreement contradicted it by stating that the latter was already in operation since commencement of the project. The Authority further stated that it had directed the Concessionaire of Delhi-Gurgaon project to maintain EA in line with the concession agreement.

The reply does not address the core issue of monitoring the project funding and its utilisation through the EA statements which is an important instrument of monitoring timely flow of funds from different sources and their utilisation for the project activities.

4.1.2 Independent auditors

As per clause 28.4 of the concession agreement, the Authority had the right but not the obligation to appoint at its cost another firm of Chartered Accountants (independent auditor) to audit and verify all those matters, expense, costs, realisations and other assurances which the statutory auditors of the Concessionaire, are required to do, undertake or certify. However, in respect of none of the projects covered in this review, did the Authority appoint independent auditors. Though the appointment of such independent auditors was not mandatory, it had become desirable in the case of the Satara-Kagal project to safeguard the Authority's financial interests, as discussed below.

- The amount of grant was fixed at 40 *per cent* of the project cost. Even after more than one year of commercial operation (December 2007), the Authority had not determined the actual cost of the project, although the Authority had so far released Rs.233.10 crore as grant. In the absence of the information on the actual amount incurred in the project, the correctness of the grant released could not be ensured (also refer para 4.4).
- Further, as per the concession agreement, the Authority was to receive 50 *per cent* of the surplus in any financial year of commercial operation (refer para 4.4). The Authority had neither demanded nor the Concessionaire furnished the details of surplus till date (March 2008).

The Authority stated that the independent auditor for Satara-Kagal project has since been appointed. In respect of Palsit-Dankuni project, the Authority stated that the audit

observation was noted for future guidance. For Tambaram-Tindivanam and Delhi-Gurgaon projects, the Authority stated that it would exercise the option of appointing independent auditors on need or case-to-case basis.

4.2 Levy of penalties

Audit observed that the Authority did not levy penalty for deficient/non-performance despite the fact that there were relevant clauses in the concession agreements. Further the clauses of the concession agreements for recovering cost of the deleted items and remuneration paid to the IC were not implemented as elaborated below.

4.2.1 Penalty for delay in completion of the project

- As per the concession agreement, Satara-Kagal project was to be completed on 2 August 2004. The Concessionaire, however, obtained provisional completion certificate for the first 86 Km. of the road on 22 October 2005 and for the balance 46.76 Km. on 24 May 2006. The Concessionaire sought extension of time by 18 months but the IC recommended extension for nine months only i.e. up to 2 May 2005. Thus there were delays of 24 weeks and 55 weeks for the first and second sections, respectively (over and above the extension of time recommended by the IC) in obtaining provisional completion certificate. Audit observed that as per the provisions of the concession agreement, the Authority was entitled to levy a penalty of Rs.2.11 crore for the delay in completion of the project. The Authority, however, had not taken any action to recover this amount from the Concessionaire so far (February 2008). The Authority stated that the delay in completion of work was attributable to Government agencies and the total concession period would remain unaltered. The reply was not tenable as the reasons attributed by the Authority for the delay were all the responsibility of the Concessionaire as per the agreement. Further non-alteration of concession period is not relevant to levy of penalty for delay in completion.
- As per the concession agreement, the commencement date of Panagarh-Palsit project was 21 June 2002 and the scheduled completion date was 20 December 2004. The project, however, was completed on 9 June 2005. The delay of 171 days in completing the project was attributed by the IC to the Authority and other external factors not under the control of the Concessionaire. Audit noted (March 2007) that nine items valuing Rs.5.60 crore were deleted from the scope of work. The proportionate 9 days required for completion of the deleted items of work were not considered either by the Authority or IC. This simple omission of 9 days meant a penalty loss of Rs.2.73 crore for the Authority which was recoverable from the Concessionaire. The Concessionaire was also given 91 days extension of time for the delay in handing over site. Audit observed that these 91 days included 20 days of delay prior to the project commencement date. The delay in handing over site prior to the commencement date could not be a ground for extension of time. As such, the extension of time for delay in handing over the site would be justified for 71 days only. This excess allowance of extension of time for 20 days resulted in non-levy of penalty of Rs.6.02 crore on the Concessionaire.

The Authority in its reply did not give explanation for allowing extension of 91 days instead of 71 days as pointed out by audit.

4.2.2 Penalty for non-completion of the punch-list items

The Concessionaire was given a provisional certificate to allow commencement of commercial operations in Satara-Kagal project subject to the condition that the punch-list items were to be completed within 120 days from the date of issue of provisional certificate. Audit observed that the Concessionaire had not completed the punch-list items (February 2008) and as per the provisions of the concession agreement, the Authority is entitled to levy a penalty of Rs.1.89 crore for delay in completion of punch-list items. Audit, however, observed that the Authority had not recovered any penalty from the Concessionaire.

The Authority stated that the penalty for non-completion of punch-list items would be computed and levied on the Concessionaire as per the concession agreement before issue of final completion certificate.

4.2.3 Penalty for non-achieving milestones

As per concession agreement provisions of BOT-Toll projects, the Authority was entitled to recover penalty for non-achievement of individual milestones on the due dates and if the project was completed within the overall time schedule, the amount so recovered would be paid back to the Concessionaire without interest. In Jaipur-Kishangarh project, there were delays in achievement of individual milestones even though the project was completed within the overall scheduled date. Audit observed that the Authority did not recover Rs.75.90 crore for non-achievement of individual milestones. By failing to recover this amount on due dates, the Authority lost the interest it would have earned up to the date of refund. The Concessionaire had also agreed (March 2005) to pay the interest at the rate of SBI-PLR plus two *per cent*. However, the Authority had not claimed Rs.3.77 crore as interest from the Concessionaire.

The Authority admitted that the Concessionaire did not achieve two milestones and after detailed examination, IC calculated Rs.34.26 lakh as the interest charges that would have been earned by the Authority. The Authority further stated that this amount has been deposited by the Concessionaire.

The reply is not tenable as the Concessionaire themselves agreed to pay penalty with interest at the rate of SBI PLR plus two *per cent*. Based on this a sum of Rs.3.77 crore should have been recovered from the Concessionaire whereas only Rs.34.26 lakh was recovered.

Similarly in Satara-Kagal project, Audit observed that the Concessionaire failed to achieve three individual milestones and the delay ranged from 16 to 51 weeks. The Authority, however, did not recover Rs.12.05 crore on account of penalty for non-achievement of individual milestones.

The Authority stated that the Concessionaire being a Maharashtra Government PSU, possibility of taking up the unresolved issues at Government level would be explored.

4.2.4 Share of IC's remuneration

As per concession agreement in respect of Satara-Kagal, the remuneration, cost and expenses of the IC were to be borne fully by the Concessionaire. The Authority was to make the initial payment to IC and the Concessionaire was to reimburse his share within 15 days of receiving such a statement of expenditure from the Authority. Audit found that the Authority could not recover Rs.8.79 crore (for the period from April 2002 to December 2006) from the Concessionaire due to failure in raising periodical invoices. Further, failure to raise monthly invoices for the reimbursement resulted in loss of interest of Rs.3.89 crore* to the Authority.

The Authority stated that the reimbursement of cost of IC would be adjusted against the outstanding grant (Rs.8.27 crore).

The fact, however, remained that the Authority failed to recover the remuneration paid by it to the IC from the Concessionaire as per provisions of the agreement.

4.2.5 Short recovery

As per Article 7.2 (h) of the concession agreement in respect of Tambaram-Tindivanam project, when change in scope of work leads to reduction in cost, the Authority shall deduct the amount equivalent to the reduction in cost along with interest as determined by the Authority based on the financing documents, in equal installments from the annuity. During execution of the project, construction of one flyover was deleted leading to a saving of Rs.21 crore as worked out by the IC. This amount would be recovered at the rate of Rs.70 lakh from the 30 half-yearly annuity payments. Audit observed that the Authority had recovered interest at 10.03 *per cent* instead of 12.67 *per cent* being the weighted average cost of debt based on the financing documents on the date of financial closure. Adoption of a lower rate of interest had resulted in an undue benefit of Rs.4.02 crore to the Concessionaire.

The Authority stated that the rate of 14.5 *per cent* was assumed by the Concessionaire for arriving at the amount of annuity whereas as per the concession agreement, the Authority shall deduct the amount equivalent to reduction in cost along with interest thereon at the weighted average rate. Accordingly, it was recovering interest at 10.03 *per cent* being the actual cost of borrowing by the Concessionaire.

The reply is not tenable as the concession agreement stipulated that the interest for the recovery of cost of deleted items would be at weighted average cost of debt based on the financing documents which was 12.67 *per cent* in the instant case.

4.3 Audit observed that the Authority did not incorporate a clause for recovery of penalty towards non-achievement of financial closure and target dates for individual milestones in BOT-Annuity projects. Audit also observed that there were instances of unintended benefits accruing to the Concessionaires due to absence of certain clauses in the agreements which would have protected the Authorities financial interests, as discussed below.

* Calculated at the rate of 12.5 *per cent per annum* for the period 2003-04 to 2007-08.

4.3.1 Financial closure

Financial closure is the date on which the financing documents providing for funding by the lenders become effective and the Concessionaire has immediate access to such funds. The Authority did not incorporate a clause for recovery of penalty for non-achievement of financial closure within a stipulated period in BOT-Annuity projects, although such a clause was incorporated in BOT-Toll projects. In the absence of a suitable penalty clause for not achieving financial closure on a given date, the Authority could not levy penalty for delay of seven and six weeks in Tuni-Anakapalli and Tambaram-Tindivanam projects, respectively.

The Authority stated that model concession agreement for BOT-Annuity projects was under finalisation and penal provisions for delay in financial closure and non-completion of punch-list items have been incorporated in the same.

4.3.2 Milestones

Audit noticed that unlike the concession agreements for BOT-Toll projects, the concession agreements in respect of BOT-Annuity projects did not stipulate target dates for individual project milestones, consequent penalty for non achievement of milestones, period within which punch-list items had to be completed and penalty for failure to adhere to the stipulated period. In the absence of such milestones in the agreements, the Authority could not monitor the progress of work against agreed/stipulated milestones and penalise the Concessionaires for non-achievement of required progress. Similarly, the Authority could not levy penalties on Concessionaires for failure to complete the punch-list items within stipulated time in respect of Panagarh-Palsit and Palsit-Dankuni projects.

The Authority admitted to non-provision of such clauses in the agreements.

4.4 Sharing of surplus

As per the concession agreement for Satara-Kagal project, the surplus* was to be shared equally between the Authority and the Concessionaire at the end of each financial year. The surplus was to be computed based on toll revenue actually collected and estimated expenses on operation and maintenance and cost of debt. Audit observed that the clause on sharing of surplus was not in the best financial interest of the Authority. In this particular case, though the project was completed in May 2006, the O&M contractor was appointed in May 2007 (also refer para 3.10). As per the agreement the estimated routine maintenance cost for the year 2006 was Rs.6.14 crore and this estimated cost would be set off against the revenue collected during the year, without any actual expenditure being incurred. Therefore, it was in the interest of the Authority to arrive at surplus based on toll revenue and the corresponding expenses actually collected/incurred. However, neither the Concessionaire paid any amount towards the Authority's share of surplus nor had he rendered relevant details for computation of the same to the Authority (December 2007).

* *Surplus being the excess of actual income over the estimated O&M expenses, expenditure on periodic maintenance, cost of debt service for any financial year and deficit, if any, for previous financial year.*

The Authority stated that at present, the concept of revenue sharing has been introduced in the model concession agreement instead of sharing of surplus.

4.5 Revenue management

4.5.1 Commencement of toll collection

In BOT-Annuity projects, the Authority was entitled to collect toll based on the toll notification issued by the GOI. It would therefore become imperative that to avoid revenue loss, the toll collection should start immediately after the project completion. The Authority issued (April 2003) a circular to all PIUs prescribing the procedure for getting toll notification issued by GOI. As per this circular, the concerned unit was to initiate preparations at least 150 days before the anticipated date of completion of project so that there was no delay in commencement of toll collection. Audit, however, noticed that in respect of all the four annuity projects test-checked, there were delays in commencement of toll collection due to delay in obtaining toll notification and synchronisation of two completed stretches, resulting in revenue loss of Rs.23.89 crore as detailed in *Annexure-4*.

The Authority stated that in Tambaram-Tindivanam project, delay in issue of toll notification was due to delay in completion of punch-list items and protest from local public over toll collection. The reply is not tenable as non-completion of punch-list items would not come in the way of commencement of toll collection and the delay was mainly due to failure in taking timely action.

For Tuni-Anakapalli project, the Authority stated that the delay in submission of toll fee notification was due to change in overall plan of toll plaza location and the length covered in each plaza. The reply is not tenable as delay of over four months in revision of overall plan was not justified.

For Palsit-Dankuni project, the Authority stated that the work of improvement of 2.899 Km. was given to a different contractor which delayed the completion of the project. The reply is not tenable as the delay was due to lack of planning in synchronising the completion of a very small stretch.

As regards Panagarh-Palsit, the Authority stated that for tolling, four laning only is not sufficient but the project should be substantially completed and safety measures should be in place. The reply is not tenable because the IC had given the provisional completion certificate in June 2005 after being satisfied that the road was substantially complete and safe for the road users. Hence, the delay in toll collection beyond June 2005 on account of safety and substantial completion was not justified.

4.5.2 Fixation of toll rates

The National Highways (rates of fee) Rules, 1997 provides the basis of fixing toll rates. The fee for projects involving conversion of existing two-lane of National Highways into four-lanes should not exceed the base capping rates at June 1997 prices and the fee fixed might be reviewed after every five years based on wholesale price index and fixed in multiple of rupees five. The Authority did not index the base rates with the latest Wholesale Price Index

available at the time of sending draft toll notification to the Ministry which resulted in fixation of lower toll rates and revenue loss of Rs.22.73 crore as detailed in **Table 10**.

Table 10: Fixation of lower toll

Sl. No.	Name of the project	Month of draft notification sent to Ministry	Month of WPI to be adopted	WPI actually adopted	(Rs. in lakh)		
					Loss of toll per month	Loss of toll till March 2008	Loss of toll till the next revision
1	Tambaram-Tindivanam	October 2004*	October 2004	2003-04	17.42	627.12	418.08
2	Tuni-Anakapalli	November 2004	October 2004	2003-04	14.64	512.40	366.00
3	Palsit - Dankuni	March 2005	February-05	2003-04	5.82	174.60	174.60
	Total					1314.12	958.68

The Authority stated that to avoid frequent change in toll rate, it had decided to use average annual WPI instead of monthly index and that if different WPI indices were used for different toll plazas, the chances of public resentment might be higher.

The reply is not tenable as the toll rates once fixed would be revised after five years only and any lower fixation would result in recurring revenue loss for the subsequent five years. The statement about public resentment is a matter of speculation. In fact toll rates for BOT toll projects are revised every year whereas the toll rates for annuity projects are revised every five years only.

4.5.3 Leakage in toll collection

The Authority started toll collection in Tambaram-Tindivanam project by engaging the services of M/s Tamil Nadu Ex-servicemen's Corporation Limited (TEXCO) with effect from 1 April 2005. Audit noticed (January 2006) that the category-wise vehicles passing through the toll plazas were not recorded by the collection agent and that the IC had not conducted monthly traffic audit from November 2004. The Chartered Accountants firm appointed in July 2005 by the Authority to check the collection of revenue also pointed out several deficiencies in toll collection such as vehicles crossing the toll plaza without paying toll, issuing multiple use tickets and monthly passes without mentioning the dates and vehicle numbers, absence of vehicle barriers in the toll plaza, etc. and estimated a toll revenue loss due to these deficiencies to be Rs.21.98 crore per annum.

The Authority stated that the security of TEXCO and other payments has been withheld and all revenue losses would be adjusted from those payments. Audit, however, observed that the payments due to TEXCO were Rs.88.39 lakh and much lower than the estimated revenue loss of Rs.21.98 crore.

*Date of completion

4.5.4 Revenue loss due to absence of toll plaza

As per the concession agreement for Panagarh-Palsit project, two toll plazas were to be constructed at Km. 519.400 and at Km. 554.600. During the execution of this project, these two toll plazas could not be constructed at the proposed locations due to construction of truck lay-by at chainage 554.600 and due to non-availability of land at Km. 519.400 as this land was owned by the Army authorities who refused to part with. The Authority decided to construct only one toll plaza and to locate the same at Km. 507 and approached Ministry for toll fee notification to collect toll at this location. The Ministry declined the proposal as the stretch between Km. 515 and 520 was only two-laned. Therefore, the Authority decided to utilise the toll plaza constructed at Km. 585.692 located in Palsit-Dankuni highway for collection of toll for Panagarh-Palsit project, obtained (July 2005) toll notification for collection of toll for Panagarh-Palsit highway (Km. 517.000 to Km. 581.000) and started collecting toll from August 2005.

Audit observed that the traffic entering Panagarh and going out before the toll plaza located in Palsit-Dankuni highway, used Panagarh-Palsit highway without paying any toll which resulted in loss of revenue. This would be evident from the fact that the actual monthly toll collections from the road users of this stretch during 2005 and 2006 were Rs.8.15 crore and Rs.23.51 crore, respectively against DPR projected revenue of Rs.18.01 crore and Rs.54.07 crore, respectively, resulting in combined revenue loss of Rs.40.42 crore during the period August 2005 to December 2006.

The Authority while accepting that there was no toll plaza in Panagarh-Palsit highway stated that the DPR toll revenue estimates could never be realistic due to various factors viz. return journey tickets, monthly passes, local concessions, exempted category etc. The reply is not tenable as the main reason for the huge difference between DPR toll projection and actual toll collection was due to the absence of toll plaza between the Panagarh-Palsit highway. The traffic could utilise the Panagarh-Palsit highway freely without payment of toll.

Recommendation No.7

The Authority should ensure that the agreement clauses relating to opening and periodical submission of escrow account and the appointment of independent auditors are complied with.

Recommendation No.8

The Authority should:

- (i) ensure commencement of toll collection through timely action to prevent loss of toll revenue and should ensure that the toll rates are fixed based on the latest available wholesale monthly price index;***
- (ii) ensure that agreement clauses relating to levy of penalty are implemented in spirit; and***
- (iii) incorporate penalty clauses for non-achievement of financial closure and individual project milestones.***