

CHAPTER I: INTRODUCTION

1.1 Profile of the audited entities

This report relates to matters arising from the audit of financial transactions of the following organisations under the Ministry of Defence:

1.1.1 Indian Navy

The Indian Navy is headed by the Chief of Naval Staff. Integrated Headquarters Ministry of Defence (Navy) is the apex body and chief management organisation responsible for command, control and administration of the Indian Navy. Operational and maintenance units of Indian Navy primarily consist of warships and submarines, dockyards, naval ship repair yards, armament and weapon equipment depots and material organisations. Indian Navy has an Aviation wing with air stations and allied repair facilities under them. Indian Navy also has warship overseeing teams which monitor the construction of ships and submarines at the concerned shipyards.

The objective of the Navy's military role is deterrence/ dissuasion against any intervention or act which is against our National interests, and the ability to inflict a crushing defeat on the adversary in the event of hostilities. Major contributions¹ of the Indian Navy to the nation during the year 2014-15 were:

- Search and rescue operation of missing Malaysian Aircraft.
- Deployment of Naval Ships to undertake evacuation of personnel from Iraq.
- Deployment of Indian Naval Ship for anti piracy activities and surveillance of the Exclusive Economic Zones of Maldives, Mauritius and Seychelles.
- Commissioning of National Command Control Communication Intelligence (NC3I) network.
- Commissioning of Offshore Patrol Vessels and Destroyer class of ships.
- Commissioning of operational squadron for MiG 29K aircraft at Goa.

¹ Source: Annual Report 2014-15 of Ministry of Defence, Government of India.

1.1.2 Indian Coast Guard

The Indian Coast Guard was created to protect the country's vast coastline and offshore wealth. The Director General, Coast Guard exercises general superintendence, direction and control of the Coast Guard. The Coast Guard has various types of patrol vessels for patrolling the coastline for illegal activities like smuggling, trespassing into Indian Maritime zones, etc. Coast Guard also has an aviation wing to patrol the coastal areas and carry out Search and Rescue Mission at sea with fixed and rotary wing aircraft. The aviation wing has Coast Guard Air stations and Air Enclaves for effectively carrying out its duties in all the coastal areas. Major achievements² of the Coast Guard during the year 2014-15 were as follows:

- Commissioning of Coast Guard stations at Frazerganj, West Bengal and Nizampatnam, Andhra Pradesh.
- Commissioning of five fast patrol vessels.
- Commissioning of four Air Cushion Vehicles.
- Commissioning of nine Interceptor Boats.
- Commissioning of Coast Guard Air Enclave at Bhubaneswar.

1.1.3 Defence Public Sector Undertakings

There are four Defence Public Sector Shipyards (DPSS) viz., Mazagon Dock Limited (MDL), Garden Reach Shipbuilders & Engineers Limited (GRSE), Goa Shipyard Limited (GSL) and Hindustan Shipyard Limited (HSL) under the administrative control of the Ministry of Defence. The four shipyards are engaged in building warships and vessels of various sizes for the maritime forces of the country. The management of the shipyards is vested in the Board of Directors headed by a Chairman & Managing Director who is assisted by Functional Directors. While MDL, GRSE and GSL are under the administrative control of Ministry of Defence, the administrative control of HSL was transferred from Ministry of Shipping to Ministry of Defence in February 2010. Major achievements of these shipyards during the year 2014-15 were as follows:

- MDL delivered first of P-15A Destroyers to Indian Navy and signed contract with Indian Navy for construction and delivery of four P-17A class frigates.

² Source: Annual Report 2014-15 of Ministry of Defence, Government of India.

- GRSE delivered first Anti Submarine Warfare Corvette, “INS Kamorta” to Indian Navy.
- GSL delivered fourth Naval Offshore Patrol Vessel to Indian Navy.
- HSL undertook repairs of various Indian Naval ships including refits of INS Darshak, INS Shakti and INS Kamorta.

The report also relates to matters arising from the audit of financial transactions of the following organisations under the Ministry of Defence:

- Defence Research and Development Organisation of Ministry of Defence and its laboratories dedicated primarily to Indian Navy.
- Defence Accounts Department dealing with Indian Navy and Coast Guard.
- Military Engineer Services dealing with Indian Navy and Coast Guard.

1.2 Authority for audit

Article 149 of the Constitution of India and the Comptroller and Auditor General’s (Duties, Powers and Conditions of Service) Act 1971 and Regulations of Audit and Accounts 2007, give authority for audit and detailed methodology of audit and its reporting.

Office of the Principal Director of Audit, Navy, New Delhi, and its three branch offices at Mumbai, Vishakhapatnam and Kochi are responsible for audit of Indian Navy, Indian Coast Guard and other related organisations. MDL, GRSE, GSL and HSL are audited by the Principal Director of Commercial Audit & Ex-officio Member Audit Board IV, Bengaluru.

1.3 Audit methodology and procedure

Audit is prioritised through an analysis and evaluation of risks so as to assess their criticality in key operating units. Expenditure incurred, operational significance, past audit results and strength of internal control are amongst the main factors which determine the severity of the risks. An annual audit plan is formulated to conduct audit on the basis of risk assessment.

Audit findings of an audited entity are communicated through Local Test Audit Reports/Statement of Cases. The response from the audited entity is considered which may result in either settlement of the audit observation or referral to the next audit cycle for compliance. Serious irregularities are processed as draft paragraphs for inclusion in the Audit Reports which are submitted to the President of India under Article 151 of the Constitution of India, for laying them before each House of Parliament. Performance Audits are done through structured exercise by defining scope of audit, holding entry conference, sampling of units, exit conference, inclusion of feedback on draft report and issuance of final report.

1.4 Defence Budget

The Defence budget is broadly categorised under Revenue and Capital expenditure. While Revenue expenditure includes pay and allowances, stores, transportation and work services, etc., Capital expenditure covers expenditure on acquisition of new ships, submarines, weapons, ammunition and replacement of obsolete stores, construction work, etc. Details of Defence expenditure during 2010-11 to 2014-15 is reflected in the Table below:

Table 1.1: Total Defence Budget allocation and Actual expenditure

(₹ in crore)

Description	Year				
	2010-11	2011-12	2012-13	2013-14	2014-15
Budget allocation	1,56,127	1,78,891	1,98,526	2,17,649	2,54,000
Actual expenditure	1,58,723	1,75,898	1,87,469	2,09,789	2,37,394

The Defence expenditure in the previous five years registered an increase of 49.56 *per cent* from ₹1,58,723 crore in 2010-11 to ₹2,37,394 crore in 2014-15. Defence expenditure in 2014-15 increased by 13.16 *per cent* over the expenditure of previous year. The share of Indian Navy in the total expenditure on Defence Services in 2014-15 was ₹36,622 crore *i.e.*, 15.43 *per cent*.

1.5 Budget and Expenditure of Navy

The summarised position of appropriation and expenditure during 2010-11 to 2014-15 in respect of Indian Navy is reflected in the Table below:

Table 1.2: Appropriation and Expenditure

(₹ in crore)

Description		Year				
		2010-11	2011-12	2012-13	2013-14	2014-15
Final Grant	Capital	16,905	17,922	17,066	19,386	21,807
	Revenue	10,010	12,347	12,755	13,364	14,536
	Total	26,915	30,269	29,821	32,750	36,343
Actual Expenditure	Capital	17,140	19,212	17,760	20,359	22,270
	Revenue	10,145	12,059	12,119	13,472	14,352
	Total	27,285	31,271	29,879	33,831	36,622
Total Excess/ Savings (+)/(-)	Capital	(+)235	(+)1,290	(+)694	(+)973	(+)463
	Revenue	(+)135	(-)288	(-)636	(+)108	(-)184
	Total	(+)370	(+)1,002	(+)58	(+)1,081	(+)279

Source: Year-wise Appropriation Accounts of Defence Services.

An analysis of the Appropriation Accounts, Defence Services for each of the five years had been included in the Report of the Comptroller and Auditor General of India for the relevant years, Union Government– Accounts of the Union Government.

1.5.1 Navy Expenditure

A broad summary of expenditure of Indian Navy is given in the Table below:

Table 1.3: Expenditure of Indian Navy

(₹ in crore)

Description	Year				
	2010-11	2011-12	2012-13	2013-14	2014-15
Total Defence Expenditure	1,58,723	1,75,898	1,87,469	2,09,789	2,37,394
Total Expenditure of Navy	27,285	31,270	29,879	33,831	36,622
Percentage change over previous year	(+)18.96	(+)14.61	(-) 4.45	(+)13.23	(+)8.25
As a percentage of total Defence Expenditure	17.19	17.78	15.94	16.13	15.43
Revenue Expenditure	10,145	12,059	12,119	13,472	14,352
Capital Expenditure	17,140	19,211	17,760	20,359	22,270

Source: Year-wise Appropriation Accounts of Defence Services

The total expenditure incurred by the Indian Navy during 2010-2015 ranged between 15.43 and 17.78 *per cent* of the total Defence expenditure. In the year 2014-15, the expenditure of Indian Navy rose by 8.25 *per cent* from ₹33,831 crore to ₹36,622 crore as compared to the previous year.

1.5.2 Capital Expenditure

The average annual distribution of expenditure over different categories for the last five years (2010-11 to 2014-15) for Indian Navy is depicted in the Table below:

Table 1.4: Capital Expenditure of Indian Navy

(₹ in crore)

Head	Year				
	2010-11	2011-12	2012-13	2013-14	2014-15
Naval Fleet	10,620 (62%)	10,320 (54%)	11,074 (62%)	8,151 (40%)	13,355 (60%)
Naval Dockyard	720 (4%)	648 (3%)	752 (4%)	633 (3%)	635 (3%)
Aircraft and Aero-Engine	3,187 (19%)	4,336 (23%)	1,695 (10%)	7,746 (38%)	3,248 (15%)
Construction Works	637 (4%)	515 (3%)	527 (3%)	516 (3%)	646 (3%)
Other Equipment ³	1,578 (9%)	2,583 (13%)	2,773 (16%)	2,630 (13%)	3,654 (16%)
Others	398 (2%)	809 (4%)	939 (5%)	683 (3%)	731 (3%)
Total	17,140	19,211	17,760	20,359	22,270⁴

Source: Year-wise Appropriation Accounts of Defence Services.

The Capital expenditure of the Indian Navy rose from ₹17,140 crore to ₹22,270 crore *i.e.*, by 29.93 *per cent* during five year period from 2010-11 to 2014-15. As compared to previous year, the Capital expenditure of the Indian Navy increased by 9.39 *per cent i.e.*, from ₹20,359 crore in 2013-14 to ₹22,270 crore in 2014-15. During the year 2014-15, a significant portion (60 *per cent*) of Capital expenditure was incurred on naval fleet, 16 *per cent* and 15 *per cent* was spent on

³ Other equipment includes Electrical/Electronics, Weapon, Space and Satellite, Electronic Warfare, etc.

⁴ The Actual figure is ₹22,269.66 crore, which is rounded off to ₹22,270 crore.

other equipment and aircraft and aero engine respectively and 3 per cent was spent each on naval dockyard, construction works and others.

1.5.3 Revenue Expenditure

The distribution of expenditure over different categories of Revenue expenditure for the last five years is depicted below:

Table 1.5: Revenue Expenditure of Indian Navy

(₹ in crore)

Head	Year				
	2010-11	2011-12	2012-13	2013-14	2014-15
Pay and allowances	3,731 (37%)	4,508 (37%)	4,697 (39%)	5,085 (38%)	5,788 (40%)
Stores	3,437 (34%)	4,173 (35%)	3,982 (33%)	4,619 (34%)	4,151 (29%)
Works	701 (7%)	763 (6%)	760 (6%)	1,031 (8%)	1,124 (8%)
Transport	288 (2%)	353 (3%)	380 (3%)	347 (3%)	355 (3%)
Repair/ Refit	606 (6%)	768 (6%)	654 (5%)	593 (4%)	863 (6%)
Others	1,382 (14%)	1,494 (12%)	1,646 (14%)	1,797 (13%)	2,071 (14%)
Total	10,145	12,059	12,119	13,472	14,352

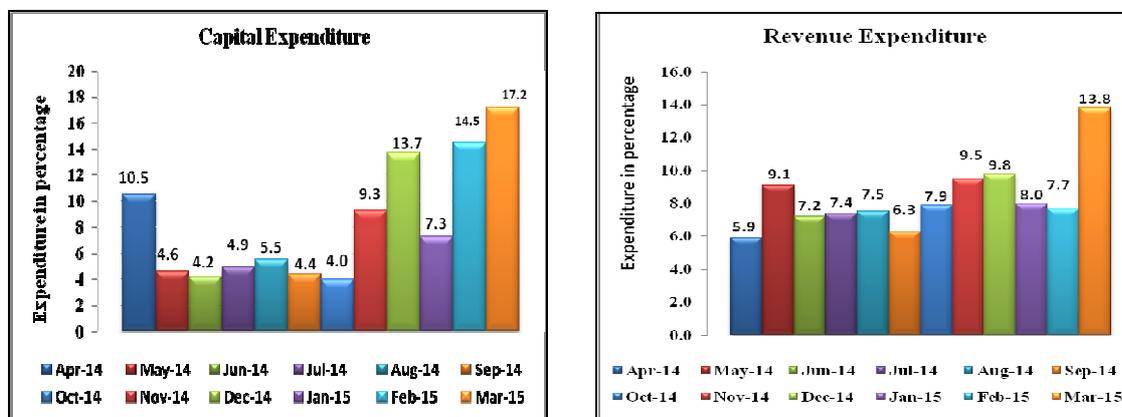
Source: Year-wise Appropriation Accounts of Defence Services

Revenue expenditure of the Indian Navy increased by 41 per cent from ₹10,145 crore to ₹14,352 crore during five year period from 2010-11 to 2014-15. As compared to previous year, the Revenue expenditure of the Indian Navy increased by 6.53 per cent i.e., from ₹13,472 crore in 2013-14 to ₹14,352 crore in 2014-15. The Revenue expenditure of the Indian Navy was mainly incurred on pay and allowances and stores contributing 40 per cent and 29 per cent respectively.

1.5.4 Flow of Expenditure of Indian Navy during the year

The flow of Capital and Revenue expenditure during 2014-15 is indicated below:

Figure: 1.1 Flow of Expenditure of Indian Navy during 2014-15



Source: Information provided by Ministry of Defence (Finance) Budget-I Section.

Scrutiny of flow of expenditure revealed that Navy incurred about 17.2 per cent of Capital expenditure in the month of March 2015 and about 39 per cent in the last quarter of the financial year which exceeded the limit of 15 per cent for the month of March and 33 per cent for the last quarter as prescribed by the Ministry of Finance. The Revenue expenditure of Navy was within the limits prescribed by Ministry of Finance.

1.6 Budget and Expenditure of Coast Guard

Budget of the Coast Guard forms part of the Civil Grant of the Ministry of Defence. The amount provided for revenue and capital are under the Major Head 2037- 'Customs (Preventive and other functions- Coast Guard Organisations)' and 4047- 'Capital Outlay of Fiscal Services, Customs (Coast Guard Organisation)' respectively. Separate Major heads for Coast Guard expenditure under Ministry of Defence have not been opened.

1.6.1 Expenditure of Coast Guard

A broad summary of allotment and expenditure is given in the Table below:

Table 1.6: Expenditure of Coast Guard

(₹ in crore)

Description		Year				
		2010-11	2011-12	2012-13	2013-14	2014-15
Final Grant/ Appropriation	Capital	1,200	1,600	1,565	1,060	1,140
	Revenue	816	933	960	1,018	1,295
	Total	2,016	2,533	2,525	2,078	2,435
Expenditure	Capital	1,201	1,575	1,565	1,070	1,142
	Revenue	814	926	945	1,048	1,286
	Total	2,015	2,501	2,510	2,118	2,428

(Source: Information provided by Coast Guard Headquarters)

The total expenditure of Coast Guard ranged between ₹2,015 crore and ₹2,510 crore from 2010-11 to 2014-15. The expenditure increased by 14.64 *per cent* in 2014-15 as compared to the previous year. In absolute terms the expenditure of Coast Guard increased from ₹2,118 crore in 2013-14 to ₹2,428 crore in 2014-15.

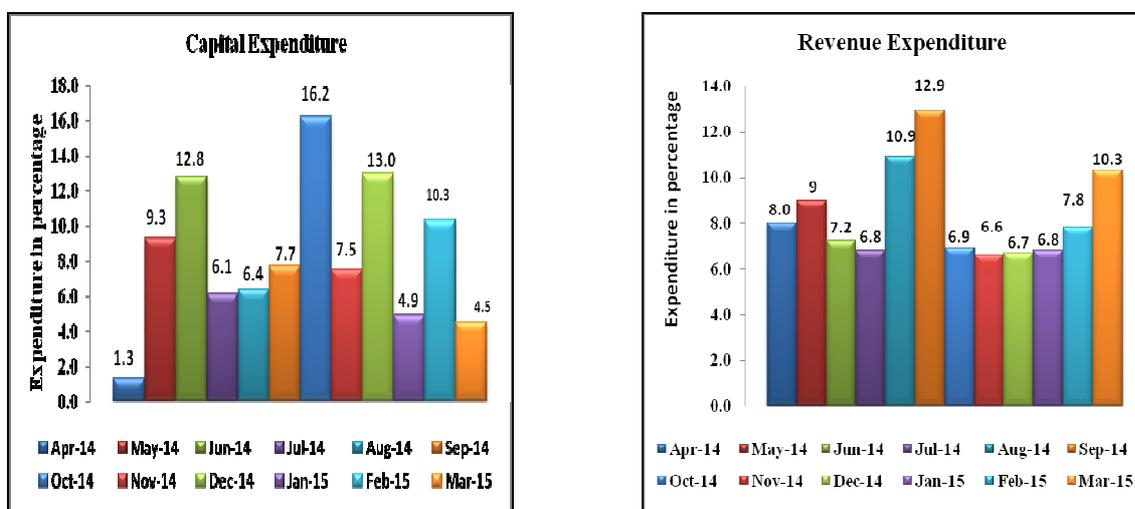
The Capital expenditure of Coast Guard ranged between ₹1,070 crore and ₹1,575 crore during the five year period from 2010-11 to 2014-15, whereas the Revenue expenditure of Coast Guard has shown an increase of 57.98 *per cent* during the five year period from 2010-11 to 2014-15 *i.e.*, from ₹814 crore in 2010-11 to ₹1,286 crore in 2014-15.

The Capital expenditure of Coast Guard increased by nearly 6.72 *per cent* from ₹1,070 crore to ₹1,142 crore in the year 2014-15 as compared to the previous year. The Revenue expenditure of Coast Guard increased by nearly 22.71 *per cent* from ₹1,048 crore to ₹1,286 crore in the year 2014-15 as compared to the previous year.

1.6.2 Flow of Expenditure during the year

Audit examined flow of Capital and Revenue expenditure during the year 2014-15, which is indicated below:

Figure: 1.2 Flow of Expenditure of Coast Guard during 2014-15



(Source: Information provided by Coast Guard Headquarters)

Scrutiny of expenditure revealed that Coast Guard incurred about 4.5 per cent of the Capital expenditure in the month of March 2015 and about 19.7 per cent in the last quarter which was within the limit of 15 per cent for the month of March and 33 per cent for the last quarter as prescribed by the Ministry of Finance. The Revenue expenditure was also within the limits prescribed by the Ministry of Finance.

1.7 Receipts of the Navy and Coast Guard

The details of receipts and recoveries pertaining to the Indian Navy and Coast Guard during the last five years ending 2014-15 for the services that they provided to other organisations/departments are given in the Table below:

Table 1.7: Revenue Receipt of Indian Navy and Coast Guard

	(₹ in crore)				
Year	2010-11	2011-12	2012-13	2013-14	2014-15
Receipt and Recoveries in respect of Navy	165.68	154.94	285.07	437.89	673.13
Receipt and Recoveries in respect of Coast Guard	13.33	06.73	34.41	27.19	24.60

Source: Figures of actual receipts as given in Defence Service Estimates for each year (For Navy) and Information provided by Coast Guard Headquarters

The receipt and recoveries in respect of Navy increased from ₹165.68 crore to ₹673.13 crore *i.e.* by 306.28 *per cent* during the five year period from 2010-11 to 2014-15, whereas the receipt and recoveries in respect of Coast Guard ranged between ₹6.73 crore and ₹34.41 crore during the five year period from 2010-11 to 2014-15.

The receipt and recoveries in respect of Navy have shown an increase of 53.72 *per cent* as compared to previous year *i.e.* from ₹437.89 crore in 2013-14 to ₹673.13 crore in 2014-15, whereas the receipts and recoveries in respect of Coast Guard have shown a decline of 9.52 *per cent* from the previous year *i.e.* from ₹27.19 crore in 2013-14 to ₹24.60 crore in 2014-15.

1.8 Response to Audit

1.8.1 Action Taken Note on Audit Paragraphs of earlier Reports

With a view to enforce accountability of the executive in respect of all issues dealt with, in various Audit Reports, the PAC desired that Action Taken Notes (ATNs) on all paragraphs pertaining to the Audit Reports for the year ended 31 March 1996 onwards be submitted to them, duly vetted by audit, within four months from the laying of the Report in Parliament.

Status of outstanding ATNs on Audit paragraphs relating to the Navy and Coast Guard as on 31 January 2016 is shown as under:

Table 1.8: Status of ATN

Status of ATN	Navy and Coast Guard	Defence Shipyards
Audit Paragraphs/ Reports on which ATNs have not been submitted by the Ministry even for the first time	3	1
Audit Paragraphs/ Reports on which revised ATNs are awaited.	27	0

1.8.2 Response of the Ministry to Draft Audit Paragraphs

The Ministry of Finance (Department of Expenditure) issued directions to all the Ministries in June 1960 to send their response to the Draft Audit Paragraphs proposed for inclusion in the Report of the Comptroller and Auditor General of India within six weeks.

Draft Performance Audit Report on “Construction of Indigenous Aircraft Carrier” was forwarded to the Secretary, Ministry of Defence through demi-official letter in February 2015 and revised Draft was issued in October 2015. Similarly, Draft Paragraphs were also forwarded between December 2015 and January 2016 drawing attention to the audit findings and requesting a response within six weeks.

Despite the instructions of the Ministry of Finance, no replies to the Audit Paragraphs including Performance Audit mentioned in this Report were received. Thus, the response of the Ministry could not be included in respect of these Paragraphs.

1.9 Savings at the instance of Audit

Following savings of prominent nature were made at the instance of Audit amounting to ₹4.09 crore:

A. Cancellation of sanction for construction of Shopping Complex

Para 3.42.1 of Scales of Accommodation, Defence Services (SADS) stipulates that a shopping centre may be provided if no shopping facility exists within two kms from the main married complex.

Audit observed (October 2011) that Administrative Approval (AA) was accorded (March 2011) by Headquarters Western Naval Command (HQWNC), Mumbai for the work “Provision of Deficient Integrated Shopping Centre, Bank and Post Office at Sailors Married Accommodation at Colaba, Mumbai” at an estimated cost of ₹3.38 crore despite the fact that two shopping complexes existed within a distance of two kms of the planned facility.

In pursuance of the audit observation (October 2011), the user unit, *i.e.*, INS Angre recommended (April 2014) to HQWNC that the work be cancelled due to the changed socio-economic aspirations of its personnel. HQWNC intimated (February 2015) that the AA for the work at a cost of ₹3.38 crore was cancelled (April 2014) at the instance of audit.

The Ministry, in its reply (March 2016) accepted that AA was cancelled at the instance of Audit.

B. Cancellation of sanction for construction of Unit Run Canteens

Unit Run Canteens (URCs) are the retail face of Canteen Store Department. There is no provision in the Scale of Accommodation for construction of URCs.

Audit observed (May 2014) that three sanctions⁵ were issued by Coast Guard Headquarters (CGHQ), New Delhi between October 2006 and February 2013 at a total cost of ₹90.04 lakh⁶. Construction of two out of three URCs⁷ costing ₹42.79 lakh had been completed.

Accepting the audit contention, CGHQ stated (September 2015) that the two URCs already constructed would be re-appropriated. CGHQ further intimated (February 2016) that the sanction for the third URC for ₹39.35 lakh had been cancelled (December 2015).

The fact remains that notwithstanding the cancellation of third sanction, re-appropriation of two URCs constructed at a cost ₹42.79 lakh is also irregular.

C. Cancellation of supply orders for transmitters

Audit observed (August 2014) that none of the communication equipment was received *vis-à-vis* three supply orders placed by the Coast Guard (CG) between May

⁵ For construction of URC at three CG stations *viz*; Okha, Daman and Kochi

⁶ ₹90.04 lakh (Okha ₹23.14 lakh + Daman ₹27.55 lakh + Kochi ₹39.35 lakh)

⁷ Construction of URCs completed at Okha in September 2008 and at Daman in January 2012

Report No. 17 of 2016 (Navy and Coast Guard)

and September 2013 at a total cost of ₹31.94 lakh and the requirements were being met through alternate sets⁸.

The CG intimated (January 2015) audit that all the three supply orders placed on the firm had been cancelled thereby resulting in a saving of ₹31.94 lakh.

The matter was referred to the Ministry (January 2016); their reply was awaited (April 2016).

1.10 About the Report

This report contains a Performance Audit and 10 Audit Paragraphs included in four chapters namely:

- Chapter-II containing a Performance Audit on “Construction of Indigenous Aircraft Carrier”
- Chapter-III on issues related to Ministry of Defence containing two Audit Paragraphs.
- Chapter-IV on issues related to Indian Navy containing seven Audit Paragraphs.
- Chapter-V on issues related to Indian Coast Guard containing one Audit Paragraph.

⁸ The units are additionally supplied with communication sets which serves for redundancy in the event of any of the set becoming defective/obsolete