CHAPTER-IV: COMMERCIAL ACTIVITIES

Section-I

4. Overview of State Public Sector Undertakings

4.1 Introduction

4.1.1 The State Public Sector Undertakings (PSUs) consist of State Government Companies and Statutory Corporations. The State PSUs are established to carry out activities of commercial nature while keeping in view the welfare of people. In Jammu and Kashmir, the State PSUs occupy a moderate place in the state economy. The Working PSUs registered a turnover of ₹ 4409.87 crore in 2010-11 as per their latest finalised accounts as of 30th September 2011. This turnover was equal to 9.24 *per cent* of State Gross Domestic Product (GDP) of ₹ 47709 crore in 2010-11. Major activities of Jammu and Kashmir State PSUs are concentrated in power and finance sectors. The working PSUs earned a profit of ₹ 500.37 crore in the aggregate as *per* their latest finalised accounts as of 30th September 2011. They had employed 0.25 lakh employees as on 31 March 2011. The State PSUs do not include two[*] prominent Departmental Undertakings (DUs), which carry out commercial operations but are a part of Government departments.

4.1.2 As on 31 March 2011, there were 24 PSUs as *per* the details given below. Of these, one company[§] was listed on the stock exchanges.

Type of PSUs	Working PSUs	Non-working PSUs[ψ]	Total
Government Companies	18	3	**21**
Statutory Corporations	3	Nil	**3**
Total	**21**	**3**	**24**

4.1.3 During the year 2010-11, one PSU viz. Jammu and Kashmir Bank Financial Services Limited was established.

Audit Mandate

4.1.4 Audit of Government companies is governed by Section 619 of the Companies Act, 1956. According to Section 617, a Government company is one in which not less than 51 *per cent* of the paid up capital is held by Government(s). A Government company includes a subsidiary of a Government company. Further, a company in which 51 *per cent* of the paid up capital is held in any combination by Government(s), Government companies and Corporations controlled by Government(s) is treated as if it

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* Consumer Affairs & Public Distribution Department and Government Press

§ Jammu and Kashmir Bank Limited.

ψ Non-working PSUs are those which have ceased to carry on their operations.

were a Government company (deemed Government company) as *per* Section 619-B of the Companies Act,1956.

4.1.5 The accounts of the State Government companies (as defined in Section 617 of the Companies Act, 1956) are audited by Statutory Auditors, who are appointed by CAG as *per* the provisions of Section 619(2) of the Companies Act, 1956. These accounts are also subject to supplementary audit conducted by CAG as *per* the provisions of Section 619 of the Companies Act, 1956.

4.1.6 Audit of statutory corporations is governed by their respective legislations. Out of three statutory corporations, CAG is the sole auditor for Jammu and Kashmir State Road Transport Corporation and Jammu and Kashmir State Forest Corporation*. In respect of Jammu and Kashmir State Financial Corporation, the audit is conducted by Chartered Accountants and supplementary audit by CAG.

Investment in State PSUs

4.1.7 As on 31 March 2011, the investment (capital and long-term loans) in 24 PSUs was ₹ 5225.63 crore as *per* details given below.

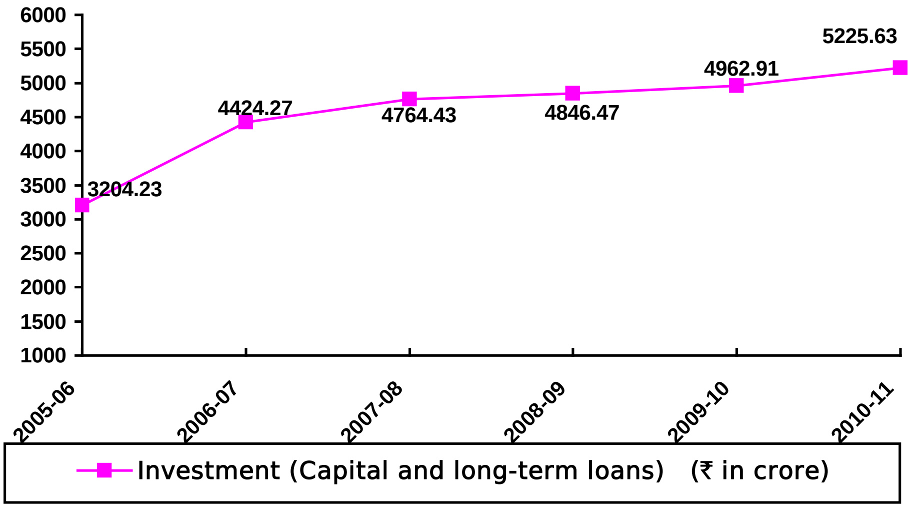
(₹. In crore)

Type of PSUs	Government Companies			Statutory Corporations			Grand Total
	Capital	Long Term Loans	Total	Capital	Long Term Loans	Total	
Working PSUs	250.94	4194.53	4445.47	237.19	539.57	776.76	**5222.23**
Non-working PSUs	2.57	0.83	3.40	Nil	Nil	Nil	**3.40**
Total	**253.51**	**4195.36**	**4448.87**	**237.19**	**539.57**	**776.76**	**5225.63**

A summarised position of government investment in State PSUs is detailed in **Appendix 4.1**

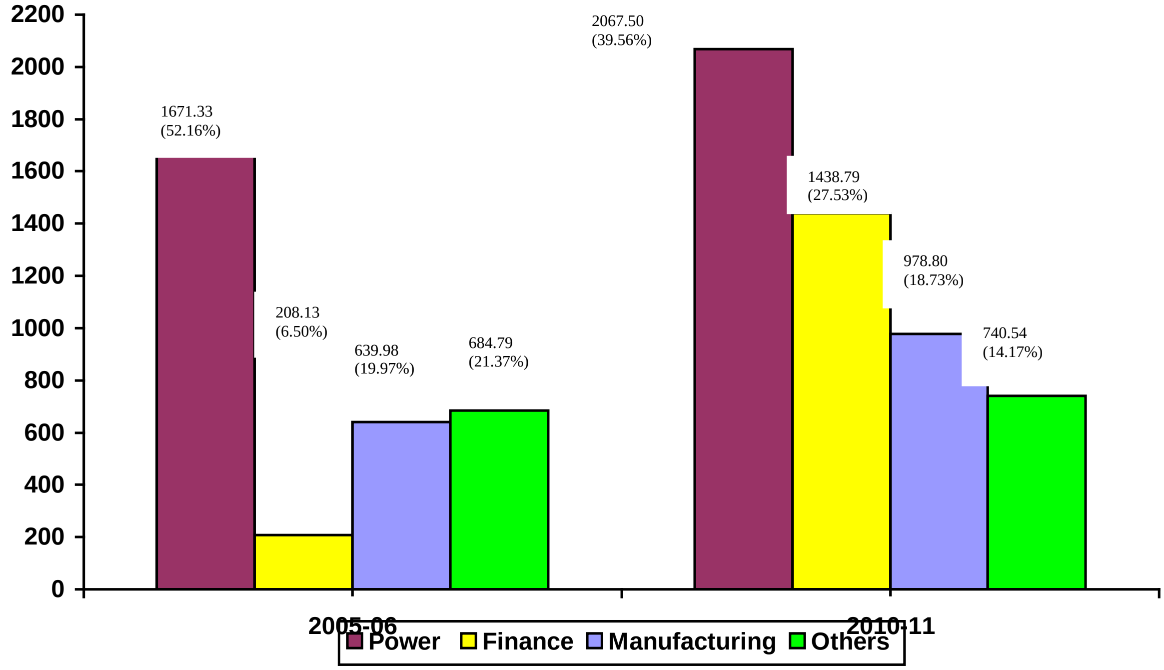
4.1.8 As on 31 March 2011, of the total investment in State PSUs, 99.93 *per cent* was in working PSUs and the remaining 0.07 *per cent* in non-working PSUs. The total investment consisted of 9.39 *percent* towards capital and 90.61 *per cent* in long-term loans. The investment has grown by 63.09 *percent* from ₹ 3204.23 crore in 2005-06 to ₹ 5225.63 crore in 2010-11 as shown in the graph below.

* Jammu and Kashmir State Forest Corporation was incorporated in 1978-79 and its audit was entrusted to CAG with effect from 1996-97. The Corporation, however, had never submitted its accounts to CAG for audit for any of the years.



4.1.9 The investment in various important sectors and percentage thereof at the end of 31 March 2006 and 31 March 2011 are indicated below in the bar chart. Though the highest investment during 2010-11 was in power sector (39.56 *per cent*), the thrust of PSU investment was mainly in finance sector during the six years which has seen its percentage share rising from 6.50 *per cent* in 2005-06 to 27.53 *per cent* in 2010-11.

(Rs in crore)



Budgetary outgo, grants/subsidies, guarantees and loans

4.1.10 The details regarding budgetary outgo towards equity, loans, grants/ subsidies, guarantees issued, loans written off, loans converted into equity and interest waived in respect of State PSUs are given in **Appendix 4.3.** The summarised details are given below for three years ended 2010-11.

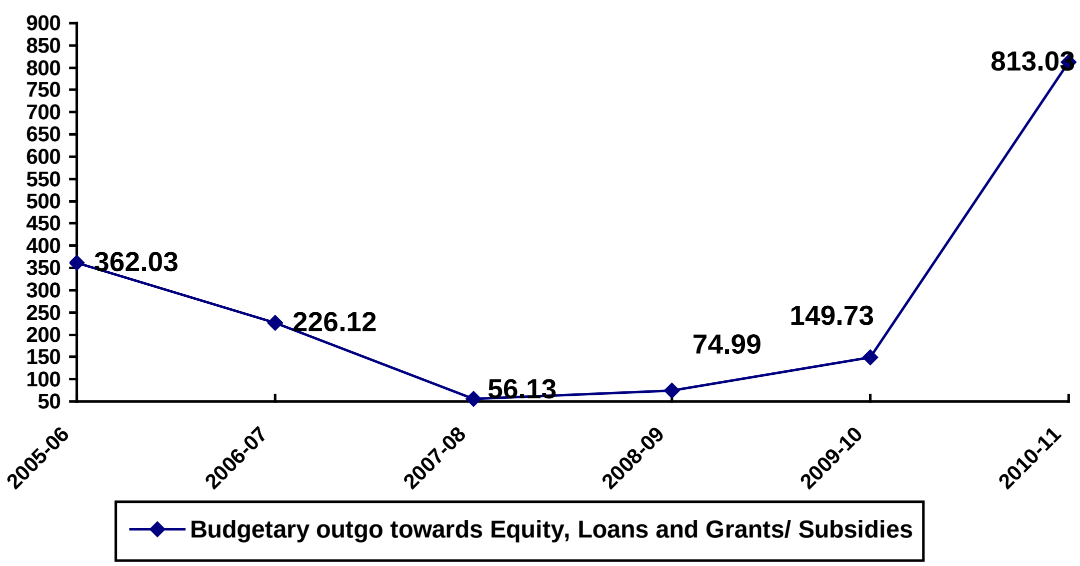
(₹ in crore)

Sl. No.	Particulars	2008-09		2009-10		2010-11	
		No. of PSUs	Amount	No. of PSUs	Amount	No. of PSUs	Amount
1.	Equity Capital outgo from budget	3	7.63	4	17.09	3	7.00
2.	Loans given from budget	9	43.76	9	56.57	10	488.54
3.	Grants/Subsidy received from State Government.	8	23.60	4	76.07	6	317.49
4.	Total Outgo (1+2+3)	12#	74.99	11#	149.73	14#	813.03
5.	Interest/Penal interest written off	2	21.79	1	4.04	1	3.69
6.	Total Waiver	2	21.79	1	4.04	1	27.78*
7.	Guarantees issued	3	7.51	2	485.54	2	2.70
8.	Guarantee Commitment	10	2194.72	8	2598.77	9	2411.39

*# Actual number of PSUs which received budgetary support. ,*Includes waiver of loan repayment of ₹24.09 crore.*

4.1.11 The details regarding budgetary outgo towards equity, loans and grants/ subsidies for past six years are given in a graph below.

(Rs in crore)



The budgetary outgo of the State Government towards equity contribution, loans, grants and subsidy was all time high in 2010-11 at ₹ 813.03 crore during the preceding six years. The downward trend of budgetary outgo can be seen during 2005-06 to 2007-08 with marginal increase during 2008-09 and stood at ₹ 813.03 crore in 2010-11.

4.1.12 The guarantees issued by the State Government received during the year 2010-11 was ₹ 2.70 crore and outstanding at the end of 31 March 2011 was ₹ 2411.39 crore. More than 96 *per cent* of these guarantees outstanding were on the loans raised by Jammu and Kashmir State Power Development Corporation Limited from various Financial Institutions. However, the State Government has not charged any guarantee commission or fee from the PSUs during 2010-11.

Reconciliation with Finance Accounts

4.1.13 The figures of equity, loans and guarantees outstanding as per records of State PSUs should agree with that of the figures appearing in the Finance Accounts of the State. In case the figures do not agree, the concerned PSUs and the Finance Department should carry out reconciliation of differences. The position in this regard as at 31 March 2011 is stated below.

(₹ in crore)

Outstanding in respect of	Amount as per Finance Accounts	Amount as per records of PSUs	Difference
Equity	441.06	357.69	83.37
Loans	833.80	1512.96	(-) 679.16
Guarantees	2411.39	2411.39	Nil

4.1.14 Audit observed that the differences occurred were due to misclassification and were under reconciliation. Reasons therefor, though called for, were not intimated (September 2011). The Government and the PSUs should take concrete steps to reconcile the differences in a time bound manner.

Performance of PSUs

4.1.15 The financial results of PSUs, financial position and working results of working statutory corporations are detailed in **Appendices 4.2, 4.5 and 4.6** respectively. A ratio of PSU turnover to State GDP shows the extent of PSU activities in the State economy. Table below provides the details of working PSU turnover and State GDP for the period 2005-06 to 2010-11.

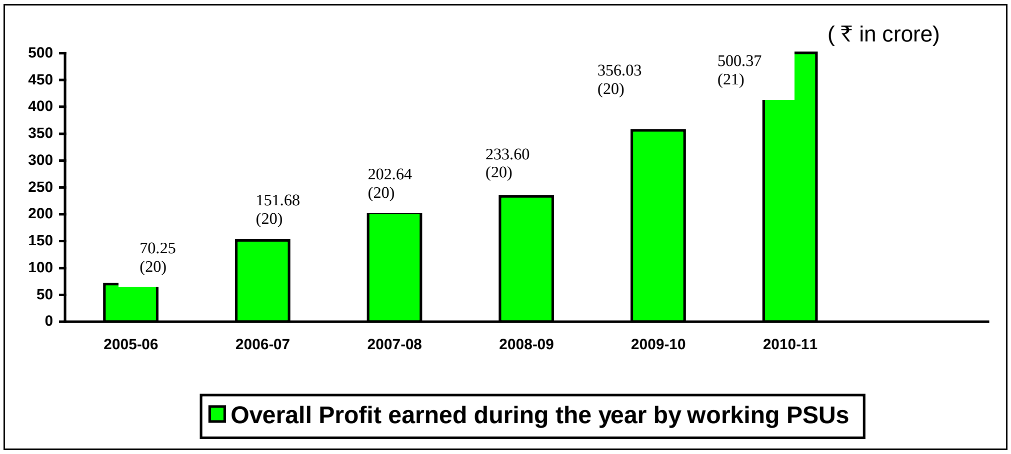
(₹ in crore)

Particulars	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Turnover[∝]	2539.27	2679.33	3595.92	3206.88	3700.38	4409.87
State GDP	26537	29030	31793	34805	38298	47709
Percentage of Turnover to State GDP	9.57	9.23	11.31	9.21	9.66	9.24

∝ Turnover as per the latest finalised accounts as of 30 September 2011

The percentage of turnover to State Gross Domestic Product was 9.57 *per cent* during 2005-06 which increased to 11.31 *per cent* in 2007-08 but marginally decreased to 9.24 *per cent* during 2010-11. This was due to the increase in State Gross Domestic Product in 2010-11.

4.1.16 Profit earned by State working PSUs during 2005-06 to 2010-11 are given below in a bar chart.



(Figures in brackets show the number of working PSUs in respective years)

During the year 2010-11 out of 21 working PSUs, six PSUs earned profit of ₹ 654.31 crore and 13 PSUs incurred loss of ₹ 153.94 crore. One working PSU (Jammu and Kashmir State Cable Car Corporation Limited) had not prepared the Profit and Loss Account while one PSU (Jammu & Kashmir State Forest Corporation Limited) had not submitted its accounts since 1996-97 when its audit was entrusted to C&AG. The major contributors to profit were Jammu and Kashmir Bank Ltd (₹ 615.20 crore) and Jammu and Kashmir State Power Development Corporation (₹ 37.17 crore). The heavy losses were incurred by Jammu and Kashmir State Road Transport Corporation (₹ 52.52 crore), Jammu and Kashmir Industries Limited (₹ 42.31 crore) and Jammu and Kashmir State Financial Corporation (₹ 26.22 crore).

4.1.17 The losses of working PSUs are mainly attributable to deficiencies in financial management, planning, implementation of projects, running their operations and monitoring. A review of latest Audit Reports of C&AG shows that the State PSUs incurred losses to the tune of ₹ 226.11 crore which were controllable with better management. Year wise details from Audit Reports are stated below.

(₹ in crore)

Particulars	2008-09	2009-10	2010-11	Total
Net Profit	233.60	356.03	500.37	**1090.00**
Controllable losses as per CAG's Audit Report	14.04	27.05	185.02	**226.11**

4.1.18 The above losses pointed out by Audit Reports of CAG are based on test check of records of PSUs. The actual controllable losses would be much more. The above table shows that with better management, the losses can be minimised. The above situation points towards a need for professionalism and accountability in the functioning of PSUs.

4.1.19 Some other key parameters pertaining to State PSUs are given below.

(₹ in crore)

Particulars	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Return on Capital Employed (*Per cent*)	13.94	7.17	8.85	10.91	10.83	9.61
Debt	2806.26	4023.13	4361.59	4435.99	4495.58	4734.93
Turnover*	2539.27	2679.33	3595.92	3206.88	3700.38	4409.87
Debt/ Turnover Ratio	1.11:1	1.50:1	1.21:1	1.38:1	1.21:1	1.07:1
Interest Payments	1098.72	1977.53	1697.43	2063.75	2000.65	2250.07
Accumulated losses[*f*]	1172.45	1230.70	1285.72	1338.05	1384.70	1529.98

The debt/turnover ratio improved in 2010-11 as compared to 2009-10. This was due to higher increase in turnover during 2010-11 with reference to the increase in debts.

4.1.20 As per the latest finalised accounts, six PSUs earned an aggregate profit of ₹ 654.31 crore and only one PSU (Jammu and Kashmir Bank Ltd.) declared a dividend of ₹ 126.04 crore.

Arrears in finalisation of accounts

4.1.21 Under Sections 166, 210, 230, 619 and 619-B of the Companies Act, 1956, the accounts of the Companies for every financial year are required to be finalised within six months from the end of the relevant financial year. Similarly, in case of Statutory Corporations, their accounts are finalised, audited and presented to the Legislature as per the provisions of their respective Acts. The table below provides the details of progress made by working PSUs in finalisation of accounts by September 2011.

Sl. No.	Particulars	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
1.	Number of Working PSUs	20	20	20	20	20	21
2.	Number of accounts finalised during the year	11	12	12	15	10	34
3.	Number of accounts in arrears	203	211	219	224	236[†]	223
4.	Average arrears *per* PSU (3/1)	10.15	10.55	10.95	11.20	11.70	10.62
5.	Number of Working PSUs with arrears in accounts	19	19	19	19	19	19
6.	Extent of arrears	1 to 18	2 to 19	3 to 19	4 to 19	4 to 20	2 to 20

4.1.22 Most of the working PSUs had failed to finalise even one account in each year causing accumulation of the arrears. The main reasons for non-finalisation of the

* Turnover of working PSUs as *per* the latest accounts (Position up to 30th September 2011).

f This represents the losses of all the working and non-working PSUs

† Includes two accounts received from a new Company viz., J&K Bank Financial Services, for the years 2008-09 and 2009-10, not earlier included as accounts in arrears.

accounts by the PSUs noticed during audit were non-constitution of the Boards, non-holding of regular Board meetings, delay in audit of accounts by the Statutory Auditors and lack of trained staff.

4.1.23 In addition to above, there were also arrears in finalisation of accounts by non-working PSUs. All the three non-working PSUs (all companies) had gone into liquidation process. The accounts of non-working PSUs are in arrears for the period ranging between 11 to 21 years.

4.1.24 The State Government had invested ₹ 1347.83 crore (equity: ₹ 118.44 crore, loans: ₹ 739.27 crore, grants: ₹ 476.98 crore and subsidy: ₹ 13.14 crore) in 16 PSUs during the years for which accounts are in arrears as detailed in ***Appendix 4.4***. In the absence of finalization of accounts and their subsequent audit, it can not be ensured whether the investments and expenditure incurred have been properly accounted for and the purpose for which the amount was invested has been achieved or not and thus Government's investment in such PSUs remain outside the scrutiny of the State Legislature. Further, delay in finalisation of accounts may also result in the risk of fraud and leakage of public money apart from violation of the provisions of the Companies Act, 1956.

4.1.25 The administrative departments have the responsibility to oversee the activities of these entities and to ensure that the accounts are finalised and adopted by these PSUs within the prescribed period. Though the concerned administrative departments and officials of the Government were informed every quarter by the Audit, of the arrears in finalisation of accounts, no remedial measures were taken. As a result of this the net worth of these PSUs could not be assessed in audit. The matter of arrears in accounts was also taken up with the Finance Secretary in April 2011 to expedite the backlog of arrears in accounts in a time bound manner.

4.1.26 In view of above state of arrears, it is recommended that:

- **The Government may set up a cell to oversee the clearance of arrears and set the targets for individual companies which would be monitored by the cell.**

- **The Government/PSUs may consider outsourcing the work relating to preparation of accounts wherever the staff is inadequate or lacks expertise.**

Winding up of non-working PSUs

4.1.27 There were three non-working PSUs (all companies) as on 31 March 2011 and all three[♥] were under liquidation process. The numbers of non-working companies at the end of each year during past six years are given below.

♥ Tawi Scooters Limited, Himalayan Wool Combers Limited and Jammu and Kashmir State Handloom Handicrafts Raw Material Supplies Organisation Limited.

Particulars	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
No. of non-working Companies	3	3	3	3	3	3

4.1.28 The Stages of closure in respect on non-working PSUs are given below.

S.No.	Particulars	Companies	Statutory Corporations	Total
1	Total No. of non-working PSUs	3	Nil	3
2	Of (1) above, the No. under			
(a)	Liquidation by Court (liquidator appointed)	2*	--	2
(b)	Voluntary winding up (liquidator appointed)	1	--	1

4.1.29 During the period October 2010 to September 2011, no company was finally wound up. The companies which have taken the route of winding up by court order are under liquidation for more than eight years. The process of voluntary winding up under the Companies Act is much faster and needs to be adopted for closure of non-working companies.

Accounts Comments and Internal Audit

4.1.30 Thirteen working companies forwarded their audited 32 accounts to Audit during the period October 2010 to September 2011. Of these, thirteen accounts of eight companies were selected for supplementary audit. The audit reports of statutory auditors appointed by CAG and the supplementary audit of CAG indicated that the quality of maintenance of accounts needed to be improved substantially. The details of aggregate money value of comments of statutory auditors and CAG are given below.

(₹. in crore)

S.No.	Particulars	2008-09		2009-10		2010-11	
		No. of accounts	Amount	No. of accounts	Amount	No. of accounts	Amount
1	Decrease in profit	1	0.03	--	--	6	18.17
2	Increase in loss	1	0.74	1	0.86	12	43.76
3	Non-disclosure of material facts	3	31.14	4	8.32	4	15.66
4	Errors of classification	--	--	3	28.11	9	217.20

4.1.31 During the year, the statutory auditors had given unqualified certificates for four accounts, qualified certificates for 19 accounts, and disclaimers (meaning the auditors are

* Himalayan Wool Combers Limited and Jammu and Kashmir State Handloom Handicrafts Raw Material Supplies Organisation Limited.

unable to form an opinion on accounts) for nine accounts. The compliance of companies with the Accounting Standards remained poor as there were 22 instances of non-compliance.

4.1.32 Some of the important comments in respect of accounts of companies finalised during the year 2010-11 are stated below:

Jammu and Kashmir Power Development Corporation (2005-06)

- The Fixed Assets were overstated by ₹` 7.56 crore due to charging of depreciation at 15 *per cent* on Plant and Machinery and Miscellaneous Assets instead of at 25 *per cent* applicable.
- The Company had not disclosed contingent liability in respect of four court cases where the Hon'ble court has passed awards worth ₹ 7.45 crore against Company

4.1.33 During 2010-11, one Statutory Corporation (Jammu and Kashmir State Financial Corporation) forwarded one account (2006-07) and another Statutory Corporation (Jammu and Kashmir State Road Transport Corporation) had furnished the revised accounts for one year (2005-06) during the period October 2010 to September 2011. Jammu and Kashmir State Forest Corporation had never submitted its accounts to CAG since 1996-97 when its audit was entrusted to CAG. The details of aggregate money value of comments of statutory auditors and CAG are given below:

(₹ in crore)

S.No.	Particulars	2008-09		2009-10		2010-11	
		No. of accounts	Amount	No. of accounts	Amount	No. of accounts	Amount
1	Decrease in profit	-	-	-	-	-	-
2	Increase in loss	-	-	1	5.80	1	25.87
3	Non-disclosure of material facts	-	-	-	-	1	0.84
4	Errors of classification	-	-	-	-	1	1.00

Some of the important comments in respect of Accounts of Statutory Corporations are stated below:

Jammu and Kashmir State Financial Corporation (2006-07)

- The Capital included ₹ 0.80 crore contributed by the State Govt. towards share capital for which no shares had been allotted. The amount should have been reflected as capital pending allotment.
- Against outstanding advances of ₹ 32.23 crore, the advances worked out ₹ 31.09 crore after taking into account outstanding advances as on March, 2006, additions recovery and provision, thus indicating variation of ₹ 1.14 crore.

Jammu and Kashmir State Road Transport Corporation (2005-06)

- The Capital included ₹ one crore received from the State Government as grant-in-aid. Treatment of grant-in aid as Equity capital has resulted in overstatement of Share Capital.
- Interest of ₹ 11.60 crore payable as outstanding balances of Contributory Provident Fund, State Life Insurance and Life Insurance Corporation for the last fifteen years had not been accounted for. This had resulted in understatement of current liabilities and provisions as well as loss by ₹ 11.60 crore.
- Non-accountal of outstanding electricity charges payable to Power Development Department had resulted in understatement of current liabilities as well as loss to the extent of ₹ 53.55 lakh.
- Non-accountal of outstanding rent payable to Srinagar Municipal Corporation for use of City Services yard had resulted in understatement of current liabilities as well as loss to the extent of ₹ 61.91 lakh.
- Non-accountal of compensation payable on account of Motor Accidental claims awarded by MACT against Corporation had resulted in understatement of current liabilities as well as loss by ₹ 40.84 lakh.

4.1.34 The Statutory Auditors (Chartered Accountants) are required to furnish a detailed report upon various aspects including internal control/ internal audit systems in the companies audited in accordance with the directions issued by the CAG to them under Section 619 (3) (a) of the Companies Act, 1956 and to identify areas which needed improvement. The Statutory Auditors had stated that internal audit system in respect of twelve companies was either not in place or internal audit reports were not furnished as given below:

Nature of comments made by Statutory Auditors	Number of companies where recommendations were made	Reference to serial number of the companies as per Appendix-4.2
Non-maintenance of records pertaining to fixed assets	06	A: 7,11,13,15,16,17
Non-conducting of physical verification/Non production of records of physical verification of inventories of raw material, stores, spares etc.,	06	A: 7,11,14,15,16,17
Non-valuation of stocks	05	A: 11,14,15,16,17
Absence of internal audit system	06	A: 7,11,13,14,15,16
Company irregular in depositing statutory dues like PF, ESI, Income Tax, TDS, Sales tax etc	03	A: 11,13,15
Incorrect accounting system	02	A: 7,16
Non-produciton of records	03	A: 15, 16, 17

Status of placement of Separate Audit Reports

4.1.35 The following table shows the status of placement of various Separate Audit Reports (SARs) issued by the CAG on the accounts of statutory corporations in the Legislature by the Government.

Sl. No.	Name of Statutory corporation	Year up to which SARs placed in Legislature	Year for which SARs not placed in Legislature		
			Year of SAR	**Date of issue to the Government**	**Reasons for delay in placement in Legislature**
1.	Jammu and Kashmir State Financial Corporation	2005-06	2006-07	05 July 2011	-

Disinvestment, Privatisation and Restructuring of PSUs

4.1.36 The State had not carried out any disinvestment or restructuring of the PSUs during 2010-11. Further, it did not intimate about any plans for disinvestment, privatization or restructuring of the non-performing PSUs.

SECTION-II

PART-A

FINANCE DEPARTMENT

THE JAMMU AND KASHMIR BANK LTD.

4.2 Performance Audit on the working of Jammu and Kashmir Bank Limited.

Executive Summary

The Jammu & Kashmir Bank Limited (Bank) was incorporated on 01 October 1938 under the provisions of the then Jammu & Kashmir Companies Regulation No. XI of 1977 Samvat (1920 AD). The Bank is also regulated by the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949.The Reserve Bank of India (RBI) notified (October 1971) the Bank retrospectively as a Scheduled Commercial Licensed Bank. As on 31 March 2011, the Bank had 11 Zonal offices controlling a network of 548 branches (excluding extension counters) spread over 20 States and one Union Territory of the country. The turnover (income) of the Bank was ₹ 4077.89 crore during 2010-11as against ₹ 2059.54 crore during 2006-07. The Bank employed 7939 employees as on 31 March 2011. The paid up capital as on March 2011 was ₹ 48.49 crore. The performance audit of the Bank for the period from 2006-07 to 2010-11 was conducted to assess the performance of core activities of the Bank viz: Advances, Priority Sector Lending and Investments.

Advances

Though the overall achievements against the targets of advances were satisfactory, inter- zone disparity required attention. Credit Deposit Ratio of the Bank declined from 69.02 per cent in the year 2006-07 to 59.67 per cent in 2010-11 and remained on lower side as compared to average CD Ratio of all Scheduled Commercial Banks (SCB) in India. The Bank lacked in monitoring the credit facilities. The percentage of NPA to total advances of the Bank ranged between 2.89 and 1.95 during 2006-11. However, huge inter-zonal disparities existed on this account. In the course of settlement of Loan cases under One Time Settlement (OTS), the Bank had ended up sacrificing principal amount of ₹ 33.35 crore and ₹ 147.47 crore towards interest during the years 2006-11.

Priority Sector lending

The Bank's achievement under agriculture sector was dismal. Consequent upon shortfall of targets on this account, the Bank had to invest an amount of ₹ 2862.74 crore in low yielding (interest rate off three to six per cent per annum) Rural Infrastructure Development Fund (RIDF) for a period of three to seven years, leading to loss of interest to the tune of ₹ 334.49 crore. The Bank had not been able to recover NPA under Priority Sector, leading to

increase in NPA levels by ₹214.37 crore to ₹ 312.44 crore during 2006-11. The Bank had not been able to achieve the targets under centrally/State sponsored schemes leading to tardy implementation of various programmes. Under Lead Bank Segment, the Bank had not been able to discharge its responsibilities.

Investments

For maximizing the yield and boosting the profitability, the Bank holds investment portfolio. Funds are deployed in SLR and Non-SLR Securities. The return on investments portfolio remained below seven per cent which was not financially prudent. Bank had written off NPIs leading to loss to the tune of ₹49.72 crore during 2007-10.

Conclusion and Recommendations

The Bank had suffered huge losses on account of low CD Ratio, Consortium advances, settlement cases under OTS Scheme, non-achievement of targets under Priority Sector Lending, low yield on investment. By achievement of targets under advances, increase of CD ratio, effective monitoring, reduction of Zonal level NPA, avoiding sacrifice of Principal amount under OTS Scheme, achievement of targets under Priority Sector Lending and strengthening the investment portfolio, the Bank can avoid losses and increase income. The performance audit contains seven recommendations to improve Bank's performance and to minimise losses.

4.2.1 Introduction

The Jammu & Kashmir Bank Limited (Bank) was incorporated on 01 October 1938 under the provisions of the then Jammu & Kashmir Companies Regulation No. XI of 1977 *Samvat* (1920 AD). It commenced business on 04 July 1939. After the extension (November 1956) of the Companies Act 1956 to the State of Jammu & Kashmir, the Bank became a Government Company in terms of Section 617 of the Companies Act, 1956. The Bank is also regulated by the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949.

The Reserve Bank of India (RBI) notified the Bank retrospectively as a Scheduled Commercial Licensed Bank in October 1971 by including it in the Second Schedule to the RBI Act 1934.

As on 31 March 2011, the Bank had 11 Zonal offices controlling a network of 548 branches (excluding extension counters) spread over 20 States and one Union Territory of the country. Under Branch expansion programme, the Bank opened 119 new branches during 2006-11 as against 146 branches approved by the RBI.

The Management of the Bank is vested in a Board comprising 12 Directors[*] including Chairman. The day-to-day activities are managed by the Chairman who is also its Chief Executive Officer. He is assisted by two Executive Directors and a Secretary.

The turnover (income) of the Bank was ₹ 4077.89 crore during 2010-11 and it employed 7939 employees as on 31 March 2011.

4.2.2 Objectives

The main objects of the Bank are as follows:

- establish and carry on business of a Banking Company;
- borrow or raise money;
- establish and carry on the business of a Savings Bank and to provide Custodial & Depository services;
- lend money by making loans and advances;
- buy, sell, collect and deal in bills of exchange, hundies, promissory notes, drafts, bills of lading, debentures & other instruments;
- deal in stocks, shares, debentures, securities and investment of all kinds;
- buy and sell foreign exchange including foreign notes; and
- act as agents for Government or local authorities.

4.2.3 Scope of Audit

A review on the working of the Bank was incorporated in the Report of the Comptroller and Auditor General of India for the year ended 31 March 1995. The review was discussed in the Committee on Public Undertakings (COPU) during 1997-99. Besides, a performance review on the Information Systems of the Bank was incorporated in the Stand Alone Report of the Comptroller and Auditor General of India for the year ended 31 March 2006. The Report presented in the State Legislature on 31 August 2009, had not been taken up for discussion by the COPU as of October 2011.

The Performance Audit, conducted between March 2011 and July 2011, covers the performance of the Bank during the period from 2006-07 to 2010-11. The Performance Audit mainly deals with core activities of the Bank viz., ***Advances, Priority Sector Lending and Investments.*** The audit examination involved scrutiny of records at the Corporate Office of the Bank at Srinagar, Treasury Operations and Investment Department at Mumbai, five[†] out of 11 Zonal Offices covering 279 branches. In addition detailed check of relevant record of 60 branches of five Zones was carried out at respective Zonal Offices.

[*] Two: Government nominee, one: RBI nominee, two: Executive directors of the Bank and seven: Independent directors nominated by the shareholders.

[†] Bangalore, Delhi, Jammu Central, Kashmir Central and Mumbai

4.2.4 Audit Objectives

The objectives of the performance audit were to assess:

- whether the guidelines/instructions of the RBI Act, 1934, Banking Regulation Act, 1949, Companies Act, 1956 and Securities and Exchange Board of India (SEBI) Act, 1992 concerning the areas covered under the performance audit have been complied with,
- the achievement of targets as per Annual Business Plan and growth of advances,
- the efficacy of the monitoring system relating to advances,
- the Implementation of NPA Recovery Policy and effect of One Time Settlement Scheme,
- the achievements of the targets under Priority Sector Lending as fixed by the RBI and impact of shortfall there against,
- the efficiency in implementation of the Central/State Sponsored Schemes,
- the extent of growth of Investment vis-a-vis income,
- the impact of write off and one time settlement of Non Performing Investments.

4.2.5 Audit Criteria

Audit criteria adopted for assessing the achievements of the audit objectives were:

- Reserve Bank of India Act, 1934 and guidelines of the RBI issued from time to time,
- Banking Regulation Act, 1949, Companies Act, 1956 and SEBI Act 1992,
- Annual Business Plans,
- Policy of the Bank with regard to Credit, Investment, Recovery of NPA, etc.,
- Guidelines of Central/State Sponsored and Lead Bank Schemes.

4.2.6 Audit Methodology

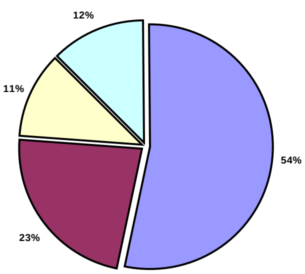
The methodology adopted for attaining the audit objectives consisted of obtaining and studying the minutes of the meetings of Board of Directors (BoD), scrutiny of records and statistical data at Corporate Office and selected Zonal offices, analysis of data, raising of audit queries, discussion of audit findings with the Management of the Bank and issue of draft performance audit report to the Management/Government for comments.

4.2.7 Financial Position and working results

4.2.7.1 The Authorized Share Capital of the Bank as on 31 March 2011 was ₹ 100.00 crore divided into 10 crore shares of ₹ 10 each. The paid up capital as on that date was ₹ 48.49 crore contributed by Government of Jammu and Kashmir

(₹ 25.78 crore), Foreign Institutional Investors (₹ 11.23 crore), Resident Individuals (₹ 5.57 crore) and others (₹ 5.91 crore including amount of forfeited shares). The percentage of the shareholding pattern as on 31 March 2011 is given below in the pie-chart:

Shareholding pattern



4.2.7.2 The Bank had been maintaining its annual account in accordance with the provisions of Section 29 of the Banking Regulation Act, 1949 read with Section 211 of the Companies Act, 1956.

The financial position and the working results of the Bank as per audited annual accounts for the five years ending 2010-11 are given below:

<u>Financial Position</u>

(₹ in crore)

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
A. Liabilities					
a) Paid up Capital	48.49	48.49	48.49	48.49	48.49
b) Equity Share Warrants	-	28.10	-	-	-
c) Reserve and Surplus	1960.24	2232.33	2574.37	2961.97	3430.19
d) Deposits	25194.30	28593.26	33004.10	37237.16	44675.94
e) Borrowings	620.19	751.79	996.63	1100.21	1104.65
f) Other Liabilities and Provisions	823.31	1102.02	1069.67	1198.97	1248.88
Total	**28646.53**	**32755.99**	**37693.26**	**42546.80**	**50508.15**
B. Assets					
a) Cash & Bank Balance	1854.77	3219.97	2302.95	2744.73	2974.96
b) Balance with Banks & Money at Call & Short Notice	1758.99	1217.28	2971.81	1869.51	573.85
c) Net Investments*	7392.19	8757.66	10736.34	13956.25	19695.77
d) Net Advances†	17079.94	18882.61	20930.41	23057.23	26193.63
e) Fixed Assets	183.45	192.00	199.41	204.13	393.77
f) Other Assets	377.19	486.47	552.34	714.95	676.17
Total	**28646.53**	**32755.99**	**37693.26**	**42546.80**	**50508.15**
Net Worth‡	**2008.73**	**2308.92**	**2622.86**	**3010.46**	**3478.68**

* After provisions for depreciation
† After provisions for NPA
‡ Aggregate of Paid up Capital, Share Warrants and Reserves & Surplus

From the above it would be seen that:

- Total Reserves and Surplus had increased by 74.99 *per cent* from ₹ 1960.24 crore as on March 2007 to ₹ 3430.19 crore as on March 2011.
- Total deposits had grown by ₹ 19481.64 crore (77.33 *per cent*) from ₹ 25194.30 crore as on March 2007 to ₹ 44675.94 crore as on March, 2011.
- Total advances (net) had increased by ₹ 9113.69 (53.36 *per cent*) *per cent* crore from ₹ 17079.94 crore as on March 2007 to ₹ 26193.63 crore as on March 2011.
- Investment (net) had increased by ₹12303.58 crore (166.44 *per cent)* from ₹ 7392.19 crore in March 2007 to ₹ 19695.77 crore in March 2011. Major increase during 2010-11 was mainly because of surplus funds, due to low credit demand, which were deployed in Commercial Papers/Certificate of Deposits.
- Net worth had increased by ₹ 1469.95 crore (73.18 *per cent*) from ₹ 2008.73 crore as on March 2007 to ₹ 3478.68 crore as on March 2011.
- The Capital to Risk Weighted Assets Ratio (CRAR) of the Bank ranged between 12.80 *per cent* and 14.81 *per cent* during the years 2006-11 which comfortably exceeded the norms of nine *per cent* stipulated by the RBI. Despite this, the Bank had raised a subordinate debt (10 year NCD[*]-9% coupon) of ₹ 600 crore (₹ 500 crore from LIC[†], ₹ 75 crore from SICOM Ltd. and ₹ 25 crore from IFCI[‡] Ltd.) during 2009-10 and serviced an interest of ₹ 54 54 crore upto the end of March 2011, putting an additional burden of interest on the Bank to that extent.

[*] Non-Convertible Debentures
[†] Life Insurance Corporation of India Limited
[‡] Industrial Finance Corporation of India

Working Results

(₹ in crore)

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
1. Income					
a). Interest Earned	1899.33	2434.23	2988.12	3056.88	3713.13
b). Other Income	160.21	245.01	245.05	416.24	364.76
Total	**2059.54**	**2679.24**	**3233.17**	**3473.12**	**4077.89**
2. Expenditure					
a). Interest Expended	1131.48	1623.79	1987.86	1937.54	2169.47
b). Operating Expenses	372.44	403.62	470.86	577.37	758.93
c).Provisions and Contingencies	281.13	291.83	364.61	445.83	534.29
Total	**1785.05**	**2319.24**	**2823.33**	**2960.74**	**3462.69**
3. Net Profit	**274.49**	**360.00**	**409.84**	**512.38**	**615.20**
4. Total	**2059.54**	**2679.24**	**3233.17**	**3473.12**	**4077.89**
5. Appropriations					
a). Statutory Reserve	68.62	90.00	102.33	128.89	153.80
b). Revenue & Other Reserves	140.64	182.09	211.59	258.71	314.42
c). Final Dividend Proposed	55.75	75.14	81.97	106.65	126.04
d). Tax on Dividend	9.48	12.77	13.93	18.13	20.94
Total	**274.49**	**360.00**	**409.82**	**512.38**	**615.20**
Operating Revenue[*]	928.06	1055.45	1245.31	1535.58	1908.42
Operating Profit[†]	555.62	651.84	774.45	958.21	1149.49
Return on Average Net worth[‡] **(In *per cent*)**	14.42	16.68	16.62	18.19	18.96
Earning Per Share (₹)	56.62	74.26	84.54	105.69	126.90
Dividend Per Share (₹)	11.50	15.50	17.00	22.00	26.00

From the above it would be seen that:

- Income by way of interest had increased by 1813.80 crore (95.50 *per cent*) from ₹ 1899.33 crore in 2006-07 to ₹ 3713.13 crore in 2010-11.
- Net Profit had increased by 340.71crore (124.12 *per cent*) from ₹ 274.49 crore in March 2007 to ₹ 615.20 crore in March 2011 and operating profit by ₹ 593.87 crore (106.88 *per cent*) from ₹ 555.62 crore in 2006-2007 to ₹ 1149.49 crore in 2010-11.
- The Bank had declared a dividend of ₹ 26 per share during 2010-11 as against ₹ 11.50 per share during 2006-07 registering an increase of 126.09 *per cent*.

4.2.7.3 The Bank decided (July 2007) to raise additional capital of ₹ 700 crore by way of issue of American/Global Depository Receipts (A/GDRs). Since raising of additional capital necessitated raising of corresponding shareholding of the State Government, the

[*] Total Income minus Interest expended.
[†] Netting of income and expenditure (excluding provisions & contingencies)
[‡] Percentage of Net Profit to Average Net Worth

Bank issued (September 2007) convertible warrants on preferential basis to the State Government to be converted into shares on the date of allotment of shares or within the 18 months from the date of issue of warrants, whichever was earlier, for which State Government deposited (2007) ₹ 28.10 crore (10 *per cent* advance of the warrants). The Bank decided (March, 2009) to postpone the issuance of GDR and by the time this decision was taken, the Bank had incurred an expenditure of ₹ 99.52 lakh on GDR issue which was rendered wasteful.

The State Government also decided (December 2008) not to exercise its right for conversion of warrants into shares on preferential basis with the result the Bank in terms of the SEBI (DIP)[*] Guidelines 2000, forfeited (March 2009) the advance payment of ₹ 28.10 crore and credited the same to Capital Reserve (2008-09). It was, however, noticed that the Bank had subsequently (September 2009 to March 2010) compensated the State Government for the whole amount of ₹ 28.10 crore by way of adjustment in interest rate on the overdraft facility, thereby, extending undue favour to the State Government.

4.2.8 Audit Findings

The audit objectives were explained to the Bank during an 'entry conference' held on 21 March 2011. Audit findings were reported (August 2011) to the Bank and to the State Government and were also discussed (12 October, 2011) in an 'exit conference' held with the Commissioner Secretary, State Finance Department and Chairman of the Bank. The views expressed by the Management have been incorporated at suitable places. The audit findings are discussed below.

4.2.9 Deposits

The position of Deposits and growth of Deposits of the Bank during the years 2006-11 is tabulated below:

(₹ in crore)

Year	Deposits	YoY Growth	Growth (*per cent*)
2006-07	25194.30	1709.70[†]	7.28
2007-08	28593.26	3398.96	13.49
2008-09	33004.10	4410.84	15.43
2009-10	37237.16	4233.06	12.83
2010-11	44675.94	7438.78	19.98
Total Growth during 2006-11		**19481.64**	**77.33**

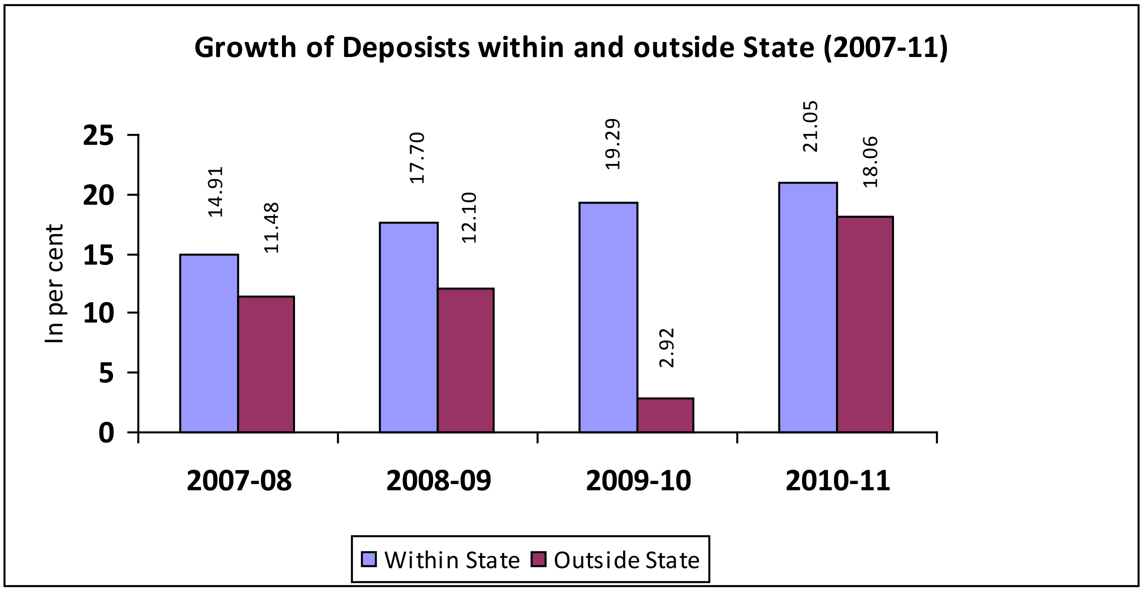
YoY: Year Over Year

There had been 77.33 *per cent* growth in deposits during 2006-11. The Year over Year (YoY) growth increased from 7.28 *per cent* in 2006-07 to 19.98 *per cent* in 2010-11.

[*] Securities and Exchange Board of India (Disclosure and Investor Protection)

[†] Calculated on Deposits during 2005-06: ₹ 23484.60 crore

Growth of deposits within State and Outside the State during the years 2007-11 is depicted in the graph below:



Audit analysis revealed that growth of deposits within the State had been increasing over the years whereas it had been un-even in zones outside the State. During 2006-11 the growth of deposits within the State stood at 95.32 *per cent* as against 51.85 *per cent* outside the State.

4.2.10 Advances

4.2.10.1 <u>Shortfall in achievement of Targets of Advances</u>

The Bank approves the business plan for each year wherein the targets for Advances (Gross) are fixed in respect of each Zone/Branch. The position of targets vis-à-vis achievements in respect of advances for the last five years ending 2010-11 is tabulated below:

(₹ in crore)

Year	Targets (Gross)	Achievements	Shortfall	Shortfall (In *per cent*)
2006-07	19,822.00	17,388.20	2,433.80	**12.28**
2007-08	21,683.00	19,164.28	2,518.72	**11.62**
2008-09	23,367.00	21,219.71	2,147.29	**9.19**
2009-10	24,921.00	23,455.20	1,465.80	**5.88**
2010-11	29,868.00	26,659.22	3,208.78	**10.74**

Though the overall achievements had been satisfactory, audit analysis of inter-zone data revealed uneven spread with shortfall in zones as high as 71.65 *per cent* (Mohali/2006-07), 28.78 *percent* (Jammu-North/2010-11), 22.57 *per cent* (Ladakh/2008-09), 21.43 *per cent* (Mumbai/2007-08) and 17.65 *per cent* (Delhi/2009-10).

Division-wise analysis revealed that shortfall in Kashmir Division had remained at 14.91 *per cent*, in Jammu Division 17.79 *per cent* and in Zones outside the State 19.08 *per cent* during the years 2006-11 which was on higher side than the overall shortfall during each year.

Non-achievement of targets had resulted in keeping the funds idle to the extent of shortfall occurred and subsequent loss of earnings at Prime Lending Rate (PLR) to the Bank. Audit also observed that the 'Cash actually retained' in all the zones remained far in excess of 'Cash retention limit' fixed by the Bank.

The Management stated (August 2011) that the persistent political disturbance in the State for three consecutive years (ending 2010-11) forced the Bank to reallocate the Advance targets in respect of various zones and higher targets were assigned to zones outside the State so as to make good the loss suffered by the zones of Kashmir division, as a result large chunk of shortfall was observed in those zones. The contention of the Management is not acceptable as the shortfall was higher during the years 2006-08 and not during the years of political disturbance, as claimed by the Bank.

4.2.10.2 Decline in Growth of Advances

Growth of Advances (Gross) of the Bank during the period from 2006-11 is tabulated below:

(₹ in crore)

Year	Advances	YoY Growth	Growth (*per cent*) of advances	Growth (*per cent*) of deposits
2006-07	17388.20	2668.78*	18.13	7.28
2007-08	19164.28	1776.08	10.21	13.49
2008-09	21219.71	2055.43	10.73	15.43
2009-10	23455.20	2235.49	10.53	12.83
2010-11	26659.22	3204.02	13.66	19.98
Total Growth during 2006-11		**9271.02**	**53.32**	**77.33**

Though there was 53.32 *per cent* increase in advances during 2006-11, the Year over Year (YoY) growth which stood at 18.13 *per cent* in 2006-07 had declined to 10.53 *per cent* during 2009-10 with marginal increase during 2010-11. The growth of advances, however, did not commensurate with the growth of the deposits except in 2006-07.

The growth of Advances at Zonal Office level had remained as low as 5.84 *per cent* (Delhi/2006-07), negative 0.52 *per cent* (Mumbai/2007-08), 2.88 *per cent* (Bangalore/2008-09), negative 16.44 *per cent* (Bangalore/2009-10) and 13.28 *per cent* (Jammu-West/2010-11).

Inter-Division analysis revealed that growth in Kashmir Division had ranged between 12.35 *per cent* and 35.96 *per cent*, in Jammu Division between 13.63 *per cent* and 36.51 *per cent* and in Zones outside the State between 2.48 *per cent* and 38.59 *per cent* during the period 2006-11.

* Calculated on Advances for 2005-06: ₹ 14719.42 crore

The Management stated (August 2011) that overall decline in growth was due to global economic recession in the year 2007 and disturbance in the home State for three consecutive years from 2008-09, whereas zone-wise meager/negative growth was due to shifting of composition of advances from large corporate lending to small and medium enterprises lending in home State.

4.2.10.3 Credit Deposit Ratio

Credit Deposit (CD) Ratio is an index of the health of banking system in terms of demand for credit in proportion to total deposit growth in the Banking sector. A declining CD ratio implies inadequate lending compared to the deposit available and results into weakened profitability owing to reduced spread.

Table below indicates the CD Ratio of the Bank during the years 2006-07 to 2010-11:

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
Bank (as a whole)	**69.02**	**67.02**	**64.24**	**62.99**	**59.67**
Zones within J&K State	49.76	52.31	51.89	51.06	37.99
Zones Outside J&K State	96.28	88.50	84.61	85.88	100.85
Urban (Branches)	67.32	66.74	60.26	58.96	42.88
Rural (All branches within State)	33.39	37.98	37.38	38.22	38.33
Semi-urban (Branches)	39.35	42.96	36.41	37.77	40.36
Metro (Branches)	100.42	92.53	96.31	102.74	111.76

CD Ratio declined from 69.02 *per cent* in the year 2006-07 to 59.67 *per cent* in 2010-11 and was far below the overall national average of Scheduled Commercial Banks (SCBs) during the years 2008 to 2010 as would be seen from the comparison in the box.

Credit-Deposit Ratio - Comparison

(Ending March/Per cent)

Banks	2008	2009	2010
Overall	74.60	73.80	73.60
Public Sector	73.30	72.60	73.20
Private Sector	67.40	64.50	67.10
J&K Bank	67.02	64.24	62.99

(Source: RBI)

Audit analysis revealed that the CD Ratio during 2006-11 in the Zones outside the State was better (ranging between 84.61 *per cent* and 100.85 *per cent*) as compared to that of the Zones within the State (ranging between 37.99 and 52.31 *per cent).* Further it was on the lower side in Rural and Semi-urban area (Branches) as compared to Metro and urban area (Branches).

The Management attributed (August 2011) the reasons of decline in CD Ratio to political disturbances in the State for successive three years. The Bank should have, however, concentrated in zones outside the State to improve the CDR.

4.2.10.4 Position of Net Advances

Table below indicates the position of net advances under various categories and securities held for total net advances for the period from 2006-07 to 2010-11:

(₹ in crore)

Category of Net Advances	2006-07	2007-08	2008-09	2009-10	2010-11
Bills purchased and discounted Y-o-Y Growth (*per cent*)	619.16 -	714.15 (15.34)	637.85 (-10.68)	364.74 (-42.82)	570.56 (56.43)
Cash credits, overdrafts and loans repayable on demand Y-o-Y Growth (*per cent*)	5990.38 -	6546.52 (9.28)	6538.24 (-0.13)	7508.80 (14.84)	5950.17 (-20.76)
Term loans Y-o-Y Growth (*per cent*)	10470.40 -	11621.94 (11.00)	13754.32 (18.35)	15183.68 (10.39)	19672.90 (29.57)
Total Net Advances	**17079.94**	**18882.61**	**20930.41**	**23057.22**	**26193.63**
Secured by Tangible Assets	11486.66	15208.73	18277.28	19076.42	21190.24
Covered by Bank/Govt. Guarantees	3204.00	1146.15	696.78	320.52	360.12
Unsecured	2389.28	2527.73	1956.35	3660.28	4643.27
Total	**34159.88**	**37765.22**	**41860.82**	**46114.44**	**52387.26**
Percentage of Unsecured to total advances	13.99	13.39	9.35	15.87	17.73

The following points emerged from the table:

- The Bank had made advances under the classification 'unsecured' and the percentage of unsecured advances to total net advances had increased from 9.35 *per cent* in 2008-09 to 17.73 *per cent* in 2010-11 indicating that the interest of the Bank had not been safeguarded to that extent.
- The impact of earnings of the Bank due to decline in various categories of advances was not ascertainable as the Bank had not maintained the data showing income under each category of advances separately. The Bank had also not maintained data under each category of Advances showing classification into Secured by Tangible Assets, Covered by Bank/Govt. guarantees and Unsecured. Non-maintenance of basic data has the chances of affecting the decision making process of the Bank.

The Management stated (September 2011) that 51 *per cent* unsecured advances as on 31 March 2011 comprised advances to salary class from whom no collateral securities had been obtained and are classified as unsecured. However, the fact remains that the balance 49 *per cent* (₹ 2275.20 crore) was unsecured.

As regards non-maintenance of data, the Management stated (September 2011) that the Management Information System (MIS) Department had been formulated which was at infancy stage and when fully functional, would enable the Bank to generate such type of information.

4.2.10.5 <u>Valuation of properties charged to the Bank</u>

Credit Policy of the Bank (2007-08) stipulates that the valuation of Mortgaged/hypothecated properties including plant and machinery is required to be got done through the valuers approved by the Bank, and in case of land, by the Revenue Authorities.

Test check of 71 cases sanctioned by the Bank during 2008-11 in five Zonal Offices[*] revealed that the land securities in all the cases had been valued by approved valuers instead of Revenue authorities, which was in violation of the Bank's own credit policy.

The Management stated (August 2011) that the Branch managers had been instructed to get the valuation of land securities done from the Revenue Authority.

4.2.11 Monitoring of Advances

For an effective monitoring of advances, it is imperative for Banks to undertake a review of the advances portfolio on a regular basis. Credit Policy of the Bank stipulates that a close supervision and follow up of advances at the post disbursal stage is to be carried out with the aim of timely detection of warning signals and taking effective/preventive measures for avoiding possible slippage into Non-Performing Advances (NPA).

We noticed that the Bank's monitoring of the credit facilities had been inadequate in many areas as discussed in the succeeding paragraphs.

4.2.11.1 Working Capital (WC) Limit Accounts

Credit Policy of the Bank stipulates that all WC Limit accounts should be reviewed/renewed on a yearly basis. In case of low rated category/high risk category, six monthly time schedules for review of the Credit limits have to be followed.

Audit, however, observed that the Bank had not identified the accounts falling under high risk category required to be reviewed/renewed on six-monthly basis to avoid slippage to NPA. Besides, the Bank had not reviewed/renewed all the WC limit accounts, as laid in Credit Policy, and there was a shortfall in review/renewal of accounts to the extent of 1291 and 3918 accounts ranging between four and 7.51 *per cent* (up to 13.44 *per cent* at Zonal Offices level) during the years 2006-11. The following table indicates the position of WC accounts reviewed/renewed during 2006-11.

(in numbers)

S. No.	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
A	Total number of accounts (WC) targeted	32267	42175	46547	53426	57736
B	Number of accounts reviewed/renewed	30976	39009	43108	49965	53818
C	Number of accounts not renewed/reviewed	1291	3166	3439	3461	3918
	Percentage of non renewal/review	4.00	7.51	7.39	6.48	6.79
D	Age-wise analysis					
	(i). Up to 3 months	1146	2781	3045	2950	3441
	(ii). 3-6 months	115	353	211	227	441
	(iii). 6 months & above	30	32	183	284	36

[*] Kashmir Central: 18, Jammu Central: 16, Mumbai: 10, Bangalore: 13 and Delhi: 14.

Age-wise analysis of accounts revealed that a large number of accounts ranging between 1146 in 2006-07 to 3441 in 2010-11 had remained un-reviewed/un-renewed for periods up to three months and 145 to 511 accounts for more than three months during the same period, which was in contravention of the Credit Policy of the Bank enhancing the chances of slippage to NPA.

The Management stated (June 2011) that non-availability of financial statements and other data from the borrower resulted in delay in renewal/review of the WC accounts. The reply is not convincing as it is the responsibility of the management to obtain the relevant data from the concerned borrowers and to ensure that all the WC limit accounts are renewed/reviewed in accordance with the Credit Policy of the Bank.

4.2.11.2 Stock Audit

Stock audit is an effective post-disbursement tool for monitoring advances and ensuring end use of funds. It helps in assessing the value of security correctly and enhances the reliability of stock valuation. Credit Policy of the Bank stipulates that annual stock audit (including book debts) should be conducted in all cases of fund based credit limit of ₹ one crore and above and also in such cases which are recommended (by CHQ (A&AP[*])/Zonal Head) where the limit is below ₹ one crore. The Policy further stipulates obligatory annual stock audit in all cases of high risk[†] accounts having credit limit of ₹ 50.00 lakh and above.

The following significant points were noticed in audit.

- The Bank had not identified the high risk accounts involving ₹ 50 lakh and above for conducting annual stock audit during 2006-11.
- No account with credit limit below ₹ one crore had been recommended by the CHQ (A&AP)/Zonal Heads for the stock audit during the audit period.
- A significant number of accounts falling under the category of ₹ one crore and above, which qualified for annual stock audit, had not been audited during 2006-11 with shortfalls ranging between 10.45 per *cent* and 21.67 *per cent*

The Management attributed (June 2011) the reasons for shortfall to a) accounts turned NPA, b) most of the accounts being under Consortium, c) failure of the Chartered Accountants (Auditors) to take up the audit and d) adjustment/settlement of accounts. Audit, however, observed that the major shortfall (nearly 50 *per cent*) was due to failure of the Auditors to take up the audit and it was the responsibility of the Bank to ensure that the Auditors completed the Stock Audit within the stipulated time. Besides, the Bank should have conducted the stock audit of NPA accounts as the unit continues to hold

[*] Corporate Head Quarters (Advances and Assets Planning Department)
[†] Risk Grade-V and above

stock even after the account is declared NPA. Non-conducting of Stock Audit enhances the chances of slippage to NPA which, otherwise, could be avoided.

4.2.11.3 Credit Audit

Credit Audit is an effective tool for constantly evaluating the quality and risk of loan portfolio of the Bank to bring about qualitative improvement in credit administration through overall financial health assessment of the borrower entities with the aim to pick up early warning signals and suggest remedial measures. Credit Policy of the Bank and further directions (December 2007) of the Audit Committee of the Board stipulate that all borrower accounts having total exposure of ₹ one crore and above be subject to credit audit annually.

Table below indicates the shortfall ranging between 6.84 *per cent* and 44.79 *per cent* in conducting the Credit Audit by the Bank during 2007-11:

(*in numbers*)

Year	Targets/planned	Actually conducted	Shortfall	Percentage of shortfall
2007-08	259	143	116	44.79
2008-09	643	514	129	20.06
2009-10	760	708	52	6.84
2010-11	956	794	162	16.95

Further, it was seen that 773 observations relating to deficiencies in documentation and securities, infirmities in insurance cover, arrears in installments/interest, unauthorized Temporary Overdraft (TODs), pending valuation of properties, inspection of unit/properties, etc. had remained un-rectified as of 30 June 2011, indicating that the Bank had no mechanism in place to ensure rectification of the irregularities immediately after reporting.

The Management stated (September.2011) that the Bank had a mechanism in place to ensure conducting of credit audit/rectification of irregularities immediately after reporting. The fact, however, remains that huge observations continued to remain un-attended as of 30 June 2011, periodicity of which could not be ascertained, as the Bank had not done age-wise analysis of un-rectified irregularities.

4.2.12. Restructured/Re-schedulement of loan accounts

In case a borrower faces difficulties in meeting his repayment obligations due to certain internal and external factors, the Bank restructures the account, in accordance with the guidelines issued by RBI from time to time. Restructuring proposals have to be considered after assessing viability of the units and ascertaining certainty of repayment.

The position of restructured /rescheduled loan accounts and amount sacrificed during the last three years ending 2010-11 is tabulated below.

(Amount: ₹ in crore)

Category of advance	Particulars	Year			Total
		2008-09	**2009-10**	**2010-11**	
Standard	No of borrowers	7075	119	2357	**9551**
	Amount involved	574.31	615.59	648.46	**1838.36**
	Amount Sacrificed(diminution in value)	16.60	25.41	17.25	**59.26**
Sub-standard	No of borrowers	240	6	-	**246**
	Amount involved	26.85	0.25	-	**27.10**
	Amount Sacrificed(diminution in value)	0.49	0.01	-	**0.50**
Doubtful	No of borrowers	1	2	-	**3**
	Amount involved	6.00	0.06	-	**6.06**
	Amount Sacrificed(diminution in value)	0.44	0.001	-	**0.44**
Total	**No of borrowers**	**7316**	**127**	**2357**	**9800**
	Amount involved	**607.16**	**615.90**	**648.46**	**1871.52**
	Amount Sacrificed (diminution in value)	**17.53**	**25.42**	**17.25**	**60.20**

Audit noticed that of the 9800 restructured/rescheduled accounts during 2008-11 on which an amount of ₹ 60.20 crore had been sacrificed, 82 accounts (sacrificed amount: ₹ 1.38 crore) had turned NPA.

Since the restructuring was to be considered after assessing viability of the units and ascertaining certainty of repayment, turning of 82 accounts as NPA is indicative of the fact that the Bank had not assessed the viability of the units correctly and also that the certainty of the repayment had not been ensured.

The Management stated (August 2011) that unforeseen circumstances and unprecedented unrest during 2008-09 till 2010-11 had an impact on the earning of the borrowers accounts which otherwise were considered as viable unit. Under these circumstances the RBI had permitted the Banks for taking up the restructure for second and more times. The reply is not convincing as the guidelines stipulate that only such accounts are to be rescheduled where the repayment is certain. Turning of accounts as NPA, after restructure, defeated the purpose of restructuring the accounts. Besides, the Bank had not restructured these accounts the second time.

4.2.13 Non-Performing Assets

4.2.13.1 The Bank is exposed to credit and operational risks in credit/loan portfolio and, as such, is required to classify the advance as per Income Recognition and Assets Classification norms formulated by the RBI. An asset which ceases to generate income for the Bank becomes a Non-Performing Asset (NPA).

Table below indicates the movement of gross NPA of the Bank during the years from 2006-07 to 2010-11

(₹ in crore)

S. No.	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11	Total
1.	Total advances at the end of each year	17388.20	19164.28	21219.71	23455.20	26659.22	
2.	NPA at the beginning of the year	370.18	501.83	485.23	559.27	462.31	
3.	Additions during the year	273.57	227.93	401.89	188.78	289.15	1381.32
4.	**Total NPA during the year(2+3)**	**643.75**	**729.76**	**887.12**	**748.05**	**751.46**	
5	**Less**						
5a	Upgraded accounts	141.92*	42.39	103.67	127.78	44.61	318.45
5b	Actual recoveries made		132.55	151.94	126.58	113.57	666.56
5c	Written off		69.59	72.24	31.38	74.45	247.66
6.	**Total (5a+5b+5c)**	**141.92**	**244.53**	**327.85**	**285.74**	**232.63**	**1232.67**
7.	**NPA at the end of each year(4-6)**	**501.83**	**485.23**	**559.27**	**462.31**	**518.83**	
8.	Targets of recoveries of NPA	211.50	250.95	194.08	292.15	128.38	
9.	Percentage of targets of recoveries fixed to NPA at the beginning of each year(8/2X100)	57.13	50.00	40.00	52.24	27.77	
10.	Percentage of actual recovery to total NPA at the beginning of each year(5b/2X100)	38.34	26.41	31.31	22.63	24.57	
11.	Shortfall (Percentage) {(8-5b)/8x100}	32.89	47.18	21.71	56.66	11.54	
12.	Percentage of NPA to total gross advances(7/1X100)	2.89	2.53	2.64	1.97	1.95	

Audit analysis revealed the following:

- Total reduction of NPA of ₹ 1232.67 crore during 2006-11 comprised 54.08 *per cent* (₹ 666.56 crore) as actual recovery and the remaining 45.92 *per cent* was on account of up-gradation (₹ 318.45 crore/25.83 *per cent)* and write-off of NPA (₹ 247.66 crore/20.09 *per cent)*. The decrease of NPA from 2.89 *percent* in 2006-07 to 1.95 *percent* in 2010-11 was mainly due to writing off huge amount.

- Of ₹ 1381.32 crore NPAs added during 2006-11, ₹ 722.13 crore (52.28 *per cent*) came from three zones viz. 336.95 crore (24.39 *per cent*/Kashmir-Central), ₹ 205.49 crore (14.88 *per cent*/Delhi Zone) and ₹ 179.69 crore (13.01 *per cent*/Jammu-Central) which were considerably very high. Besides, the *percentage* of NPA to total advances was as high as 7.58 *per cent* (Mohali Zone/2010-11), 6.15 *per cent* (Bangalore Zone/2006-07), and 5.77 *per cent* (Kashmir-North/2007-08), indicating the failure of the Bank to effectively check the slippage of advances to NPA. The Management attributed (September 2011) the slippage of advances to NPA mainly to increase in advance portfolio. The fact, however, remains that huge inter-zone disparities need to be analysed and remedial measures taken to check slippage to NPA.

Non-Performing Assets - Comparison

(Ending March/Per cent)

Banks	2008	2009	2010
Overall	2.3	2.3	2.39
Public Sector	2.2	2.0	2.19
Private Sector	2.3	2.4	2.32
J&K Bank	2.53	2.64	1.97

(Source: RBI)

- Despite having fixed low targets (ranging between 27.77 *per cent* and 57.13 *per cent* of total NPA) for recovery of NPA during 2006-11, the overall shortfall in recovery

* Taken as recoveries made during the year as bifurcation was not available

ranged between 11.54 and 56.66 *per cent*. Audit analysis revealed that shortfall in achievement of recovery targets of NPA at Zonal level remained as high as 63.75 *per cent* (Delhi/2006-07), 68.23 *per cent* (Bangalore/2007-08), 70.49 *per cent* (Bangalore/2008-09), 79.08 *per cent* (Mumbai/2009-10) and 94.90 per *cent* (Mumbai/2010-11). Non-achievement of targets is indicative of the fact that the Management had not taken effective steps towards the targeted recovery of NPAs. The Management, however, attributed (September 2011) the reasons of shortfall to general recession in the market at global level and non-conducive atmosphere in the valley. The reply is not acceptable as the shortfall had remained high even in zones outside the State.

4.2.13.2 Deficient appraisal/inadequate securities leading to write off the NPA

The Bank[*] sanctioned (June/October 2002) Cash Credit (CC) limit of ₹ two crore, term loan of ₹ 3.56 crore, Letter of Credit (LOC) of ₹ 4 crore and Bank Guarantee (BG) of ₹ 0.50 crore in favour of a Company[†] against the primary security of hypothecation of raw material, finished goods, book debts and first charge on Plant and Machinery valuing ₹ 13.25 crore, built-up shed valued at ₹ 1.35 crore and equitable mortgage of 2.70 acre land valued at ₹ 0.40 crore, besides collateral security of equitable mortgage of commercial-cum-residential building valued at ₹ one crore, land valued at ₹ 12 lakh and personal guarantee of all the directors of the Company.

In June 2004, the Bank accorded the sanction of fresh Term Loan facility of ₹ 1.10 crore and enhancement of existing CC limit to ₹ 3.50 crore, LOC to ₹ 20.00 crore, BG to ₹ one crore for setting up of a Palmoline/Palm oil refinery unit. The enhancement was granted against primary securities of the hypothecation of current assets, first charge on Plant and machinery, tool, equipments in addition to earlier primary and collateral securities.

After availing enhanced credit facilities the Company was irregular in repayment and the Bank classified the account as NPA on 31 December 2006 with an outstanding NPA balance of ₹ 24.41 crore. After taking over the securities under SARFAESI[‡] Act, 2002, the mortgaged properties were re-assessed at ₹ 15.37 crore in September 2007. The Bank had not been able to dispose off the property as of June 2011.

Audit observed that the Bank enhanced the credit facilities in June 2004 from ₹ 10.06 crore to ₹ 29.16 crore without taking adequate securities to safeguard its interest proportionate to the exposure. Further, appraisal made at the time of enhancing the limits indicated that the Company was running successfully and had well established network for its oil products in the States of Andhra Pradesh and Karnataka. However, within two years of enhancing the credit facilities, the account was declared NPA and the borrower got the unit declared as sick. This was indicative of the fact that the appraisal of the

[*] J.N. Road , Hyderabad Branch
[†] M/s Lohiya Vanaspati (P) Ltd.
[‡] The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act

proposal/valuation of the mortgaged properties had not been done correctly at the time of enhancement leading to a loss of ₹ 24.41 crore to the Bank which had been written off (May 2009).

The Management stated (July, 2011) that the value of Plant & Machinery depleted drastically to scrap and the value of land was badly affected because of Telengana issue in Andhra Pradesh. The reply is not convincing as the value of securities could not deplete to such an extent within two years of advancing credit facilities indicating that the appraisal/valuation of the mortgaged property was not done correctly.

4.2.13.3 Classification of NPA

As per norms formulated by the RBI, the banks are required to classify NPAs further into three categories viz: Sub-standard, Doubtful and Loss Assets. The position of category-wise NPAs during 2006-11 is tabulated below:

(₹ in crore)

Classification	2006-07		2007-08		2008-09		2009-10		2010-11	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
Sub-standard (percentage of total)	8152	185.62 (36.99)	1124	178.25 (36.74)	10427	248.37 (44.41)	6274	96.85 (20.95)	7242	104.72 (20.18)
Doubtful (percentage of total)	13427	269.32 (53.67)	14725	269.48 (55.53)	15732	266.18 (47.60)	16509	309.53 (66.95)	15038	320.61 (61.80)
Loss (percentage of total)	2530	46.89 (9.34)	3728	37.49 (7.73)	4380	44.71 (7.99)	4469	55.93 (12.10)	5768	93.50 (18.02)
Total	**24109**	**501.83**	**19577**	**485.22**	**30539**	**559.26**	**27252**	**462.31**	**28048**	**518.83**

The Bank had failed to effect recoveries in case of chronic NPA cases as a result the NPA under the loss assets category had increased from ₹ 46.89 crore (9.34 *per cent*) involving 2530 accounts during 2006-07 to ₹ 93.50 crore (18.02 *per cent*) involving 5768 accounts during 2010-11. Similarly, doubtful assets had increased from ₹ 269.32 crore (53.67 *per cent*) involving 13427 accounts to ₹ 320.61 crore (61.80 *per cent*) involving 15038 accounts during the same period.

The Management stated (September 2011) that increase in doubtful and loss category of NPAs was marginal as compared to increase in Advance portfolio. The Bank needs to strengthen the recovery mechanism.

4.2.13.4 Position of NPA cases under litigation

As of March 2011, out of 28,048 NPA accounts, 2349 cases (8.37 *per cent*) were under litigation. Age-wise analysis of the pendency of the litigation cases is depicted in the following table:

(₹ in crore)

Particulars	Suit filed cases		Decreed cases				Total Suit filed & Decreed cases	
			Cases where decree not executed		Cases where decree executed but realisation pending			
	Number	Amount	Number	Amount	Number	Amount	Number	Amount
Below 1 year	211	88.49	76	2.64	120	54.66	407	145.79
1-5 years	857	140.40	191	6.54	196	40.78	1244	187.72
5-10 years	279	114.60	28	0.48	121	36.56	428	151.64
10 years and above	190	61.57	26	0.59	54	3.27	270	65.43
Total	**1537**	**405.06**	**321**	**10.25**	**491**	**135.27**	**2349**	**550.58***[*]**

Audit noticed that despite lapse of considerable time, the Bank had failed to effect recovery or dispose off the assets of the borrowers in 812 cases involving ₹ 145.52 crore, decreed in favour of the Bank as of March 2011. The figures included 229 cases (₹ 40.90 crore) where the decision had been pronounced five to over 10 years back**.**

The Management attributed (September 2011) the delay to changing of residence by the borrowers and new addresses were not traceable, stay against proceeding under J&K Stay of Proceedings (Migrants) Act, 1997 and complications in application of SARFAESI Act, 2002 in the State of Jammu and Kashmir.

4.2.13.5 Non-execution of decree led to Doubtful recovery of dues.

The Bank, assessing the financial position as quite satisfactory and the net worth strong, sanctioned (December 2000) credit facility (under Multiple Banking arrangement) by way of financial restructuring (augmenting working capital) of ₹ 10 crore in favour of a Company[†] for expansion of its production capacity. The facility was secured against *pari-passu*[‡] first charge on entire fixed assets of the Company.

The Bangalore branch of the Bank disbursed (January 2001) ₹ 10 crore to the Company. The Company right from the beginning was irregular in servicing the interest and the account eventually turned NPA in March 2004 with an outstanding NPA balance of ₹ 9.15 crore. The Bank restructured (June 2005) the facility under Corporate Debt Restructuring (CDR) package along with other lenders where the same was to be repaid in seven years, commencing from 2008-09. The CDR package failed in February 2008 as the Company did not continue its operations and filed a document in Bureau of Industrial and Financial Reconstruction (BIFR) for declaring the unit as sick. The Bank filed (October 2008) a recovery suit for ₹ 19.48 crore in Debt Recovery Tribunal, Bangalore, which was decreed (November 2009) in favour of the Bank, execution of the decree had been pending (July 2011).

* This is inclusive of interest component.
† M/S BPL Engineering Ltd.
‡ In proportion to

Audit observed that the Bank had failed to correctly assess the viability of expansion programme of the Company for which the working capital was released and also to ensure proper monitoring of the end use of the facility as the funds had been diverted by the company towards other sister concerns which consequently led to account turning NPA. Moreover, the value of the assets had not been ascertained by the Bank before releasing the facility and no documentation of the securities was done proportionate to the amount of advance which was in contravention of the terms and conditions of the sanction**.** Bank had also failed to take appropriate action against the Company by way of taking over securities and also to execute the decree which had resulted in non-recovery of outstanding amount of ₹ 28.95 crore (Principal: ₹ 9.15 crore and unapplied interest: ₹ 19.80 crore) for more than seven years (as of June 2011). The chances of recovery are bleak as the Bank had classified the NPA as loss.

The Management replied (July 2011) that all the other lenders of the Company had proceeded against the company under SARFAESI Act, 2002 and possession of the mortgaged property (Hyderabad unit) had been taken over by IDBI[*] on behalf of the lender Banks.

The reply is not convincing as taking over the mortgaged property by the IDBI does not guarantee that the Bank (J&K Bank) would get its share in full as documentation of the securities had not been done proportionate to the amount of advance before releasing the facility.

4.2.14 Consortium Advances

4.2.14.1 Credit Policy authorizes the Bank to make advances under Consortium arrangements to share credit risk, stipulating that in addition to the appraisal made by the leader bank, the Bank should also make an independent appraisal regarding viability of the project. The Bank might consider opting out from the consortium, where it is not satisfied with the financial/operational performance of the borrower.

The Bank had made advances to the tune of ₹ 7359.66 crore (101 loan cases) during 2006-11 to Corporate houses/Companies under the Consortium arrangements where the Projects were financed by a number of Financial Institutions with one financial institution acting as a leader. The outstanding advances under Consortium stood at ₹ 5763.77 crore (145 cases) as at the end of March 2011.

The following points were noticed.

- NPA under Consortium advances amounted to ₹ 141.72 crore as on 31 March 2011 which constituted 2.46 *per cent* of the total advances under consortium as against the overall NPA of 1.95 *per cent.*

[*] Industrial Development Bank of India

- Slippage of ₹ 106.05 crore into NPA during 2006-11 resulted in increase in NPA by 44 *per cent* as of March 2011 as compared to 2006 level.
- The recovery of NPA during 2006-11 ranged between zero and 12.14 *per cent* indicating that the position of recovery of NPA under Consortium Advances was not satisfactory.
- Out of total reduction of ₹ 65.80 crore in NPA under consortium during 2006-11, ₹ 30.46 crore (46.29 *per cent*) had been by way of write off.
- It was seen that the Bank, in contravention of its Credit Policy, largely depended on the appraisals made by the leader Bank and had not made any independent appraisal of the financial strength of the borrower. Further, it had also not revalued the securities to safeguard its interests where it was not satisfied with the performance of the borrower, as a result the Bank had to write off considerable amount leading to loss to the Bank.

The cases noticed in the performance audit are discussed below.

4.2.14.2 In December 2004, a credit facility of ₹ 755 crore (₹ 395 crore as Term Loan (TL), Bank Guarantee (BG) ₹ 240 crore and Cash credit ₹ 120 crore) was sanctioned in favour of a Company[*] by a consortium of 12 Banks with State Bank of India as Leader Bank. The Bank (Worli Mumbai-Branch) also participated and sanctioned (December 2005) ₹ 41.50 crore (TL: ₹ 36.50 crore and BG: ₹ 5.00 crore). However, the Company availed only ₹ 34.66 crore up to 17 September 2005. The TL was disbursed against the security of first charge on all present and future assets of the Company including personal guarantee of two Indian Promoter Directors and NRI[†] director having combined net worth of ₹ 25 crore.

From the very beginning the Company did not run well and incurred losses due to failure in arranging key resources for smooth running of the plant. The Company defaulted in repayment of loan and finally the account was declared as NPA (December 2007), within two and a half years of disbursement of loan, with NPA balance ₹ 33.20 crore. Later, the consortium arranged (November 2008) the CDR[‡] but the Company failed to arrange the equity and the CDR could not be finalized. Thereafter, the Bank approved (March 2010) ₹ 24.90 crore as full and final settlement of the NPA under OTS, thereby, sacrificing ₹ 8.30 crore being Principal amount and ₹ 11.09 crore un-applied interest. The borrower had not deposited the settlement amount so far (August 2011)

Audit observed that the Bank had sanctioned the facility on the assumption that the Project was reasonable and satisfactory and was expected to meet its debt servicing obligations towards the project and overall financial liquidity and profitability

[*] GPT Steel Industries Limited incorporated in December 2003 to manufacture Cold Rolled and Tinplate products in Gujarat.

[†] Non-Resident Indian

[‡] Corporate Debt Restructuring

parameters. Moreover, the Bank did not conduct appraisal independently before lending huge money, in contravention of Bank's Credit Policy. The Bank also had not assessed the value of the Assets of the Company before advancing the credit facilities as it had first charge on all assets (present and future) of the Company and should have got the valuation of the assets done to safeguard the interest of the Bank. Non-conducting the appraisal and non-assessing the value of mortgaged securities led to non-recovery of ₹ 44.29 crore.

The Management stated (August 2011) that SBI as a leader Bank was working out a negotiated settlement package for entire credit facilities on behalf of all lenders including J&K Bank. The fact remains that in any case the Bank would not get the entire recoverable amount and was bound to suffer loss.

4.2.15 One Time Settlement

4.2.15.1 To eliminate or reduce NPA, Banks have the option of settling the accounts through compromises/negotiated settlements or resorting to legal action. The recovery through negotiated settlements is preferred in view of the advantage of recovering maximum dues in less time with minimum expenses.

The Bank had formulated (2004) a policy /guidelines for recovery of NPA by way of compromise/negotiated settlement and write off under the guidelines of the RBI for reducing its NPA level. The policy was required to be revised periodically in the light of the instructions issued by the RBI from time to time. The Bank submitted (October 2006) a draft revised policy to the Board which was, however, not approved as the Board desired some changes regarding marketability of securities. It was noticed in audit that recast policy as desired by the Board had not been submitted to it for approval (September 2011).

The Bank, following the unrevised policy/guidelines (2004) read with guidelines of RBI issued from time to time, settled 6073 NPA cases during 2006-11 under "One Time Settlement" (OTS) Scheme through compromise/negotiated settlements where the chances of recovery were remote.

The position of cases settled under OTS, recovery effected and amount waived off (Principal and Interest) during 2006-11 is indicated in the table below:

(₹ in crore)

Year	No. of cases settled	Balance Outstanding		Settlement Amount		Amount waived off/sacrificed		Total waiver
		NPA	Un-applied interest	NPA	Un-applied interest	NPA	Un-applied interest	
2006-07	716	53.82	32.19	47.14	5.99	6.68	26.20	32.88
2007-08	966	40.30	18.36	39.22	3.87	1.08	14.48	15.56
2008-09	1021	29.00	24.60	27.11	2.46	1.89	22.14	24.03
2009-10	1765	134.08	68.80	114.42	2.66	19.67	66.15	85.82
2010-11	1605	46.60	23.10	42.57	4.59	4.03	18.50	22.53
Total	**6073**	**303.80**	**167.05**	**270.46**	**19.57**	**33.35**	**147.47**	**180.82**

An analysis of the data reveals the following.

- The settlement under OTS had resulted in sacrifice of Principal amount of ₹ 33.35 crore and interest of ₹ 147.47 crore.
- Zone-wise analysis revealed waiver to the extent of ₹ 63.85 crore (35.31 *per cent* of total waiver of ₹ 180.82 crore*)* in Mumbai, ₹ 43.02 crore (23.79 *per cent*) in Kashmir-Central, which is comparatively on higher side. Similarly, at the division level, waiver under OTS had been of the order of 58.58 *per cent* in the Zones outside the State and 29.51 *per cent* in Kashmir Division.

Further, it was seen that out of the total reduction of NPA amount of ₹ 1232.67 crore during 2006-11(*indicated in paragraph 4.2.13.1*), ₹ 303.80 crore (24.65 *per cent*) was settled under OTS Scheme by waiving off ₹ 180.82 crore (Principal: ₹ 33.35 crore and Un-applied Interest ₹ 147.47 crore).

Zone-wise analysis revealed that 46.51 *per cent* of the total reduction of NPA (2006-11) had been made through OTS Scheme in Mumbai, 33 *per cent* in Mohali, 35.32 *per cent* in Kashmir (Central), 23.49 *per cent* in Delhi and 20.95 *per cent* in Bangalore Zones. This is indicative of the fact that the reduction in NPA was mainly through settlement under OTS rather than recovery of NPA through normal course.

The Management stated (August 2011) that since the recovery through negotiated settlement involves less time with minimum expenses, it has proved to be effective tool to reduce NPA level, thereby, making option of recycling of funds possible. It further stated that on an average the settlements were made in NPA accounts with age of three years and above and had recovered around 90 *per cent* of NPA balances through settlement under OTS during last five years.

The reply is not convincing as the purpose of holding the securities (primarily 1.25 times of loan amount as per Credit Policy besides collateral securities) at the time of sanctioning the loan is defeated when the cases are preferably settled under OTS without taking over/realization of securities in NPA cases.

4.2.15.2 The guidelines for negotiated settlement of NPA cases (OTS) formulated (2004) by the Bank, read with the RBI directives issued from time to time, provide for settlement of only chronic NPAs emphasizing 100 *per cent* recovery of the NPA balance leaving no space to cover cases of wilful default, fraud and malfeasance. Audit, however, noticed that in most of the test-checked cases the settlement under OTS was made in cases which were not chronic in nature and where the borrowers were wilful defaulters. Besides, principal amount was also sacrificed contrary to the prescribed guidelines. Following are some interesting cases noticed in audit:-

4.2.15.3 The Bank[*] sanctioned (September 1997) a term loan (TL) of ₹ 5.18 crore and Cash Credit of ₹ 1.40 crore to a Company[†] for setting unit of spinning raw cotton yarn and meeting its working capital requirements, enhanced from time to time, last enhanced in October 2008. All the credit facilities were primarily secured by hypothecation of Plant and Machinery (valuing ₹ 3.13 crore), raw materials, semi finished and finished stocks and book debts and collateral security of five plots (valuing ₹ 3.34 crore), besides, personal guarantee of directors of the Company. The Bank sanctioned (July 2003) additional TL of ₹ 13.50 lakh for installation of one more Diesel Generator Set.

The Company failed to adhere to the repayment schedule. On request of the promoter, the Bank rescheduled (March/October 2005) the repayment. The Company could not manage to run the factory even after sanctioning (July/October 2005) of an additional *adhoc* cash credit facility of ₹ 25 lakh and reduction (July 2007) of interest rate from 13 to 10 *per cent*.

Despite all the concessions, the Company continued to default in its repayment schedule suggesting that the default was willful. Finally, the account was termed as NPA in June 2009 (within eight months of enhancing the limits in October 2008) with NPA balance of ₹ 4.05 crore. The Bank settled (September 2010) the loan case at ₹ three crore under OTS within 15 months of turning the accounts as NPA violating the prescribed guidelines ibid.

Audit observed that Bank failed to recover the outstanding amount from the defaulting Company by invoking the primary as well as collateral securities clauses of the sanction. Instead, the Bank settled the account under OTS sacrificing principal amount of ₹ 1.05 crore and un-applied interest of ₹ 0.24 crore which was in contravention of the settlement guidelines of the OTS Scheme, resulting in loss to the Bank to the tune of ₹ 1.29 crore.

The Management stated (August 2011) that settlement was made in line with the general policy guidelines of the Bank for compromise/negotiation under OTS. The reply is not acceptable as the case had been settled in contravention of the guidelines of the scheme.

4.2.15.4 The Bank[‡] sanctioned (March 2005) a term loan of ₹ 45 crore in favour of M/s Hassan Sons for acquisition of land measuring 940 *kanals* and development of housing colony at Zakura, Naseem Bagh, Srinagar against the primary security of hypothecation of all materials and machinery at site, collateral security of land valued not less than ₹ 50 crore and personal guarantee of all the partners of the firm. The loan was to be repaid completely during 2008-09.

However, the loan could not be disbursed in favour of the borrower as the firm did not have a clear title over the land offered as a collateral security and the sanction lapsed.

[*] Badohi (Uttar Pradesh) Branch
[†] M/S MAMB Private Ltd
[‡] Air Cargo Branch, Srinagar

The Bank subsequently revalidated the sanction (November 2005) and accepted another land valuing ₹ 33 crore. The Bank released (December 2005) an amount of ₹ 45 crore.

Audit observed that despite lapse of two and half years the borrower neither executed the project nor repaid the loan suggesting that the borrower was a willful defaulter. On turning the account irregular, the Bank classified (June 2008) the account as NPA with outstanding balance of ₹ 45.92 crore. Within one year of turning the account as NPA, the Bank settled (May 2009) the NPA account under OTS for an amount of ₹ 43.50 crore in contravention of the prescribed guidelines, thereby, sacrificing ₹ 2.42 crore principal amount and ₹ 16.99 crore un-applied interest. Besides, the Bank had not taken over/realized the collateral security and instead settled the case under OTS.

The Management stated (August, 2011) that the case had been settled under Bank's compromise/remission scheme considering all aspects of the case. The reply is not tenable as the settlement under OTS scheme was preferred against taking over the mortgaged securities having ignored the interests of the Bank to the extent of ₹ 19.41 crore (NPA balance: ₹ 2.42 crore and unapplied interest: ₹ 16.99 crore) besides, violating the prescribed guidelines of the OTS Scheme.

4.2.15.5 The Bank [*] advanced (April 1987) cash credit facility of ₹ 10 lakh in favour of M/s Wani Carpets for manufacturing, export/local sale of carpets. The facility was enhanced from time to time, last renewed in August 2006, to the extent of ₹ 4.45 crore for a period of one year (CC ₹ 0.90 crore, PCL[†] ₹ 0.90 crore, WCTL ₹ 1.60 crore and PSL[‡] ₹ 1.05 crore), against the primary security of hypothecation of stocks, book debts, ECGC[§] cover, title of goods and proceeds of export bill etc. and collateral security of mortgage of house property valued at ₹ three crore and third party guarantee of two persons with net worth of ₹ 3.63 crore.

The account holder defaulted in repayment within seven months of availing enhanced facility indicating that the borrower was a wilful defaulter. The Bank declared the account as NPA on March 2007 with an outstanding NPA balance of ₹ 3.84 crore.

We noticed that the Bank decided (August 2009) to file a Civil Suit for recovery against the party, but on the recommendation of the branch (September 2009) it settled (February 2010) the account under OTS scheme for an amount of ₹ two crore sacrificing ₹ 2.75 crore (Principal ₹ 0.83 crore and Un-applied interest ₹ 1.92 crore) after adjusting ECGC claim of ₹ 1.01 crore. Settlement of case under OTS was in contravention of OTS guidelines being a case of wilful default, which resulted in loss to the Bank to the tune of ₹ 2.75 crore. Further, the Bank had not invoked personal guarantees obtained at the time of sanctioning the limits.

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[*] International Banking Division Zonal Office Srinagar branch

[†] Packing/Pre-Shipment Credit Limit

[‡] Post Shipment Credit Limit

[§] Export Credit and Guarantee Corporation

The Management stated (July 2011) that one time settlement was approved keeping in mind all aspects of cost involved in legal course and the account was fully provided for and it had no impact on the profitability of the Bank. The reply is not convincing because the provisions are made out of the profits of the Bank and any adjustment made there against tantamounts to loss. Moreover, the settlement made was in contravention of OTS.

4.2.15.6 Contrary to the policy of the Bank of not considering the cases of Flour Mills, the Bank* sanctioned (January 1999), as a special case, term loan of ₹ 69.70 lakh and a cash credit facility of ₹ 41 lakh in favour of M/s Shree Vaishno Flour mills Ltd. for establishment and running of flour mills at Jammu. The CC limit was reviewed/enhanced from time to time, last in September 2006 to the extent of ₹ 150 lakh. The entire loan was secured against primary securities of land and building, Plant & Machinery and other assets having realizable value of ₹ 107.08 lakh, hypothecation of stocks and Collateral securities having realizable value of ₹ 146.86 lakh, besides, personal guarantee of four persons.

The borrower adjusted (February 2007) the term loan but defaulted in repayment of the enhanced cash credit limit of ₹ 150 lakh. Audit observed that immediately after availing the enhanced limit, the borrower willfully defaulted the repayment and the Bank declared the account as NPA on 30 September 2007 i.e. within one year of the date of last enhancement of CC limit. Despite being a wilful defaulter, the Bank approved (February 2008) i.e. within 5 months of declaring the account as NPA, the settlement under OTS at an amount of ₹ 152.66 lakh (principal only) which, however, did not mature. Later on, the Bank settled (November 2008) the account at an amount of ₹ 110 lakh, thereby, sacrificing ₹ 42.66 lakh Principal amount and ₹ 35.24 lakh un-applied interest resulting in loss to the Bank to the tune of `₹ 77.90 lakh which was in contravention of the guidelines of OTS Scheme.

4.2.16. Assignment of rights to Assets Reconstruction Companies

4.2.16.1 The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) provides for acquisition by any reconstruction company of any right or interest of any bank and financial institution in any financial assistance for the purpose of realization of such financial assistance.

The Board of Directors (BOD) of the Bank desired (November 2007) that the Bank should explore the possibility of selling a portion of its NPAs to Assets Reconstruction Company (ies) (ARC) as an additional measure. During 2006-11, the Bank had assigned the rights to Asset Reconstruction Companies to sell only two NPA cases.

4.2.16.2 A Company†, dealing in manufacture of steel bars, had been availing working capital facility from the SBI and secured overdraft from SCB* . The Bank†, in

* I/C Bari-Brahmna Branch, Jammu
† M/S Golden Rathi Star Industries Ltd., New Delhi

view of satisfactory performance and expansion programme of the Company, took over (August 2007) all the credit facilities availed by the Company and sanctioned (August 2007) Cash Credit facility of ₹ 25 crore. The Credit facility was secured against the primary security of first charge on current assets, hypothecation of stocks and book debts, besides, collateral securities of equitable mortgage of factory Land (valuing ₹ 34.59 crore), Building (₹ 1.11 crore), Plant/Machinery (₹ 15.77 crore), residential property (₹ 6.03 crore), Personal Guarantee of all the Directors and third party guarantee of shareholders. In addition, the Bank sanctioned (June 2008) *adhoc* credit facility of ₹ two crore.

Consequent upon the non-servicing of the interest the account was declared NPA in September 2008 with an outstanding NPA balance of ₹ 27 crore. Due to some family dispute and death of one of the Directors (October 2008), the activities of the Company came to a halt. The Bank took over (July 2009) the possession of mortgaged properties including land under SARFEASI Act, 2002 and the revaluation done (July 2009) placed the market value of the land at ₹ 19.44 crore only as against ₹ 34.59 crore valued at the time of sanction of credit facility.

Audit observed that the valuation of the land had not been done through Revenue Authorities as laid down in the Credit Policy and instead was got done by the approved valuer, which was overvalued (July 2009) to the extent of ₹ 15.15 crore. The Bank, sensing that it was not in a position to recover the entire outstanding balance due to overvaluation of land, assigned (January 2011) its rights to M/S Invent Asset and Reconstruction Company, Mumbai and recovered (January 2011) ₹ 25.51 crore thereby, losing an amount of ₹ 10.05 crore (Principal: ₹ 1.49 crore, un-applied Interest ₹ 8.09 crore, SARFAESI Expenses: ₹ 0.29 crore and Enforcement Agency BWFL ₹ 0.18 crore).

The Management stated (May 2011) that the valuation of the properties was got carried out by the approved valuer of the Bank which got decreased probably due to unfortunate death of a partner and subsequent closure of the unit. The reply is not convincing in view of the fact that the closure of the unit might affect the value of the Plant/Machinery/Building but not the value of land as had happened in this case.

4.2.17 Priority Sector Lending

4.2.17.1 National Credit Council emphasized (July 1968) that Commercial Banks should increase their investment in financing of priority sector. Only those sectors were included as part of the priority sector, that impact large sections of the population, weaker sections and sectors which were employment intensive such as Agriculture and Micro and Small Enterprises.

* Standard Chartered Bank

† Branch at Vikas Marg New Delhi

Initially targets for Priority Sector Lending were not fixed. However, presently all Commercial Banks are advised by the RBI to lend under priority sector at 40 *per cent* of Adjusted Net Bank Credit (ANBC) on the rate of interest as determined from time to time. Accordingly, the Banks are required to take effective steps to achieve the recommended targets and monitor the priority sector lending from quantitative and qualitative aspects.

On the basis of the guidelines and recommendations of the RBI, the Bank made Advances under Priority Sector, but not to the extent of targets fixed. Table below indicates the shortfall in lending under Priority Sector by the Bank during the period 2006-11.

(₹ in crore)

S. No	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
1.	**ANBC[*] for determination of Priority Sector Lending**	**14854.91**	**14897.41**	**16756.16**	**18412.05**	**20082.88**
2.	Percentage of Targets fixed by the RBI/Bank for Priority Sector Lending of ANBC	40	40	40	40	40
	(i)Agriculture and allied Sector	18	18	18	18	18
	(ii) Micro & Small and other Enterprises	22	22	22	22	22
3.	Priority Sector Advance required to be made vis-à-vis ANBC/**Targets**					
	(i)Agriculture and allied Sector	2673.88	2681.53	3016.11	3314.16	3614.91
	(ii)Micro & Small and other Enterprises.	3268.08	3277.43	3686.35	4050.66	4418.24
	Total Targets	**5941.96**	**5958.96**	**6702.46**	**7364.82**	**8033.15**
4.	**Achievement**					
	a) Agriculture and Allied Sector					
	(i) Direct[†]	401.08	491.30	1154.74	1484.77	1619.31
	(ii) Indirect[‡]	295.80	335.78	747.23	809.21	1302.27
	Total Agriculture Sector	**696.88**	**827.08**	**1901.97**	**2293.98**	**2921.58**
	b) Micro & Small and Other Enterprises	2918.03	4681.69	5512.75	6025.15	7556.33
	(i). Direct	[§]NA	NA	NA	NA	NA
	(ii). Indirect	NA	NA	NA	NA	NA
	Total Other sectors	**2918.03**	**4681.69**	**5512.75**	**6025.15**	**7556.33**
	Total Achievements	**3614.91**	**5508.77**	**7414.72**	**8319.13**	**10477.91**
5.	**Shortfall (3-4)**					
	(i) Agriculture and allied Sector (percentage)	1977.00 (73.94)	1854.45 (69.16)	1114.14 (36.94)	1020.18 (30.78)	693.33 (19.18)
	(ii) Micro & Small and other Enterprises (percentage)	350.05 (10.71)	Nil	Nil	Nil	Nil

The following points were noticed.

- There was huge shortfall during 2006-11 in lending under Agriculture Sector (₹ 6659.10 crore), ranging between ₹ 693.33 crore and ₹ 1977 crore (19.18 *per cent* to 73.94 *per cent*).
- Lending under Micro, Small and other Enterprises was in excess of the targets.
- Reasons for shortfall in achievement of targets in Agriculture Sector and excess lending in Micro, small and other Enterprises were not found on record. The Bank

[*] Previous Year's Gross advances less Provisions and Ways & Means Advance to State Government
[†] Advance made directly to the beneficiary
[‡] Advances made through financial institutions like Tata Motors, Kotak Mahindra, etc.
[§] Not available with the Bank

had not maintained data of Direct and Indirect lending under Micro & Small and other Enterprises.

As per RBI guidelines issued from time to time, Banks having shortfall in lending to Priority Sector target (40 *per cent* of ANBC) or Agriculture Sector target (18 *per cent* of ANBC) are required to contribute, to the extent shortfall occurs, to RIDF[*] on rate of interest, ranging between three to six *per cent*, as a penalty for non-achievement of Priority Sector lending targets. Consequent upon shortfall of targets in lending under Agriculture sector, the Bank had to invest an amount of ₹ 2862.74 crore[†] in RIDF, SIDBI[‡] and NABARD[§] for a period of three to seven years at an interest rate of three to six *per cent* per annum, which is lower than the average rate (ranging between nine *per cent* to 12.5 *per cent*) of lending under Priority Sector, leading to loss of interest to the tune of ₹ 334.49 crore[**].

The Management attributed (August 2011) the shortfall in Agriculture sector lending mainly to the prevailing turmoil. The reply is not convincing as in sectors other than Agriculture sector (Micro, Small and other Enterprises) the Bank had made advances far in excess of targets (2007-11) under the same conditions. The Bank, however, expressed hope to achieve the targets in Agriculture sector in future.

4.2.17.2 <u>Movement on NPA under Priority Sector Lending</u>

In Priority Sector Lending, the Bank had huge NPA. The table below indicates the movement of NPA of the Bank under Priority Sector Lending during 2006-11:

(₹ in core)

S. No	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
1.	NPA at the beginning of each year	180.99	214.37	225.12	263.39	267.36
2.	Additions during the year	33.38	10.75	38.27	3.97	45.08
3.	Total NPA	**214.37**	**225.12**	**263.39**	**267.36**	**312.44**
4	Less Total Recoveries	**Nil**	**Nil**	**Nil**	**Nil**	**Nil**
5	NPAs at the end of each year(3-4)	**214.37**	**225.12**	**263.39**	**267.36**	**312.44**
6.	Lending under Priority Sector (Gross)	**3614.91**	**5508.77**	**7414.72**	**8319.13**	**10477.91**
7	Percentage of NPA to Lending under Priority Sector (Gross) (5/6X100)	**5.93**	**4.08**	**3.55**	**3.21**	**2.98**
8.	Overall percentage of NPA of the Bank	2.89	2.53	2.64	1.97	1.95

The NPA under Priority Sector remained on higher side as compared to overall NPA of the Bank. The Bank had neither fixed any targets for recovery of NPA nor could make any recovery of NPA in any of the years under audit period resulting in increase of NPA from ₹ 180.99 crore in April 2006 to ₹ 312.44 crore ending March 2011. It was further observed that within the NPA, the Doubtful Assets increased from ₹ 109.47 crore to ₹ 198.60 crore (81.42 *per cent*) and Loss assets from ₹ 25.30 crore to ₹ 49.45 crore

[*] Rural Infrastructure Development Fund

[†] ₹ 43.87 crore in 2006-07, ₹ 243.54 crore in 2007-08, ₹ 801.92 crore in 2008-09, ₹ 586.11 crore in 2009-10 and ₹ 1187.30 crore in 2010-11

[‡] Small Scale Industrial Development Bank of India

[§] National Bank for Agriculture and Rural Development

[**] ₹ 12.81 crore in 2006-07, ₹ 66.68 crore in 2007-08, ₹ 154.37 crore in 2008-09, ₹ 56.25 crore in 2009-10 and ₹ 44.38 crore in 2010-11

(95.45 *per cent)* during the same period. The Bank had neither analyzed the reasons of increase in doubtful and loss assets nor had it taken any measures to settle/recover the chronic cases of NPA under Priority Sector Lending.

The Management stated (October, 2011) that constant pursuance, monitoring and follow-up had resulted in decline of NPA from 5.93 *per cent* to 2.98 *per cent* during 2006-11. The reply is not acceptable as there had been nil recovery on account of NPA during 2006-11 and NPA had increased from ₹ 214.37 crore in 2006-07 to ₹ 312.44 crore in 2010-11.

4.2.17.3 Tardy implementation of the Central/State Sponsored Schemes

The Bank is providing credit assistance to the beneficiaries through Centrally Sponsored Schemes viz. (i) SGSY* (ii) SJSRY† (iii) PMEGP‡ and JKSES§ - a State sponsored scheme under Priority Sector Lending. The main objective of these schemes is to (a) bring the assisted poor families (*Swarojgaris*) above the poverty line, (b) provide assistance to individual urban poor beneficiaries and provide gainful employment to unemployed and under-employed youth encouraging setting up of self-employment ventures, (c) generate employment opportunities in rural as well as urban areas through setting up of new self employment ventures/projects/micro enterprises etc. and (d) address unemployment problems in respect of all these schemes.

The position of targets, achievements and shortfall under Centre/State Sponsored schemes for the period 2006-11 are detailed in the following table.

(₹ in crore)

Particulars	2006-07	2007-08	2008-09	2009-10	2010-11
Targets					
SGSY	19.41	22.07	25.31	26.50	33.03
SJSRY	7.51	12.82	7.88	5.73	4.71
PMRY/PMEGP	22.39	21.96	8.48	69.81	75.17
JKSES	45.40	50.99	62.87	58.11	80.53
Total	**94.71**	**107.84**	**104.54**	**160.15**	**193.44**
Achievements					
SGSY	8.94	11.49	11.90	13.77	14.69
SJSRY	1.96	5.83	2.82	2.45	2.06
PMRY/PMEGP	13.46	20.11	1.33	37.66	45.80
JKSES	25.04	32.91	34.18	45.39	55.62
Total	**49.40**	**70.34**	**50.23**	**99.27**	**118.17**
Shortfall					
SGSY (Percentage)	10.47 (53.94)	10.58 (47.94)	13.41 (52.98)	12.73 (48.05)	18.34 (55.52)
SJSRY (Percentage)	5.55 (73.90)	6.99 (54.52)	5.06 (64.21)	3.28 (57.24)	2.65 (56.26)
PMRY/PMEGP (Percentage)	8.93 (39.88)	1.85 (8.42)	7.15 (84.31)	32.15 (46.05)	29.37 (39.07)
JKSES (Percentage)	20.36) (44.85)	18.08 (35.45)	28.69 (45.63)	12.72 (21.88)	24.91 (30.93)
Total	**45.31 (47.84)**	**37.50 (34.77)**	**54.31 (51.95)**	**60.88 (38.01)**	**75.27 (38.91)**

* *Swaran Jayanti Gram Swarozgar Yojana*

† *Swaran Jayanti Shahri Rozgar Yojana*

‡ Prime Minister Employment Generation Programme

§ Jammu and Kashmir Self Employment Scheme

Audit observed that these schemes were not implemented fully and there was huge shortfall in achievement of targets ranging between 8.42 *per cent* and 84.31 *per cent* during the years 2006-11, as a result of which the purpose of launching the schemes was defeated. Besides, the Bank had not framed any plan for implementing the schemes effectively.

The Management stated (August 2011) that 100 *per cent* achievement was not possible because of non-completion of requisites by the beneficiaries or sometimes the beneficiaries were not interested to establish their units due to personal reasons. The reply is not convincing as the Banks have a proactive role to play in the implementation of these scheme by way of involving themselves in the planning and preparation of projects, pre-sanction appraisal, etc. The Bank had, however, failed on this front leading to shortfall occurring as high as 84.31 *per cent* (2008-09/PMRY & PMEGP).

Audit further observed that percentage of NPA to the total amount advanced under these schemes ranged between 12.50 and 25.83 *per cent* during the years 2006-11 which was alarming when compared with overall NPA position of the Bank. The recovery of NPAs was nominal/nil during the audit period. The Bank had not classified NPAs into Sub-standard, Doubtful and Loss Assets though required under the guidelines of RBI.

The Management stated (August 2011) that efforts were on to make recoveries to the maximum.

4.2.17.4 Lead Bank Schemes (LBS)

The Lead Bank Scheme came (December 1969) into existence as per the directives of the RBI with objectives of improvement in branch expansion, deposit mobilization and lending to the priority sectors especially in rural/semi-urban areas. The scheme envisaged allotment of districts to banks to enable them to assume leadership in bringing about banking developments in the respective districts by (a) Surveying the resources and potential for banking development in the districts; (b) Surveying the number of industrial and commercial units and other establishments and farms which do not have banking accounts or depend mainly on money-lenders; (c) Surveying the facilities for stocking of fertilizers and other agricultural inputs and repairing and servicing of equipments; (d) Recruiting and training staff, for offering advice to small borrowers and farmers in the priority sectors and for follow up and inspection of end use of loans and (e) Assisting other primary lending agencies.

The functions of the scheme envisaged appointment of Lead District Managers (LDMs) by the Bank who shall be responsible for drawing up the road map for banking penetration, preparation of one time comprehensive Development Plan for the district, associate with the setting up of Financial Literacy and Credit Counseling Centers (FLCCS), setting up of Rural Self Employment Training Institutes (RSETIs), holding annual sensitization workshops for banks and government officials with participation by NGOs/PRIs, arranging for quarterly awareness, feedback public meetings, etc.

The Jammu and Kashmir Bank had been assigned (between 1969 and 2007) lead bank responsibility in respect of 12 districts out of the total 22 districts across the State. In audit it was observed that though the Bank had appointed Lead Bank Officers (LBOs) in all the 12 districts and had drawn the Annual Credit Plan, the LBOs had not discharged their duties to the extent that:

- FLCCCs and RSETI had not been set up in any of the districts,
- Annual sensitization workshops for Banks/Govt. officials and arrangements for quarterly awareness and feedback public meetings, redressal of grievances, etc. had not been held,
- Surveys with regard to potential for banking development, identify the industrial units which do not have banking accounts or depend on money lenders, examine the facilities for marketing and agriculture produce, stocking of fertilizers and other agricultural inputs, recruiting and training staff, etc. had not been conducted.

The Management stated (August 2011) that the Bank was in the process of implementation of the Lead Bank responsibilities. However, the fact remains that the approach of the Bank towards this vital activity had been lackadaisical.

4.2.18 Investments

4.2.18.1 With a view to provide a basic structure and framework for effective management of investment portfolio, the Bank had put in place Investment Policy to be reviewed from time to time (last reviewed in January 2011).

The Investment portfolio of the Bank comprised SLR[*] Investment (Government Securities) and Non-SLR Investments (Bond, Debentures etc.).

SLR is the percentage of Demand and Time maturities that Bank needs to have in the form of Cash, Gold and approved Government securities. Non-SLR securities on the other hand, comprise PSU Bonds, Corporate Debentures, Commercial papers (CP), Certificate of Deposits (CD) etc. The investment policy of the Bank prohibits investment under a particular sector beyond 25 *per cent* of the total non-SLR portfolio of investments.

Table below indicates the position of Investments (Gross), SLR and non-SLR during 2006-11: -

[*] Statutory Liquidity Ratio – 24 *per cent* of the Demand and Time Liabilities (DTL)

(₹ in crore)

Investments	2006-07	2007-08	2008-09	2009-10	2010-11
SLR					
1. Govt Securities	4524.32	5215.09	6483.53	8055.10	9539.07
2. Treasury Bills	1007.08	1721.69	1122.21	405.26	787.65
3. Trustee Securities	39.07	37.08	20.86	11.42	10.28
Total (A)	**5570.47**	**6973.86**	**7626.60**	**8471.78**	**10337.00**
Non-SLR					
1. Equity	52.79	49.84	58.10	65.89	288.72
2. Preference Shares	36.96	31.92	24.87	11.29	23.30
3. Bonds & Debentures(including suit filed)	962.67	956.16	1100.96	1423.84	1932.26
4. Mutual funds	122.50	117.00	92.00	185.00	18.30
5. RIDF, NABARD, SIDBI	258.90	436.74	1124.55	1545.05	2479.61
6. Commercial Paper (CP) / Certificate of Deposit (CD)	268.67	-	539.67	2037.27	4607.48
7. Security Receipts	-	-	-	-	3.24
8. Investment in Sponsored Institute*	9.82	9.82	22.11	22.11	22.11
9. Investment in Joint venture	132.50	220.27	220.27	220.27	-
10. Investment in Subsidiary†	-	-	5.00	5.00	5.00
11. Venture capital	-	-	-	5.00	10.00
Total (B)	**1844.81**	**1821.75**	**3187.53**	**5520.72**	**9390.02**
Grand Total (A+B)	**7415.28**	**8795.61**	**10814.13**	**13992.50**	**19727.02**
Year-Over-Year Growth (*per cent*)	-	**1380.33 (18.61)**	**2018.52 (22.95)**	**3178.37 (29.39)**	**5734.52 (40.98)**
Income					
SLR (*Per cent of income to investment*)	365.41 (6.56)	445.18 (6.38)	527.25 (6.91)	540.96 (6.39)	670.77 (6.49)
Non-SLR (*Per cent of income to investment*)	119.21 (6.46)	88.39 (4.85)	127.47 (4.00)	172.89 (3.13)	403.76 (4.30)

An analysis of the above table revealed the following:

- As on March 2011, total Investments (SLR and Non-SLR) stood at ₹ 19727.02 crore against ₹ 7415.28 crore as on March 2007, registering 166.03 *per cent* increase. Year-over-Year growth of investments increased from 18.61 *per cent* in 2007-08 to 40.98 *per cent* in 2010-11.
- SLR investments increased from ₹ 5570.47 crore in 2006-07 to ₹10337.00 crore in 2010-11, registering 85.57 *per cent* increase. The income generated from SLR investments ranged between 6.38‡ *per cent and* 6.91 *per cent* during the same period at an average annual return of 6.54 *per cent*.
- Non-SLR investment increased from ₹ 1844.81 crore in 2006-07 to ₹ 9390.02 crore in 2010-11 registering 409 *per cent* increase. The income generated ranged between 3.13 *per cent* and 6.46 *per cent* during the same period at an average annual return of 4.19 *per cent*, which was low as compared to income under SLR investments. Despite low return under Non-SLR portfolio, the Bank enhanced its investment under this portfolio.

* J&K Grameen Bank

† JKB Financial Services Ltd.

‡ All the percentage of income to investments are calculated on the basis of closing balances of investments at the end of each year.

- The Bank had invested ₹ 2037.27 crore during 2009-10 and ₹ 4607.48 crore during 2010-11 under Commerciasl papers (CP) and Certificate of deposit (CD) sectors of Non-SLR portfolio which accounted for 36.90 *per cent* and 49.07 *per cent* of total Non-SLR investments respectively as against the prescribed 25 *per cent* limit.

The Management stated (July 2011) that actual average returns on SLR & Non-SLR portfolio are 6.92 *per cent* and 6.46 *per cent* respectively calculated on the basis of average balances of investments maintained during each year and included the trading income, but low average yield on Non-SLR investments as compared to SLR portfolio was mainly due to Bank's investment in priority sector substitutes viz. RIDF, NABARD, SIDBI at low rate of interest.

Audit, however, observed that failure of the Bank to achieve the targets under Priority Sector Lending forced it to invest under RIDF (as discussed in paragraph 4.2.17.1).

4.2.18.2 Movement of Non-Performing Investments

Similar to NPA, Investments, where interest/installment (including maturity proceeds) remains unpaid/stagnant for more than 90 days, are termed as Non-Performing Investments (NPI).

The Bank had Non-Performing Investments (NPI) of ₹ 113.97 crore at the beginning of March 2006 which declined to ₹ 20.01 crore at the end of March 2011 and are under litigation. Table below indicates the movements of NPIs during the period from 2006-07 to 2010-11:-

(₹ in crore)

S. No.	Particulars	2006-07	2007-08	2008-09	2009-10	2010-11	Total
1.	Total NPIs at the beginning of each year	113.97	79.07	89.55	74.75	20.01	
2.	Additions during the year	Nil	15.48	5.15	Nil	Nil	**20.63**
3.	**Total NPIs (1+2)**	**113.97**	**94.55**	**94.70**	**74.75**	**20.01**	
4	NPIs written off	Nil	5.00	10.75	49.74	Nil	**65.49**
5.	Recovery made						
	a). In full	Nil	Nil	0.15	5.00	Nil	**5.15**
	b).Byway of settlement	23.00	Nil	3.60	Nil	Nil	**26.60**
	c). Amount waived off under OTS	11.90	Nil	5.45	Nil	Nil	**17.35**
6	**Total adjustments made (4+5a+5b+5c)**	**34.90**	**5.00**	**19.95**	**54.74**	**Nil**	
7	**Total NPIs at the end of each year (3-6)**	**79.07**	**89.55**	**74.75**	**20.01**	**20.01**	

Audit analysis revealed the following.

- During 2006-11, Investments of ₹ 20.63 crore turned NPI, whereas the Bank had recovered ₹ 5.15 crore only during 2008-10. No recovery was made during 2006-07, 2009-10 and 2010-11, which showed lack of concern of the Bank with regard to recovery under this category.

- The Bank had written off NPIs of ₹ 65.49 crore during 2007-10, out of which ₹ 15.77 crore were subsequently recovered between June 2009 and March 2011 leading to loss of ₹ 49.72 crore.
- The Bank had settled NPIs amounting to ₹ 43.95 crore under OTS Scheme during the years 2006-09 whereby recovery of ₹ 26.60 crore was made and ₹ 17.35 crore were waived off.
- Other than NPIs, the Bank had also written off investments under Equity (Non-SLR), valuing ₹ 2.60 crore during 2007-09. Besides, the Bank scarified the Principal amount of Bonds/Debentures (Non-SLR) during 2007-08 amounting to ₹ 1.70 crore by waiver, leading to further loss of ₹ 4.30 crore.

The Management stated (July 2011) that the investments were over due since long and largely comprised either suit filed or Corporate Debt Restructured (CDR) and had to be written off due to very poor financial position of the Companies where the chances of recovery were bleak. Besides, it was done with a view to cleaning up of the books of accounts by writing off the amount against the provisions made.

The reply is not convincing as the Bank had subsequently recovered ₹ 15.77 crore between June 2009 and March 2011 after writing off NPIs during 2007-10 indicating that the Bank had not taken all out efforts to effect recoveries before writing off the NPIs whereas the scope of recovery always remained there.

Audit test-checked cases of write off/waiver as discussed in the succeeding paragraphs.

4.2.18.3 On the request of a Company*, the Bank made an investment of ₹ 25 crore (10 July 2001) in 14 *per cent* unsecured and unrated redeemable NCD, due for payment on 9 December 2002 (in 17 months) to fill the working capital gap. The Company defaulted in redemption on due date.

It was observed that the Bank had made investment earlier in the same Company in 1996 and again in March 2001 but on both the occasions the Company demanded roll over, which was granted, and after some delay it redeemed the debts. Despite that, the Bank invested ₹ 25 crore in unsecured NCD simply on the speculation that it was a lucrative one which ultimately turned to be loss making investment.

Since the investment of the Bank made on 10 July 2001 was unsecured/unrated, the Bank's persuasion for redemption proved unfruitful. The Bank, considering the liquidity problems, inadequate working capital, etc. of the Company, restructured the investment (February 2006) by converting the outstanding amount of NCDs (₹ 25.97 crore) into Rupee Term Loan (RTL) of ₹ 10.06 crore, Funded Interest Term Loan (FITL) of ₹ 1.17 crore and Zero Coupon Principal Bond (ZCPB) of ₹ 14.74 crore. Conversion of

* M/S Himachal Futuristic Communications Limited

Investment (NCD) into RTL and FITL was, however, not in line with the Investment Policy of the Bank.

Rescheduling the repayments did not yield any results and the Bank, having convinced that the recovery had become doubtful, settled (April 2010) the case under OTS accepting ₹ 6.43 crore as full and final payment by sacrificing ₹ 23.03 crore including un-booked interest of ₹ 3.74 crore resulting in loss to the Bank to that extent.

The Management stated (July 2011) that the Bank had no option but to settle the case under OTS keeping in view the poor financial health of the Company. The contention is not acceptable on the grounds that the Bank should have assessed the financial health of the Company before making huge investment of ₹ 25 crore in unsecured NCDs.

4.2.18.4 The Bank invested (between October 2001 and May 2002) ₹ 15 crore in 12.25 *per cent* NCDs with a Company[*]. The Company serviced the interest up to August 2002 and thereafter defaulted in payment of interest on due dates and also in repayment of Principal amount. The Bank had to accept (May 2005) ₹ 8.23 crore as CDR package[†] against the total outstanding of ₹ 16.46 crore sacrificing ₹ 8.23 crore. Despite restructuring, the Company defaulted in payment of interest on term loan from February 2006 and offered (March 2008) ₹ 1.60 crore towards full and final settlement of the dues which was accepted (March 2008), by the Bank, thereby, sacrificing an additional amount of ₹ 2.52 crore leading to a total loss of ₹ 10.75 crore to the Bank.

Audit observed that the Bank invested in un-secured/un-rated NCDs without analyzing the financial position of the Company which resulted in loss of ₹ 10.75 crore which otherwise could have been avoided had the Bank shown prudence and analyzed the financial position correctly before making investment of ₹ 15 crore.

The Management stated (July 2011) that the investment was made keeping in mind good brand image, strong financials and good track record of the Company.

The fact remains that the Bank had not analyzed the financial position of the Company before making investments but invested on the request of the Company, considering only its brand image which ultimately proved to be an imprudent decision leading loss to the Bank to the tune of ₹ 10.75 crore.

[*] M/S BPL Ltd.

[†] ₹ 4.11 crore as upfront payment, conversion of ₹ 2.06 crore into non-convertible non-cumulative preferential shares and ₹ 2.06 crore into term loan @ 8 *per cent*.

4.2.19 Conclusion

Advances

- Though the overall achievements against the targets of advances were satisfactory, inter- zone disparity in achievements existed.
- Credit Deposit Ratio of the Bank declined from 69.02 *per cent* in the year 2006-07 to 59.67 *per cent* in 2010-11 indicating that the Bank was not able to lend corresponding to the deposit of the Bank.
- The Bank lacked in monitoring the credit facilities under renewal of Working Capital Limit Accounts, Stock Audit and Credit Audit.
- Due to writing-off huge amounts, the percentage of NPA to total advances declined from 2.89 *per cent* in 2006-07 to 1.95 *per cent* in 2010-11. The inter Zones NPA were on higher side.
- NPA under consortium advances constituted 2.46 *per cent* of the total advances as against overall NPA of 1.95 *per cent*. Besides, recovery of advances was unsatisfactory.
- The Bank had not maintained data with regard to category-wise income of the Advances and sub-classification under each category.
- By settling 6073 cases under OTS during the years 2006-11, the Bank apart from sacrificing interest to the tune of ₹ 147.47 crore, sacrificed the principal amount of ₹ 33.35 crore resulting in loss to that extent.

Priority sector lending

- The Bank failed to achieve the targets under agriculture sector. Consequently the Bank had to invest an amount of ₹ 2862.74 crore in Rural Infrastructure Development Fund (RIDF) for a period of three to seven years at lower interest rate of three to six *per cent* per annum leading to loss of interest to the tune of ₹ 334.49 crore.
- The Bank had neither fixed any targets for recovery of advances made under Priority Sector nor had made any recovery of NPA in any of the years during performance audit period leading to increase of NPA.
- The Bank failed to achieve the targets under Central/State Sponsored Schemes leading to tardy implementation of various programmes.
- Despite lapse of four years since lead bank responsibilities had been assigned in respect of 12 districts, the Bank was still in the process of implementation of the Lead Bank functions.

Investments

- The return on investments portfolio remained below seven *per cent* during the audit period which was not financially prudent.
- The Bank did not take effective steps to recover overdue investments leading to huge financial loss by way of NPIs write-off.

4.2.20 Recommendations

- The Bank needs to strengthen its mechanism to ensure that cash is not retained in excess of limit fixed and the same is utilized to achieve the targets of Advances at Zonal Office/Branch level.
- The Bank needs to improve the monitoring system of advances so as to ensure that high risk accounts are identified in time and corrective steps are taken to prevent slippage to NPA. The Bank must take effective steps to reduce the NPA at Zonal Level/Branch level to a comfortable position.
- The Bank must settle the cases under OTS strictly in accordance with policy/guidelines and ensure realization of 100 *per cent* Principal amount.
- The Bank should make all-out endeavours to achieve the targets under Priority Sector lending to avoid investment on low interest rates.
- The Bank must fix targets for recovery of NPA under Priority Sector lending to reduce the NPA level.
- The Bank must take steps to implement the centrally/State sponsored schemes effectively so as to extend the benefits of the schemes to the targeted classes.
- The Bank needs to strengthen its investment portfolio in order to maximize return on investment.

PART-B: Transaction Audit Observations

Social Welfare Department

Jammu and Kashmir Scheduled Castes, Scheduled Tribes and Backward Classes Development Corporation Limited

4.3.1 Unauthorised Diversion

The Company unauthorizedly diverted share capital contribution amounting to ₹ 1.15 crore received for financing the targeted groups towards payment of salary.

The Jammu and Kashmir Scheduled Castes, Scheduled Tribes and Backward Classes Development Corporation Limited (the Company), declared (February 2008) as a 'Service Institution' is responsible for providing self employment avenues to the target groups viz., Scheduled Castes, Scheduled Tribes, Backward classes and Notified Minorities. To achieve the objectives, the Company acts as State Channelizing Agency (SCA) for five Apex Level Corporations of the Government of India (GOI)[*] for various financing schemes. The Company being a 'Service Institution' depends upon the budgetary support from the State Government and also has an earning by way of interest from the funds obtained from Apex Corporations pending disbursement as loan to the target groups. The schemes in collaboration with the Apex Corporations are financed in the ratio of 85:10:05 by the Apex Corporations, the Company and the promoter contribution, respectively.

The Apex Level Corporations release funds to the Company for financing the income generating units amongst the targeted groups strictly in accordance with the standard conditions of the 'Term Loan Schemes' which stipulates that 10 *per cent* of the project cost is to be financed by the Company by way of subsidy and Margin Money Loan (MML). The Company meets its share of 10 *per cent* contributions from the Share Capital Contribution which is released by the State Government for financing under all categories.

During the years 2008-11, the State Government sanctioned and released ₹ 2.20 crore[†] in favour of the Company as contribution towards share capital which was to be utilized as 10 *per cent* share for welfare of Scheduled Castes, Scheduled Tribes and Other Backward Classes. The sanctions stipulate that no diversion of funds was allowed and progress

[*] National Scheduled Castes Finances and Development Corporation (NSFDC) New Delhi, (for Scheduled Castes) (from 1992-93); National Scheduled Tribes Finances and Development Corporation (NSTFDC) New Delhi, (for Scheduled Tribes) (from 2001); National Minorities Development and Finance Corporation (NMDFC) New Delhi (for National Minorities Male members) (from 1995-96); National Backward Classes Finance and Development Corporation (NBCFDC) New Delhi, (for Backward Classes) (from 1995-96)' National Handicapped Finance and Development Corporation (NHFDC), New Delhi (for male Handicapped members) (from 2007-08)

[†] 2008-09 : ₹ 0.20 crore, 2009-10: ₹ 1.00 crore and 2010-11: ₹ 1.00 crore

report of the utilization of funds was required to be furnished on monthly basis to the Administrative Department of the State Government.

Audit, however, observed (September 2010) that instead of utilizing share capital so released for the intended purpose, the Company diverted ₹ 1.15 crore* (2009-11) towards payment of salary to the staff without seeking consent/approval of the State Government, which was not only unauthorized and irregular but also deprived the beneficiaries of the benefits of the schemes to set up income generating units. Besides, it was seen that details of monthly utilization of funds had not been sent to the Administrative Department as was stipulated in the sanction governing the release of the Share Capital Contribution leading to violation of the terms and conditions of the Government sanctions.

The Management stated (October 2010/June 2011) that it had no regular income to meet its salary and administrative expenses. It further stated that though the Government was constantly approached for grant of enhanced budgetary support than what was being granted, sufficient budgetary support was not provided, consequently the share capital contribution was diverted for payment of salary and other administrative expenses. The reply is not convincing as the Company should have obtained special sanction of the Government for diversion of the share capital contribution which it had failed to do, rendering the diversions unauthorized and irregular besides denying benefits of financing schemes to the targeted beneficiaries.

The matter was referred to Government in July 2011; the reply had not been received (October 2011).

The State Government must provide sufficient funds for running the day to day affairs of the Company to ensure that no diversions from scheme funds meant for up-liftment of the underprivileged classes are made. The Company should also not resort to such irregular diversions without the consent/approval of the State Government.

* 2008-09 : Nil, 2009-10: ₹ 58.40 lakh and 2010-11: ₹ 56.41 lakh

Public Works Department

Jammu And Kashmir Projects Construction Corporation Limited

4.3.2 Undue favour to Contractor

Allotment of work without inviting tenders and payment of unsecured interest free mobilization advance to the contractor resulted in undue favour to contractor and interest loss of ₹ 1.64 crore.

The Jammu and Kashmir Projects Construction Corporation Limited (the Company) signed (December, 2006) a Memorandum of Understanding (MOU) with J&K Power Development Corporation (JKPDC) (both State Public Sector Undertakings) for construction of Motorable R.C.C Bridge at Ganpat, Doda at a cost of ₹ 29.95 crore, which included 15 *per cent* supervision charges (Company's share) of ₹ 4.49 crore, for completion by February 2009. An amount of ₹ 5.99 crore was received (December 2006/March 2007) by the Company from the JKPDC as Mobilization Advance against a Bank Guarantee for the full amount. The Company allotted (February 2007) the work to a sub-contractor[*] at the cost of ₹ 25.46 crore for completion within 25 months i.e., by February 2009. The work, however, had not been completed as of June 2011.

Audit scrutiny (February 2011) revealed the following:

- The Company, while sub-contracting the work, instead of following a transparent and competitive tendering process, had allotted work to the sub-contractor on the recommendation (January 2007) of a committee set up by the Company which had opined that the said contractor had the capacity to undertake such works and had, in the past, already executed some of the bridge projects with the Company. Scrutiny of records, however, revealed that though the committee had recommended allotment of work in January 2007, as per records the work had already been started by the contractor in November 2006, rendering the process meaningless. The Company stated (September 2011) that the work had been allotted to the firm by an MOU between the Company and the sub-contractor. The reply is not tenable as mere entering into an MOU does not absolve the Company of the responsibility of following prescribed procedure laid down in the State Financial Code as well as the guidelines of the Central Vigilance Commission (CVC) with regard to allotment of contracts, which provide for transparent tendering process.

- The CVC guidelines (October 1997/June 2004/April 2007) prohibit payment of unsecured and interest free mobilization advance. The guidelines provided that decision to provide such advance should rest at the level of Board of Directors (with concurrence of Finance) in the organization. The guidelines further provide

[*] M/S A.K. Constructions, Jammu

that the advance should be released in stages depending upon the progress of the work, there should be a security by way of Bank guarantee of an equal amount, a fixed re-payment scheduled and provision of an interest element in the event of failure to repay. In violation of the above guidelines, it was seen that the sub-contractor was paid an interest free mobilization advance of ₹ 5.09 crore[*] immediately (February/March 2007) on start of the work. No safeguards to secure the advance by way of a bank guarantee of equivalent amount were insisted upon even though the Company had itself taken the mobilization advance from the JKPDC against a Bank Guarantee. Audit noticed that out of total value of work done of ₹ 13.06 crore ending June 2011, the contractor had submitted bills to the tune of ₹ 3.80 crore in March 2008 and no other claim had been preferred since then. An amount of ₹ 1.50 crore only out of the mobilization advance had been adjusted (March 2008) and the balance amount remained unadjusted as of June 2011. The payment of unsecured and interest free mobilization advance paid in violation of the instructions of the CVC, thus, resulted in interest loss of ₹ 1.64 crore[†] (for the period from March 2007 to March 2011) besides, extension of undue favour to the contractor. The Management stated (August 2011) that the advance had been given as per the agreement with the contractor. The reply does not justify payment of advance in violation of guidelines thereby, extending undue benefit to the contractor.

The matter was taken up with the Government (July 2011); the reply was awaited (October 2011).

The Company should take immediate steps for recovery of the advance and henceforth ensure compliance with the guidelines/rules in the matters of allotment of contracts and mobilization advance.

[*] ₹ 1.20 crore in February 2007 and ₹ 3.89 crore in March 2007

[†] Calculated at the rates (9.5 *per cent* , 10.75 *per cent* and 11.25 *per cent*) charged by Jammu and Kashmir Bank on State Government's Overdraft from time to time

Public Works Department

Jammu and Kashmir Projects Construction Corporation Limited

4.3.3 Non-receovery of labour cess

Failure to collect labour cess on the works executed by the Company resulted in non-recovery of ₹ 2.68 crore.

Government of India (GOI) enacted 'Building and Other Construction Workers Welfare Cess Act', 1996 to regulate employment and conditions of service of building and other construction workers and to provide for their safety, health and welfare measures and for other matters connected therewith or incidental thereto, through the Boards constituted by the State Governments under Building and Construction Workers Ordinance.

As per the Act;

- Cess is payable by the employer which includes owner of an establishment, specified authority of any department of the Government carrying on construction work or the head of the department, at the rate not exceeding two *per cent* but not less than one *per cent* of the cost of construction incurred by the employer.
- The cess collected, as such, is to be paid by the employer to the Cess-collector appointed by the State Government within 30 days of completion of the construction or within 30 days of the date on which assessment of cess payable is finalized, whichever is earlier. However, where the duration of the construction work exceeds one year, cess is to be paid within 30 days of completion of one year from the date of commencement of work and every year thereafter.
- If an employer fails to pay cess within the specified period, the Assessing Officer may impose a penalty not exceeding the amount of such cess and also charge interest at the rate of two *per cent* for every month or part thereof.

Though the Act was enacted by GOI in 1996, a notification for formation of the Jammu and Kashmir Buildings and Other Construction Works Board (Board) was issued belatedly in July 2007. Reasons for delay in issue of notification though called for (July 2011) from the Government, were awaited (August 2011).

In the State, all works of roads and buildings, estimated to cost ₹ 15 lakh and above, are executed by the State-owned Jammu and Kashmir Projects Construction Company (Company), under instructions of the State Government. Audit scrutiny (January 2011) revealed that despite having executed work to the tune of ₹ 772 crore[*] since enactment of the Act to March 2010, the Company had neither levied nor paid to the Cess-collector the minimum one *per cent* cess on the value of work done including material. Viewed from the fact that the levy and collection of cess was to augment the resources for the Labour

[*] July 2007 to March 2008: ₹ 198 crore, 2008-09: ₹ 272 crore; 2009-10: ₹ 302 crore

welfare, the non-adherence to the provisions of the Act had resulted in non-recovery of ₹ 7.72 crore from the works executed by the Company. Out of this recovery of cess of ₹ 2.68 crore on 154 completed works on which an expenditure of ₹ 268.42 crore (out of ₹ 772 crore) had been incurred as of March 2011, was doubtful.

The Management attributed (June 2011) reasons for non-implementation of the provisions of Cess Act to lack of awareness. It was further stated that measures to recover the amounts in respect of contracts started earlier and still under execution were under way by revision of cost offers and submission thereof to the concerned project authorities and in respect of new projects cost offers were loaded with the cess component. The fact, however, remains that the Company had failed to take cognizance of the provisions of the Act in right earnest by which it had missed the opportunity to recover the statutory dues of ₹ 2.68 crore, besides depriving the labour force of the State of the intended benefits.

The matter was taken up with the Government (May 2011); the reply was awaited (October 2011).

The Company must take immediate steps to comply with provisions of the Act.

Tourism Department

Jammu and Kashmir Cable Car Corporation

4.3.4 Wasteful expenditure due to deficient planning

Execution of work without administrative approval and proper technical advice resulted in blocking of ₹ 45.28 lakh besides wasteful expenditure of ₹ 17.77 lakh incurred on foundation.

The Managing Director (MD), J&K State Cable Car Corporation (Company) issued (August 2006) orders for construction of a centrally heated restaurant to be constructed at Apharwat (Gulmarg) without Administrative approval (AA)/Technical sanction (TS) or approval by the Board of Directors (BoD).

We noticed (March 2010) that the structural designs for the restaurant were got prepared (August 2006) by a consultant. The work orders for supply, erection, fixing, cutting and hoisting of structural steel were issued (October 2006) to a firm at an estimated cost of ₹ 90.65 lakh. The firm supplied (December 2006) the ordered quantity of 870 quintals of structural steel for which an amount of ₹ 60.90 lakh was paid by the Company. The Company simultaneously allotted base work of the restaurant to piece workers and an amount of ₹ 17.37 lakh had been incurred as of March 2007. It was seen that apart from supply of the steel, no other components of the work order viz., erection, fixing, cutting and hosting of structural steel design had been undertaken by the firm concerned with the result the steel supplied had not been used as of March 2010. It was further seen that a Committee constituted (March 2007) by the BoD, to ascertain the status of work, noticed that the steel members supplied were of very high specifications and had ordered for its disposal and construction of the restaurant by erection of a structure similar to the one that had been erected by army for its use at Apharwat. However, no action to start the works on foundation works already executed or to dispose off the material was taken till October 2010 when the Company allotted the construction work to J&K Housing Board (Board) at an estimated cost of ₹ 2.59 crore. It was, however, seen (July 2011) that the Board had lifted only 200 quintals of steel valued at ₹ 15.62 lakh for meeting of its full requirement for the restaurant. The remaining quantity of 670 quintals valued at ₹ 45.28 lakh was lying un-utilised and the Corporation contemplated its disposal by way of transfer to other needy PSUs or State Government Departments which, however, was pending as of September 2011. It was further revealed that the foundation already constructed had not been put to use by the Board as the new restaurant was being constructed at a place away from the previous location. This had resulted in non-utilisation of the already constructed plinth and thus, rendered the expenditure incurred on it wasteful.

Thus, action of the Corporation in embarking upon the project without proper planning resulted in blocking of ₹ 45.28 lakh for about five years and wasteful expenditure of ₹ 17.77 lakh[*].

The matter was referred to the Government (September 2011); reply was awaited (October 2011).

The Company must refrain from taking up works in an adhoc manner and without Administrative approvals and Technical Sanction. Planning and implementation aspects should be given due consideration to avoid loss on account of faulty project implementations.

[*] Construction of plinth: ₹ 17.37 lakh and Consultant charges: ₹ 0.40 lakh

Consumer Affairs and Public Distribution Department

4.3.5 Misappropriation due to absence of monitoring mechanism

Non-adherence to prescribed system of monitoring and control of the stocks lying in CAPD, Store Udhampur, resulted into misappropriation of food grains stocks.

Assistant Director, Consumer Affairs and Public Distribution Department (CAPD), Udhampur in the course of visit/inspection (August 2010) of Food Store, CAPD at Udhampur noticed huge shortages in the food grains stocks. A physical verification ordered (August/November 2010) by the Director CAPD, Jammu revealed shortages in the stock of Wheat, Atta, Rice and Sugar to the tune of ₹ 64.57 lakh* and the store keeper (In-charge)†, a class IV employee posted at the Food Store since 01 February 2010, was placed under suspension. Subsequent to suspension, the defaulting storekeeper had deposited ₹ 16.24 lakh in treasuries at Udhampur and Jammu. Thus, net shortage of food grains worth ₹ 48.33 lakh was assessed as recoverable from the defaulting storekeeper, which had remained unrecovered as of August 2011. The case had been referred (August 2010) to Crime Branch Jammu without conducting a departmental enquiry.

Audit observed as follows:

➢ The delinquent official, despite being a Class IV employee and entrusted with job of Store keeper had been a chronic defaulter. The official had been placed under suspension in September 1993 in Udhampur and reinstated in August 2000 treating the whole period as 'on duty'. Subsequently he had mis-appropriated food grains during his tenure as Salesman/Storekeeper at CAPD Stores at Chenani (2000) and Basantgarh (2002). The official had also obtained a loan of ₹ 1.25 lakh (August 2008) from a Co-operative Bank by forging the signatures of Tehsil Supply Officer on which he had defaulted. Before his posting in CAPD Udhampur, the official had mis-appropriated food grains worth ₹ 4.48 lakh as salesman (June 2009) at his previous place of posting viz., CAPD Store, Ramnagar which had subsequently (November 2009) been recovered by the Department.

We noticed that the Department had not taken any disciplinary action against the official and instead the official had been posted as Storekeeper of the Udhampur store, the biggest in the region, in February 2010. The official after assuming (February 2010) the charge had mis-appropriated food grains by the end of July 2010 as highlighted above.

➢ As per the Departmental Manual, physical verification of food grain stocks, lying in various stores/sale depots, should be conducted by the designated teams of the

* Total shortage: ₹ 74.82 lakh less unaccounted permits (issue slips): ₹ 10.25 lakh.

† Shri Babu Ram

Department during first quarter of succeeding financial year in collaboration with the Tehsil Supply Officer (TSO), Storekeeper and Salesman in position. The responsibility for arranging the physical verification (PV) lies with the Director who should immediately after the close of financial year constitute a team and fix dates for conducting the verification and submission of Report thereof. The PV report is to be submitted to the Assistant Director of the District concerned and a copy thereof is sent to Director CAPD.

It was, however, noticed that despite teams for Physical verification of various stores including the Udhampur store having been constituted (June 2010) by the Director CAPD, physical verification of the stocks lying in Udhampur store had not been conducted.

- The departmental manual further provides that a monthly off-take statement and monthly abstract of stock position showing opening stock, receipts, issues and closing stock of food grains is to be prepared by the Store Keeper and sent to Assistant Director duly countersigned by the TSO. It was seen that though these statements had been submitted, no verification of facts and figures were carried out at the TSO/Joint Director/Directorate level rendering the preparation and submission of these statements futile.

- There was nothing on record to suggest that follow up action by way of calling for the physical verification report or ascertaining the reasons for not carrying out of the physical verification by the designated team and verification of the monthly stock statements, had been taken at the Directorate/Joint Director/TSO level. The lapse had resulted into non-detection of the shortage of food grains for a longer spell. Failure on part of the departmental officers to enforce the system of monitoring and control over the stocks had facilitated the misappropriation.

- Financial rules provide that the officials entrusted with the duty of handing of cash and stores must furnish personal security in the form of an indemnity bond to safeguard the interests of the Government. In the instant case it was seen that no such security had been obtained from the storekeeper.

- After placing (August 2010) the delinquent Storekeeper under suspension, no disciplinary action as warranted under rules had been initiated by the Department.

Thus, failure of the Department;

- to take cognizance of the past record and conduct of the official before entrusting him with the responsibility of managing the Store,
- to take timely and appropriate disciplinary action under Rules for the past mis-conducts of the delinquent store keeper,

- to adhere to the procedure of conducting timely physical verification of the stock of food grains and obtaining monthly off take/stock statements, led to mis-appropriation/shortage of food grains to the extent of ₹ 74.82 lakh out of which shortages worth ₹ 48.33 lakh still remains to be recovered (August 2011).

The Director, CAPD Department Jammu did not offer (March/August 2011) any reasons for lapses on the part of the Department.

The matter was referred to Government in September 2011; reply was awaited (October 2011).

The Department must put in place a strong internal control and monitoring mechanism to ensure that pilferages and misappropriations are detected/tapped in a timely manner.

Srinagar/Jammu **(Venkatesh Mohan)**
The **Principal Accountant General**

Countersigned

New Delhi **(Vinod Rai)**
The **Comptroller and Auditor General of India**