Chapter III

3. Review relating to Statutory corporation

Rajasthan Financial Corporation

3.1 Recovery performance of Rajasthan Financial Corporation

Highlights

Overall recovery performance of the Corporation was abysmally low. It could recover only 5.60 *per cent* to 7.63 *per cent* of old dues and 33.92 to 58.35 *per cent* of current dues during the last five years upto 2004-05.

(Paragraph 3.1.8)

Out of loans of Rs.2,399.47 crore disbursed upto 2004-05, Rs.1,457.08 crore were outstanding at the end of March 2005. More than 72 *per cent* of overdues were more than two years old indicating poor recovery efforts.

(Paragraph 3.1.10)

Targets for recovery were progressively reduced from 25.61 *per cent* of total overdues in 2000-01 to 19.38 in 2004-05. The Corporation failed to achieve even these modest targets and recovery remained between 67.68 to 92.22 *per cent* of the target.

(Annexure 13)

The percentage of Non Performing Assets (NPA) ranged between 40.33 and 50.95 during 2000-05 indicating an alarming position. Doubtful and loss assets as a percentage of NPA increased from 76.51 to 87.38 during the five years under review.

Out of 611 loans (Rs.62.70 crore) sanctioned during 2001-02, 71 loan accounts (Rs.6.13 crore) became NPA within a short span of two years and out of 628 loans (Rs.84.33 crore) sanctioned during 2002-03, 37 loan accounts (Rs.4.34 crore) became NPA within one year.

The achievement against the target of reduction of NPA to less than 10 *per cent* was only 40.33 *per cent* at the end of March 2005.

(Paragraph 3.1.9)

Lack of internal control over project appraisals and non-adherence to the policy resulted in the Corporation's failure to recover Rs.11.95 crore owing to sanction of loans to unviable units/insufficient securities/doubtful credit worthiness. Risk management by the Corporation was deficient.

(Paragraphs 3.1.13 to 3.1.15 and 3.1.22)

The Corporation suffered losses amounting to Rs.97.03 crore due to delayed action, non- identification of properties of promoters/guarantors and imprudent settlement of dues.

(Paragraphs 3.1.16, 3.1.20 to 3.1.21)

Introduction

3.1.1 Rajasthan Financial Corporation (Corporation) was established in 1955 under Section 3 (i) of the State Financial Corporations (SFC) Act, 1951. The main objective of the Corporation as envisaged in the SFC Act is to provide medium and long-term credit to medium and small-scale industrial units in the State. The source of finance of the Corporation is loans from SIDBI* and commercial banks.

Financial assistance is provided to eligible industrial units based on detailed project reports, socio-economic viability of the projects, promoters' background, their technical ability and experience in the proposed activity, product and its marketability, financial capabilities of the promoters, security/collateral security and personal guarantee offered for loan and contribution to be brought in by promoters. Disbursement of loan is made after execution of prescribed agreement including creation of securities in favour of the Corporation. In the event of default by the loanee, action under section 29 of the SFC Act is initiated under which the unit is taken over by the Corporation. In cases where outstanding amount are not fully recovered in the sale of assets, deficit amount is recovered by selling the collateral security and invoking the personal guarantee of the promoters under section 31(1) and 32(G) of the Act ibid.

General Manager (Development) is the head of Follow up and Recovery (FR) Section, who is assisted by three Dy. General Managers (FR) incharge of allotted regions. There are seven Regional offices, each headed by a Dy. General Manager (Region). There are 39 branches under these Regional offices headed by Manager /Dy. Managers who are primarily responsible for monitoring and recovery of dues.

Upto March 2005, the Corporation financed Rs.2205.26 crore to 57,112 Small Scale Industrial (SSI) units out of 2,62,881 SSI units (registered with the Commissioner of Industries, Government of Rajasthan) representing 21.73 *per cent* of total SSI units. Besides, Rs.194.21 crore were also financed to 533 medium scale industries.

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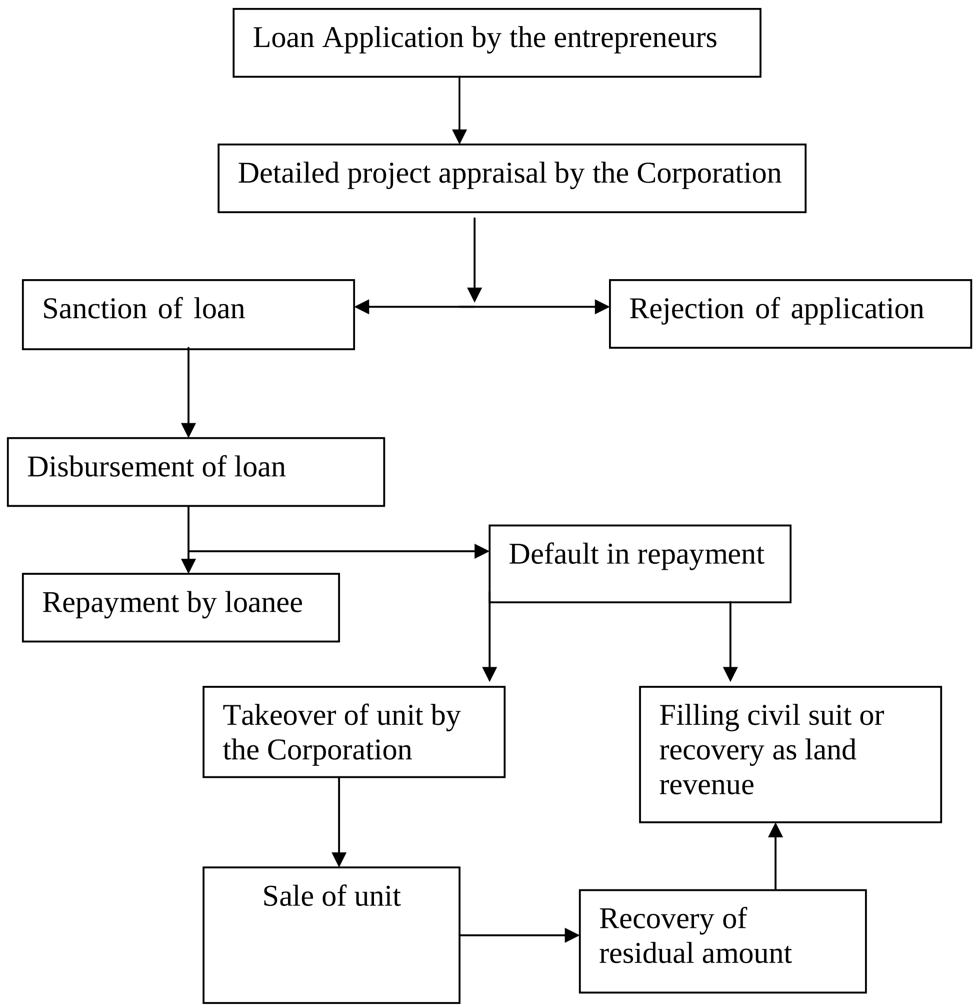
* Small Industrial Development Bank of India.

A flow chart indicating the process of financing and recovery thereof is depicted below:

Process of Financing & Recovery



Scope of Audit

3.1.2 The recovery performance of the Corporation was last reviewed and included in the Report of the Comptroller and Auditor General of India for the year ended 31 March 1999 (Commercial), Government of Rajasthan. The review was discussed by the Committee on Public Undertakings between December 2004 to September 2005. The recommendations are awaited.

The present review covers the recovery performance of the Corporation for the last five years upto 2004-05, based on test check of records at its head office and seven branch* offices conducted during September 2004 to February 2005. Selection of branches was made on the basis of highest number of default cases in which first disbursement was made after March 1999 with overdue amount exceeding Rupees five lakh (143 cases) and also cases with overdue amount of more than Rupees one crore (74 cases) irrespective of year of disbursement. Of the total 395 cases in 39 branches, 217 cases (55 *per cent*) involving an overdue amount of Rs.212.20 crore (18.87 *per cent*) as on 31 December 2004 against total overdue amount Rs.1,124.83 crore were selected for test check.

The audit findings were reported (April 2005) to the Government/Management and discussed at the meeting of the Audit Review Committee for Public Sector Enterprises (ARCPSE) on 19 July 2005 where Government was represented by the Dy. Secretary (Industries) and the Corporation was represented by the Chairman and Managing Director, General Manager (Finance) and General Manager (Loans). The review was finalised after considering views of the Government/management.

Audit objectives

3.1.3 Audit of recovery performance of the Corporation was carried out with a view to assessing whether:

- the system of recovery and action in case of default was robust to ensure timely recovery of principal and interest thereon;

- management of the Corporation was efficient to safeguard its interest against possible risk of default in recovery;

- the corporation had put in place a system to address the risk associated with loan sanctioning and disbursement as also effective monitoring of its dues;

- the internal control system of the Corporation was sufficiently sensitive to highlight the lapses and irregularities and provided sufficient assurance for safeguarding the financial interest of the organisation;

* Alwar, Bhilwara, Bhiwadi, Jaipur (City), Jaipur (Rural), Jodhpur and Sikar

- timely and appropriate action for recovery was taken against the defaulters as per the SFC Act;

- the Corporation maintained records to facilitate age analysis, analysis of overdues to facilitate meaningful recovery action;

- the Corporation had put in place a reliable MIS* system to obtain correct and timely information to be able to monitor recovery effectively.

Audit criteria

3.1.4 The performance of the Corporation was assessed against the provisions of the SFC Act, its own laid down procedures for sanction, disbursement and monitoring of recovery, examining the deficiencies in sanction and disbursement of loan and lapses in follow up, monitoring and recovery of dues.

Audit methodology

3.1.5 Based on the preliminary findings of the Pilot Study conducted during November 2003, the risk in the Corporation was perceived to be high. The thrust areas of audit were increasing trend in overdues, Non-Performing Assets (NPA), efficiency and effectiveness in follow up and monitoring of recovery. The following methodology for scrutiny of loan accounts was adopted:

Detailed testing of documents relating to sanction, disbursement and recovery, units taken into possession and sold under section 29 of the SFC Act and cases of settlement of overdues by settlement committees was done with a view to assessing the internal control and efficiency of the recovery system.

Audit findings

Recovery performance

Even after 50 years of its existence the Corporation was unable to meet the gap in amount of disbursement and recovery.

3.1.6 During the five years up to 2004-05, the Corporation disbursed loans amounting to Rs.781.91 crore whereas the total recovery including interest during this period was only Rs.588.83 crore (75.30 *per cent*). This indicated that the Corporation was unable to recover the amount of disbursement whereas it has to repay its borrowings together with interest in a rigid time frame. Thus to meet the gap in amount of disbursement and recovery, the

* Management Information System

Corporation had to go for additional borrowings from commercial banks and other financial institutions.

Sanction and disbursement of loan

3.1.7 A comparative statement showing the receipt of applications, sanctions and disbursements of term loans during the last five years ended 2004-05 is given below:

(Amount: Rupees in crore)

Particulars	**2000-01**		**2001-02**		**2002-03**		**2003-04**		**2004-05**	
	No.	**Amount**	**No.**	**Amount**	**No.**	**Amount**	**No.**	**Amount**	**No.**	**Amount**
Applications pending at the beginning of year	121	59.46	23	17.50	36	24.38	10	3.16	56	50.64
Add: applications received	1679	335.41	1746	315.09	1643	349.33	2207	513.53	2139	626.31
Total applications	1800	394.87	1769	332.59	1679	373.71	2217	516.69	2195	676.95
Less: applications lapsed/rejected /withdrawn	646	181.08	566	133.83	506	167.75	641	224.88	753	353.90
Percentage of rejection/ lapsed withdrawal	35.89	45.87	32.00	40.24	31.25	44.89	28.91	43.52	34.31	52.28
Net balance	1154	213.79	1203	198.76	1173	205.96	1576	291.81	1442	323.05
Targets of sanctions	-	180.00	-	170.00	-	190.00	-	230.00	-	300.00
Loans sanctioned	1131	196.29	1167	174.38	1163	202.80	1520	241.17	1419	301.60
Targets of disbursement	-	145.00	-	130.00	-	140.00	-	160.00	-	200.00
Loans disbursed	953	146.13	908	128.79	911	139.92	1087	168.64	1144	198.43
Applications pending at the close of year	23	17.50	36	24.38	10	3.16	56	50.64	23	21.15

It would be seen from the table that the amount of sanction as well as disbursement decreased during 2001-02 but progressively increased during subsequent years mainly due to introduction of loans rollover cum principal replenishment scheme in year 2001-02. Under the scheme the amount of old loan was considered as recovery of the year and amount of new loans taken as sanction and disbursement of the year. It was observed in audit that increase in sanction of loan during 2002-03 and 2003-04 was mainly due to this scheme as Rs.23.64 crore and Rs.25.23 crore were rolled over during 2002-03 and 2003-04 respectively, and the targets of sanction and disbursement were thereby achieved in these years.

3.1.8 The Corporation disbursed loans aggregating Rs.2,399.47 crore up to 2004-05. Out of this, Rs.1,457.08 crore as principal, interest and other charges were outstanding as on 31 March 2005. The details of term loans due for recovery, targets fixed for recovery and amounts recovered during the last five years upto 2004-05 are given in **Annexure-13**.

It would be seen from the annexure that the targets for recovery as a percentage of net recoverable had been progressively reduced over the years to the level of 19.38 *per cent* in 2004-05 from 25.61 *per cent* in 2000-01. Even the low targets were not achieved. The actual recovery against targets remained between 67.68 to 92.22 *per cent*. Government stated (July 2005) that the targets for recovery were fixed only for the amounts recoverable from the borrowers who were regular in their payments i.e. after excluding the amounts relating to BIFR cases, court cases, closed units, units in possession and deficit cases. Thus, the targets were fixed at a satisfactory level of 52.01 to 60.30 *per cent* during 2000-01 to 2004-05 of the net recoverable amount. The reply is not tenable in view of the fact that targets of recovery of 52.01 to 60.30 *per cent* of amount recoverable from healthy borrowers cannot be said to be a satisfactory level. The declining effectiveness in recovery performance led to increase in overdues from Rs.685.91 crore in 2000-01 to Rs.1,124.83 crore in 2004-05.

Recovery of 5.60 to 7.63 *per cent* of old dues and 33.92 to 58.35 *per cent* of current dues during five years upto March 2005 indicates abysmally low performance of recovery.

Audit further observed that separate targets for recovery of old and current dues were not fixed which had adverse effect on the recovery of old dues as the percentage of recovery of old dues constituted only 5.60 to 7.63 *per cent* of the recoverable amount for the five years upto 2004-05 as compared to 33.92 to 58.35 percent for current dues. In the absence of separate targets for old dues, the performance of recovery against old dues could not be checked in audit.

3.1.9 Classification of assets

In the case of State Financial Corporations, Industrial Development Bank of India (IDBI) had classified (March 1994) the loans into the following four categories depending upon their chances of realisation: -

Standard assets - where repayments are regular.

Sub standard assets - where loan as well as interest remain overdue over a period of six months but not exceeding two years.

Doubtful assets - where loan as well as interest remain overdue beyond two years.

Loss assets - where losses are identified but not written off at the end of the year.

The loan assets other than standard assets are known as Non-Performing Assets (NPAs).

The details of NPA for the five years up to 2004-05 are presented in the table given below:

(Amount: Rupees in crore)

Sl. No.	Particulars	2000-01	2001-02	2002-03	2003-04	2004-05
1.	Loans outstanding at the close of the year	730.93	738.71	756.16	773.65	825.91
2.	Amount disbursed during the year	146.13	128.79	139.92	168.64	198.43
3.	Outstanding at close of the year excluding current year's disbursement.	584.80	609.92	616.24	605.01	627.48
4.	Classification of loans					
a)	Standard assets	376.09	364.73	370.91	401.05	492.83
b)	Sub-Standard assets	83.33	101.44	81.16	74.69	42.02
c)	Doubtful assets	236.99	246.96	284.53	281.99	278.12
d)	Loss assets	34.53	25.57	19.56	15.92	12.94
5.	Total NPA (b+c+d)	354.85	373.97	385.25	372.60	333.08
6.	Percentage of NPA to total outstanding (5 to 1)	48.55	50.62	50.95	48.16	40.33
7.	Percentage of NPA to net outstanding (5 to 3)	60.68	61.31	62.52	61.58	53.08
8.	Percentage of doubtful and loss assets to total NPA(4(c)+(d) to 5)	76.51	72.87	78.93	79.95	87.38

It would be seen from the above that the percentage of NPA to total outstanding dues ranged between 40.33 and 50.95 *per cent* during 2000-05. Moreover, since loans disbursed during a year did not become NPA in that year, after exclusion of such loans from the closing balance of total loans, percentage of NPA net of such loans would reach a level of 53.08 to 62.52 *per cent* during the above period indicating an alarming position of NPA. As per MOU* executed (December 2003) between the Corporation, State Government and SIDBI, the Corporation agreed to bring down NPA to less than 10 *per cent* during the next five years. During the period of two years,

* Memorandum of Understanding

however, the NPA level could be reduced from 50.95 *per cent* during 2002-03 to only 40.33 *per cent* in 2004-05.

The doubtful and loss assets percentage to total NPA in 2004-05 reached to 87.38 *per cent*, indicating alarming position.

The percentage of doubtful and loss assets to total NPA increased from 76.51 *per cent* in 2000-01 to 87.38 *per cent* in 2004-05 which indicated that the quality of loan assets was deteriorating due to lack of recovery efforts in case of old dues.

Lack of proper appraisals and effective control on NPA.

Audit analysis revealed that out of 611 loans (Rs.62.70 crore) sanctioned during 2001-02, 71 loan accounts (Rs.6.13 crore) became NPA within a short span of two years. Likewise out of 628 loans (Rs.84.33 crore) sanctioned during 2002-03, 37 loan accounts (Rs.4.34 crore) became NPA within one year. This is indicative of lack of proper project appraisals and effective control on NPA as discussed in paragraphs 3.1.13 to 3.1.15.

3.1.10 Erroneous classification of outstanding

Over 72 *per cent* of overdues were more than two years old indicating poor recovery efforts.

The Corporation neither maintained records showing age-wise details nor analysed total over dues to facilitate meaningful recovery action. Up to 2003-04, however, the age-wise analysis of amount overdue against regular accounts (as shown in Operational Statistics) were published by bi-furcating it in four age groups on a fixed percentage basis showing only 10.67 *per cent* overdue as more than 24 months old. On this being pointed out by Audit, the Corporation revised the age of overdues as on 31 March 2005 according to which Rs.163.82 crore, representing 72.65 *per cent* of net over dues of Rs.225.50 crore, were due for more than two years as against 10.67 *per cent* shown during earlier years.

3.1.11 Reason for low/non recovery

The rapid recovery of dues facilitates recycling of funds for further finance. The Corporation did not make effective efforts to improve the recovery of its long over dues. It was observed during audit that the main reasons for low/non recovery of dues were deficiencies in sanction and disbursement of loans, lack of follow up and inaction for recovery, system deficiencies, delay in disposal of units and not taking action for recovery of residual amount as discussed in the succeeding paragraphs.

Deficient Sanction and disbursement of loan

3.1.12 An effective appraisal of a project to be financed is of vital importance not only in protecting the financial interests of the Corporation but also in achieving the objective of accelerating industrial growth. The following deficiencies in sanction and disbursement of loans were pointed out in the Report of Comptroller and Auditor General of India (Commercial) for 1998-99:

- Loan without evaluating satisfactory performance of unit already financed;

- Loan to promoters having doubtful creditworthiness;
- Lack of monitoring/ inspection;
- Delay in disposal of units taken over; and
- Inaction for recovery.

Audit review revealed that the Corporation failed to ensure compliance with its own instructions with regard to the project appraisal system to avoid recurrence of such deficiencies. Further deficiencies noticed in 15 cases (out of a total 217 cases) during test check in sanction and disbursement of loans are discussed below. The details of these cases are given in **Annexure-14**.

3.1.13 Loans to unviable projects

Due to improper project appraisal the Corporation failed to recover dues of Rs.6.18 crore from nine units.

The Corporation did not have a dependable mechanism for critical examination of viability of the projects through market research. Even the available information / data were not kept in view while sanctioning loans. It is evident from the **Annexure-14** that while making project appraisal in nine cases, the Corporation failed to appraise projected income as well as source of promoter's contribution, suitability of location for the project, profitability of the existing project, prevailing stiff competition in the market of proposed project and failure of similar industries financed earlier by the Corporation. In one case, the loan was sanctioned even without ascertaining the technical and financial viability of the project. As a result the Corporation could not recover Rs.6.18 crore from these nine units. Government stated (July 2005) that the instructions for increase in promoters' contribution and security margins were issued from time to time. The fact remains that the Corporation failed to follow its instructions / procedures which resulted in non-recovery of the dues.

3.1.14 Sanction of loan without sufficient security

The Corporation provides loans against hypothecation of financed assets. In case of high risk projects, the Corporation insists on furnishing of collateral security to safeguard its interest. The Corporation prescribed the norms of obtaining collateral security for sanctioning working capital loan. No such norms in case of sanction of other loans based on the degree of risk involved in the proposed project were prescribed by the Corporation.

Due to insufficient security an amount of Rs.1.58 crore could not be recovered.

It was observed during audit that in cases of sanction of working capital loans to six borrowers, the collateral security was accepted based on the certificate of a private valuer instead of verification by the technical officer of the Corporation. The security was subsequently found to be of lower value and as a result the amount of Rs.1.58 crore could not be recovered from these units.

Government stated (July 2005) that the relevant records were not available. The cases had been referred to District Collector for recovery action. The reply is contradictory and not tenable as without records / details, the chances of recovery through the Collector are bleak.

3.1.15 Loans to promoters having doubtful creditworthiness

Loans to promoters having doubtful creditworthiness led to non-recovery of Rs.4.19 crore.

While making project appraisal, the Corporation is required to verify the creditworthiness of the promoters. It was observed during audit that inspite of doubtful creditworthiness of the promoters, the Corporation granted loans to four units as detailed in **Annexure-14**, which defaulted in repayment of Corporation dues and as a result, an amount of Rs.4.19 crore could not be recovered from the units mentioned in the annexure.

Lack of follow up and inaction for recovery

3.1.16 After disbursement of loan the Corporation was required to follow up recovery of dues and in case of default suitable action under Section 29 to 32 of SFC Act, should have been taken. Audit analysis revealed that the Corporation had not taken timely action for recovery of dues, the details of such cases alongwith the Government views on each case are given in **Annexure-15**. It would be seen from the annexure that:

Corporation's failure to initiate timely action for recovery of dues from defaulting units resulted in non-recovery of Rs.19.47 crore.

- In three cases (Sl. no. 2,3 and 9) involving dues of Rs.6.72 crore, the Corporation had not taken over the units inspite of continued default and the units were subsequently registered with BIFR* /taken over by official liquidator.

- In two cases (Sl. no. 4 and 5) involving dues of Rs.2.13 crore, the High Court granted stay against dispossession of the units upto March 2000 but the Corporation had not taken over the units thereafter under the wrong impression that the court stay was continuing.

- Despite continued default for more than five years by three units (Sl. no. 1,8 and 10), the Corporation had not initiated action under Section 29 or 32 (G) for recovery of Rs.8.31 crore. In one case the unit taken in possession was even handed back without obtaining 10 *per cent* amount of outstanding dues as required under the procedure and guidelines.

- Despite having heavy overdues (Rs.1.58 crore), the Corporation in one case (Sl. no.6) released easily marketable collateral security of high value in exchange of low value security. Further the case to take possession of the collateral security was not pursued properly in the court. In another case (Sl. no. 7) the Corporation had not initiated action under Section 32 (G) for recovery of deficit amount of Rs.72.65 lakh.

Thus due to inaction, the Corporation could not recover dues of Rs.19.47 crore from the above units. Government stated (July 2005) that recovery action had been initiated.

* Board for industrial and financial reconstruction

Units sold under Section 29 of SFC Act

3.1.17 Section 29 of the SFC Act, inter alia, empowers the Corporation to take over possession of the units in default. As on 31 March 2005, total 7,792 units were in default, of which 6,680 units were in default for more than two years. The Corporation was, however, having possession of only 438 units. It was observed that the Corporation had not prescribed any guidelines regarding timeframe for possession of defaulting unit. Age-wise analysis of 438 units in possession involving Rs.114.29 crore is given below:

(Amount: Rupees in crore)

Period	**No. of Units**	**Amount outstanding**
Upto 12 Months	110	25.72
1 to 3 Years	82	22.23
3 to 5 Years	64	24.06
5 to 20 Years	182	42.28
Total	438	114.29

Failure to take remedial measures to speed up the disposal of assets of 438 units in possession led to accumulation of outstanding of Rs.114.29 crore.

It was seen during audit that though the Corporation had taken steps for auction 5 to 40 times in these cases it could not dispose off the assets of the units due to non-receipt of suitable offers. In view of this, the possibility of unrealistic market realizable value of assets in auction cannot be ruled out. The Corporation, however, did not take remedial measures like revaluation of assets, hiring the services of commission agents to speed up the disposal of assets. Government stated (July 2005) that the Corporation had reduced the number of units under possession from 558 units as on 31 March 2004 to 438 units as on 31 March 2005 by making extra efforts for disposal of units. The fact remains that 438 units involving outstanding of Rs.114.29 crore were still lying with Corporation out of which more than 50 *per cent* were lying for periods ranging from 3 to 20 years.

Audit review revealed that the delay in disposal of units was also due to not taking timely action by the Corporation on the offers received by it as discussed below.

3.1.18 Loss due to non-finalisation of sale of unit

The Corporation jointly with RIICO* and State Bank of Bikaner and Jaipur (SBBJ) had sanctioned (December 1982) financial assistance of Rs.2.36 crore to Kalyan Sunderam Cement Industries Limited (KSCIL) Banswara on pari passu basis. The assets of KSCIL were taken over by the Corporation on 3 January 1994 due to default in payment. The Corporation received (October 1996) an offer of Rs.4.63 crore in the second auction from Shram Shakti Polytex Private Limited (SSPPL) against assessed market realisable value of Rs.7.02 crore. The Sale Committee recommended re-auction. In the third auction in November 1996, the same offer was repeated and the sales committee comprising the representative of the Corporation and RIICO

* Rajasthan State Industrial Development and Investment Corporation Limited.

recommended the sale consideration of Rs.4.63 crore. On that day, the representative of SBBJ did not attend the auction proceedings.

It was noticed that the Corporation delayed action for obtaining consent of SBBJ (located adjoining to Corporation's head office) for finalisation of the sale. In the meanwhile, the SSPPL withdrew its offer. In the subsequent auction, an offer of Rs.1.11 crore was finalised (June 2004) on deferred payment basis. The delayed action on the part of the Corporation in finalisation of approval of sale resulted in loss of Rs.40.74 lakh (Corporation share) in addition to loss of interest (Rs.36.03 lakh) on this amount for seven years. Government stated (July 2005) that after finalisation of apportionment of sale proceeds, action would be taken under Section 32 (G) of SFC Act for recovery of the deficit amount.

3.1.19 Loss due to not communicating acceptance of offer to bidder

The assets of the Ganganagar Vanaspati Refinery Limited were taken over in October 1996 due to default in payment. The Corporation failed to communicate acceptance of the highest bid of Rs.1.75 crore to the bidder. Meanwhile the High Court granted stay (August 1997) on sale of the unit on a petition by the promoter. The stay was vacated in October 1997. Even after vacation of the stay, the Corporation did not inform the successful bidder about acceptance of his bid. The bidder withdrew his bid after waiting for more than five months. In view of non-receipt of bids equal to MRV in 16 auctions held (during August 1998 to December 2003) the assets had to be sold (March 2004) for Rs. 81 lakh against the outstanding dues of Rs.1.10 crore (inclusive of interest of Rs. 48 lakh). Thus the Corporation suffered a loss of Rs.29.13 lakh due to slackness in taking action for disposal of the unit. No action was, however, taken against the delinquent officers of the Corporation.

Government stated (July 2005) that as per norms, the opportunity to the original borrowers was given to bring a higher offer alongwith 25 *per cent* of the offer price. The reply is not acceptable in view of the fact that the promoter of the unit was present in the auction proceedings (July 1997) but did not make any reservation on the offer received.

Residual recovery

3.1.20 For recovery of deficit amounts, which remained unrecovered after sale of units, the Corporation had to initiate action to invoke personal guarantees of the promoters by filing civil suits or by issuing certificates of demand to the District Collector for recovery as arrears of land revenue.

As on 31 March 2004, the deficit amount outstanding in respect of 1,974 units sold up to March 2004 was Rs.97.67 crore. The Corporation neither did the age-wise analysis of the above amount nor maintained any consolidated records showing the action taken for its recovery. It was, observed in audit that in 853 cases involving Rs.45.88 crore (47 *per cent*), the Corporation could not take any action for recovery of the deficit amount mainly due to non-availability of collateral security/ personal guarantees of promoters.

Non-identification of properties of the promoters/ guarantors caused non-recovery of Rs.19.36 crore.

Further analysis of 125 cases (dues of Rs.28.97 crore) having deficit of more than Rs.10 lakh each in respect of units sold prior to 31 March 2003 revealed that in 25 cases (Rs.6.81 crore) the promoters /guarantors were not traceable which was mainly due to delay in sale of primary security and not keeping regular contact with the promoters. In 62 cases involving Rs.14.43 crore, the Corporation could not take recovery action due to non-identification of properties of the promoters/guarantors.

The Corporation received decree orders from various courts in 467 cases for Rs.14.33 crore, out of which decree execution applications were not filed in 164 cases involving Rs.4.93 crore mainly due to non identification of properties of the borrowers for attachment. The age- wise details of decrees pending for execution were not maintained by the Corporation.

The Government, while accepting the audit findings, stated (July 2005) that the Corporation was making efforts for recovery of the amounts and Branch Managers were advised to hold regular meetings of Deficit Case Review Committee.

Settlement of over dues

Corporation suffered loss of Rs.58.20 crore in settlement of dues of 1,623 cases during 1999-2004.

3.1.21 With a view to redress the grievances of the loanees, to provide adequate and timely relief and to decide each case on merit, Grievance Redressal Committees were set up at District level (DLC), Head Office level (HOLC) and State level (SLC). During 1999-2004, 1,623 loan accounts were settled for Rs.61.02 crore against outstanding of Rs.119.22 crore thereby suffering loss of Rs.58.20 crore. The percentage of loss ranged between 40.18 and 57.92.

A few cases highlighting deficiencies in settlement are discussed below:-

- The Corporation sold (March 1988) assets of a sick unit to Mayur Sheetalaya, Kota (MSK) for Rs. 10 lakh on deferred payment basis which was reduced to Rs.8.73 lakh (July 1996) due to short possession of 5,600 Square feet of land under encroachment by outsiders. MSK did not make any payment after taking possession of the assets and applied (September2002) for settlement of the case before the SLC. The Deputy General Manager recommended settling for Rs.57.17 lakh considering MRV of assets of Rs.60 lakh against the outstandings of Rs.68.80 lakh. It was seen in audit that the SLC settled (January 2004) the case for Rs. 20 lakh only and also handed over 5,600 square feet of land released from encroachment to MSK free of cost for which sale consideration had already been reduced. The decision of SLC extending undue benefit of Rs.50.07 lakh to the borrower at the cost of the Corporation lacked justification.

Government stated (July 2005) that considering the genuine problem of the entrepreneur, the SLC settled the case against the recommendation of Dy. General Manager. The reply is silent about the inability of the DGM in considering the genuine problems of the entrepreneur.

- Fixed assets of Times Motors, Bhiwadi were taken into possession (October 1995) and auctioned for Rs.32 lakh on 11 March 1999 but on the request of the borrower possession was given back (May 1999) on payment of Rs.10 lakh with assurance to clear the balance dues up to August 2000. The borrower did not make any further payment and possession of the unit was therefore taken back (October 2003). On the request (January 2004) of the borrower, the SLC settled (February 2004) the case for Rs.25 lakh against the outstanding of Rs.47.64 lakh, despite MRV of Rs.47 lakh of assets including land worth Rs. 40 lakh. In view of the possibility of recovery of Rs.47 lakh from disposal of the assets, the decision of the SLC for settlement of case for Rs.25 lakh lacked justification.

Government stated (July 2005) that considering the total payment of Rs.35.02 lakh made by the unit against the loan amount of Rs.18.75 lakh, the Corporation settled the case for Rs.25 lakh. The fact remains that in spite of having an opportunity for recovery of total dues by way of sale of financed assets, the Corporation waived Rs.22 lakh.

- Mohan Metal Industries, Kota defaulted in repayments and, therefore, possession of the unit was taken in September 1990. The unit could not be sold due to litigation. In January 2004, an offer of Rs.25.11 lakh received in auction was not approved for want of current MRV of the assets, which worked out to Rs.27.20 lakh as on 21 January 2004. The amount payable by the borrower on 1 January 2004 was Rs.24.08 lakh. In the meantime the borrower approached the SLC for settlement of his case and handing over possession of the unit. Instead of approving sale of the unit for Rs. 25.11 lakh, SLC settled (March 2004) the account for Rs.12 lakh, which caused loss of Rs.12.08 lakh to the Corporation.

The Government stated (July 2005) that 50 *per cent* interest for the possession period was waived considering that the promoter should not be penalised for the long period the unit remained in possession with the Corporation. The reply is not based on facts as the promoter himself was responsible for litigation in the matter causing non-disposal of unit for a long period.

- Mewar Industrial Corporation having outstanding dues of Rs.1.66 crore (as on October 2001 including interest of Rs.1.31 crore) approached (May 2001) SLC for one time settlement of its dues. It was observed in audit that the SLC settled the case at Rs.1.35 crore ignoring the MRV of assets at Rs.1.91 crore (Land Rs.1.54 crore, Building Rs.22 lakh and Plant & Machinery Rs.15 lakh) assessed by the Corporation causing loss of Rs.31.06 lakh to the Corporation.

Government stated (July 2005) that the Committee while deciding the cases not only takes into consideration the MRV of assets but also factors like, nature of default, status of unit, capacity of promoters, problems faced by the unit etc. The reply is not acceptable as none of these considerations were on record.

Risk management and Internal Control

The Corporation did not design any policy and procedure to identify, assess and control risks.

3.1.22 Operating in a liberalised and globalised environment, the Corporation is exposed to various kinds of risks, and effective risk management is essential for achieving financial soundness and profitability. The Corporation is primarily exposed to Credit risk i.e. risk of defaults in repayments by the loanees due to project failure or otherwise, Market risk i.e. risk of fluctuation in interest rates that may lead to higher interest rate on borrowings, Operational risk involving risk of loss due to clerical errors, organisational deficiencies, delays, fraud, system failure etc and Liquidity risk i.e. the possibility that the Corporation may not meet its maturing commitments or may do so by borrowing at excessive cost. It is a fact that risk cannot be completely eliminated but it should be managed/mitigated through internal controls. The abysmally high level of NPA (paragraph 3.1.9), however, is indicative of the fact that the Corporation did not design any effective policy and procedure to identify, assess and control these risks as discussed below:

- The Corporation did not fix prudent exposure limit for each industry/ sector with a view to diversify its risk. Government stated (July 2005) that in the tough competitive market, it is futile to fix a financing limit for a particular sector. The fact, however, remains that to minimize the risk in case of failure of a particular sector, fixing of exposure limits is essential.

- The Corporation did not design different interest rates to be charged from different borrowers based on the degree of risk associated. Government stated (July 2005) that a high power committee had been delegated power to reduce the rates of interest upto one *per cent* from the prevailing rates based on the background of the borrowers, their past dealing with the Corporation / bank, nature of project and quantum of quality business. The Corporation has, however, not prescribed different parameters along with their weightage for hike/cut in prevailing rate of interest to be charged from a particular project.

To mitigate the operational risk, the internal control system should be made effective. The internal control system of the Corporation, however, was not effective, as would be seen from the following system deficiencies observed in sanction, disbursement and recovery of loans.

- The Corporation did not devise a suitable mechanism for critical examination of viability of projects through market research. It did not maintain updated data bank regarding performance in various industrial units of different sectors in the State. As a result, financial assistance was given to units, which were unviable at the appraisal stage as discussed in paragraph 3.1.13.

- The details of immovable properties of promoters\directors against personal guarantee are furnished in the loan applications. Before accepting personal guarantees, the Corporation neither obtained and verified the title deeds, valuation reports etc. of these properties nor created any charge on these properties for the currency of the loan. Cases noticed in audit where the details of properties were not available with the Corporation have been discussed in para 3.1.17.

- The Corporation did not maintain databank of physical and financial achievements of units financed vis-à-vis projections considered at the time of sanction of loan. During the ARCPSE meeting (July 2005). The Management stated that due to large number of loan accounts, it was not feasible to maintain such data bank. To monitor the progress of assisted units, however, the Corporation should maintain such data bank of the selected units.

- The Corporation not only failed to appoint its directors on the Board of assisted units after 1990 despite being empowered under the SFC Act but also withdrew (September 2000) all such directors appointed earlier. In their absence the Corporation could not effectively watch its interests.

- The Corporation did not ensure receipt of audited annual accounts and periodical returns on physical and financial performance of the units assisted as required under the terms and conditions for grant of loan.

- The Corporation, for knowing the health of the units and for effecting recoveries, had prescribed the norms for inspection of units by different officers at branch/ head office level. But it did not maintain any consolidated records showing details of inspections carried out and action taken on reports of such inspections. CMD of the Corporation in the ARCPSE meeting (July 2005) stated that necessary instructions had been issued to maintain proper records of the visits in future.

- In five cases of rescheduling of loan accounts of Bhilwara city branch, the Corporation did not charge the correct rate of interest and consequently suffered loss of revenue of Rs.17.28 lakh which could not be recovered as the accounts were already closed and the documents released.

Conclusion

Recovery performance of the Corporation was hampered due to sanction of loan to unviable projects, lack of sufficient security and creditworthiness of the promoter, contributing to high level of non-performing assets and lower percentage of recovery against net amount recoverable.

Lack of timely and appropriate recovery action, abnormal delays up to 20 years in disposal of taken over units and absence of recovery action in majority of default cases also contributed to low recovery.

Injudicious settlement of sticky accounts under One Time Settlement sacrificing about 50 *per cent* dues and not taking steps to counter various risks involved in the financing business adversely affected the recovery profile.

Recommendations

The Corporation should:

- **strengthen its project appraisal system so as to avoid/minimize possible risk of default in repayments by the borrowers;**
- **evolve a system of closely monitoring assisted units to ensure timely and speedy recovery of it's dues;**
- **devise a mechanism to avoid delays in taking suitable recovery action under various provisions of the SFC Act;**
- **ensure prompt disposal of units taken into possession to avoid blocking of funds and loss due to depreciation.**
- **determine a time frame to initiate and pursue the cases for recovery of residual amounts;**
- **ensure standarisation and uniformity in settlement of dues so as to recover maximum amount from borrowers with minimum sacrifice; and**
- **adopt risk management techniques to minimize various kinds of risks involved in its business.**