HUNDRED AND SECOND REPORT

PUBLIC ACCOUNTS COMMITTEE (1981-82)

(SEVENTH LOK SABHA)

CHITARANJAN LOCOMOTIVE WORKS—SURI TRANSMISSION AND REVERS IN GEAR BOXES FOR DIESEL SHUNTERS

MINISTRY OF RAILWAYS

(RAILWAY BOARD)

Presented in Lok Sabha on.......

Laid in Rajya Sabha on

LOK SABHA SECRETARIAT
NEW DELHI

April, 1982/Chaitra, 1904 (S)

Price: Rs. 3.00

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	MANIPUR	
38.	Shri N. Chaoba Singh, News Agent, Ramlal Paul High School Annexe, Imphal.	77
	AGENTS IN FOREIGN COUNTRIES	
39.	The Secretary, Establishment Department, The High Commission of India, India House, Aldwych, LONDON, W. C.—2.	59

CORRIGENDA TO 102ND REPORT OF THE PUBLIC ACCOUNTS COMMITTEE (SEVENTH LOK SABHA)

Page	Para	Line	For	Read
1	2	2	S	ST
2	3	9-10	July 1971 March 1972	July 1971 March 1972
2	3	10	1,97,501	1,97,601
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8	11	15	-	28.85
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45	Sl.No.7	last line	KTC	KPC
46	Sl.No.7	5	theri	their
47	Sl.No.8	1	and	had
49	Sl.No.12	6	suitable	suitably

CONTENTS

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**Ceased to be a member of the Committee consequent on his retirement from Rajya Sabha w.e.f. 2-4-1982.

INTRODUCTION

I, the Chairman of the Public Accounts Committee, as authorised by the Committee do present on their behalf this Hundred and Second Report of the Public Accounts Committee (Seventh Lok Sabha) on Paragraph 9 of the Advance Report of the Comptroller and Auditor General of India for the year 1979-80, Union Government (Railways) relating to Chittaranjan Locomotive Works—Suri Transmission and reversing gear boxes for diesel shunters.

2. The Advance Report of the Comptroller and Auditor General of India for the year 1979-80, Union Government (Railways) was laid on the Table of the House on 12 March 1981.

3. Audit Paragraph 9 deals with the supply of Suri Transmission and reversing gear boxes by M|s. Kirloskar Pneumatic Co. Ltd., Pune to Chittaranjan Locomotive Works for diesel locomotives. This firm is the only indigenous manufacturer of the aforesaid equipment. The Committee's examination has revealed that unjustified price increases were allowed to this firm from time to time. While the order placed in 1967 was for Rs. 2.20 lakhs per set, it increased to Rs. 3.18 lakhs in 1974 and to Rs. 5.73 lakhs in 1979. No cost examination had been conducted at the time of placing the orders nor had the firm at any time produced authenticated data to substantiate its demand for escalation in prices. In this Report, the Committee have expressed the view that no indigenous manufacturer should be allowed to take undue advantage of its monopolistic position to dictate terms in respect of prices of the equipment supplied by it and the Government should insist upon cost audit and authenticated data before agreeing to such escalation in costs. The Committee have also recommended that Government should determine its policy in regard to cases where it is found that a sole indigenous manufacturer of any equipment is found to be taking advantage of its monopolistic position and forcing the Government to agree to escalation in prices which are not justified.

4. The Committee (1981-82) examined paragraph 9 on the basis of the written information furnished by the Ministry of Railways (Railway Board). The Committee considered and finalised the Report at their sitting held on 16 April, 1982. Minutes of the sitting of the Committee form Part II of the Report.

5. For reference, facility and convenience the observations and recommendations of the Committee have been printed in thick type in the body of the Report and have also been reproduced in a consolidated form in Appendix II to the Report.

6. The Committee would like to express their thanks to the Ministry of Railways (Railway Board) for the cooperation extended by them in giving information to the Committee.

7. The Committee also place on record their appreciation of the assistance rendered by the Office of the Comptroller and Auditor General of India in the examination of this paragraph.

NEW DELHI;
April 17, 1982
Chaitra 27, 1904 (*Saka*)

SATISH AGARWAL
Chairman
Public Accounts Committee.

REPORT

CHITTARANJAN LOCOMOTIVE WORKS—SURI TRANSMISSION AND REVERSING GEAR BOXES FOR DIESEL SHUNTERS

Audit Paragraph

I. Introduction

1. The diesel locomotives (WDS4|WDS 4B), produced at Chittaranjan Locomotive Works (CLW) were, in the initial stages, provided with Suri Transmission (ST) and a reversing gear box (RGB) to enable working of the locomotives for both shunting and shuttle services, the transmission being hydraulic at low speeds and mechanical at higher speeds. Currently, the locomotives manufactured for shunting services are provided with hydraulic transmission (HT) only i.e. without the mechanical portion.

II. Procurement of transmission and gear boxes

2. In July 1967, the Ministry of Railways (Railway Board) decided that CLW should manufacture S and RGB for the 48th locomotive and onwards, requirements of the earlier ones having been arranged by import. Considering the heavy diversification programme of CLW and the limited time available to develop and manufacture these equipments, the Ministry of Railways (Railway Board) later advised (September 1967) CLW to obtain them from firm 'A'*, the only indigenous industry to manufacture HT and heavy duty gear boxes. Accordingly, CLW has been procuring these equipments since November 1967 from the sole manufacturer who later (July 1971) also obtained a licence for manufacture of ST.

3. The procurement by CLW was made after obtaining quotations on single tender basis (till 1976, when open tenders were invited but the technically acceptable offer was from firm 'A' only) and negotiating a price thereafter with the firm. The table below indicates the various orders for ST|HT and RGB placed during November 1967—November 1979, the prices negotiated, the value of the orders, the price increase over the last purchase price and the percentage thereof.

*M/s Kirloskar Pneumatic Co. Ltd., Pune.

Month of order	No of sets ordered	Price per set	Value of order (Rs in lakhs)	Increase over previous price	
				Amount (Rs.)	Percentage
November 1967	18 ST&RGB	2,20,183	39.63	..	..
March 1970	30 ,,	2,17,032	65.11		
November 1970	30 ,,	2,53,695	76.11	..	..
July 1971	50 ,,	2,71,306	135.65	17,610	6.9
July 1971	30 ,,	1,91,888	57.57		..
March 1972	30 ,,	1,97,501	59.28	..	..
March 1972	43 ,,	2,81,533	121.06	16,278	6.0
March 1974	31 ,,	3,18,000	98.58	36,467	13.0
May 1977	32 HT 32 RGB	4,12,150	131.89	94,150	29.6
April 1978	46 HT 40 RGB	4,27,210	179.43	15,160	3.7
December 1978 January 1979	24 HT 30 RGB	4,51,530	126.53	24,220	5 to 6
November 1979	39 HT 30 RGB	5,73,350	223.65	1,21,920	27.0
	TOTAL	1314.49			
Conversion cost of 50 sets (See* below)		47.40			
	GRAND TOTAL	1361.89			

*These orders, originally for supply of components, were converted (March/April, 1974) into orders for 50 complete sets allowing conversion cost of Rs. 94,809 per set over the price indicated above, the comparable price per set being thus Rs. 2,86,697 and Rs. 2,92,410 respectively.

NOTE: (1) The price for the first order of November, 1967 was settled on ad-hoc reference to the cost of imported ST and RGB (of para 9.4 below), poviding also for 5 per cent reduction in price for additional 30 sets, which was availed of in the next order of March, 1970.

(2) The price for the first two orders was inclusive of the cost of housings for ST and RGB; these formed free supply items by CLW for the subsequent orders except those of May 1977 and onwards, for which the price included the cost of housings for HT. For comparison purposes, the cost of housings and other free supply items as varied from time to time has been excluded from the price allowed for the various orders.

(3) The price for March, 1972 order in the above table is after reduction of Rs. 6,050 for deletion of certain components due to simplifying the ST by eliminating its mechanical portion.

4. The price (Rs. 2.2 lakhs) settled for the November 1967 order, exclusive of certain imported components (c.i.f. value: Rs. 0.95 lakh) supplied free by CLW, included about 30 per cent price preference over the contemporaneous cif cost (Rs 2.6 to 2.7 lakhs) of imported complete ST and RGB.

5. The price for the initial order was treated by the High Level Tender Committee (HLTC) as the base price for settlement of price for the subsequent contract taking into account escalation for wages, materials etc. over the previous contract as indicated by the firm and to the extent agreed to during negotiations. This procedure was followed while negotiating the subsequent contracts also even though the firm did not produce, at any stage, any authenticated data and/or documentay evidence to substantiate adequately its demand for the escalations. The alternative method of price fixation based on cost audit was not resorted to, as the HLTC felt (August 1973) that "it may adversely affect the interests of CLW in view of the high price rise during 1973 as well as the likely price rise during the next 2/3 years". In the absence of adequate data and/or documentary evidence in support of the escalations claimed, there was no means of verifying the reasonableness of the price demanded/agreed to for the various orders.

6. A review in audit of the prices fixed from time to time revealed that the price increases allowed on certain counts were not justified, as discussed below:—

(a) For November 1970 contract, the firm asked for an increase of Rs. 60,763 on the following counts and quoted a price of Rs. 2.57 lakhs.

(a) Increased cost of forgings	30,000
(b) Wage escalations	12,000
(c) Margin of Profit	18,763
Total:	60,763

After negotiations, increased of Rs. 57,358 was agreed to and the price was settled at Rs. 2.54 lakhs.

N.B.: The increase of Rs. 60,763 is not of the cost (Rs. 20,695) of housing included in the previous contract price (Rs. 2.17 lakhs) but forming free supply items by CLW for the November 1970 order.

Even presuming that the reduction of Rs. 3,405 accepted by the firm was in its profit margin, the latter amounted to Rs. 15,358 i.e. 36.5 per cent of the price increase of Rs. 42,000 on materials and wages. As against this, the profit margin adopted in the later tender deliberations was 10 per cent. On this basis, increase in profit margin of Rs. 4,200 only would have been jusfified as against Rs. 15,350 allowed in this order. HLTC had not reviewed this increase with reference to the margins allowed in the earlier contract.

The extra margin of profit amounting to Rs. 11,158 per set allowed, without establishing its reasonableness, involved an extra payment of Rs. 3.35 lakhs for 30 sets ordered in November 1970.

CLW stated (September 1980) that the assumption of 10 per cent profit by HLTC was only for the purpose of estimation and that the option of CLW as buyer was singularly restricted, as the firm was only established indigenous source for procurement.

As mentioned earlier, the profit element was actually reckoned at 10 per cent by HLTC in negotiating the prices with the firm. The plea that the option of CLW as buyer was 'singularly' restricted need not have prevented necessary examination to enable fixation of reasonable profit/price.

(b) During the negotiations (December 1971) for settlement of price for the March 1972 order, the firm asked for an increase of Rs. 16,278 over the price contracted in July 1971. This increase was justified by the firm on the grounds, *inter alia*, that it would have to incur inventory carrying charges on stockpiling of forgings necessitated by their procurement much ahead of the delivery schedule of ST and RGB. The HLTC accordingly allowed an inventory carrying charge of Rs. 4,603 per set (7.5 per cent of Rs. 61,376 being the cost of the forgings) and, in addition, financing charges at 10 per cent i.e. Rs. 460 on the inventory carrying charge. Since advance payment (25 per cent of the order) by CLW in terms of contractual provisions, according to the HLTC, could be utilised by the firm for advance procurement of the forgings, price increase in excess of that justified by the interest rate (6 per cent) on the advance was not warranted. The extra price increase (Rs. 920) allowed because of the interest differential of 1.5 per cent (7.5-6) of the cost of forgings plus the additional financing charge allowed (Rs. 460) resulted in the firm obtaining a fortuitous gain of Rs. 0.59 lakh at the rate of Rs. 1,380 per set for 43 sets ordered in March 1972.

(c) The price (Rs. 3.18 lakhs) allowed for the March 1974 order was higher than the last contract price (Rs. 2.82 lakhs) by Rs. 36,467 per set. This included an increase of Rs. 7,835 which was justified (August 1973) by the firm on the ground that one of its sub-contractors had offered a discount if the components were given to it (sub-contractor) in batches (5 nos.) instead of piece-meal, but that ordering in batches was not possible as it would involve extra cost. The team of Senior Scale Officers of CLW who visited (July 1973) the firm's works allowed Rs. 7,000 on this account but the HLTC conceded (August 1973) the increase of Rs. 7,835 without either spelling out the reasons for enhancing the amount recommended by the team of Senior Scale Officers or ascertaining the quantum of the discount offered by the sub-contractor. The firm had also declined to show any evidence or documents to establish this claim stating that it would "more or less tantamount to audit of books which had not been agreed to by them in principle". The increase (Rs. 7,835) allowed for the notional loss of discount was disproportionately high compared to the total cost (Rs. 16,655) of the portion of work relating to the two sub-contractors.

(d) The firm had also pointed out (August 1973) that the cost break up given during the earlier negotiations for the March 1972 order for forgings and other material processing etc. was not correct although the overall cost indicated then was correct. The cost of forgings was stated to be Rs. 60,000 as against Rs. 61,376 indicated for the March 1972 order and the current cost of about Rs. 64,000 per set. On this basis the HLTC allowed a price increase of Rs. 4,000 for the forgings without verifying the correctness of either the revised cost of forgings for the March 1972 order or the then current cost as stated by the firm.

The extra price increase of Rs. 1,376 (due to revision of the cost of forgings), conceded by the HLTC involved an additional payment of about Rs. 0.43 lakh for 31 sets ordered in March 1974.

(e) Another element of price increase (Rs. 3,000) allowed for the March 1974 order was in consideration of the change in the method of allocation of the cost of heat treatment shop by the firm on the ground that its earlier practice of charging one third of the shop cost to ST and RGB assembly was found to be not reasonable and correct, as more work was involved in this assembly than in the other activities of the shop. The HLTC considered the revised method reasonable without obtaining the details of the heat treatment shop cost structure, allocation system, etc., though promised to be furnished by the firm, and examining the reasonableness of the increase demanded. Ultimately, the firm furnished data showing only the reasons for the increase in heat treatment cost instead of the cost structure of the heat treatment shop and the method of cost allocation. The entire increase (Rs. 3000) on his account conceded by the HLTC, without adequate examination amounted to Rs. 0.93 lakh for 31 sets ordered in March 1974.

(f) For the order of May 1977, the firm initially wanted (December 1976) 36 per cent escalation over the last contract price on account of price increases over the period of 3-1|2 years since May 1973. After negotiations, the firm quoted a revised price of Rs. 4.12 lakhs representing an increase of about 30 per cent, which was considered reasonable by the HLTC as according to its assessment the price escalation since May 1973 till October/November 1976 had been about 31-32 per cent. As, however, the last contract (March 1974) price based on the quotation of May 1973 had been settled with adequate escalation to cover deliveries upto September 1976, it would have been appropriate to take into account escalation beyond September 1976 only and not from May 1973 for fixation of price for the subsequent order. The escalation of Rs. 76,500 (on prorata basis) for the period May 1973—September 1976 as allowed in the price lacked justification and involved financial implication of Rs. 24.48 lakhs for 32 sets ordered in May 1977.

(g) For the November 1979 order, the firm initially quoted Rs. 6.83 lakhs and explained the increase of Rs. 2.31 lakhs over the December 1978 contract price (Rs. 4.52 lakhs) as being due to increases in cost of raw materials, petroleum products, bought out components etc. and the likely increase during the currency of the contract but without furnishing itemwise details. On being asked by the HLTC during negotiations (September 1979) to evolve a price variation formula for itemising the increase asked for, the firm withdrew the price variation clause in its offer. It, however, offered a revised price of Rs. 5.73 lakhs, which though 27 per cent more than the last contract price, was agreed to by the HLTC without going into its reasonableness.

III. Delayed Ordering

7. By June 1970, the Ministry of Railways (Railway Board) had placed orders on CLW for manufacture of 179 diesel locomotives. The requirements of ST and RGB for 47 locos having been arranged by import, the balance 132 loco sets were left for procurement from the indigenous source. Against this, CLW ordered 78 sets on the firm upto November 1970. Order for 50 more sets was placed in July 1971 at Rs. 2.71 lakhs per set, i.e. Rs. 17,610 more than the price settled for the previous order of November 1970. The belated coverage of 50 sets thus resulted in extra expenditure of Rs. 8.81 lakhs.

8. CLW stated (September 1980) that ST/RGB sets for the locomotive order (60 nos.) placed by the Ministry of Railways (Railway Board) in June 1970 could not be covered in the contract of November 1970 as the lead time of five months was insufficient for ordering.

9. It may be mentioned that negotiations were conducted with the firm in July 1970, the tender finalised in September 1970 and the formal contract for 30 sets placed in November 1970. The requirements of ST/RGB for the locomotive order placed by the Ministry of Railways (Railway Board) in June 1970 could have, therefore, been included in the contract

of November 1970, by suitably phasing the delivery schedule, if necessary, to match the locomotive production programme.

10. For manufacture of ST|RGB in CLW, 30 sets of ST|RGB components were ordered in July 1971 at Rs. 1.92 lakhs per set, stipulating delivery between July 1972 and May 1973. Another order for 30 sets of components was placed in March 1972 at Rs. 1.98 lakhs per set for delivery by August 1974, although CLW had apprehended (February 1972) delay and teething troubles in establishing and proving the local assembly and manufacture of ST and RGB. Ultimately, both the component orders were converted (March|April 1974) into supply of completely assembled sets on the ground that diesel locomotives manufacture had been limited to 280 nos., the firm being allowed an extra Rs. 94,809 per set as conversion cost. In the context of the anticipated delay and teething troubles in establishing and proving local assembly of ST|RGB especially when the components due against the earlier order (July 1971) would have enabled CLW to develop local assembly, the second order of March 1972 was not warranted. The conversion of the March 1972 components order for 30 sets in April 1974 resulted in extra expenditure of Rs. 3.26 lakhs compared to what would have been payable if these had been initilaly ordered as complete sets.

11. The Ministry of Railways (Railway Board) decided (July-August 1971) to simplify the ST by eliminating its synchronising coupling and multiple plate clutch. Meanwhile, (July 1971), CLW placed an order for 30 sets of components for fulfledged ST. The subsequent ordering in March 1972 for components and complete sets was also for ST. Although the later orders were suitably modified (March|June 1973) to delete the synchronising coupling etc. (cost: Rs. 6,050), there was omission to amend the July 1971 component order price accordingly while converting it (April 1974) into supply of 20 complete sets resulting in avoidable expenditure of Rs. 1.21 lakhs.

IV. Summing up

(a) There was no means of verifying the reasonableness of the prices demanded|allowed for the various orders by up-dating the last contract price on the basis of the escalations asked for by the firm, without being supported by authenticated data.

(b) Price increase amounting to Rs. 28.85 lakhs conceded on the items detailed below did not appear justified. These increases would also have got built into the prices fixed for the later orders, in view of the procedure for price fixation followed. Accordingly the total financial implication of these increases would be Rs. 121.29 lakhs for the orders placed upto November 1979.

	Rs. in lakhs
(i) Extra margin of profit (Cf. para 9.6(a) (above)	3.35
(ii) Inventory carrying charges for advance purchase of materials covered by advance payments against the orders. (Cf. para 9.6(b) above)..	9.59
(iii) Extra price increase due to downward revision of the cost of forgings content by the firm. .. (Cf. para 9.6(d) above).	0.43
(iv) Escalation for about 3½ years already allowed in the previous contract and re-allowed in settling the price for the subsequent contract. (Cf. para 9.6(f) above).	24.48

(c) In addition, CLW incurred extra expenditure of about Rs. 13.28 lakhs due to:

(i) Delay in placement of orders (Cf. para 9.7 above) .	8.81
(ii) Conversion of component order into supply of complete sets (Cf. Para 9.10 above)	3.26
(iii) Omission to modify the purchase price consequent on the deletion of Suri transmission components (Cf. para 9.11 above)	1.21
	13.28

12. This para was issued to CLW on 13th November 1980, its reply is awaited (January 1981).

[Audit paragraph 9 of the Advance Audit Report of the Comptroller & Audit General of India for the year 1979-80—Union Government (Railways)].

13. The Audit para indicates that Chittaranjan Locomotive Works (CLW), which is a manufacturing unit under the Ministry of Railways (Railway Board), placed various orders on the firm M/s. Kirloskar Pneumatic Co. Ltd. Pune (KPC) for supply of Suri Transmission (ST)/hydraulic transmission (HT) and reversing gear box (RGB) during November 1967—November, 1979. The firm was the only indigenous unit to manufacture HT and heavy duty gear boxes. Accordingly, CLW has been procuring these equipments since November 1967 from this sole manufacture

who later (July 1971) also obtained a licence for manufacture of S.T. The procurement by CLW was made after obtaining quotations on single tender basis (till 1976) when open tenders were invited but the technically acceptable offer was from firm M/s. Kirloskar P-neumatic Co. Ltd. Pune (KPC only) and negotiating a price thereafter with the firm. A review in audit of the prices fixed from time to time revealed that the price increases allowed on certain counts were not justified.

14. The Committee desired to know the basis of the 30 per cent price preference allowed over the CIF cost of imported equipment and whether its reasonableness was examined during the negotiations for settling the price of the first order of November 1967 and again later while settling the price of the subsequent orders. In reply, the Ministry of Railways (Railway Board) have stated in a written note:—

- "For the determination of prices of indigenously procured items for the first time which is hitherto imported, the purchase policy is governed by the directives of the Government of India, based on the recommendation of the Stores Purchase Committee appointed by the Government of India. An extract from Railway Board's letter No. 55/645/5|RE dated 18-5-1956 on the subject is as under:

'Government's purchase policy should, in our view, admit generally a price preference upto 15 per cent to indigenous products over the imported goods, *including customs duty.* We have also carefully considered whether industries protected through tariff or otherwise should enjoy this preference and have come to conclusion that such industries should not be excluded from the purview of this policy. The preference margin should be increased to 25 per cent for certain specified classes of stores where admittedly the indigenous industry is not in a position to compete with foreign manufacturers within the general limit of 15 per cent because of low import duties, or small turnover, or higher costs of raw materials and components etc. A list of such items should be specified. Price preference even in excess of 25 per cent should not be ruled out for lines of manufacture where unfair competition is feared or where special development is required if the Government is convinced of its justification. However, in respect of lines of manufacture which are the monopoly of a single firm or a group of firms, the degree of price preference to be given may be subject to examination of costs of manufacture by Government where considered necessary.' "

"It is rather difficult to cost the manufacture of a new product in the initial stages of development and if such costing method is adopted, the price would include the initial developmental costs which when added would result in a very inflated indigenous price. Therefore, as a broad guideline to contain the indigenous prices in relation to the imported prices, an overall pricing policy was enunciated which sets a price preference depending upon the nature of the product."

15. It has been further stated in the note that:—

"It may be mentioned that the first order of November 1967 was placed taking into consideration the landed cost based on Mak's price as quoted on 28-4-1967 which worked out to Rs. 3,62,000/- as against which KPC's quotation @Rs. 3,50,000/-. It would therefore be seen that the price negotiated with M/s. KPC was in conformity with the policy of the Government. The Audit have compared the imported CIF cost with that of the indigenous price which is not in accordance with the policy of the Government of India. If viewed in terms of the directives of the Government of India, it will be seen that no price preference was given and as a matter of fact the indigenous price was even less than the landed cost."

16. The Committee wanted to know how in the absence of authenticated data or documentary evidence to substantiate adequately the manufacturer's demand for escalation over the previous contract price, the High Lever Tender Committee (HLTC) checked the reasonableness of the prices so demanded. The Ministry of Railways (Railway Board) informed the Committee in a note that:—

"The normal procedure is to compare the price demanded with respect to the last purchase rate and the price increase which had occurred in the different inputs in the interregnum. For this purpose the manufacturers are asked to indicate the reasons for the increase in their prices. These are checked with reference to the data produced by them and also cross checked with reference to other collateral indices on the price situation and this procedure has been followed while finalising all the tenders. Moreover the Tender Committee by virtue of dealing with a number of cases become familiarised with the contemporary market conditions and this also comes into play in the general assessment in finally arriving at a negotiated settlement. A rigid arithmetical verification of the negotiated price covering all factors is not possible and hence an assessment on the overall is attempted as the only workable solution......It is also mentioned that in some cases the premises of the firm have also been visited and the data to the maximum possible extent verified."

17. The Ministry of Railways (Railway Board) have further stated:—

"In view of the above, it would be seen that in the absence of cost audit and legal compulsion for the firm to furnish authenticated detailed price break up, the Tender Committee is left with no other alternative but to come to an overall assessment and while doing so, getting as much information as possible from the manufacturers."

18. The Committee enquired why the Department of Heavy Industry was not approached for a cost probe by Bu reau of Industrial Costs and Prices whereas such a study of the pricing policy of seamless steel tubes for which M/s. Indian Tube Co. is the sole manufacturer, was carried out by the BICP. In reply, the Ministry of Railways (Railway Board) have stated in a subsequent note as follows:

"Orders were placed on the firm only after Tender Committee had examined the reasonableness of the price demended over the last order rates. For this purpose, the T.C. had asked the manufacturer to indicate the reasons for the increase in his price. These were checked with the data furnished and also cross-checked with the related economic indices. The T.C. after getting convenced of the increase asked for by the firm on an overall basis recommended the rates for acceptance. Hence a reference to BICP was not felt necessary.

However, the Bureau of Industrial Costs and Prices has clarified on a reference now made to them, that the Bureau does not normally undertake the study of the Cost/Price function of an individual unit, leave alone an individual item. Further, in terms of the official resolution setting up the Bureau, it is expected to focus attention on industry-wise studies with particular reference to aspects such as cost reduction, raising of industrial efficiency, energy saving, upgrading of technology, etc. and *inter alia* to recommend fair prices to Government relating to any product it has studied. The Bureau is presently engaged in major studies as steel, coal, commercial vehicles automobile tyres, tubes, etc.

The BICP has further stated that if Railways want any product to be studied, it would take up such a study even if it is produced by a single source, provided the issues go beyond the mere determination of fair ex-factory prices and cover other aspects of the industry as well.

It is only where technical and pricing angles are intimately tied together, BICP has in the past taken up studies, pertaining to even individual companies."

19. The Committee desired to know whether in the light of the fact that M/s. KPC, the sold established supplier, were neither furnishing any authenticated data in support of their quoted prices nor agreeing to cost audit, was it not desirable for the Railway Board to refer the matter to the Monopolies and Restrictive Trade Practices Commission under Section 31 of the MRTP Act. In reply, the Ministry of Railways (Railway Board) have stated in a note that:—

"The Tender Committee was satisfied with the increase in price asked for over the last purchase rate, after verifying the data furnished for the increase and cross-checking the same with the collateral indices on the price situation. Moreover, the Tender Committee, by virtue of dealing with other similar cases, became familiar with the contemporary market conditions. The Tender Committee also obtained further data after visiting the premises of the firm. It is again mentioned that the price increases allowed on an overall basis from year to year were found to be quite reasonable, keeping in view the price trend obtaining for the related period. Hence a reference to MRTP was not considered necessary by the Administration.

However, it may be mentioned that on a reference received from MPTP, they have been advised that the Ministry of Railways have no objection to the Commission holding an inquiry in this case on their own."

20. The Committee desired to know the basis of the apprehension of the HLTC that price fixation based on cost audit may adversely affect the interests of CLW. In a written note the Ministry of Railways (Railway Board) have stated:—

"This observation refers to the remarks of the Tender Committee while finalising the purchase order of March, 1974. It was/is the practice for the HITC to compare the previous purchase rate known as LPR with the current price offered and adjudge the price in relation to the cost escalation in the intervening period. M/s. KPC were not wanting to submit themselves to this kind of a cost comparison and therefore, the Committee took the view that they must ask the firm to submit themselves to a cost audit. It was only a suggestion made by HLTC possibly with a view to pressuring the firm to bring down the prices. Subsequently, the firm reduced the prices and gave certain explanations with regard to the increased prices compared to the previous purchase rate. In the year 1973 and onwards there was a certain spurt for increase of prices due to a hike in oil prices and therefore, HLTC might have considered it prudent not to pursue the cost audit angle lest it may result in disadvantages to the Railways."

21. It has further been stated in the note:—

"As regards the enforcement of the cost audit, this could be resorted to only if the firm agreed to submit their accounts audit. As per the present provision in the Companies Act or in any other Act, the private sector can be subjected to cost audit only if they agree. KPC had refused on principle to this and even in the recent tender for 1982-83 requirements, while the representatives of KPC provisionally agreed to a cost audit provision, their higher management declined to submit themselves to a cost audit."

22. The Committee enquired about the profit element included in the November 1967 contract price and its comparison with the profit element of 36.5 per cent conceded for November 1970 order. The Ministry of Railways have stated:

"The November 1967 order was placed based on the landed cost as per instructions for ordering indigenous items which was hitherto imported, and therefore the question of profit margin did not arise at any stage. The landed cost was worked out to Rs. 3,62,000/- including customs duty based on the offer of overseas supplier (M/s. Mak) whereas KPC's quotation was at Rs. 3,50,000/-. The firm could not be persuaded to reduce the cost further as they had to develop this item indigenously. After deducting the cost of free supply items, KPC's price was arrived at Rs. 2,20,183/-. At the same time it was agreed that if a further order for 30 sets beyond the first order for 18 sets was placed, there would be a 5 per cent reduction in rates. As regards 36.5 per cent alleged profit element for November 1970 order, it is mentioned that the firm had not committed officially about the increase in price of Rs. 60,763/- demanded by them over the last order price. During discussions with the firm and the Committee they had given an approx. analysis which had been recorded by the negotiating committee. In the minutes that was finalised the Tender Committee had mentioned as follows:

"As commented in the note of discussion, the Committee went into details regarding the reasonableness of the prices quoted by the firm and their plea that the increase in the price quoted by them to the extent of Rs. 60,763/- over the price of the earlier order, was due to increase in the labour wages structure, increase in the cost of steel, increase in overheads in their work and also for defraying part of initial capital expenditure on the first order indicated. The firm, representative were not in favour of giving datails of increase in writing as this was not their practice.

"The firm's representative indicated details of increases in labour rates in their works as between 1966 and 1970 which works out to 27 per cent. The steel price increase and the increase in the cost of forgings was at the rate of Rs. 5,000/- per M/T. Overall the Committee was satisfied that the price increase asked for by the firm is within the reasonable limits...."

"Therefore the conclusions drawn on the basis of the break up as recorded, in the note of discussion are hypothetical and inferential, particularly, item (e)—margin of profit. This item was not reflected in any of the firms documents. The Tender Committee in the proceeding have mentioned certain increases other than increased cost of forging and wage escalation such as increase in overhead etc. all of which has been taken together by Audit as a margin of profit. The Tender Committee had stated that "Overall, the Committee was satisfied that the price increases asked for by the firm is within the reasonable limits...." The Tender Committee had not accepted any elements on a margin of profit in the final Tender Committee proceedings. The November 1970 order involved an increase of Rs. 57,358/- over the earlier order out of which Rs. 15,358/- has been taken by the Audit as margin of profit and this figure has been worked out as a percentage of the balance increase namely Rs. 42,000/- working out to 36.5 per cent. Even if the entire amount of Rs. 15,358/- is to be taken as margin of profit, although this is not so for reasons already explained on the earlier order this should have been included along-with the profit to arrive at the overall profit margin on the contract price vide calculations made as shown below:

	Rs.
(a) Total new cotact price	2,53,695.00
(b) Assumed profit margin included in the earlier price say at 10% Rs. 2,20,183	22018.00
(c) Addl. profit margin according to Audit	15,358.00
(c) Total profit	37376.00
(e) Percentage on the total price of Rs. 2,53,695 . .	14.7 percent

From the above it would be seen that taking the contract as a whole, as it should be, the profit margin works out to only 14.7 per cent and not 36.5 per cent.

23. The Audit para states that the increase of Rs. 15,358/- allowed as margin of profit worked out to 36.5 per cent of the increases for material and wages and not of the overall price allowed for November 1970 order. In this context, the Committee wanted to know the rationale of the contention that the increase, even if conceded, for margin of profit should be related to the overall contract price. The Committee also enquired whether even in the Railway Board's own calculation, the total profit element allowed was not much more than the normal 10 per cent. In reply, the Committee have been informed by the Ministry of Railways as follows:

"Overall the Tender Committee was satisfied that the price increases allowed for were within the reasonable limit. The T. C. had not accepted any element on a margin of profit in the final TC proceedings. The calculations indicated in the reply only stated that the profit margin as stated by audit was not 36.5 per cent but was only 14.7 per cent even if Rs. 15,358 was taken as profit. However, since the increase of Rs. 15,358 is not all towards profit, the notional fiqure of 14.7 per cent worked out is not comparable with 10 per cent."

24. In the record notes of discussion with the firm, the Tender Committee had recorded that the increase of Rs. 60,763 over the last contract price was explained by the firm as due to increase in the price of forgings and wage escalation accounting for Rs. 30,000 and Rs. 12,000 respectively and the balance (Rs. 18,763) as their margin of profit. The Committee enquired whether the firm gave any details other than those

mentioned during discussion in support of its demand for price increase and if not on what basis it was mentioned in the Tender Committee proceedings (September 1970) that the increase over the last order price was due to increase in labour, increase in cost of steel, increased overheads, etc. The Ministry have stated in a further note that "no details other than these mentioned during discussions are available in the files".

25. The Ministry of Railways have further stated that:—

"It can also be seen from the economic indices for the related items that there had been an increase of 20 per cent to 29 per cent in general for these items. The related indices are as below:

Item	Year		Increase in percentage
	From	To	
Semis	77.6	100.00	29%
Fuel	83.2	100.00	20%

26. Asked to state the basis on which the HLTC accepted the demand for inventory carrying charges (7.5 per cent) and financing charges (10 per cent) when the advance payment made by CLW (carrying 6 per cent interest) was available for utilisation by the firm for procurement of forging, the Railway Ministry have informed the Committee in a note:—

"This refers to the order placed in March 1972. While 7.5 per cent accepted by the Tender Committee is on the cost of forging the 10 per cent referred to as financing charges is not on the cost of the forging but on the inventory carrying charges. In other words this works out to only 0.75 per cent of the cost of forging making a total of 8.25 per cent (7.5 + .75) on this account. In regard to this, the Tender Committee had recorded as under:

"In this connection it was seen that the present difficulties of M/s. KPC in their inability to supply transmission and reversing gear boxes well in advance of CLW's production requirements had been mostly due to their inability to procure the forgings from their associates M/s. Bharat Forge in time. M/s. Bharat Forge in turn are solely dependent for their steel elsewhere and considering the long lead for arranging the special steel and as M/s. Bharat Forge themselves were having a lot of back log orders, it was considered essential by this administration that M/s. KPC should be given a longer lead time than the 8 or 10 months lead time given in the order hitherto placed, for commencing supplies from the date of placement of orders by CLW".

"....the firm indicated that in the context of CLW's wanting to procure these forgings much ahead of the KPC's delivery schedule of Suri Transmission and Reversing Gear Box as hitherto obtained for various reasons the firm have to incur inventory carrying charges of stock piling of these forgings and they wanted to provide 7.1/2 per cent margin in their prices to cater for the carrying cost of these forgings".

"It would therefore be seen that in the special circumstances then obtaining as brought out in the Tender Committee minutes, the Tender Committee had considered the payment, which will not cover all the charges incidental to inventory carrying cost which is to be reckoned on cost of storage etc. Had these two items been eliminated M/s. KPC might have enhanced the advance payment from 25 per cent to some higher figure. It may further be mentioned that only 6 per cent increase was allowed as a whole over the value of last order."

27. The Committee were further informed in a subsequent note furnished by the Ministry of Railways:—

"Bharat Forge were dependent on their steel requirement elsewhere. As these steel items were long lead items and considering the backlog of orders on M/s. Bharat Forge, M/s. KPC were given a longer lead time. This would have enabled M/s. KPC to place orders on M/s. Bharat Forge earlier.

In order to enable M/s. KPC to supply ST & BGB well in advance of C.L.Ws production requirements, M/s. KPC. were required to procure these forgings much ahead of CLW's requirements. This would have compelled M/s. KPC to keep some of these forgings in stock.

The data regarding the exact period for which these were stockpiled is not available."

28. Explaining the basis of the increase of Rs. 7,835/- demanded by the firm on account of increase in cost of sub-contract operations, the Ministry of Railways (Railway Board) have stated in a note:

"This pertains to March, 1974 order. A team of officers was deputed to firm's premises at Poona to examine in detail the basis of the increase of Rs. 7,835/- demanded by the firm on account of increased cost of sub-contract operations. The extract from the note given by the team in this connection is reproduced below which will explain the position:—

"Increased rate of subcontract operations at Walchandnagar and Udhana: (Rs. 7,835/-)

It is noteworthy that the increase indicated under this heading was Rs. 9225/- as against Rs. 7,835/-. Tod substantiate this M/s. KPC showed us the office copy of their letter No. SCS/SGB/463 dated 19-8-1972 wherein the rates for gear grinding for counter shaft, Jack shaft pinion and gear 134A were indicated as Rs. 7,270/-, Rs. 8,410/- and Rs. 3,825|- each respectively In this very letter they had included the following sentence— "Please note that the old rates are just doubled." Based on this sentence. M/s. KPC indicated that the rates for each one of the items mentioned above for gear grinding as on 1-1-1972 were Rs. 3,630/-, Rs. 4,200/- and Rs. 1,905|- respectively. When M/s. KPC Officers were asked to show us a quotation/bills from M|s. WIL or any other proof of having paid M/s. WIL at these rates during Dec. '71/Jan. '72 when the prices were last established they said that the same will more or less tantamount to audit of books which had not been agreed to by them in principle. The total price as on 1-1-72 at the above rates works out to Rs. 9,735/- for one of each of the above 3 items viz. Counter-shaft, Jack shaft Pinion and Gear 134A. In order to establish the current rates M/s. KPC showed us a joint minutes of discussion between their officers and the officers of M/s. WIL held on 7.4.73 and the rates as were effective from 1-5-73. In this joint minutes, the revised rates as indicated by M/s. WIL and agreed to by M/s. KPC were Rs. 5,325/-, Rs. 9,755|- and Rs. 8.515/- for each one of the above items respectively. Further to this, the rebate offered by M/s. WIL was Rs. 300/- per piece if these were supplied in batches of 3 and Rs. 600/- per piece if these were supplied in batches of 5. The method adopted by M/s. KPC in calculating the increase on account of M/s. Walchandnagar alone as below:—

The total price as per new rates effective from 1-5-73 is eyual to Rs. 23,595/s per set consisting one of each minus the price per set as on 1-1-72 *i.e.*, Rs. 9,735/- — Rs. 13,860/-.

Since M/s. KPC intend having only 2 pieces of each to be ground by M/s. WIL per month (the balance to be done by M/s. KPC themselves) the approximate extra charges to M/s. WIL per month works out to Rs. 13,860/- x 2—Rs. 27,720/-. 4 ST and RGB per month—Rs. 6,930/-. per ST and RGB extra. 'When M/s. KPC Officers were asked that instead of 4 they should consider 5 ST and RGB per month, they advised that they had not achieved the figure of 5 as yet and therefore, they had considered 4 ST and RGB per month only. Thus out of the increase of Rs. 7,835/- on account of increased rate of sub-contract operations at Walchandnagar along, the increase is Rs. 6,930/- which can be said to have been only partly substantiated since M/s. KPC did not give us any proof of rates paid by them to M/s- WIL on the basis of which the last prices were established."

With regard to the balance amount of Rs. 905/- out of Rs. 7835/-, the same is on account of the increase in sub-contract operations by M/s. SRM/Udhna. This was substantiated as per copies of sub-contracts placed by M/s. KPC on M/s. SRM/Udhna."

29. It has further been stated in the note that:—

"The Senior Scale Officers' Committee who visited Poona previously had allowed for Rs. 7,000/- against Rs. 7835/- asked for in view of the fact that one of the sub-contractors had offered a discount if the components are given to them in batches instead of piecemeal. M/s. KPC stated that it was not possible for them to order in batches as this would entail building up of inventories which would involve extra costs.

They also stated that this was not a practicable preposition. In view of this the negotiating committee consider that the increase in cost of Rs. 7835/-asked for by them is reasonable."

30. The Committee enquired as to why the firm M/s. KPC could not avail of the discount offered by the sub-contractors. In reply the Ministry have stated that the two sub-contractors were M/s. Walchandnagar Industries, Walchandnagar and M/s. SRM, Udhna. As far as known to the administration, these firms were not associates of M/s. KPC. M/s. Walchandnagar

Industries offered to KPC a discount of Rs. 300/- per piece if the gear were supplied in batches. of 3 sets and Rs. 600/-per piece if they were supplied in batches of 5. As the total requirement was 4 and out of this M/s. KPC themselves had developed their capacity for processing two sets they could only give 2 sets to their sub-contractors and hence they could not avail of the discount offered to them which was for a minimum of 3 sets.

31. Asked how the claim was a legitimate charge on CLW, the Ministry have stated that CLW was procuring the complete ST/RGB from M/s. KPC. The cost of sub-contract materials naturally was a part of the price of ST/RGB quoted for by the firm and therefore the claim was a legitimate charge on CLW as part of the price for ST/RGB.

32. In a subsequent note, the Ministry have further stated that:—

> "A supplier has necessarily to build up all the costs in his pricing. His cost is based on all the expenditure involved and as such the loss of discount due to valid reasons which he had incurred would also account for increase in price. Hence, the loss of discount which the supplier had incurred is a legitimate charge on the buyer."

33. Asked whether the subsequent contracts with the firm contain the 'Book Examination' clause, in terms of the decision (1975) of the Railway Board to introduce it in Stores Contracts, the Ministry have stated that book Examination Clause was not included in any of the contracts placed on the firm. In any case even if such a clause had been insisted upon, it was doubtful if the firm would have agreed to it as seen from their general reluctance to cost audit etc.

34. To a query whether the revised cost of forgings for the earlier order and the current cost, as indicated by the firm in August, 73, were verified by the HLTC from the suppliers of forgings and/or wih reference to the wholesale price indices for the relevant period, before conceding the price increase on this account, the Ministry of Railways have stated in a note:

> "Before placing the March '74 order a Sr. Scale Officers' team was deputed to examine the increase asked for by the firm. In respect of the forgings they stated in their note that they were shown a comparative statement showing the last purchase price and the current quoted prices of M/s. Bharat Forge to establish the increase of 14.8 per cent for one set of forgings consisting of 26 items (Rs. 63,552-55,469). They added that this was based on the quotation submitted by M/s. Bharat Forge under their quotation No. E/70-95, dt. 5-5-73. The Sr. Scale Officers' Team also visited M/s. Bharat Forge and discussed the issue with their Commercial Manager and Asstt. General Manager. They (Bharat Forge) stated in their latest quotation they

had asked for an increase of approx. 15 per cent over the last price of forgings. It would therefore, be seen that the increase in the price of forgings had been checked with reference to the data available both with the supplier of forgings namely M/s. Bharat Forge and also the documents available with KPC. The HLTC also visit M/s. KPC subsequently. They have recorded that "with regard to the forgings the cost of Rs. 61,376/- included certain forgings which were required for simplified transmission and as such the cost of forgings would actually be approx. Rs. 60,000/- per set for simplified transmission whereas the present day cost work out to Rs. 64,000/- i.e. Rs. 63,662 for the forgings obtained by them from their main contractors." From the papers it is seen that while the cost of the non-simplified transmission was Rs. 61,376/- the corresponding cost of the simplified transmission for the same orders is Rs. 55,469/- as indicated by the Sr. Scale Officers' Team. Adding Rs. 4,603/- for the inventory carrying charges allowed in the previous contract the total would, therefore, work out to approx. Rs. 60,000/- as pointed by the HLTC. Keeping this in view and the revised price for the simplified transmission on Rs. 63,662/- plus 400/- for cost of forgings for small items obtained from other sources making a total of Rs. 64,000/- the Tender Committee had agreed for an increase of Rs. 4000/-.

Incidentally it may be mentioned that the wholesale price index as published in Statement No. 21 by Reserve Bank of India in their Report on Currency and Finance for basic metals, iron steel and ferro alloy was 142.6 for the year 73-74 with base 100 for 70-71. It would therefore, be seen that during three year period there was an increase of 42.6 per cent in the whole sale price-index of iron, steel and ferro alloy and 67 per cent in semis. In the light of this, 15 per cent increase allowed for 73 order with reference to '72 price is corroborated by the price indices of the relevant period."

35. The Committee enquired if the Ministry of Railways (Railway Board) were aware that the suppliers of forgings to the firm had made large profits over the years ending 1979-80 and whether this aspect was ever kept in view by the HLTC. In reply, the Committee have bee informed that the HLTC considered the reasonableness of the price demanded in each tender with reference to last purchase rate and subsequent increase of various inputs. They had no recourse to details of the actual profits made by the sub-contractors of the main supplier.

36. The Committee enquired how the Railway Board/CLW reconciled their contention regarding verification of available data by HLTC by visit to M/s. KPC witn the reply to the Draft audit para stating :

> "The firm on their own had advised the correct position that earlier cost should have been Rs. 60,000/- and not Rs. 61,376. As there was no reason to believe that a firm of repute on whom crores worth of orders were being placed, would on such a minor issue give a false picture and considering the amount involved, the HLTC had apparently taken into account the correct position as advised by them and allowed increase on this basis."

In reply, the Ministry have furnished an extract from the notes of discussions held with M/s. KPC, Poona on 27th and 28th August, 1973 by the negotiating committee consisting of FA&CAO, CME(W) and COS. The note is reproduced below:

> "After discussions with M/s. KPC administration agreed to work on the basis of fixation of the price against the present tender with reference to the last purchase price. In support of this, M/s. KPC authorities indicated the increase since their last quotation in December, 1971 vide S. No. 101 duly signed by M/s. KPC. The increase in price asked for by M/s. KPC were discussed in detail and the comments of the negotiating committee are indicated below:

> Material increase Rs. 14,801—The material cost consist of mainly forgings and other materials. In accordance with the break-up given by M/s. KPC against last order the cost of forgings was valued at Rs. 61,376 and other materials at Rs. 48,762. M/s. KPC stated that there was abnormal price increase specially during the first part of this year and the cost of forgings and other materials had gone up to the extent of 15 to 25 per cent. M/s. KPC also pointed out that the break-up of the costs given at the negotiations held against last order for forgings and other materials/processing was also not quite correct as found out by them subsequently, although the overall circumstances as given were correct. With regard to the forgings, the cost of Rs. 61,376 included certain forgings which were required for simplified transmission and as such the cost of the forgings would actually be approximately Rs. 60,000 per set for simplified transmission whereas the present day cost works out to Rs. 64,000 i.e. Rs. 68,632 for forgings obtained by them for their main contractors and approximately Rs. 400 per forging obtained for smaller items obtained by

them from other sources. Thus, there was an increase of Rs. 4,000 on forgings. The negotiating committee consider that this increase is reasonable.

With regard to other materials, the negotiating committee consider that the increase of 15 per cent since December, 1971 and taking into consideration that the contract would remain in force for about 2/3 years is reasonable and this would work out to 15 per cent of Rs. 48,762 minus Rs. 4,624 for simplified version (Rs. 6,000—1,376)=Rs. 44,138+Rs. 6,621. As such, the total cost would work out to Rs. 50,759."

37. It has been further stated by the Ministry of Railway:—

"It would be seen from the above extract from the Negotiating Committee's note, that escalation has been assessed for 'forgings' and 'other materials' at more or less the same percentage and in that context, the cost of individual items, namely, 'forgings' and 'other materials' is not very material for judging the reasonableness of the total price. Further, the Negotiating Committee had with it the report of the senior scale officers who had earlier visited M/s. KPC and examined their records. As indicated in an earlier reply, the price of 'forging has been assessed at Rs. 60,000, based on the report of the senior scale officers. Since this corresponded with the figures given by M/s. KPC, the Negotiating Committee seems to have accepted the same. There is, therefore, no substantial contradiction between the Railway's reply stating that HLTC had scrutinized the available data with M/s. KPC and the reply to Audit para. It may kindly be appreciated in this context that a more specific reply is not possible, because no record has been kept on the file of the documents and the specific items scrutinized by the HLTC during their visit to KPC."

38. *Increase in Heat Treatment shop cost*

The Committee wanted to know the reasons for HLTC's agreeing to the reasonableness of the revised method of allocation of heat treatment shop cost proposed by the firm without even looking into the shop cost structure, the earlier method of allocation etc. The Committee also desired to know whether the firm furnished the details of shop cost structure, method of allocation etc. as promised during the negotiations and did they indicate the time involved in that treatment of ST & RGB as compared to other items, justifying the higher allocation thereto. In reply, the Ministry of Railways have furnished the following information:—

"This has reference to the order placed in March, 1974. When the Senior Scale Officer's team visited the firm for examining the broad break-up of price increase demanded by the firm, it was indicated that the process charges in respect of heat treatment cost would be higher by Rs. 4,000, KPC explained to the Sr. Scale Committee that earlier in the cost, the heat treatment cost was distributed equally between the various activities of the firm viz. air-conditioning, pneumatic, transmission. Now after the review of the costing method it has been assessed that the major portion of the work done in the heat treatment was on the components of transmission only and as such by realistic allocation of heat-treatment cost, they had arrived at Rs. 4,000 as higher heat-treatment cost allocable to HT/RGB manufactured by them. Besides, they indicated that a new Gas Carbonising Furnance installed in their works had contributed to a certain extent towards increase in the heat-treatment cost. Since KPC had not shown authenticated records in support of the demand for Rs. 4,000 extra heat-treatment charges, the HLTC visited M/s. KPC's Works and finally recommended an increase of Rs. 3,000 on this account instead of Rs. 4,000 demanded. There is no record to indicate what actual documents they had checked but it is to be presumed that they would have examined the costing procedure, methods of allocation, before arriving at the conclusion.

The firm later on indicated that the increase in heat-treatment cost was to the extent of Rs. 1.91 per kg. due to method of allocation of heat treatment expenses and Rs. 0.73 per kg. was due to increase in prices of fuel, quenching oil, salts etc. Based on approximately 1600 kgs. weight of components for HT/RGB to be heat-treated, the total increase in cost was indicated at Rs. 4,224."

39. The Committee desired to know the considerations on which the escalations for the period May, 1973—September, 1976 already built into the March, 1974 contract period were again allowed in settling the price for the May, 1977 order, which was 29.66 per cent higher than the price in the previous contract. In reply, the Ministry have stated as follows:—

"It is not correct to presume that escalations built into March, 1974 contract price were again allowed in settling the price for May, 1977 order. March, 1974 order did not and could not have provision for all the escalations in cost actually taken place between March, 1974 and May, 1977 when the next order was given. Audit have perhaps come to the conclusion that adequate escalation was included in the price of March, 1974 order because of mention in the T.C. Note of 1974 order regarding probable increase in price over the long period of the order. It is true that a supplier does keep a margin in his pricing for price increase in certain areas which cannot be predicted but this cannot cover the price increases taken place if commitments are entered into at subsequent dates by long periods. The contention that the delivery period was to be put up-to September, 1976 and therefore the probable price increase upto September, 1976 should be considered to have been included in the price of March, 1974 order, is not accepted as correct. M/s. KPC was given advance against each order with the express object of their ordering the forgings and other bought out items immediately after the receipt of the order and therefore the price paid for by KPC for the bought out items against March, 1974 order will not account for the price which they had paid for against May, 1977 order. The IMA fromula as applied by the Tender Committee was, therefore, fully justified. While placing further order in May, 1977 the price comparison with 1974 order was quite in order. It is mentioned that during 1974 and 1977 the price increase in the following major categories had taken place:

Index No. of whole sale prices (Statement No. 21) as published by the Reserve Bank of India in their 'Report on Currency and Finance.

'78-79, Vol. II—100 Base 70-71

	1973-74	1974-75	1975-76	1976-77	%
Fuel, Power and Lubricants .	130.6	198.3	219.2	230.8	76.7%
Basic metals, Iron Steel & Ferro alloy	142.6	171.3	183.6	186.9	31.1%
All India Consumer price Index for Industrial Workers . .	250	317	313	301	20.1%
Semis	167.1	200	215.2	221.3	32.4%

It would be wholly incorrect to presume that all these price increases had been taken into account while accepting the March, 1974 order. Further, the order placed in May, 1977 was also completed around September, 1978 and therefore certain portion of the price increase would also be necessary to cover the increase in the cost during the delivery period. This happens in every contract and is not a new phenomenon. The price increase while considering a new order is always compared, with the last price.

The Audit had stated that in regard to orders placed in May, 1977 based on the quotation of December, 1976 the escalation would be allowed beyond September, 1976. While this procedure of providing for escalation beyond the period of quotation is acceptable and workable in practice where escalation clauses are provided, this for obvious reasons, cannot be done for fixed price contracts."

40. It has been stated by the Ministry of Railways that a supplier does keep a margin in his pricing for price increase during the currency of the order but that this cannot cover all the increases that take place since the last contract|quotations. In this regard, the Committee enquired whether it was not desirable to identify the quantum of increase built into the price of March, 1974 order valid for deliveries upto September, 1976 and deduct the same from the escalation assessed for the period May, 1973 to October| November, 1976 for settling the May, 1977 order price? In reply the Ministry have informed the Committee as follows:—

"Since escalation that may occur during the future is not available, as per practice on the Railways, purchases are made with reference to last price and the escalation which had taken place in the past. This is the normal procedure followed in the Railways for placing orders."

41. Asked to state the basis for asseptance by the HLTC the price offered by the firm for the November, 1979 order, which was 27 per cent than the price in the previous contract and whether any assessment was made of the escalations for the materials, components, wages etc. since the last order of December, 1978, the Ministry of Railways informed the Committee as follows:

"The firm had furnished details of increases in price in respect of major items involved in the production of this assembly, viz. pig iron, steel, petroleum products, etc. *vide* their letters dated 20-8-79 and 21-8-79. Besides, they also indicated the increases on other important items such as excise duty, labour wages etc. as given prices:

(i) **Increase in the steel prices:**

(a) Pig iron price increased from Rs. 1200 M/T to Rs. 1773 M/T *i.e.*, increase of 47.75 per cent.

(b) **Increase** in Alloy Steel Price—Price increased from Rs. 8,101 M|T to Rs. 10,565 M|T for EN-36, an increase of 30.41 per cent. Another Alloy Steel EN1345 price increased from Rs. 6550 to Rs. 8,345 in June, 79—increase of 25.5 per cent.

(ii) Increase in price of petroleum products—to the tune of 35 per cent. (It is seen that Furnace Oil Price of Rs. 971-1 per K/L in June'79 was revised to Rs. 1,246.12 per K/L in August'79, representing an increase of 34.52 per cent.

(iii) Excise duty increase on purchase items:—

There was an increase of 3 per cent on this account.

(iv) Labour price increase:

The firm had also indicated that there will be 3 to 8 per cent price increase in the labour rates as the previous agreement with their labour force expired in June'79.

Apart from persuading the firm, to withdraw the price variation clause initially asked for by them, the HLTC also, as a result of negotiations brought down the price from Rs. 6.83 lakhs to Rs. 5.73 lakhs after going into the reasonableness of the increase on the various factors and also keeping in view that the deliveries against this order extended upto Oct. '81, a period of 23 months from the date of quotation on a firm price basis. Even though the negotiated offer is more than the last contract price, it would be seen that the reasonableness thereof has been examined and found justified.

Incidentally it may be mentioned that the price indices for the material period as available now confirmed that the prices negotiated were justified as shown below:

All India Consumer price Index number for Industrial workers increased from 327 to 360 from June'78 to Aug.'79, representing an increase of 10.1 per cent (Source IEMA). It is also mentioned that the whole-sale price index number for 'manufactured intermediate product' increased from 353.9 in June'78 to 439.9 in Aug. 79 representing an increase of 24.2 per cent. Source (IEMA), further the wholesale price index for Iron & Steel, Ferro Alloys also increased from 191.5 to 258 representing an increase of 34.7 per cent (Source IEMA).

The index for Semi also increased from 241.8 in 78-78 to 307.1 in 1979-80 i.e. a rise of 28.5 per cent."

42. Further elucidating the position in a subsequent note, the Ministry have further stated:—

"It is not correct to say that assessment of the impact of increase in the cost of raw material, wages etc. was not made while considering the reasonableness of the price increase demanded/conceded for November 1979 order. The firm had indicated the figures for increase in the cost of steel price, petroleum products and labour. The product is material intensive and therefore an increase in price of pig iron by 47.75 per cent that of alloy steel by 25.5 per cent to 30.41 per cent and petroleum products by 34.52 per cent adequately justify the price increase of 27 per cent finally conceded. In fact the firm had asked for price variation clause looking to indefinite price situation but they were persuaded to withdraw the same."

43. Asked as to why the Railway Board did not work out the extent of escalation since the last contract by applying the IEMA formula, as had been done for the May 1977 order, to verify the reasonableness of the price increase demanded by the firm for the November, 1979 order, the Committee have been informed in a further note:

"The firm in their offer had quoted the following price variation clause:—

(iii) The above prices are based on the present day raw material cost, such as Steel, Alloy Steel, Fuel, Electricity, etc. and also emoluments paid by us to our employees, which goes into our costing. Any increase in the cost of raw material, increase in the total emoluments paid to our employees due to entering into fresh agreement with our Labour and escalation due to statutory levies that may be imposed by State or Central Government and/or any competent authorities, which we will have to pay while purchasing the materials will result in escalation of prices and will be claimed against sufficient evidence."

The Tender Committee after negotiation with firm had recorded as under:—

"8.11 The firm in their quotation had indicated that their prices are based on the present day raw material cost viz. Steel, Alloy Steel, Fuel etc. and also emoluments paid by them to their employees which goes into their costing. Any increase in the cost of raw material and increase in the total emoluments to their employees due to entering into fresh agreement with their labour will force them to revise their prices.

In order to itemise such increase, KPC was asked to evolve a formula for price variation on the basis of those adopted by Electricity Equipment Manufacturers. M/s. KPC indicated that this will be looked into by them and they will try to evolve reasonable formula for adoption for the next contract, but at present they are unable to evolve any such formula. After much persuation, the firm withdrew the price variation clause, which itself means a reduction in future escelation in prices during pendency of the contract."

It is clear that the firm were not agreeable to pricing based on any formula against the purchase in question. CLW unilaterally could not, therefore, apply IEMA formula."

44. The Committee wanted to know the justification for CLW ordering components in March, 1972 in preference to complete sets, when supplies against the earlier component order of July 1971 were pending and teething troubles as also delays were anticipated in the local manufacture of ST & RGB. In reply, the Ministry of Railways have stated that at the time of finalising order of component as well as for fully assembled HT&RGB, the Tender Committee had taken into consideration the following:

(i) The capacity of CLW to quickly gear up the manufacture of components, Suri transmission and reversing gear boxes in Chittaranjan.

(ii) The necessity for a cushion of 21 sets (4 months outturn) against delays and teething troubles in establishing and proving the local assembly and manufacture.

(iii) The necessity of CLW for supplying the complete locos in time to other Railways and Steel Plants and Public Sector Undertakings; and

(iv) Also for supplying adequate spares to the User Railways and recommended—

(a) complete ST and RGB—40 sets @ Rs. 2,87,583/- per set FOR Poona, CST and other terms and conditions.

(b) 30 Locos sets of components parts of ST & RGB @ Rs. 2,03,590/- per set FOR Poona, CST and other are as per (a) above.

Therefore, it will be seen that the Tender Committee had taken into consideration the anticipated loco outturn, supply of shares etc. and the probabilities of developing the manufacture of ST & RGB in CLW. The anticipations which were envisaged in 1972, however, did not materialise as will be seen from the extract of T.C. proceedings of 1973 and note made by the Purchase Committee in 1974 reproduced below:

Extract of T.C. Committee of August 1973:

"In view of the need for CLW to gear itself to step up the outturn to 75 Diesel Shunters it would not be possible to take over manufacture of complete STs and RGBs as a regular measure at CLW, nor it would be feasible to manufacture complete STs|RGBs availing certain components from M|s. KPC beyond the first lot of 30 sets of components ordered on M/s. KPC. It was, therefore, considered that the order for components placed on M/s. KPC at item 6 of para 2.2 should be converted into an order for supply of complete ST/RGBs. In asmuchas, the other items of components including special forgings etc. required to be separately ordered and procured by CLW complementary to the components ordered on M/s. KPC for completing the assembly of corresponding number of sets of transmissions and gear boxes, have not yet been indented for/ordered, the proposed conversion of the 2nd order for 30 sets of components into an order for supply of complete STs/RGBs will not lead to any problem in regard to excess matching materials."

Note made by Purchase Committee in 1974

"In this context of the changed conditions at Chittaranjan and in the context of the WDS-4 manufacture coming to a close by 280th locomotive, it has been decided that CLW will restrict the manufacture of assembly of ST and RGB only to the extent of 10 sets and the balance 20 sets may be got assembled through M/s. KPC only. For this purpose, a negotiation meeting was held with KPC's representative at Chittaranjan on 15-2-1974 and a record note of discussions is kept at S. Nos. 9 and 10". It is to be appreciated that the order is based on the projected requirements of locomotive outturn and the earlier orders placed were in acordance with the anticipated|projected locomotive outturn. However, the condition changed in 1974. It was therefore not possible to order the 30 sets in 1972."

45. In addition there was a sharp increase in the manufacture of Traction Motor and Mak Diesel Engine from 1973-74 onwards as can be seen from the figures of production as under:

Year	TAO-659	Mak Diesel Egnines
70-71	..	12 Nos.
71-72	12 Nos.	30 Nos.
72-73	78 Nos.	41 Nos.
73-74	195 Nos.	50 Nos.
74-75	255 Nos.	42 Nos.
75-76	384 Nos.	31 Nos. +Overhaul/heavy repair of 14 Diesel Engines.
76-77	306 Nos.	36 Nos. +Overhaul/heavy repair of 14 Diesel Engines.

46. In view of the facts that the factors taken into consideration for ordering components of ST & RGB and completely assembled ST & RGB in March 1972, did not include traction motor manufacture which has been pleaded to be one of the reasons for not undertaking local assembly of ST & RGB at CLW as orginally at the time of ordering, the Committee enquired whether this aspect of traction motor manufacture, if taken into account, coupled with the anticipated delay and teething troubles in establishing local manufacture of ST and RGB would not have justified ordering of completely assembled sets in lieu of components even in 1972? In reply the Ministry of Railways have stated in a note:—

"It is correct that the Tender Committee while justifying the order of components in March, 1972 did not mention about the probability of increase in outturn of traction motors. At this stage it can only be stated that as actually happened later, there was an increase in the out put of traction motors from 1973-74 onward which can be taken to be an added reason for converting the component orders into fully assembled order for ST & RGB, indicating CLW's limitations in undertaking the manufacture of ST & RGB."

47. The Committee desired to know the circumstances under which the contract price for July 1971 was left un-amended for deletion of certain components not required for simplified transmission. In reply, the Committee have been informed in a note as follows:—

"Initially an order for 30 sets of components for non-simplified version of Suri Transmission was placed on M|s KPC. Subsequent to placing of this order a decision was taken for a simplifiled version of Suri Transmission. In taking into account the supplies of components already received and other factors, it was decided to convert 20 sets of components of non-simplified design into fully assembled Suri Transmission and Reversing Gear Box of simplified version and on this basis a conversion contract was fixed up with M|s KPC. are stating that this conversion cost takes into acount credit on account of certain components rendered redundant under the simuplified design. The matter is under correspondence with them."

48. The Committee enquired whether the Ministry of Railways were aware that the firm had made large profits over the years ending 1979-80 and how did the HLTC satisfy itself about the reasonableness of the profit element by the firm, a single established source. The Ministry of Railways informed the Committee in a note as follows :—

"The first order on the firm was placed at a price which was less than the contemporary landed cost of the equipment and thereafter orders were placed after examining the reasonableness of the price increase demand over the last order rates. The question whether the firm made large profit over the years ending 1979-80 can be found out only by a rigid cost audit of the firm's account. The firm have not so far agreed to this procedure."

49. Asked whether any alternative source has been developed for supply of ST and RGB, the Ministry of Railways have stated in a note:-

"As far as the ST (or HT) is concerned no suitable offer have been received although CLW started issuing open tenders from 1976 onwards. For RGB however one developmental order was placed in 1979 for 5 sets of RGB on M/s. New Allenberry Works, Calcutta. The firm were on prolonged lock-out and hence they have not been able to deliver the prototype as yet. It is mentioned that the average off-take is less than 40 sets a year and that possibly is one reason that other firms have even now not come up to develop items though initially for quite sometime KPC were the only firm who possessed the sophisticated facilities required to manufacture these items. It is mentioned that against open tender for 1982-83 requirements, under finalisation, while there was no offer from other than M|s KPC for Hydraulic Transmission, there is an offer from M|s. GKW, Calcutta for Reversing Gear Box in addition to KPC's. The rate quoted by them is Rs. 6,29,118|- each as against comparable rate of KPC at Rs. 4,59,403|- each. In addition, they have also asked for Rs. 2,00,000|- as cost of production of tooling and fixtures and Rs. 10,00,000|- as cost of equipment required for testing, complete gear box, etc. The offer is also subject to a minimum quantity of 20 stes. During for 5 sets at the same rate as quoted by M|s. KPC. There is no further response from M|s GKW and Tender Committee have therefore recommended not to place any development order at a cost which is 36 per cent higher than that of M|s KPC."

50. The diesel locomotives produced at Chittaranjan Locomotives Works (CLW) were in the initial stages provided with Suri transmission (ST) and a reversing gear box (RGB) to enable working of the locomotives for both shunting and shuttle services. Earlier these ST and RGB were being imported, but since November, 1967, CLW has been procuring these equipment from an indigenous manufatcurer M|s Kirloskar Pneumatic Co. Ltd., Pune. This is the only firm which manufactures hydraulic transmission equipment and heavy duty gear boxes. In July 1971, this firm also obtained a licence for manufacture of ST.

51. The procurement of the equipment was made after obtaining quotations on single tender basis a negotiating a price thereafter with the firm. From 1976, open tenders were invited but the technically acceptable offer was from this firm only. The price for the initial order exclusive of certain imported components supplied free by CLW included about 30 per cent preference over the contemporaneous CIF cost of imported complete ST and RGB. For the subsequent orders, the price for the initial order was treated as the base price taking into account escalation for wages, materials etc. over the previous contract as indicated by the firm and to the extent agreed to during negotiations.

52. The Committee note that there has been substantial increase in the price of the equipment in subsequent orders. While in November, 1967 when the first order was placed, the price per set was Rs. 2,20,183, the same increased to Rs. 3,18,000 per set in March, 1974 and Rs. 4,51,530 in January 1979. Within ten months i.e. in November, 1979 the price further increased to Rs. 5,73,450 per set i.e. an increase of Rs. 1,21,880 per set. A review in the audit of the prices fixed from time to time has revealed that the price increases allowed on several accounts were not justified.

53. The Committee have been informed by the Ministry of Railways that the prices for the first order of November 1967 were determined by the purchase policy as governed by the directives of the Government of India based on the recommendation of the Stores Purchase Committee. However, it is seen from the letter of Railway Board dated 18 May, 1956 on the subject that in the purchase policy, it has been laid down that 'in respect of lines of manufatcure which are the monopoly of a single firm or a group of firms, the degree of price preference to be given may be subject to examination of costs of manufacture by Government where considered necessary'. The Committee are, however, surprised to note that no cost examination has been conducted either at the time of placing the first or even subsequent order, nor the firm had at any stage produced authenticated data or documentary evidence to substantiate their demand for escalation in prices. The Committee are not convinced with the reply of the Ministry of Railways that in the absence of cost audit and legal compulsion for the firm to furnish authenticated detailed price break-up, the Tender Committee is left with no other alternative but to come to an overall assessment and while doing so, getting as much information as possible'. The Committee are of the firm view that no indigenous manufacturer should be allowed to take undue advantage of its monopoly position to dictate terms in respect of price of the equipment supplied by them and the Railways should have insisted upon cost audit and authenticated detailed break-up supported by documentary proof before agreeing to such escalation in costs which in many cases were not justified.

54. The Committee note that to a query from them as to why the Department of Heavy Industry was not approached for a cost probe by the Bureau of Industrial Costs and Prices whereas such a study of the pricing policy of Seamless Steel Tubes for which M|s Indian Tube Co. is the sole manufacturer was conducted by the BICP, the Ministry of Railways have replied that 'the Tender Committee after getting convinced of the increases asked for by the firm on an overall basis recommended the rates for acceptance. Hence, a reference to BIGP was not felt necessary.' The

Committee fail to understand how in the absence of a cost study and authenticated data in respect of escalation in costs, the Tender Committee could decide that the escalation in prices asked for by the firm was justified. The Committee cannot but conclude that the whole matter has been dealt with in a very casual manner in utter disregard of principles of financial propriety.

55. The Committee note that for November 1970, contract, the firm had asked for an increase of Rs. 60,763 including Rs. 30,000 for increased cost of forgings and Rs. 12,000 for wage escalations. After negotiations, increase of Rs. 57,358 was agreed to. Even presuming that the reduction accepted by the firm was in its profit margin, the later amounted to Rs. 15,458 i.e. 36.5 per cent of the price increase of Rs. 42,000 on materials wages. The Ministry of Railways have, however, stated that this item viz. 'margin of profit' was not reflected in any of the firm's documents. They have, however, admitted that according to the Minutes of the Tender Committee, the 'firm's representatives were not in favour of giving details of increase in writing as this was not their practice'. In view of the reluctance of the firm to give any further details except in respect of escalation in the cost of forgings and wages and also in view of the statement of the Ministry of Railways that no details other than those mentioned during discussions are available in the files', the Committee have no option but to conclude that the remaining escalations in cost granted to the firm were in respect of increase in their profit margin. The Ministry of Railways have further stated that even if the entire amount of Rs. 15,358 is taken as margin of profit, this would come to 14.7 per cent on the total price of Rs. 2,53,695. While the Committee would not like to go into the controversy whether the margin of profit allowed was 36.5 per cent as stated by audit or 14.7 per cent as claimed by the Ministry of Railways, the fact remains that the firm was allowed more than usual margin of profit of 10 per cent. The Committee cannot but express their dissatisfaction at the manner in which the firm was allowed such a high margin of profit.

56. The Committee further note that the price allowed for the March, 1974 order was higher than the last contract price by Rs. 36,467 per set. This included an increase of Rs. 7,835 which was justified by the firm on the ground that one of its sub-contractors had offered a discount if the components were given to it (sub-contractor) in batches instead of in piecemeal but the ordering in batches was not possible as it would involve extra cost. The team of Senior Scale officers of CLW who visited the firm's works allowed Rs. 7,000 on this account but the High Level Tender Committee (HLTC) conceded the increase of Rs. 7.835. The firm also declined to show any evidence or document to establish this claim stating that it would 'more or less tantamount to audit of books which had not been agreed to by them in principle'. The Ministry of Railways have stated that

they had asked M|s KPC officers to accept 5 ST & RGB per month but the firm did not agree to the same on the ground that they had not achieved the figure of 5 as yet and therefore, they had considered 4 ST and RGB per month only. Further, although the sub-contractor had offered a discount if the components were given to them in batches instead of piecemeal, M|s KPC stated that it was not possible for them to order in batches as this would entail building up of inventories which would involve extra costs. The Committee fail to understand why Railways should be required to pay an additional amount of Rs. 7,835 per set in order to compensate the firm for the loss of discount which the firm had forgone to suit their own convenience. This further fortifies the conclusion that by taking advantage of their position as sole indigenous supplier of the equipment, the firm had been dictating terms to the Railways to which the latter was meekly submitting. What is more disturbing is that the Ministry of Railways have tried to justify this increase by stating that 'A supplier has necessarily to build up all the costs in his pricing. His cost is based on all the expenditure involved and as such the loss of discount due to valid reasons which he had incurred would also account for increase in price'. The Committee find this argument totally untenable.

57. The Committee furter note that another element of price increase amounting to Rs. 3,000 per set was allowed to the firm in March 1974 order on the ground that the firm had revised the method of allocation of heat treatment shop cost. While earlier in the cost, the heat treatment shop cost was distributed equally between the various activities of the firm, they had now assessed that the major portion of the work done in the heat treatment was on the components of transmission only. The firm made a claim of Rs. 4,000|- extra heat treatment charges but did not show authenticated records in support of the claim. Ultimately an increase of Rs. 3,000 was agreed to after the visit of HLTC (High Level Tender Committee) to firm's works. The Ministry of Railways have stated that 'there is no record to indicate what actual documents they (H.L.T.C.) had checked but it is presumed that they would have examined the costing procedure, methods of allocation before arriving at the conclusion'. The Committee do not agree with this presumption, particularly in view of the fact that the firm had not shown any authenticated records in support of their demand. The Committee are of the view that this increase of Rs. 3,000 per set allowed to the firm was totally unjustified

58. The Committee note that the price of the equipment for March 1974 order was settled after providing for adequate escalation to cover deliveries upto September 1976. However, for the order of May, 1977, the firm was given a revised price of Rs. 4.12 lakhs representing and increase of 30 per cent to cover the price escalation between May, 1973 to

September 1976. Audit has pointed out that since March 1974 prices settled after providing for escalation upto September 1976, the escalation beyond this date only should have been taken into account while fixing the price for May 1977 order. The Ministry of Railways have stated that "it is incorrect to infer that 1974 order included all the elements of price in creases which had taken place after placement or order." It has however, been admitted by the Ministry of Railways that "a supplier does keep a margin in his pricing for price increases during the currency of the order but this cannot cover all the increases that take place since the last contract|quotation.". The Committee find that while fixing the price for May, 1977 order, the entire price escalation between May 1973 to September 1976 was taken into consideration. The Committee feel that while fixing the price for 1977 order the Ministry of Railways should have excluded this margin which the supplier had kept for meeting the price increases and the failure to do so has resulted in the fixation of price in 1977 order at a much higher level than warranted. This failure on the part of the Ministry of Railways has resulted in undue benefit to the firm.

59. The Committee note that in 1975, the Railway Board had taken a decision to introduce the 'Book Examination' clauses in stores contracts. However, the Committee regret to note that this clause was not included in any of the contracts entered into with the firm. The Committee are surprised at the contention of the Ministry of Railways that "in any case even if such a clause had been insisted upon, it is doubtful if the firm would have agreed to it as seen from their general reluctance to cost audit etc." The Committee feel that in view of the decision of the Railway Board, it was incumbent on the Tender Committee to have taken up the matter with the firm and insisted upon it. That the Tender Committee did not even take up the matter with the firm clearly shows that the Tender Committee was meekly submitting to all the demands made by the firm without even making any efforts to enforce the decision of the Railway Board..

60. While fixing the prices for November 1979 order in order to itemise the increase, the firm was asked to evolve a formula for Price variation on the basis of those adopted by Electrical Equipment Manufacturers. The Railways, however, could not enforce the formula as the firm did not agree to the same and indicated that at present they were unable to evolve any such formula and CLW could not unilaterally apply IEMA formula. In the view of the Committee, this is yet another instance where the Railways failed to persuade firm to accept such a reasonable demand.

61. The Committee find that in July-August 1971, the Ministry of Railways (Railway Board) decided to simplify the ST by eliminating its synchrnoising coupling and multiple plate clutch.. Meanwhile, in

July 1971 an order for 30 sets of fullfledged ST was placed on the firm The subsequent order in March 1972 was also for components and complete sets for ST. Although the later orders were suitably modified to delete the synchronising coupling, the earlier order placed in July 1971 was not amended which resulted in an avoidable expenditure of Rs. 1.21 lakhs. The Committee express their unhappiness over this lapse on the part of officials and would like the matter to be gone into to fix responsibility.

62. From the foregoing paragraphs, the Committee cannot but conclude that the firm (M/s. KPC Ltd., Pune) have taken undue advantage of their position as monopoly indigenous supplier of Suri Transmission (ST) and Reversing Gear Box (RGB) equipment and have been dictating their terms to the Railways in the matter of price fixation. While the formalities of having negotiations were gone through at the time of placing orders, in actual practice, practically all the demands of the firm were being agreed to. The firm not only did not agree to cost audit, but also refused to produce any authenticated evidence to support their demand for escalation in prices from time to time. Once the imports were stopped in 1967, no efforts were made by the Ministry of Railways to ascertain the international prices of similar equipment. No serious efforts have also been made to develop an alternative source of supply as is evident from the fact that it was only in 1979 that a developmental order was placed for 5 sets on another firm and even the same has not been seriously pursued. What is really surprising is that inspite of the decision of Railway Board in 1975, 'book examination' clause was not included in any of the contracts. The Committee would like to express their displeasure at the indulgence shown to this firm all along. The Committee would recommend that this is a fit case to be examined by the Cost Accounts Organisation of the Ministry of Finance to determine how far the increase in prices given to the firm from time to time were justified and the extent to which the manufacturer had derived undue benefit. The Committee would also like the matter to be examined at higher level to determine the policy of Government in regard to such cases where a sole indigenous manufacturer of any equipment taking advantage of his monopolistic position has been dictating terms to Government and forcing them to agree to escalations in pirces which in many cases are not justified.

NEW DELHI;
April 17, 1982
Chaitra 27, 1903 (*Saka*)

SATISH AGARWAL
Chairman
Public Accounts Committee

PART II

MINUTES OF THE SITTING OF THE COMMITTEE HELD ON 16th APRIL, 1982.

The Committee sat from 15.00 hrs. to 17.00 hrs.

PRESENT

Shri Satish Agarwal — *Chairman*

2. Shri Tridib Chaudhury
3. Shri Ashok Gehlot
4. Shri Hari Krishna Shastri
5. Shri Satish Prasad Singh
6. Shri N.K.P. Salve
7. Shri Indradeep Sinha.

REPRESENTATIVES OF AUDIT

1. Shri G. N. Pathak — *Director of Audit (Defence Services)*
2. Shri R. S. Gupta — *Director, Receipt Audit*
3. Shri N. Sivasubramaniam — *Director, Receipt Audit.*
4. Shri K. H. Chhaya — *Joint Director (Railways)*
5. Shri G. R. Sood — *Joint Director (Reports)*
6. Shri N. C. Roychoudhury — *Joint Director (Receipt Audit)*

Secretariat

1. Snri H. G. Paranjpe — *Joint Secretary*
2. Shri D. C. Pande — *Chief Financial Committee Officer*
3. Shri K. C. Rastogi — *Senior Financial Committee Officer*
4. Shri K. K. Sharma — *Senior Financial Committee Officer*

The Committee then took up for consideration and adopted the draft 92nd, 98th, 99th, 102nd and 103rd Reports with minor amendments|modifications. The Committee also approved some amendments| modifications arising out of factual verification by Audit.

The amendments|modifications made in the draft 102nd Report are indicated in Annexure.

The Committee then adjourned

ANNEXURE I

(*Vide* Part II of the Report)

Modifications/amendments made by the Public Accounts Committee in the draft 102nd Report on Para 9 of C&AG's Advance Report for the year 1979-80 (Railways) relating to Chittaranjan Locomotive Works—Suri Transmission and reversing gear boxes for dies shunters

Page	Para	Line	Amendments
20	1.27	15	*Insert* 'was Rs. 9225' *after* 'this heading'
33	1.41	29	*Read* 'indices' *for* 'indicates'
39	1.46	13	*Read* 'completely' *for* 'completing'
44	1.51	5	*Read* 'during' *for* 'doing'
46	1.54	10	*Read* 'increases' *for* 'increased'
50	1.56	6	'*Insert* 'in' *after* 'to order'
53	1.58	18	'excluded' *for* 'taken into accounts'
		19	*Read* 'had kept' *for* 'keeps'
55	1.60	9—10	*Read* 'Railways failed to persuade the firm to accept such a reasoanable demand.' *for* 'firm did not accept even a very reasoable demand of the Railways.'
57	1 62	9	*Insert* 'far' *after* 'detrmine how'

APPENDIX-I

STATEMENT OF CONCLUSIONS AND RECOMMENDATIONS

S.No.	Para No.	Ministry/Deptt. concerned	Conclusions/Recommendations
1	2	3	4
1	50	Railways	The diesel locomotives produced at Chittaranjan Locomotives Works (CLW) were in the initial stages provided with Suri Transmission (ST) and a reversing gear box (RGB) to enable working of the locomotives for both shunting and shuttle services. Earlier these ST and RGB were being imported, but since November, 1967, CLW has been procurring these equipment from an indigenous manufacturer M/s. Kirloskar Pneumatic Co. Ltd., Pune. This is the only firm which manufactures hydraulic transmission equipment and heavy duty gear boxes. In July 1971, this firm also obtained a licence for manufacture of ST.
2	51	Do.	The procurement of the equipment was made after obtaining quotations on single tender basis and negotiating a price thereafter with the firm. From 1976, open tenders were invited but the technically acceptable offer was from this firm only. The price for the initial order exclusive of certain imported components supplied free by CLW included about 30 per cent price preference over the contemporaneous CIF cost of

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			imported complete ST and RGB. For the subsequent orders, the price for the initial order was treated as the base price taking into account escalation for wages, materials etc. over the previous contract as indicated by the firm and to the extent agreed to during negotiations.
3	52	Railways	The Committee note that there has been substantial increase in the price of the equipment in subsequent orders. While in November, 1967 when the first order was placed, the price per set was Rs. 2,20,183 the same increased to Rs. 3,18,000 per set in March, 1974 and Rs. 4,51,530 in January 1979. Within ten months i.e. in November, 1979 the price further increased to Rs. 5,73,450 per set i.e. an increase of Rs. 1,21,880 per set. A review in the audit of the prices fixed from time to time has revealed that the price increases allowed on several counts were not justified.
4	53	Do.	The Committee have been informed by the Ministry of Railways that the prices for the first order of November 1967 were determined by the purchase policy as governed by the directives of the Government of India based on the recommendation of the Stores Purchase Committee. However, it is seen from the letter of Railway Board dated 18 May, 1956 on the subject that in the purchase policy, it has been laid down that 'in respect of lines of manufacture which are the monopoly of a single firm or a group of firms, the degree of price preference to be given may be subject to examination of costs of manufacture by Government where considered necessary'. The Committee are, however, surprised to note that

			no cost examination has been conducted either at the time of placing the first or even subsequent order, nor the firm had at any stage produced authenticated data or documentary evidence to substantiate their demand for escalation in prices. The Committee are not convinced with the reply of the Ministry of Railways that in the absence of cost audit and legal compulsion for the firm to furnish authenticated detailed price break-up, the Tender Committee is left with no other alternative but to come to an overall assessment and while doing so, getting as much information as possible'. The committee are of the firm view that no indigenous manufacturer should be allowed to take undue advantage of its monopoly position to dictate terms in respect of price of the equipment supplied by them and the Railways should have insisted upon cost audit and authenticated detailed break-up supported by documentary proof before agreeing to such escalation in costs which in many cases were not justified.
5	54	Do.	The Committee note that to a query from them as to why the Department of Heavy Industry was not approached for a cost probe by the Bureau of Industrial Costs and Prices whereas such a study of the pricing policy of Seamless Steel Tubes for which M/s. Indian Tube Co. Is the sole manufacturer was conducted by the BICP, the Ministry of Railways have replied that 'the Tender Committee after getting convinced of the increases asked for by the firm on an overall basis recommended the rates for acceptance Hence, a reference to BICP was not felt necessary.' The Committee fail to understand how in the absence of a cost study and authenticated data in respect of escalation in costs, the Tender Committee could decide that the escalation in prices asked for by the firm

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			was justified. The Committee cannot but conclude that the whole matter has been dealt with in a very casual manner in utter desregard of principles of financial properiety.
6	55	Railways	The Committee note that for November 1979, contract, the firm had asked for an increase of Rs. 60,763 including Rs. 30,000 for increased cost of forgings and Rs. 12,000 for wage escalations. After negotiations, increase of Rs. 57,358 was agreed to. Even presuming that the reduction accepted by the firm was in its profit margin, the latter amounted to Rs. 15,358, *i.e.* 36.5 per cent of the price increase of Rs. 42,000 on materials and wages. The Ministry of Railways have, however, stated that this item viz. 'margin of profit' was not reflected in any of the firm's documents. They have, however admitted that according to the Minutes of the Tender Committee, the 'firm's representatives were not in favour of giving details of increase in writing as this was not their practice'. In view of the reluctance of the firm to give any further details except in respect of escalation in the cost of forgings and wages and also in view of the statement of the Ministry of Railways that 'no details other than those mentioned during discussions are available in the files', the Committee have no option but to conclude that the remaining escalations in cost granted to the firm were in respect of increase in their profit margin. The Ministry of Railways have further stated that even if the entire amount of Rs. 15,358 is taken as margin of profit, this

			would come to 14.7 per cent on the total price of Rs. 2,53,695. While the Committee would not like to go into the controversy whether the margin of profit allowed was 36.5 per cent as stated by audit or 14.7 per cent as claimed by the Ministry of Railways, the fact remains that the firm was allowed more than usual margin of profit of 10 per cent. The Committee cannot but express their dissatisfaction at the manner in which the firm was allowed such a high margin of profit.
7	56	Do.	The Committee further note that the price allowed for the March, 1974 order was higher than the last contract price by Rs. 36,467 per set. This included an increase of Rs. 7,835 which was justified by the firm on the ground that one of its sub-contractors had offered a discount if the components were given to it (sub-contractor) in batches instead of in piecemeal but the ordering in batches was not possible as it would involve extra cost. The team of Senior Scale officers of CLW who visited the firm's works allowed Rs. 7,000 on this account but the High Level Tender Committee (HLTC) conceded the increase of Rs. 7,835. The firm also declined to show any evidence or document to establish this claim stating that it would 'more or less tantamount to audit of books which had not been agreed to by them in principle'. The Ministry of Railways have stated that they had asked M/s. KPC officers to accept 5 ST & RGB per month but the firm did not agree to the same on the ground that they had not achieved the figure of 5 as yet and therefore, they had considered 4 ST and RGB per month only. Further, although the sub-contractor had offered a discount if the components were given to them in batches instead of piecemeal, M|s. KTC stated that it was not possible for them to order

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			in batches as this would entail building up of inventories which would involve extra costs. The Committee fail to understand why Railways should be required to pay an additional amount of Rs. 7,835 per set in order to compensate the firm for the loss of discount which the firm had foregone to suit their own convenience. This further fortifies the conclusion that by taking advantage of their position as sole indigenous supplier of the equipment the firm had been dictating terms to the Railways to which the latter was meekly submitting. What is more disturbing is that the Ministry of Railways have tried to justify this increase by stating that 'A supplier has necessarily to build up all the costs in his pricing. His cost is based on all the expenditure involved and as such the loss of discount due to valid reasons which he had incurred would also account for increase in price'. The Committee find this argument totally untenable.
8	57	Railways	The Committee further note that another element of price increase amounting to Rs. 3,000 per set was allowed to the firm in March, 1974 order on the ground that the firm had revised the method of allocation of heat treatment shop cost. While earlier in the cost, the heat treatment shop cost was distributed equally between the various activities of the firm, they had now assessed that the major portion of the work done in the heat treatment was on the components of transmission only. The firm made a claim of Rs. 4,000 extra heat treatment charges but did not show authen-

			ticated records in support of the claim. Ultimately an increase of Rs. 3,000 was agreed to after the visit of HLTC (High Level Tender Committee) to firm's works. The Ministry of Railways have stated that 'there is no record to indicate what actual documents they (H.L.T.C.) and checked but it is presumed that they would have examined the costing procedure, methods of allocation before arriving at the conclusion'. The Committee do not agree with this presumption, particularly in view of the fact that the firm had not shown any authenticated records in support of their demand. The Committee are of the view that this increase of Rs. 3,000 per set allowed to the firm was totally unjustified.
9	58	Railways	The Committee note that the price of the equipment for March, 1974 order was settled after providing for adequate escalation to cover deliveries upto September, 1976. However, for the order to May, 1977, the firm was given a revised price of Rs. 4.12 lakhs representing an increase of 30 per cent to cover the price escalation between May, 1973 to September, 1976. Audit has pointed out that since March, 1974 prices were settled after providing for escalation upto September, 1976, the escalation beyond this date only should have been taken into account while fixing the price for May, 1977 order. The Ministry of Railways have stated that it is incorrect to infer that 1974 order included all the elements of price increases which had taken place after placement of order". It has however, been admitted by the Ministry of Railways that "a supplier does keep a margin in his pricing for price increases during the currency of the order but this cannot cover all the increases that take place since the last contract/quotation". The Committee find that while fixing the price for May, 1977

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			order, the entire price escalation between May, 1973 to September, 1976 was taken into consideration. The Committee feel that while fixing the price for 1977 order the Ministry of Railways should have excluded this margin which the supplier had kept for meeting the price increases and the failure to do so has resulted in the fixation of price in 1977 order at a much higher level than warranted. This failure on the part of the Ministry of Railways has resulted in undue benefit to the firm.
10	59	Railways	The Committee note that in 1975, the Railway Board had taken a decision to introduce the 'Book Examination' clauses in stores contracts. However, the Committee regret to note that this clause was not included in any of the contracts entered into with the firm. The Committee are surprised at the contention of the Ministry of Railways that "in any case even if such a clause had been insisted upon, it is doubtful if the firm would have agreed to it as seen from their general reluctance to cost audit etc." The Committee feel that in view of the decision of the Railway Board, it was incumbent on the Tender Committee to have taken up the matter with the firm and insisted upon it. That the Tender Committee did not even take up the matter with the firm clearly shows that the Tender Committee was meekly submitting to all the demands made by the firm without even making any efforts to enforce the decision of the Railway Board.

11	60	Do.	While fixing the prices for November, 1979 order in order to itemise the increase, the firm was asked to evolve a formula for Price variation on the basis of those adopted by Electrical Equipment Manufacturers. The Railways, however, could not enforce the formula as the firm did not agree to the same and indicated that at present they were unable to evolve any such formula and CLW could not unilaterally apply IEMA formula. In the view of the Committee, this is yet another instance where the Railways failed to persuade the firm to accept such a reasonable demand.
12	61	Do.	The Committee find that in July-August, 1971, the Ministry of Railways (Railway Board) decided to simplify the ST by eliminating its synchronising coupling and multiple plate clutch. Meanwhile, in July, 1971 an order for 30 sets of fullfledged ST was placed on the firm. The subsequent order in March, 1972 was also for components and complete sets for ST. Although the later orders were suitable modified to delete the synchronising coupling, the earlier order placed in July, 1971 was not amended which resulted in an avoidable expenditure of Rs. 1.21 lakhs. The Committtee express their unhappiness over this lapse on the part of officials and would like the matter to be gone into to fix responsibility.
13	62	Do.	From the foregoing paragraphs, the Committee cannot but conclude that the firm (M/s. KPC Ltd., Pune) have taken undue advantage of their position as monopoly indigenous supplier of Suri Transmission (ST) and Reversing Gear Box (RGB) equipment and have been dictating their terms to the Railways in the matter of price fixation. While the formalities of having negotiations were gone through at the time of placing orders, in actual practice, practically al lthe demands of the firm were being agreed

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			to. The firm not only did not agree to cost audit, but also refused to produce any authenticated evidence to support their demand for escalation in prices from time to time. Once the imports were stopped in 1967, no efforts were made by the Ministry of Railways to ascertain the international prices of similar equipment. No serious efforts have also been made to develop an alternative source of supply as is evident from the fact that it was only in 1979 that a developmental order was placed for 5 sets on another firm and even the same has not been seriously pursued. What is really surprising is that inspite of the decision of Railway Board in 1975, 'book examination' clause was not included in any of the contracts. The Committee would like to express their displeasure at the indulgence shown to this firm all along. The Committee would recommend that this is a fit case to be examined by the Cost Accounts Organisation of the Ministry of Finance to determine how far the increase in prices given to the firm from time to time were justified and the extent to which the manufacturer had derived undue benefit. The Committee would also like the matter to be examined at higher level to determine the policy of Government in regard ot such cases where a sole indigenous manufacturer of any equipment taking advantage of his monopolistic position has been dictating terms to Government and forcing them to agree to escalation in prices which in many cases are not justified.

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