

AUDITORS' REPORT TO THE MEMBERS OF THE STATE TRADING CORPORATION OF INDIA LTD.

- 1) We have audited the attached Balance Sheet of **THE STATE TRADING CORPORATION OF INDIA LIMITED** as at 31st March, 2011, the Profit & Loss Account and the Cash Flow Statement of the Company for the year ended on that date, annexed thereto in which are incorporated the accounts of the corporate office audited by us and the accounts of branches audited by the other Auditors. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.
- 2) We conducted our audit in accordance with the auditing standards generally accepted in India. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material mis-statements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosure in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
- 3) As required by the Companies (Auditors' Report) Order, 2003 as amended by the companies (Auditor's Report) (Amendment) Order, 2004 issued by the Central Government of India in terms of Section 227(4A) of the Companies Act, 1956, we enclose in the Annexure hereto, a statement on the matters specified in paragraphs 4 and 5 of the said Order.
- 4) Further to our comments in the annexure to in paragraph 3 above, we report as follows
 - a) Reference is invited to Note No. 3(a) of Notes to Accounts, Schedule 23, relating to contracts of scrap, where transactions of purchases and sales and recoveries had not taken place in terms of contracts on behalf of Metro Machinery Traders, New Delhi (the Business Associate). The Company has alleged fraud by the Business Associate and the matter has been referred to CBI. We also understand that two ex-Directors and a General Manager have been charge-sheeted. However, in the absence of details of the charge-sheets and the inquiries, we are unable to opine if there was a fraud or suspected Management fraud and comment on any mis-statement made in these accounts in respect of the above transaction. Pending out come of legal steps initiated for recovery/ CBI probe, full provision of Rs. 8739 lacs was made in earlier years.
 - b) Reference is invited to Note No. 3(b) of Notes to Accounts, Schedule 23, relating to wheat transactions undertaken on behalf of Business Associate, disposal of goods and recovery had not taken place as per contract due to quality problems and there was stock of wheat and unrecovered amounts outstanding from the Business Associate and Supplier. Also, cases of theft and misappropriation of uplifted stocks exported to Bangladesh have come to notice for which legal actions have been initiated. Pending out come of legal steps initiated, entire dues including recoverable from FCI aggregating to Rs. 5841 lacs has been provided/written off in earlier years. Further as the matter is not yet resolved, additional amount of central sales tax liability for non-export of 30392.010 MT of wheat procured from FCI is not ascertainable. The impact on Profit & Loss Account thus is not known.
 - c) Reference is invited to Note No. 3(c) of Notes to Accounts, Schedule 23, relating to Rs. 12199 lacs dues from Jhagadia Copper Limited, the company under liquidation and in the process of reconstruction by Asset Reconstruction Company (India) Limited. Financial impact of the same cannot be ascertained at this stage.
 - d) References invited to Note No. 3(d) of Notes to Accounts, Schedule 23, relating to sundry debtor of Rs.113793 lacs due from Global Steel Philippines who have stopped operation of their plant due to extreme volatility of prices. Though the outstanding is secured by way of Pledge of stock and post dated cheques and the corporate guarantees of holding company, however, in view of non availability of detailed valuation of plant & machinery being considered for sale, financial impact on account cannot be ascertained at this stage.
 - e) Reference is invited to Note No. 3 (e) of Notes to Accounts, Schedule 23, regarding booking of claims of Rs. 8167 lacs on account of differential actual trading losses, pending financial approval from Ministry of Consumer Affairs.
 - f) Reference is invited to Note No. 3(g) of Notes to Accounts, Schedule 23, relating to unsecured overdue of Rs. 39717 lacs against exports effected under the Exim Bank Insurance linked Post shipment Credit facility.
 - g) Reference is invited to Note No. 3 (h) of Notes to Accounts, Schedule 23, regarding non provision of Sundry Debtors of Rs 494 lacs towards reimbursement of the loss in supply of PDS items during 2008-09 to M/s Gujarat State Civil supplies Government Of Gujarat.



- h) Note No 3(j) and 6(a) of Notes to Accounts, Schedule 23, relating to pending reconciliations of personal accounts and consequential adjustments
- i) Reference is invited to Note No. 4 of Notes to Accounts, Schedule 23, regarding non provision of diminution in value of investment in subsidiary company (STCL).
- 5) We further report that :
- a) We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit except for information pertaining to charges levied on two ex-Directors and a General Manager and details of inquiries in respect of transaction referred to in Para 4 (a) above, and further except as otherwise stated in the report, and the record of the cases being handled by the vigilance department of the company and the accounting of the consequential financial effect thereof on the matters under its scrutiny in such cases.
- b) In our opinion, proper books of account as required by law have been kept by the Company so far as appears from our examination of such books and proper returns adequate for the purpose of our audit have been received from the Branches not audited by us. Reports of the Branch auditors have been considered while preparing our report.
- c) The Balance Sheet, Profit & Loss Account and Cash Flow Statement referred to in this report are in agreement with the books of account;
- d) In our opinion, the Balance Sheet, Profit & Loss Account and Cash Flow Statement comply with the mandatory accounting standards referred to in Section 211 (3C) of the Companies Act, 1956.
- e) In terms of Notification No. GSR 829(E) dated 21.10.2003 issued by the Department of Company Affairs, Government of India, the provisions of Section 274(1)(g) of the Companies Act, 1956 are not applicable to the Company.
- f) In our opinion and to the best of our information and according to the explanations given to us, the said accounts, subject to our observations in paragraphs 4 (a) to (i) above, provisions and write offs in respect of which have been made in the accounts based on the existing and known circumstances as reported in the said paragraphs and read together with the Significant Accounting Policies and other Notes appearing in the Notes to the Accounts, give the information required by the Companies Act, 1956 in the manner so required and also give a true and fair view in conformity with the accounting principles generally accepted in India :
- (i) in the case of the Balance Sheet, of the state of affairs of the Company as at 31st March, 2011;
- (ii) in the case of the Profit & Loss Account, of the profit of the Company for the year ended on that date; and
- (iii) in the case of the Cash Flow Statement, of the Cash Flows of the Company for the year ended on that date.

For Chandok & Guliani
Chartered Accountants
Firm Registration No. 001199N

sd/-
(V.K. Lalla)
Partner

Membership No.080847

Date: 24.06.2011
Place: New Delhi



MANAGEMENT'S REPLY TO THE COMMENTS OF STATUTORY AUDITORS ON THE ACCOUNTS FOR THE YEAR 2010-11

Comments of the Statutory Auditors

1. Reference is invited to Note No. 3(a) of Notes to Accounts, Schedule 23, relating to contracts of scrap, where transactions of purchases and sales and recoveries had not taken place in terms of contracts on behalf of Metro Machinery Traders, New Delhi (the Business Associate). The Company has alleged fraud by the Business Associate and the matter has been referred to CBI. We also understand that two ex-Directors and a General Manager have been charge-sheeted. However, in the absence of details of the charge-sheets and the inquiries, we are unable to opine if there is a fraud or suspected Management fraud and comment on any mis-statement made in these accounts in respect of the above transaction. Pending outcome of legal steps initiated for recovery/ CBI probe, full provision of Rs. 8739 lacs was made in earlier years.

2. Reference is invited to Note No. 3(b) of Notes to Accounts, Schedule 23, relating to wheat transactions undertaken on behalf of Business Associate, disposal of goods and recovery had not taken place as per contract due to quality problems and there was stock of wheat and unrecovered amounts outstanding from the Business Associate and Supplier. Also, cases of theft and misappropriation of uplifted stocks exported to Bangladesh have come to notice for which legal actions have been initiated. Pending outcome of legal steps initiated, entire dues including recoverable from FCI aggregating to Rs. 5841 lacs has been provided/written off in earlier years. Further as the matter is not yet resolved, additional amount of central sales tax liability for non-export of 30392.010 MT of wheat procured from FCI is not ascertainable. The impact on Profit & Loss Account thus is not known.

3. Reference is invited to Note No. 3(c) of Notes to Accounts, Schedule 23, relating to Rs. 12199 lacs dues from Jhagadia Copper Limited, the company under liquidation and in the process of reconstruction by Asset Reconstruction Company (India) Limited. Financial impact of the same cannot be ascertained at this stage.

4. Reference is invited to Note No. 3(d) of Notes to Accounts, Schedule 23, relating to sundry debtor of Rs.113793 lacs due from Global Steel Philippines who have stopped operation of their plant due to extreme volatility of prices. Though the outstanding is secured by way of Pledge of stock and post dated cheques and the corporate guarantees of holding company, however, in view of non availability of detailed valuation of plant & machinery being considered for sale, financial impact on account cannot be ascertained at this stage

5. Reference is invited to Note No. 3 (e) of Notes to Accounts, Schedule 23, regarding booking of claims of Rs 8167 lacs on account of differential actual trading losses, pending financial approval from Ministry of Consumer Affairs

Management's Reply

As far as the charge sheet issued to ex-Directors and ex-GM is concerned, the same has been issued by the Vigilance Deptt. for which the documents are in the custody of Vigilance Deptt. of Ministry/Corporation which are of confidential nature. The charge sheet has been issued in connection with the procedural deficiencies and therefore no fraud or suspected management fraud has taken place. As a matter of abundant caution, a provision of Rs. 8739 lacs has been made in earlier years. The Company is confident to recover the same from the associate through legal recourse including recoveries through selling of balance stock as well as the properties of the associate, which have been attached as per Court Orders. The arbitration award has already been decided in favour of the Company and it is in the process of getting the same implemented.

The company has made a provision of Rs. 5841 lakhs including write off amounting to Rs. 547 lakhs up to 2008-09. These claims are however, recoverable from business associate and the management is confident of recovery of the same.

The export documents in respect of the total quantity released by FCI have been submitted and therefore no sales tax liability is likely to arise. Further the matter has been referred to Permanent Machinery of Arbitration (PMA) for recovering dues from FCI and to resolve the issue of submission of H and C forms.

The recoverable from Jhagadia Copper Limited are secured by way of pledge of stocks by the Company in favour of STC. The stocks are under the custody of Central Warehousing Corporation. As per latest valuation certificate issued by independent Surveyors the value of stocks is Rs.28996 lakhs as on 31/3/2011. Hence no provision is considered necessary against the dues.

The recoverable from Global Steel Philippines are secured by way of pledge of stocks worth Rs.99065 lakhs, EMD of Rs.3112 lakh, corporate Guarantee of its Holding Company and on dated cheques. The Company is in the process of selling its plant for which M/s. IDBI Capital market services, a wholly owned subsidiary of IDBI Bank has been mandated to complete transaction within 150 days. Hence no provision is considered necessary against the dues.

As per minutes dated 14.02.2011 and 25.04.2011 of Ministry of Consumer Affairs, claims for 2008-09 and 2009-10 have been revised on "sold quantity basis" and differential actual trading losses of Rs.8167 lakh have been booked in the current financial year as claim recoverable from Ministry of Consumer Affairs in accordance with the above minutes.

6. Reference is invited to Note No. 3(g) of Notes to Accounts, Schedule 23, relating to unsecured overdue of Rs. 39717 lacs against exports effected under the Exim Bank Insurance linked Post shipment Credit facility.

7. Reference is invited to Note No. 3 (h) of Notes to Accounts, Schedule 23, regarding non provision of Sundry Debtors of Rs 494 lacs towards reimbursement of the loss in supply of PDS items during 2008-09 to M/s Gujarat State Civil supplies Government Of Gujarat.

8. Note No 3(j) and 6(a) of Notes to Accounts, Schedule 23, relating to pending reconciliations of personal accounts and consequential adjustments

9. Reference is invited to Note No. 4 of Notes to Accounts, Schedule 23, regarding non provision of diminution in value of investment in subsidiary company (STCL).

10. The Company has maintained proper records showing full particulars including quantitative details and situations of its fixed assets except at Ahmadabad branch where Fixed Asset Register was not updated.

11. In our opinion, though the procedures for physical verification is in place and instructions and guidelines are issued from time to time for verification of stock/inventories but the same is not being followed strictly for all materials which are handled by and are in custody of third parties.

12. In our opinion and according to the information and explanation given to us, there are adequate internal control procedures commensurate with the size of the company and the nature of the business with regard to purchase of inventory, fixed assets and also for sale of goods. Further, on the basis of our examination and according to the information and explanations given to us, we have not observed any instance of continuous failure to correct major weaknesses in the internal control procedures. However, internal control procedures regarding review, realization of advances and other claims and reconciliation of balance of sundry debtors and creditors require strengthening.

There are delays in repatriation of export proceeds from the foreign buyers in view of slump in Jewellery and construction sector in UAE, where most of the buyers are based. The associates have sought some more time to realise the proceeds. The company has negotiated a re-structuring proposal with EXIM Bank wherein additional time ranging between 2 to 5 years is now available to the company to recover the dues from associates/their foreign buyers. Repayment of some over dues has been received and with all out efforts, which are being made, the Company is confident of full recovery hence no provision for the outstanding export bill considered necessary.

The amount is towards reimbursement of loss in supply of RBD PLN during 2008-09 to M/s. Gujarat State Civil Supplies Corporation, Govt. of Gujarat for PDS supply under the subsidized scheme of Govt. of India. The claim is under process with the Govt. of India in terms of its letter no. 12/1/2006-C&P dated 4th March 2008 specifying that the loss to the PSU's, if any, will be borne by Govt. In view of this, no provision is considered necessary.

Balances of debtors/creditors and liabilities are being reconciled at the time of settlement of individual transaction. As the settlements are done with the consent of the associates, the procedure followed is considered adequate.

The subsidiary company is a going concern, is in business and having trading profit during 2009-10. Keeping in view its long term business plan no provision is considered necessary.

Though this observation has been made only in respect of one branch, to ensure avoidance of recurrence, necessary updation is being carried out.

Instructions and guidelines have been issued from time to time to branches and divisions for verification of the inventories/stocks by nominated surveyors as well as STC officials on periodical basis. Internal Auditors have also been advised to carry out the verification of such inspection reports during their quarterly audits. Instructions have been issued again for strict compliance.

Debtors, advances and other claims are being reviewed continuously by the concerned branches/divisions. The same are also reviewed at corporate office level and necessary instructions issued from time to time to the concerned branches and divisions. A position note on debtors is submitted to Board on quarterly basis. In order to strengthen the system further, debt review committee has already been constituted for review of dues.

Sd/-
(N.K. Mathur)
Chairman & Managing Director

Sd/-
(N.K. Nirmal)
Director (Finance)