Sugar Industry Outlook

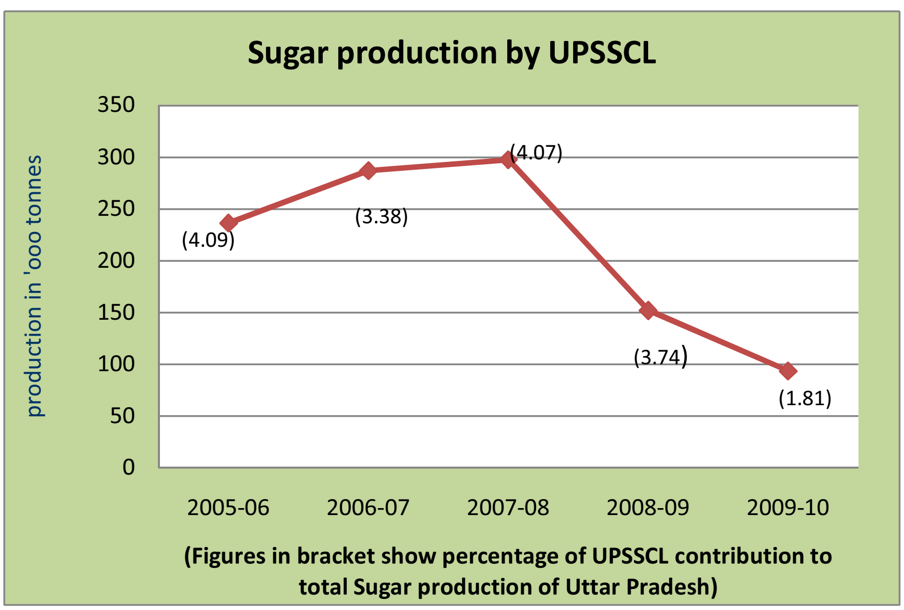
Sugar is produced in over 122 Countries across the World. It is estimated that the world production would be around 167 million metric tonne in the 2010-11 International Sugar Season (October-September). India is the second largest sugar producer in the world after Brazil. It contributes approximately 14.68 *per cent* of the total sugar production in the world. Uttar Pradesh with its share of 27 *per cent* is the second largest producer of sugar in the country after Maharashtra.

UPSSCL and its role in Sugar Industry of Uttar Pradesh

The Uttar Pradesh State Sugar Corporation Limited (UPSSCL) was established in 1971, under the Companies Act, 1956 as a wholly owned undertaking of the Government of Uttar Pradesh. During the years 1971 to 1989, 28 mills were acquired by the Company while one mill was purchased in open auction in 1974. Six mills were also established between 1974 and 1988.

During the years 2001 to 2003 the Company, while retaining 11 operating mills, transferred 18 mills (ten closed and eight unviable) to newly formed subsidiary, viz.- Uttar Pradesh Rajya Chini Evam Ganna Vikas Nigam Limited (UPRCGVNL) and four mills to three other subsidiaries of UPSSCL. Two mills (Doiwala and Kichcha sugar mills) were transferred to Uttarakhand after partition of Uttar Pradesh in the year 2002.

UPSSCL is the only Public Sector Company engaged in sugar production in Uttar Pradesh. During the period from 2005-06 to 2009-10 the production by the Company ranged from 93.54 to 297.60 thousand tonnes. The graph below depicts the contribution of the Company in sugar production in the State:



The Government of Uttar Pradesh (GoUP) decided to privatise/sell sugar mills of UPSSCL in June 2007. In execution of this decision, ten operating mills of

UPSSCL and 11 closed mills of UPRCGVNL were sold during the July 2010 -October 2010 and January 2011 to March 2011 respectively.

This Audit Report

This Audit Report deals with our findings during the audit of the sale process of the mills of UPSSCL and its subsidiary UPRCGVNL and consists of the following:

Chapter -1 Introduction

Chapter -2 The Disinvestment Process

Chapter -3 Valuation of Sugar Mills

Chapter -4 Expected Price-its Disclosure

Chapter -5 Lack of Competition in the Bidding Process

Chapter -6 Stamp Duty and Procedural Lapses

While valuation is a subjective matter and open to different interpretations, our observations on valuation of mills are based on Reports of Valuers appointed by Management of the Company. In case of 11 closed sugar mills, we have also examined the circle rates of land as notified by Office of District Magistrate of the respective areas for comparative analysis with the rates of land taken by Valuers.

Major Findings

Important audit observations are discussed below:

Valuation of Sugar Mills

UPSSCL

The Advisor(IFCI) reduced the valuation of land as worked out by the Valuers by three *per cent* to 30 *per cent* on the grounds of dispute over the land .This reduction amounted to ₹ 90 crore in case of four sugar mills[1]. Further reduction in the value of land by Advisor lacked justification as these aspects had already been taken into consideration by the Valuers.

(Paragraph 3.3)

The Advisor decided that the average value of land and building be discounted by 25 *per cent* for restricted land use, large land area, stamp duty to be paid by purchasers and other constraints for arriving at expected price.

(Paragraph 3.3.2)

The Core Group of Secretaries (CGD), on the ground that Discounted Cash Flow (DCF) value was more relevant from the point of view of prospective buyers, reversed the weightage to two-third to DCF method and one-third to the value of land and building while arriving at the value of mills, resulting in reduction of the expected price by ₹ 243.48 crore.

(Paragraph 3.3.3)

[1] Amroha, Bijnore, Bulandsahar and Saharanpur

Scrap value of ₹ 32.88 crore of the Plant and Machinery of the ten mills of UPSSCL was included in final expected price instead of its net realisable value of ₹ 114.96 crore .This resulted in undervaluation by ₹ 82.08 crore.

(Paragraph 3.4)

Reduction in valuation by ₹ 223.72 crore due to clubbing of Land of old and new mills of Saharanpur unit

(Paragraph 3.5)

UPRCGVNL

Reduction in the average market value of Land by ₹ 128.41 crore compared to the average market value given by earlier Valuers appointed in 2007-08.

(Paragraph 3.7.2)

Valuation of Plant and Machinery at scrap value lower than that suggested by the Adviser resulted in reduction of expected price by ₹ 43.20 crore.

(Paragraph 3.9)

Expected Price and its Disclosure

Disclosure of expected price to bidders and change in methodology of bidding in middle of the bid process adversely affected the bid price received. However the money value impact could not be determined. The bid prices received were far below the expected price in 14 out of the 21 mills sold.

(Paragraph 4.1)

Lack of Competition in the Bidding Process

There was complete lack of competition as two out of three competing Companies were related to each other in sale of ten operating mills of UPSSCL. In case of UPRCGVNL, all the bidding Companies bid in a concerted manner and unusual withdrawal of bids by the original highest bidders in favour of challengers indicated the cartelization / concerted bid by a group of related Companies affected the realization of fair value of sugar mills. In respect of three mills[2] of UPSSCL, only ₹ 166.85 crore could be realised against Expected Price of ₹ 291.55 crore. In case of 11 closed mills of UPRCGVNL, ₹ 91.65 crore was realised against total Expected Price of ₹ 173.63 crore. Management and CGD failed to detect these issues as they did not insist on submission of the requisite documentation by bidders.

(Paragraphs 5.1-5.7)

Stamp Duty

Acceptance of under valuation of Land by the registering authorities resulted in total loss of revenue of ₹ 100.77 crore to the State Exchequer.

(Paragraph 6.1)

2 Bijnaur, Bulandsahar and Saharanopur.

The impact of our findings has been summarized in the table below:

UPSSCL			
Chapter	**Paragraph**	**Shortcomings**	**Impact (₹ in crore)**
Chapter 3 Valuation - Sugar Mills	3.3	Reduction in value of land of sugar mills	90.00
	3.3.2	Additional discount on land and buildings of sugar mills (₹192.48 crore included in ₹243.48 crore)	
	3.3.3	Application of more weightage to discounted cash flow method	243.48
	3.4	Valuation of plant and machinery as scrap	82.08
	3.5	Reduction in valuation due to clubbing of land of old and new mills	223.72
Chapter 4 Expected Price-its Disclosure	4.1	Disclosure of expected price to bidders before submission of Request for Proposal (financial bid) and change in methodology of bidding in middle of bid process(**money value impact can not be determined)**	
	4.2	Adjustments in Expected Price	21.15
Chapter 5 Lack of Competition in the Bidding Process	5.1	Lack of competition due to related bidders (two out of three bidders) others	124.70
Chapter 6 Stamp Duty and Procedural Lapses	6.1	Short levy of Stamp duty on sale deed	53.71
	6.2	Excess payment to Advisor	1.25
	6.3	Failure to recover the cost of Repair and Maintenance from purchasers of mill	1.45
Total of UPSSCL (A)			**841.54**

UPRCGVNL			
Chapter	**Paragraph**	**Shortcomings**	**Impact (₹ in crore)**
Chapter 3 Valuation - Sugar Mills	3.7.2	Unjustified reduction in market value of land	128.41
	3.8	Undue discount for stamp duty and registration fees	10.16
	3.8.1	Discount for large size of land and non-marketability	19.29
	3.9	Valuation of plant and machinery at low scrap value	43.20
Chapter 4 Expected Price-its Disclosure	4.1	Disclosure of expected price to bidders before submission of Request for Proposal (financial bid) (**money value impact can not be determined)**	
	4.2	Adjustments in Expected Price	8.20
Chapter 5 Lack of Competition in the Bidding Process	5.3	Lack of competition due to all bidders related to each other	81.98
Chapter 6 Stamp Duty and Procedural Lapses	6.1	Short levy of stamp duty on sale deeds	47.06
Total of UPRCGVNL(B)			**338.30**
Grand Total (A+B)			**1179.84**