COMMENTS OF THE COMPTROLLER AND AUDITOR GENERAL OF INDIA UNDER SECTION 619(4) OF THE COMPANIES ACT, 1956 ON THE ACCOUNTS OF AIR INDIA LIMITED FOR THE YEAR ENDED 31 MARCH 2011.

The preparation of financial statements of **Air India Limited** for the year ended 31 March 2011 in accordance with the financial reporting framework prescribed under the Companies Act, 1956, is the responsibility of the Management of the Company. The Statutory Auditors appointed by the Comptroller and Auditor General of India under Section 619(2) of the Companies Act, 1956 are responsible for expressing opinion on these financial statements under Section 227 of the Companies Act, 1956 based on independent audit in accordance with the auditing and assurance standards prescribed by their professional body, the Institute of Chartered Accountants of India. This is stated to have been done by them vide their Audit Report dated 29 November 2011.

I, on behalf of the Comptroller and Auditor General of India (CAG), have conducted a supplementary audit of **Air India Limited** under section 619(3) (b) of the Companies Act, 1956 of the financial statements for the year ended 31 March 2011. This supplementary audit has been carried out independently with access to limited working papers of the Statutory Auditors and is also limited primarily to inquiries of the Statutory Auditors and Company personnel and a selective examination of some of the accounting records. Based on my supplementary audit, I would like to highlight the following significant matters under Section 619 (4) of the Companies Act, 1956 which have come to my attention and which in my view are necessary for enabling a better understanding of the financial statements and the related Audit Report :

A. Profit and Loss Account
Prior Period Adjustments (Net) : Rs.278.4 Million (Schedule 'U')

The above is understated by Rs.28,425.2 million due to recognition of 'Deferred Tax Asset' (DTA) in earlier years and non-writing off of the same as this is in violation of Accounting Standard (AS)-22 prescribed under Section 211(3C) of the Companies Act, 1956. This is also corroborated by the opinion of the Institute of Chartered Accountants of India that in the absence of any supporting evidence there did not exist virtual certainty (as contemplated in AS-22) that sufficient future taxable income would be available against which the DTA can be realized. The Statutory Auditors, in para 5(i) of their Report dated 29 November 2011, have also qualified in regard to amount of DTA of Rs.28,425.2 million stating that the carrying amount of DTA should have been charged off to the Profit and Loss Account in the year 2009-10 itself. Though the Company accepted the error in the Board's Report annexed to its Annual Report for 2009-10, it did not write off the DTA even in the current year through 'Prior Period Adjustments' as per provisions of AS-5 and para 26 of AS-22. This has resulted in overstatement of 'Deferred Tax Asset' (Rs.28,425.2 million) and understatement of 'Loss after tax and prior period adjustments' (Rs.68,651.7 million) each by Rs.28,425.2 million. ***Comment No. B of the CAG on the accounts of the Company about derecognition of deferred tax assets (DTA) of Rs.28,425.2 million for the period ended 31 March 2010 refers in this regard.***

Viewed in the above context, the declaration by the Management in 'Significant Accounting Policies' (Schedule 'W') that the financial statements have been prepared in compliance with the Accounting Standards referred to in Section 211(3C) of the Companies Act, 1956 is not correct as Accounting Standards 5 and 22 have not been complied to that extent.

B. Balance Sheet
Current Assets, Loans & Advances
Loans and Advances - Rs.13,806.1 Million (Schedule 'L')

The above includes Rs.1,019.9 million, depicted as recoverable from Airport Authority of India (AAI) on account of Ground Handling Arrangement. The Company in 1995 disputed the existing revenue sharing agreement with AAI in the ratio of 30:70 and proposed 50:50 sharing along with increase in the AAI's share of fixed cost from Rs.30 million to Rs.50 million respectively which had not been agreed to by AAI. However, the Company raised the claim in 2006-07 for the differential amount (20 *per cent*) and recognized revenue of Rs.1,019.9 million. As AAI had not accepted the proposed revision, realization of the said amount is uncertain and, thus, recognition thereof is not in order as per Accounting Standard 9. Therefore, provision for Rs.1,019.9 million should have been created. This has resulted in overstatement of Loans and Advances by Rs.1,019.9 million and consequent understatement of 'Prior Period Expenses' and 'Loss after tax' (Rs.68,651.7 million) each by the same amount. ***Comment No. (ii) of the CAG on the accounts of Company for the period ended 31 March 2009 under the head 'Balance Sheet -*** **Current Assets, Loans & Advances*****' refers in this regard.***

C. Others
Notes to Accounts (Schedule 'X')
Note No.5

As per scheme of amalgamation of erstwhile Air India Limited and erstwhile Indian Airlines Limited into National Aviation Company of India Limited (renamed as Air India Limited from 24 November 2010), immoveable properties of the Company were revalued on the appointed date *i.e.* 1 April 2007 as per fair values determined by the valuer appointed by the Company. One of such properties *viz.* Housing Colony at Vasant Vihar, New Delhi constructed on leasehold land was revalued at Rs.51,295.1 million as at 1 April

2007, though lease deed of the property had been cancelled by the lessor viz. Land & Development Office, New Delhi. ***Note No.5 of Schedule 'T' to the accounts of the Company* for the year 2007-08 and *Comment No. D-Others (iii) of the CAG on the accounts of Company for that year and Comment No.(ii) under the head 'Balance Sheet-Reserves & Surplus' on the accounts for the year 2008-09 refer in this regard.*** The lease rights cancelled by the lessor in November 1983 had not been reinstated in the name of the Company as at 31 March 2011.

Despite CAG's comment, the Company did not take into account the fact that even if the lease is reinstated in the name of the Company, the lessor has a claim on 50 *per cent* unearned increase in the value of leased land given to the lessee as per standard requirement of lessor.

For and on the behalf of the
Comptroller and Auditor General of India

Sd/-
Archana P. Shirsat
Principal Director of Commercial Audit
& *ex-officio* **Member, Audit Board II, Mumbai**

Place : Mumbai
Date : 27 January 2012.

MANAGEMENT REPLIES TO THE COMMENTS OF THE COMPTROLLER AND AUDITOR GENERAL OF INDIA UNDER SECTION 619(4) OF THE COMPANIES ACT, 1956 ON THE ACCOUNTS OF THE COMPANY FOR THE YEAR ENDED MARCH 31, 2011.

Sr. No.	Audit Observations	Management Reply
A.	**PROFIT & LOSS ACCOUNT** **Prior Period Adjustments (Net) : Rs. 278.4 Million (Schedule U)** The above is understated by Rs. 28,425.2 million due to recognition of 'Deferred Tax Asset' (DTA) in earlier years and non-writing off of the same as this is in violation of Accounting Standard (AS)-22 prescribed under Section 211(3C) of the Companies Act, 1956. This is also corroborated by the opinion of the Institute of Chartered Accountants of India that in the absence of any supporting evidence there did not exist virtual certainty (as contemplated in AS-22) that sufficient future taxable income would be available against which the DTA can be realized. The Statutory Auditors, in para 5(i) of their Report dated 29 November 2011, have also qualified in regard to amount of DTA of Rs. 28,425.2 million stating that the carrying amount of DTA should have been charged off to the Profit and Loss Account in the year 2009-10 itself. Though the Company accepted the error in the Board's Report annexed to its Annual Report for 2009-10, it did not write off the DTA even in the current year through 'Prior Period Adjustments' as per provisions of AS-5 and para 26 of AS-22. This has resulted in overstatement of 'Deferred Tax Asset' (Rs. 28,425.2 million) and understatement of 'Loss after tax and prior period adjustments' (Rs. 68,651.7 million) each by Rs. 28,425.2 million. ***Comment No. B of the CAG on the accounts of the Company about derecognition of deferred tax assets (DTA) of Rs. 28,425.2 million for the period ended 31 March 2010 refers in this regard.*** Viewed in the above context, the declaration by the Management in 'Significant Accounting Policies' (Schedule 'W') that the financial statements have been prepared in compliance with the Accounting Standards referred to in Section 211(3C) of the Companies Act, 1956 is not correct as Accounting Standards 5 and 22 have not been complied to that extent.	A similar comment on DTA has been reported by C&AG in the Accounts of 2009-10. It is submitted that the Company has seized recognizing Deferred Tax from 2009-10 following the decision of the Management/Audit committee and Deferred Tax Asset (DTA) only to the extent of the Deferred Tax Liability has been recognized. It may be brought to the attention of audit that airlines in India are still recognizing DTA in their Books even though they are incurring losses. Airlines abroad also have been recognizing DTA based on reasonable certainty of profits. Audit is aware that Air India has adopted a Turn Around Plan (TAP) which includes operational and financial structuring. The operational restructuring envisages improvement in the passenger load factor to 73% by 2015 & 75% by 2020. Besides this, it also contemplates increase in yields, increase in market share, aircraft utilization, improvement in operational parameters, hiving of the GH & MRO to subsidiary companies which would therefore, result in the company being EBIDTA positive by Financial Year 2013 and Cash positive by 2018 and Profit After Tax (PAT) Positive by 2020. Besides this Government of India (GOI) would infuse equity (subject to Cabinet approval) of Rs.67,500.0 million in Financial Year 2012 as well as give support in respect of the loan repayments for guaranteed loans for aircraft acquisition up to Financial Year 2021. In other words Air India is expecting an equity infusion of Rs.302,310.0 million over a period up to 2021. Reserve bank of India (RBI) has also given certain regulatory approvals to banks for the purpose of provisioning requirement which would therefore enable the FRP to be completed in the next 2/3 months. This would reduce interest cost substantially to the extent of Rs.10,000.0 million (approximately) as estimated by SBI CAPS. The induction of Boeing Dreamliner-787 and the lease out of Boeing 777-200 LRs are also likely to result in improving operational efficiencies and performance in the coming years. These initiatives are likely to result in reduction of costs, increase in revenue and curtailment of losses. This was also considered by the Board while approving the Accounts for financial year 2009-10 and the view taken by the management was endorsed.

Sr. No.	Audit Observations	Management Reply
		The Audit Committee/ Board also felt that any reversal of Deferred Tax at this stage would imply that the Management has lost its confidence on the implementation of the Turn-around plan which is not so due to the support received from the Government and Lenders in The Financial Restructuring Plan of Air India and the overall improvement in the performance during the year 2011-12. This stand is true for the year 2010-11 also. We would also like to submit that the Deferred Tax Asset which was assessed for the year ended 2010-11 (as on 31st March 2011) was to the tune of nearly Rs.116,312.0 million and Deferred Tax liability to the extent of Rs.48,068.4 Million, leaving a balance of Rs.68,243.5 million in DTA account. However based on grounds of "actual valuation", the Management has decided to account for only Rs.28,425.2 million. Therefore, entire amount has not been accounted in the books as a prudent measure. Air India is a national carrier of India with a brand equity which is popular world wide. The company has been in existence for nearly 59 years since it was first incorporated in the year 1953. Hence, any doubts regarding the company's continuance/ existence/ revival should not exist at all as the Government has committed that it wants to support Air India as a National Carrier. The GoM on 28th October 2011 and 7th February 2012 have cleared the FRP plans for issue of Government guaranteed Bonds of Rs.74,000.0 million and upfront Equity infusion of Rs.67,500.0 million. The Auditors in their Audit Report have only drawn attention in Para 5(i) of their report. In conclusion, it is submitted that there has been 'material concrete development' during the year 2010-11 and 2011-12 which leads Management to belief that the Company has made substantial progress in improving its Operational and Financial efficiencies and there is no justification for writing back the DTA created in 2007-08 and 2008-09 in the Accounts of 2010-11. Regarding the Audit comments on the Accounting Standards reference **Section 211(3C)** of The Companies Act 1956 it is submitted that **Section 211(3B)** of the Companies Act 1956 states that wherever there is a deviation in compliance of the Accounting Standards there should be sufficient disclosure of such deviation from the Accounting Standards, the reasons for such deviation and the financial effect if any, arising due to such deviation.

Sr. No.	Supplementary Audit Observations	Management Reply
		Disclosure in this regard has been provided by Management in note 44 Schedule 'X' Notes to Accounts. The Management Replies to the Audit Report of the Statutory Auditors for the Financial Year 2010-11 has also clarified the reasons for retaining the DTA amount . In view of the above context, declaration by the management that the Financial statements have been prepared in compliance with the Accounting standards specifically regarding AS-5 and As-22 has been complied.
B.	**BALNCE SHEET** **CURRENT ASSETS, LOANS & ADVANCES** **Loans and Advances : Rs.13,806.1 Million (Schedule L)** The above includes Rs. 1,019.9 million, depicted as recoverable from Airport Authority of India (AAI) on account of Ground Handling Arrangement. The Company in 1995 disputed the existing revenue sharing agreement with AAI in the ratio of 30:70 and proposed 50:50 sharing along with increase in the AAI's share of fixed cost from Rs.30 million to Rs.50 million respectively which had not been agreed to by AAI. However, the Company raised the claim in 2006-07 for the differential amount (20 *per cent*) and recognized revenue of Rs. 1,019.9 million. As AAI had not accepted the proposed revision, realization of the said amount is uncertain and, thus, recognition thereof is not in order as per Accounting Standard 9. Therefore, provision for Rs. 1,019.9 million should have been created. This has resulted in overstatement of Loans and Advances by Rs. 1,019.9 million and consequent understatement of 'Prior Period Expenses' and 'Loss after tax' (Rs. 68,651.7 million) each by the same amount. ***Comment No. (ii) of the CAG on the accounts of Company for the period ended 31 March 2009 under the head 'Balance Sheet-* Current Assets, Loans & Advances*' refers in this regard.***	A similar comment has been reported by C&AG in the accounts of 2008-09. The issue regarding dues amounting to Rs.1,019.9 million recoverable from Airport Authority effective April 1995 towards Ground Handling arrangement between Airport Authority and erstwhile Air India was again taken up with Joint. Secretary, Ministry Of Civil aviation (MOCA) vide our letter No.DF/REV/ GHA/ VVP/16 dated 3 March 2010. Further during 2010-2011 also, the matter was pursued with MOCA vide our letter No. EDF/BA/55 dated 9 September 2010 and No.EDF/BA/062 dated 10 November 2010. We are awaiting response from MOCA in this regard. Since the matter is still pending with OCA/AAI, the amount is shown as recoverable from AAI. During the financial year 2010-11 and thereafter there have been discussions between the officers of both the organizations at the Regional level and also at the Corporate level. Details for disputed amount have been requested from AAI and some of the details have been received from AAI and are being reconciled. Since there are outstanding amounts due to AAI, for various services availed of, from AAI and billed by them to us from April 1994 to November 2002, the same has been retained as outstanding liability in the books of accounts pending recovery of Rs 1,019.9 Million from AAI towards Ground handling Agreement. Since the recoverable amount would be adjusted from the amount payable, which is higher than the recoverable amount, the question of provision for doubtful debts does not arise. The reconciliation process of disputed amounts is in progress on a serious note. The fact of pending reconciliation of dues with AAI has been clarified in Note No. 46 to the notes to Accounts. The auditors have also qualified in para 4(ii) of their audit report.

Sr. No.	Supplementary Audit Observations	Management Reply
C.	**OTHERS** **Notes to Accounts : (Schedule X)** **Note No. 5** As per scheme of amalgamation of erstwhile Air India Limited and erstwhile Indian Airlines Limited into National Aviation Company of India Limited (renamed as Air India Limited from 24 November 2010), immoveable properties of the Company were revalued on the appointed date *i.e.* 1 April 2007 as per fair values determined by the valuer appointed by the Company. One of such properties *viz.* Housing Colony at Vasant Vihar, New Delhi constructed on leasehold land was revalued at Rs. 51,295.1 million as at 1 April 2007, though lease deed of the property had been cancelled by the lessor viz. Land & Development Office, New Delhi. ***Note No.5 of Schedule 'T' to the accounts of the Company*** **for the year 2007-08 and** ***Comment No. D-Others (iii) of the CAG on the accounts of Company for that year and Comment No.(ii) under the head 'Balance Sheet-Reserves & Surplus' on the accounts for the year 2008-09 refer in this regard.*** The lease rights cancelled by the lessor in November 1983 had not been reinstated in the name of the Company as at 31 March 2011. Despite CAG's comment, the Company did not take into account the fact that even if the lease is reinstated in the name of the Company, the lessor has a claim on 50 *per cent* unearned increase in the value of leased land given to the lessee as per standard requirement of lessor.	This observation was reported by Government Audit in the accounts of 2007-08 and 2008-09 when the value of the land was restated in the books at its fair value in terms of the scheme of amalgamation. In this regard, the reply to this Para given in the year 2008-09 which is valid even as of date is reproduced below : "The methodology adopted by the valuer was based on fair market rates which are otherwise referred to as the direct sale method. Under the direct sale method the market rate are obtained from brokers/agents and the transactions are assessed based on willing buyer and a willing seller based on a value which will be exchanged. The broker/agents are aware of these rates based on comparable transactions carried out in the neighborhood and an adjustment factor is incorporated for size, feasibility, irregularity, shape etc of the land/building whereby either the premium or discount is given to the rates provided by the brokers and the final rate at which the property has to be valued at is arrived. The valuers have satisfied themselves on the reasonableness of the value and the company has relied on the expert opinion of the valuers. The stipulation of sharing of 50% of unearned amount on sale was not in the knowledge of the company based on the available documents of possession and ownership at that time. However, the scheme of conversion from leasehold to freehold by payment of nominal charges instead of 50% is available in Delhi for L&DO land. We are of the understanding that the valuers have valued the property as leasehold land taking recognition of this principle while valuing the property". Efforts are on at the highest level with the Ministry of Urban Development, Delhi for the restoration of Lease Deed. However, a disclosure in the Notes to Accounts about the status of the Vasant Vihar Housing Colony, New Delhi is given vide Note No 5 Schedule X.