CHAPTER - 4

PERFORMANCE AUDIT (PSUs)

FINANCE DEPARTMENT

4 Working of Jammu and Kashmir Bank Limited

The Jammu & Kashmir Bank Limited (Bank) was incorporated with the objective to establish and carry on business of a banking Company; borrow or raise money; to lend money by making loans and advances; to buy, sell, collect and deal in bills of exchange, hundies, promissory notes, drafts, bills of lading, debentures and other instruments; to deal in stocks, shares, debentures, securities and investment of all kinds; to buy and sell foreign exchange including foreign notes; and to act as agents for Government or local authorities. A performance audit of the activities of Bank for the period 2013-14 to 2017-18 was conducted, highlights of which are:

Highlights

- **The Bank had not complied with the SEBI Regulations and some of the provisions of Companies Act, 2013 relating to corporate governance.**

  (Paragraphs: 4.5.1 & 4.5.2)

- **Profit earned by the Bank declined from ₹1,182.47 crore during 2013-14 to ₹202.72 crore in 2017-18, mainly due to increase in the Gross Non-Performing Assets (NPAs) of the Bank from ₹643.77 crore, as on 31 March 2013 to ₹6,006.70 crore, as on 31 March 2018. Percentage of NPAs to Gross Advances also increased from 1.62 *per cent* at the end of March 2013 to 9.96 *per cent* at the end of March 2018. The Bank also suffered a loss of ₹1,632.29 crore during 2016-17.**

  (Paragraph: 4.6)

- **The Bank's credit control system and financial reporting system failed to identify NPAs in time.**

  (Paragraphs: 4.6.1 & 4.6.2)

- **Although there had been 24.58 *per cent* growth in deposits during 2013-14 to 2017-18, annual growth of deposits of Bank during last four years ending March 2017 was far below overall National average of Scheduled Commercial Banks.**

  (Paragraph: 4.7.2)

- **The Bank had recorded an increase of 51.30 *per cent* in advances during 2013-14 to 2017-18, annual growth fluctuated between (-) 1.78 *per cent* and 18.28 *per cent*. Percentage of unsecured advances to total net advances had increased from 20.16 *per cent* at the end of March 2014 to 27.90 *per cent* at the end of March 2018.**

  (Paragraph: 4.7.3)

- **The Bank's concentration risk for industry-wise exposure was on higher side when compared to average of overall banking industry.**

(Paragraph: 4.7.4 (i))

- **Sanction/ release of credit facilities, without safeguarding the Bank's interest through adequate security cover, proper credit appraisal, adherence to the pre or post-disbursement conditions of the sanctions, regular monitoring, etc. not only led to NPAs but also loss/ non-recovery of ₹197.98 crore, doubtful recovery of ₹1,599.14 crore and excess payment of ₹14.10 crore in test-checked cases.**

(Paragraph: 4.7.5.2)

- **Deficiencies were noticed in Information Technology systems of the Bank due to which it could not ensure technology based solutions for some of its operations.**

(Paragraph: 4.7.6)

- **Sanctioning of one-time settlement in deviation of Bank's recovery policy resulted in sacrificing of principal amount of ₹17.97 crore in test-checked cases.**

(Paragraph: 4.7.9.1)

- **The Bank sold ten NPAs to Asset Reconstruction Companies (ARCs) during the period 2014-2018 by sacrificing principal amount of ₹671.10 crore and unapplied interest of ₹504 crore. Sale of financial asset to ARC below the reserve price resulted in loss of ₹21.89 crore.**

(Paragraph: 4.7.10)

- **Imprudent decision-making, non-invoking of guarantee and non-safeguarding of Bank's interest led to doubtful recovery/ loss of ₹180.43 crore in test-checked Non-Performing Investments.**

(Paragraph: 4.7.11.2)

- **Irregularities in recruitment of Relationship Executives and Banking Associates were noticed.**

(Paragraph: 4.10.1)

- **Bank had spent 53.09 *per cent* to 83.82 *per cent* of CSR budget during 2016-17 and 2017-18 on a single activity/ project and had also incurred 49.33 *per cent* to 95.27 *per cent* under a single segment during 2015-16 to 2017-18, which was in violation of CSR policy. Further, in contravention to Bank's CSR policy and Companies Act 2013, an irregular expenditure of ₹46.96 crore was incurred out of CSR fund.**

(Paragraph: 4.11)

4.1 Introduction

The Bank was incorporated in October 1938 under the provisions of the then Jammu & Kashmir Companies Regulations of 1977 Samvat (1920 AD) and commenced its business from 04 July 1939. After extension (November 1956) of the Companies Act, 1956 to the State of J&K, the Bank became a Government Company in terms of section 617 of the Companies Act, 1956 and is now governed by provisions of Companies Act, 2013. The Reserve Bank of India (RBI) notified (1971) the Bank as a Scheduled Commercial Bank and included it in Second Schedule to RBI Act, 1934. The Bank is also regulated by RBI Act, 1934 and Banking Regulation Act, 1949.

The J&K Bank was established to carry out the business of banking Company – borrowing, raising or taking up of money, lending and advancing of money, acting as agents of government or local authorities. It also seeks to deliver financial solutions for household, small and medium enterprises.

4.2 Audit objectives

The audit objectives were to assess:

- the achievement of targets and growth of Deposits;
- the growth of Advances, the efficacy of monitoring system of Advances, implementation of NPA Recovery Policy and One Time Settlement Scheme;
- the implementation of Investment policy of Bank and the extent of growth of Investment vis-a-vis income;
- the achievements of the targets under Priority Sector Lending as fixed by the RBI and the Bank's performance as Lead Bank; and
- whether the provisions of various Acts/ regulations governing the Bank with regard to the areas covered under the audit have been complied with.

4.3 Audit scope and methodology

A performance audit of the working of the Bank covering the period from the year 2013-14 to 2017-18 was conducted between February and June 2018. For assessing the performance of the Bank, records at Corporate Office and five zones[1] (selected on the basis of funds advanced and NPAs) were scrutinised. As audit findings discussed herein are in respect of sample zones selected for test check in audit, the management may like to exercise similar checks over its total area of action/ operations. The audit objectives were discussed (February 2018) with Management. The audit findings were reported to Management and discussed (December 2018) in an exit conference.

A Performance audit of the core activities of the Bank viz., Advances, Priority Sector Lending and Investments was incorporated in the Report of the Comptroller and Auditor General of India (C&AG) for the year ended 31 March 2011. The audit findings were partially discussed by the Committee on Public Undertakings (COPU) of the State Legislature. Its recommendations are awaited.

[1] Jammu Central-I, Kashmir Central-I, Mumbai, Delhi and Bangalore covering 272 branches

4.4 Audit criteria

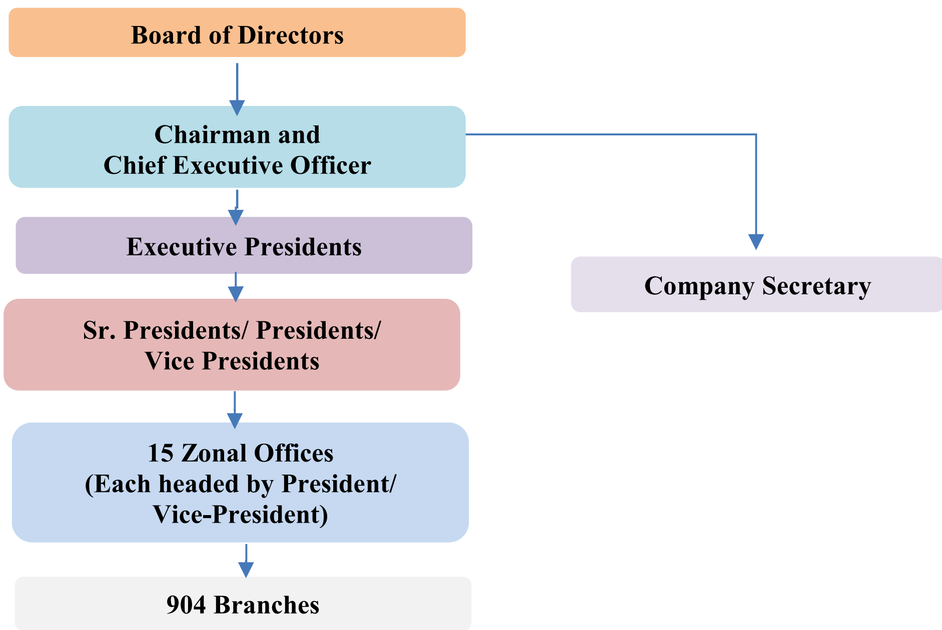
The audit findings were evaluated against criteria sourced from:

- Reserve Bank of India Act, 1934 and guidelines/ master circulars issued from time to time;
- Bank's policies on Credit, Investment, Recovery of NPA, One Time Settlement etc.;
- Banking Regulation Act, 1949, Companies Act, 2013;
- Listing Agreement and Regulations of Securities Exchange Board of India (SEBI);
- Internal targets fixed by the Bank and targets fixed by State Level Bankers Committee;
- Guidelines of Central/ State and Lead Bank Schemes.

4.5 Corporate Governance

The Management of the Bank is vested in a Board comprising of 13 Directors[2] including the Chairman and Chief Executive Officer. As on 31 March 2018, the Bank had 15 zonal offices[3] controlling 904 Branches in 20 States and one Union Territory. During 2014-18, the Bank expanded its network by opening 220 new branches while one branch was closed. The Organisational structure of the Bank is as under:

Chart-4.1: Organisational structure



[2] Four non-independent non-executive Directors; one RBI nominee; one Government nominee, one executive Director of the Bank and six independent non-executive Directors appointed by the shareholders in the Annual General Meeting

[3] Kashmir-Central-I, Kashmir-Central-II, Kashmir-North, Kashmir-South-I, Kashmir-South-II, Jammu-Central-I, Jammu-Central-II, Jammu-North-I, Jammu-North-II, Jammu-West, Ladakh, North-Delhi, Upper North- Mohali, Mumbai, South-Bangalore

4.5.1 Non-compliance with SEBI Regulations

A Company includes various stakeholders viz. investors, shareholders, customers, employees, vendor partners, government and society. Its objective is not confined to maximizing the shareholder value but should be responsible to all stakeholders. Its governance should be fair and transparent to all stakeholders in all its transactions.

J&K Bank is a listed entity on the major stock exchanges – National Stock Exchange and Bombay Stock Exchange. For a Company to be listed on stock exchange, it has to sign an agreement which is known as Listing Agreement, the main purpose of agreement is to ensure that companies are following good corporate governance. The essence of good corporate governance is derived from Clause 49 of Listing Agreement, SEBI (Listing Obligations and Disclosures Requirements) Regulations 2015 (LO&DR) on Corporate Governance. It was observed that the Bank deviated from the criterion as under:

i) Independent Directors on the Board

In terms of Clause 49 of Listing Agreement and Regulation 17 of SEBI (LO&DR) Regulations 2015, where the Chairman of the Board of Directors (BODs) is an executive Director, at least half of the Board should comprise of independent Directors. However, the Bank did not have the required number of independent Directors on the Board during 2013-14, 2014-15 and 2016-17 as detailed in **Table 4.1** below:

Table 4.1- Position of Independent Directors

Year	2013-14	2014-15	2015-16	2016-17	2017-18
Required number of independent Directors	5	5	5	4	6
Actual number of independent Directors	Nil	3	6	2	6

The Management replied (August 2018) that the Bank could not appoint required number of independent Directors during 2014-15 and 2016-17 due to restriction imposed under the Articles of Association (AOA) of the Bank.

The reply is not tenable as the responsibility to amend AOA so as to ensure appointment of requisite number of independent Directors rested with the Bank's Board.

In absence of requisite number of independent Directors on the Board, good corporate governance and corporate creditability, as discussed in succeeding paragraphs, could not be ensured in the Bank.

ii) Credit facilities availed by Independent Director

Section 20(1)(b)(i) &(ii) of the Banking Regulation Act, 1949 prohibits the banking Company to grant any loan or advance to or on behalf of any of its Directors or any firm in which any of its Directors is interested as partner, manager, employee or guarantor. Further, as per Regulation 16(1)(b)(vi)(E), an independent Director is one who is not a material supplier, service provider or customer or a lessor or lessee of the listed entity.

The Board of Directors in its meeting dated 10 August 2016, upon the recommendations of the Nomination Committee of the Board based on its due diligence, appointed Mr. Mohammad Ashraf Mir as independent Director of the Bank to fill up the casual vacancy caused due to resignation of two Directors. Consequently, the shareholders of the Bank in their meeting held on 17 June 2017 appointed him as independent Director on the Board of the Bank for a period of two years i.e. up to 16 June 2019. Furthermore, the Board recommended (June 2019) his re-appointment for a further period of two years as independent Director.

The Bank appointed Mr. Mir as an independent Director on the Board despite the fact that he was availing fund based credit facilities[4] from the Bank during the period between August 2016 and June 2019. This was in violation of provisions of Banking Regulation Act, 1949 and SEBI Regulations of 2015. This may be viewed in light of the fact that the Nomination Committee of the Board carried out (August 2016) due diligence to determine his suitability for directorship of the Bank.

The Management replied that Mr. Mir was having a working capital facility with the bank at the time of his appointment as independent Director and the same was not renewed after his appointment and the drawing power in the account was reduced to zero, which is in conformity with section 20(1)(b)(iii) and Section 20(2) of Banking Regulation Act 1949. Keeping in view his relationship with the Bank, the Director maintained his Cash Credit (CC) account as Current Deposit (CD) account without availing any credit facility from the bank.

Though the CC account of Mr. Mir was not renewed after his appointment, the drawing power of CC account was not reduced to zero as evident from the fact that fresh debits in CC account were raised even between December 2016 and August 2017. Further, there was outstanding amount of ₹9.62 lakh in Working Capital Term Loan as of July 2019. This may be viewed in light of Regulation 16(1)(b)(vi)(E) which stipulates that an independent Director is one who is not a customer of the listed entity.

iii) Audit Committee of the Board headed by non-independent Director

Clause 49 of Listing Agreement and Regulation 18(1)(d) of SEBI (LO&DR) Regulations, 2015 stipulated that Chairman of the Audit Committee shall be an independent Director.

Audit observed that in violation of the provisions the Chairman of the Audit Committee for the years 2013-14, 2014-15 and 2016-17 was a non-independent Director.

Since the independency of Audit Committee was compromised, the Committee could not exercise proper oversight over the Bank's financial reporting process as discussed in paragraphs 4.6.1 and 4.6.2.

[4] Cash Credit facility, Working Capital Term loans and Secured Overdrafts with balance of ₹1.64 crore as of August 2016

iv) Audit Committee's discussion with statutory auditors

Clause 49 of Listing Agreement and SEBI (LO&DR) Regulations, 2015 stipulated that the Audit Committee should hold discussion with statutory auditors before commencement of audit about the nature and scope of audit as well as hold post-audit discussion, to ascertain any area of concern.

Audit Committee did not hold discussion with Statutory Auditors before commencement of Audit during 2014-18.

Audit Committee of the Bank did not hold discussion with statutory auditors before commencement of audit about the nature and scope of audit during 2014-2018.

The Management stated (December 2018) that pre-audit discussions on special areas were held with the central statutory auditors by the Chief Financial Officer (CFO) and top management of the Bank before the accounts are forwarded to them for the purpose of audit.

The meeting of the statutory auditors with the CFO and management before commencement of audit is not the same as meeting with the Audit committee, two-thirds of which have to be independent Directors. The opportunity available to the Committee for independent examination of audit concerns and ascertain opinion of the statutory auditors on specific areas of interest was thus not utilized.

v) Non-review of Whistle Blower Mechanism

The above cited regulations stipulated review of the functioning of the 'Whistle Blower Mechanism'[5] by the Audit Committee. However, the Audit Committee had not reviewed the functioning of the 'Whistle Blower Mechanism' during 2014-2018.

The Management replied (December 2018) that in future the Board will review all policies of the Bank, including the Whistle blower policy of the Bank.

vi) Nomination and Remuneration Committee

Clause 49(IV)(A) of Listing Agreement and Regulation 19(1) and (2) of SEBI (LO&DR) Regulations, 2015 stipulated that each Company shall constitute Nomination and Remuneration Committee (NRC) and its Chairman shall be an independent Director.

However, the Chairman of NRC was a non-independent Director during the years 2014-15 and 2016-17. Further, the NRC was required to recommend to the Board a policy, relating to the remuneration for Directors. However, no such recommendation was made by the NRC with regard to payment of remuneration to Government nominee Director as discussed under paragraph 4.5.3 (ii) of the report.

vii) Meeting of independent Directors

Regulation 25 of SEBI (LO&DR) Regulations, 2015 required that independent Directors shall meet at least once in a year, without the presence of non-independent

[5] An act of disclosing whatever employee or former employee believes to be unethical in nature or illegal behavior in an organization to the higher management or to any external authority or to the public

Directors and shall review (a) Performance of non-independent Directors (b) Performance of Chairperson and (c) Assess the flow of information between management and BODs.

However, independent Directors did not conduct such meeting during 2018 and had not reviewed the performance of non-independent Directors and Chairman for the year 2017-18. We also observed that evaluation reports on performance of non-independent Directors/ Chairman had not been placed before the Board of the Bank for review.

The Management stated (August 2019) that the words 'in a year' were replaced (July 2017) with the word 'in a financial year' in Schedule IV (VII) (1) of the Companies Act, 2013. Accordingly, Independent Directors Meeting for financial year 2018-19 was held on 26 March 2019.

However, the independent Directors did not meet during the period between January 2018 and February 2019 with the result the performance of non-independent Directors and Chairman for the year 2017-18 could not be reviewed.

viii) Evaluation of performance of independent Directors

Regulation 17 (10) of SEBI (LO&DR) Regulations, 2015 stipulated that the BODs shall evaluate the performance of independent Directors.

However, the BODs of the Bank had not evaluated the performance of independent Directors for the year 2016-17. It was also observed that evaluation reports on performance of independent Directors for the years 2015-16 and 2017-18 had not been placed before the Board for review.

4.5.2 Non-compliance with the provisions of the Companies Act, 2013

The following provisions of the Companies Act, 2013 had not been complied with:

i) Approval of financial statements by the Board

In terms of the provisions of Section 134(1) of the Companies Act, the financial statements of the Bank should have been approved by the Board of Directors before they are signed on behalf of the Board and sent to Statutory Auditors. The Bank had not complied with these provisions and had placed the audited financial statements before the Board.

Since the draft financial statements were not got approved from the Board, the Bank's Board was not aware of the fact that the Bank downgraded advances as Non-Performing Assets only after the same were identified by the Statutory Auditors as discussed in paragraph 4.6.2.

ii) Non-placing of Annual Report in the State Legislature

The Bank had not been forwarding its annual report on its working and affairs to the State Government to enable its placement in the State Legislature, as required under provisions of Section 395 of the Companies Act, 2013.

Thus, the State Legislature could not monitor the accounting and utilisation of investments made by the Government in the Bank.

iii) Notices of Annual General Meetings

Section 136 (1) of the Companies Act, 2013 required that a copy of the financial statements, auditor's report and every other document required by law to be annexed or attached to the financial statements, which were to be laid before a Company in its general meeting, shall be sent to every member of the Company not less than 21 days before the date of the meeting. However, the comments of C&AG of India were not sent to the shareholders while sending notice of Annual General Meeting (AGM) for the year 2017-18.

iv) Non-inclusion of comments of C&AG in the Annual Report

Section 143 (6) of the Companies Act, 2013 required that any comments given by the C&AG upon, or supplement to, the Statutory Auditor's report will be placed before the Annual General Meeting of the Company at the same time and in the same manner as the Audit Report. However, the comments of C&AG were not included in the Annual Report for the year 2017-18.

The Management stated (August 2018) that the comments of C&AG of India were not available at the time of sending notice to shareholders and the same were supplied to all shareholders at AGM and were read out by Company Secretary of the Bank.

The Bank sent notices for AGM to its shareholders without waiting for the comments of C&AG of India.

v) Appointment of Chief Financial Officer

Section 203 of the Companies Act, 2013[6] stipulated that every listed Company shall have a Chief Financial Officer (CFO). Further, the RBI advised (May 2017) all scheduled commercial banks to appoint CFO in banks management structure with a minimum qualification and experience. The Regulator prescribed that only a qualified Chartered Accountant should be appointed as CFO.

However, the Bank did not appoint any CFO during the period between 1 April 2014 and 16 May 2015, thereby contravening the provisions of Companies Act, 2013. We further noticed that CFOs appointed between July 2017 and June 2019 were not qualified Chartered Accountant and did not meet the qualification criteria as fixed (May 2017) by the Regulator.

4.5.3 Board Meetings

The following observations with regard to meetings of Board of Directors were also made:

[6] Applicable from 1 April 2014

i) Participation of nominee Directors in Board meetings

The Government of Jammu and Kashmir (GoJK), being majority shareholder of the Bank, appoints[7] one nominee Director on Board of the Bank. Further, the RBI also appoints[8] one additional Director on Board of the Bank.

The Government Nominee Director (Principal Secretary, Finance, GoJK) attended 40 *per cent* and 55 *per cent* Board meetings held during 2013-14 and 2014-15, respectively. Further, RBI nominee had attended 64 *per cent*, 60 *per cent*, 58 *per cent* and 67 *per cent* of the Board meetings held during 2014-15, 2015-16, 2016-17 and 2017-18, respectively. Records also showed that the Government nominee Director had not recorded any dissent note in the Board meetings with regard to unsound decisions taken by the Board viz., irregular expenditure under CSR activities, sanctioning of credit facilities in deviation to Bank's credit policy and One Time Settlement in favour of defaulters in contravention of recovery policy of the Bank etc. as discussed in succeeding paragraphs.

The Management stated (August 2019) that the Nominee Directors having important assignment at the Government/ RBI level may have skipped Board/ Committee Meeting. However, minutes of Board/ Committee meetings are sent to the concerned Directors.

However, the purpose of appointment of a nominee Director to represent and safeguard the interest of the nominator and to play the role of a 'watchdog' in monitoring the activities and operations of the Bank could not be achieved.

ii) Remuneration to Government nominee Director

The Articles of Association (AOA) of the Bank was amended (July 2016) in 78th Annual General Meeting (AGM) of the shareholders to allow remuneration to Government nominee Director. Consequently, remuneration[9] of ₹58.80 lakh[10] was paid to the Government nominee Director during 2016-17 to 2018-19.

However, the payment of remuneration to the nominee Director (Principal Secretary, Finance, GoJK) was not in line with the best practices followed by various Government Companies/ PSU Banks viz., National Thermal Power Corporation Limited, National Hydroelectric Power Corporation Limited, Indian Oil Corporation Limited, State Bank of India, Punjab National Bank etc. Records further showed that amendment of the AOA in the AGM of the shareholders had been carried out without the approval of the Board.

> Sitting Fee and commission as percentage of profit amounting to ₹58.80 lakh was paid to the Government nominee Director during 2016-17 to 2018-19.

[7] Section 161(3) of the Companies Act, 2013 stipulates that the BOD may appoint any person as a Director who is nominated by the State Government by virtue of its shareholding in a Government company

[8] Section 36AB of the Banking Regulation Act, 1949 empowers the RBI to appoint additional Director on the Board of the Bank

[9] Sitting fee and commission as percentage of profit

[10] 2016-17: ₹16.30 lakh; 2017-18: ₹14.10 lakh; 2018-19: ₹28.40 lakh

After being pointed out by audit, the Bank amended (September 2019) the AOA to dispense with payment of remuneration to Government Nominee Directors (with full time Government employment) on board of the Bank. The matter has also been taken up with the Chief Secretary, Government of Jammu & Kashmir to examine whether the payments made were in consonance with Fundamental Rules and Supplementary Rules (FR & SR) and whether remuneration was accepted by the nominee with due approval/ knowledge of the Government. Reply is awaited (December 2019).

iii) Placing of significant issues as tabled-items before the Board

The Notes on Agenda explain each item of the Agenda in an endeavour to provide an understanding of proposal for discussion by the Board. If the Directors are to perform their duties effectively, actively contribute to the deliberations of the Board, and take informed decisions, it is necessary that they receive adequate information sufficiently in advance of the meeting. Although there is no prohibition on tabling the agenda items before the Board without sending of agenda and notes to the Directors, as a matter of best practices proposals on significant issues should not be placed before BOD as tabled items. However, records showed that certain significant issues viz., sanctioning of credit facility of ₹100 crore, approval of Strategic Debt Restructuring package in favour of a Company, approval for spending money on redevelopment of Golf course under CSR, One Time Settlement of NPA cases, confirmation of Chairman's action of appointing employees on contractual basis and their regularization, modification in recruitment rules etc. were placed before the Board as tabled items. The matter regarding tabled agenda items was also highlighted by the independent Directors of the Bank, while assessing the flow of information between management and BODs, in their meeting in March 2019.

The Management stated (August 2019) that efforts are being made to reduce tabled agenda to the minimum.

The Bank management should avoid placing significant proposals before the BOD as tabled items.

iv) Agenda and minutes of meetings of Board of Directors

The independent Directors, in their meeting in March 2019, highlighted that agenda notes of meetings of Board of Directors were unreasonably voluminous rather than well-structured documents with analysis and agenda items were not prioritized considering their importance. Further, timelines fixed for complying with directions of the Board were not recorded in the minutes of meetings.

The Management stated (August 2019) that compliance to all the decisions of the Board are reported to the Board in the subsequent meetings through Action Taken Reports.

The reply of the Bank is not tenable as quality of the agendas left a lot to be desired and no timeline was fixed for compliance of Board decisions.

v) Bifurcation of post of Chairman and Chief Executive Officer of the Bank

In order to bring in appropriate checks and balances and to ensure accountability at the Board level, the Government of India decided (April 2015) to separate the post of Chairman and Managing Directors in Public Sector Banks. While the Chairman would be non-executive and give overall policy directions to the Bank, the Managing Director and Chief Executive Officer would be the executive head and responsible for day-to-day management. Further, most of the Private Sector Banks in the country had already separated the post of Chairman and Managing Directors in accordance with the recommendations of Report of the Consultative Group of Directors of Banks/ Financial Institutions, constituted by RBI in April 2002.

It was noticed that the Board of Directors of the Bank had belatedly recommended (June 2019) for splitting the post of Chairman and Managing Director which indicated Bank's lackadaisical approach in ensuring good corporate governance.

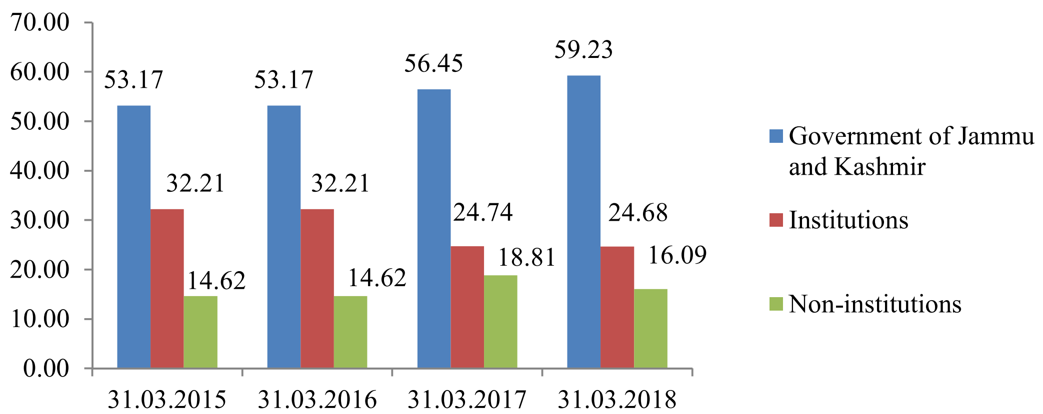
The Management stated (August 2019) that RBI advised (April 2008) the Bank to initiate action for splitting of the posts of Chairman and Chief Executive Officer. However, the Bank sought exemption from the directive issued but did not receive any response from RBI. Subsequent appointments to the post continued to be approved by the RBI.

The reply is not tenable, as timely action for bifurcation of posts for better governance was not taken despite advice of Regulator.

4.6 Financial position and working results

As on 31 March 2018, against an authorized share capital of ₹95 crore divided into 95 crore shares of ₹one each, the paid-up capital was ₹55.70 crore. Of this, the share of GoJK was ₹32.98 crore, Institutions[11] was ₹13.74 crore and Non-institutions[12] was ₹8.98 crore. During 2016-17 and 2017-18, the GoJK infused amount of ₹250 crore and ₹282 crore against which the Bank allotted 3,65,55,051 and 3,55,25,321 shares having face value of ₹one each to the GoJK at premium of ₹67.39 and ₹78.38 per share, respectively. This had resulted in increase in the shareholding of GoJK from 53.17 *per cent* by end of March 2015 to 59.23 *per cent* by end of March 2018 as depicted in the **Chart-4.2** below:

Chart-4.2: Shareholding Pattern (*in percentage*)



11 Including Foreign Institutional Investors

12 Including Resident and Non-Resident Individuals and including ₹0.02 crore amount of forfeited shares

The Bank had drawn its annual accounts in accordance with the provisions of Section 29 of the Banking Regulation Act, 1949 read with Section 133 of the Companies Act, 2013.

A) Financial position

The financial position of the Bank as per its audited annual accounts for the five years ending 31 March 2018 is given in ***Appendix-4.1.1***.

The Net Worth[13] of the Bank which was ₹5,723.61 crore as on 31 March 2014 increased to ₹6,423.97 crore as on 31 March 2016 and was ₹5,676.50 crore as on 31 March 2017, due to loss of ₹1,632.29 crore reported during 2016-17. The net worth increased to ₹6,161.21 crore as of 31 March 2018 due to profit of ₹202.72 crore and allotment of shares at premium during 2017-18. The fixed assets of the Bank had increased from ₹533.80 crore by end of March 2014 to ₹1,614.59 crore by end of March 2018. Out of increase of ₹1,080.79 crore recorded during this period, appreciation of ₹634.81 crore was on account of revaluation of fixed assets carried out by the Bank during 2016-17.

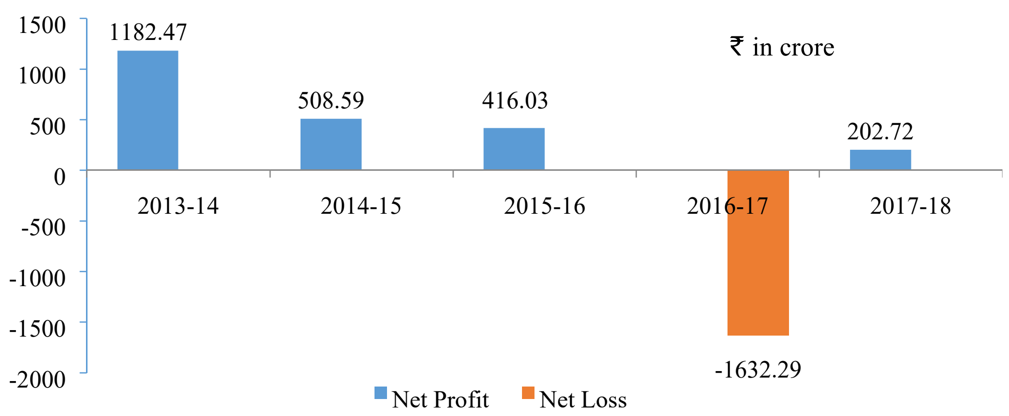
B) Working results

The working results of the Bank as per audited annual accounts for the five years ending 31 March 2018 are given in ***Appendix-4.1.1***. The Bank earned profits of ₹1,182.47 crore during 2013-14. It reported loss of ₹1,632.29 crore in 2016-17 due to creation of provision of ₹2,115.93 crore against NPAs. The Bank earned profit of ₹202.72 crore in 2017-18. The earnings per share of the Bank declined from ₹24.39 in 2013-14 to ₹3.64 in 2017-18.

- The Bank earned net profit of ₹202.72 crore in 2017-18.
- The net worth increased from ₹5,723.61 crore as on 31 March 2014 to ₹6,161.21 crore as on 31 March 2018.

The Bank's profitability during the last five years ending 31 March 2018 is shown in **Chart-4.3** below:

Chart-4.3: Profitability of the Bank



13 Net worth is aggregate of paid up share capital and reserves and surplus

The reasons for declining profitability are attributable to increase in Gross NPAs of the Bank. The Bank had gross NPAs of ₹643.77 crore as on 01 April 2013 rising to ₹6,000.01 crore as on 31 March 2017 and ₹6,006.70 crore on 31 March 2018. The percentage of NPAs to Gross Advances increased from 1.62 *per cent* at the end of March 2013 to 9.96 *per cent* at the end of March 2018. As a result of increase in NPAs over the period of five years, the Bank made higher provisions which affected its profitability.

During the year 2016-17, the Bank suffered loss of ₹1,632.29 crore mainly due to provisioning of ₹2,115.93 crore against NPAs including additional provision of ₹517.40 crore (pertaining to 2015-16) made due to divergence pointed out by RBI.

Further, Profits for the year 2017-18 had been overstated by ₹85.63 crore on account of under-provisioning as discussed in Para 4.6.1 below.

4.6.1 Under-Provisioning against Non-Performing Assets

As per prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances (IRAC) formulated by RBI, the Bank was required to classify the advances. An asset becomes a Non-Performing Asset (NPA) if it remains overdue for 90 days. Further, as per IRAC norms (July 2015), a Bank is required to make provisions against NPAs (outstanding amount) as per the classification of assets[14] viz. sub-standard, doubtful and loss asset.

- In doubtful category, the Bank had to provide for 100 *per cent* of the extent to which the advance is not covered by realistic realisable value of the security.
- For the secured portion, provision at the rates[15] depending upon the period for which the asset had remained doubtful, has to be made.

A test-check of NPA cases as on 31 March 2018, revealed that in three cases (out of 27 test-checked) as detailed in **Table-4.2** below, as per prescribed norms provision of ₹226.81 crore was required to be kept. However, the Bank had made a provision of only ₹141.18 crore, thereby leading to under-provisioning of ₹85.63 crore.

[14] An asset is classified as sub-standard which remains non-performing upto a period of twelve months. Assets which are non-performing for period above 12 months are classified as doubtful. A loss asset is one which is identified by either the Bank or the external/ statutory auditors or by the RBI inspection

[15] When the doubtful period is up to one year (DF-I): provision of 25 *per cent* of secured portion of advance is required; When the doubtful period is from one to three years (DF-II): provision of 40 *per cent* of secured portion of advance is required; When the doubtful period is more than three years (DF-III): provision of 100 *per cent* of secured portion of advance is required

Table-4.2: Details of test-checked under provisioned cases

(₹ in crore)

Particulars of the NPA	Outstanding (NPA) as of March 2018 (A)	Realisable value of securities (B)	Provision to be created[16] (C)	Provision actually created (D)	Under-provisioned amount[17] (E)
M/s ETA Engineering Private Limited	174.86	76.87	128.74	69.94	58.80
M/s Paradise Avenue	156.47	118.16	85.57	62.59	22.98
M/s Trumboo Trading Company	21.61	15.18	12.50	8.65	3.85
Total	**352.94**	**210.21**	**226.81**	**141.18**	**85.63**

(Source: Calculations based on the information provided by the Bank)

The Management replied (August 2018) that provisioning statements are being generated by the Management Information System Department and provisioning in case of NPA accounts is done as per security details. They added (December 2018) that in two[18] NPA cases, the security details in bank database had not been updated timely while finalizing the annual accounts for the year ended 31 March 2018. The database has since been updated.

The RBI guidelines for asset classification and provisioning were not adhered to which indicates deficiencies in the financial reporting system of the Bank as discussed in succeeding paragraph.

4.6.2 Divergence in asset classification and provisioning

The RBI assesses compliance by banks with IRAC norms as part of its supervisory process. Further, in order to ensure greater transparency, promote better discipline and compliance with IRAC norms, RBI directed (April 2017) all the banks to make suitable disclosures in the financial statements wherever either (a) the additional provisioning requirements assessed by RBI exceed 15 *per cent* of the published net profits after tax for the reference period or (b) the additional Gross NPAs identified by RBI exceed 15 *per cent* of the published incremental Gross NPAs for the reference period, or both. There was divergence in reporting of NPAs by the Bank for the years 2015-16 and 2016-17, as detailed in the **Table-4.3** below:

Table-4.3: Divergence in reporting of NPAs by the Bank

(₹ in crore)

Sl. No.	Particulars	2015-16	2016-17
1.	Gross NPAs as on March 31 as reported by the Bank	4,368.62	6,000.01
2.	Gross NPAs as on March 31 as assessed by RBI	6,252.32	6,909.00
3.	**Divergence in Gross NPAs (2-1)**	**1,883.70**	**908.99**
4.	Provisions for NPAs as on March 31 as reported by the Bank	2,111.80	3,425.29
5.	Provisions for NPAs as on March 31 as assessed by the RBI	2,629.20	3,546.48
6.	**Divergence in Provisioning (5-4)**	**517.40**	**121.19**
7.	Reported Net Profit After Tax (PAT) for the Year ended March 31	416.04	(1,632.29)
8.	Adjusted (notional) Net Profit After Tax (PAT) after taking into account the divergence in provisioning	(101.36)	(1,753.48)

16 C=100 *per cent* of (A-B) + 40 *per cent* of B

17 E=(C-D)

18 M/s Paradise Avenue and M/s Trumboo Trading Company

Bank had reported Gross NPAs of ₹4,368.62 crore at the end of March 2016 and ₹6,000.01 crore at the end of March 2017 and made provisions amounting to ₹2,111.80 crore and ₹3,425.29 crore, respectively. However, the RBI had assessed Gross NPAs of ₹6,252.32 crore at the end of March 2016 and ₹6,909 crore at the end of March 2017, thereby resulting in divergence of 43.12 *per cent* and 15.15 *per cent* during 2015-16 and 2016-17, respectively. As a result of divergence pointed out by RBI, the Bank had to make additional provisioning of ₹517.40 crore (pertaining to 2015-16) and ₹121.19 crore (pertaining to 2016-17) in the financial statements for 2016-17 and 2017-18, respectively.

Records further revealed that the advances of ₹246.89 crore in 2015-16, ₹936.56 crore in 2016-17 and ₹305.19 crore in 2017-18 constituting 11.56 *per cent*, 40 *per cent* and 10.90 *per cent* of the total NPAs were classified as NPAs only after the same were identified by the Statutory Auditors.

The Management replied (December 2018) that in order to ensure proper and timely identification of NPAs, the Bank has in place a system level asset classification wherein the accounts are automatically downgraded as per their asset class on monthly basis from the effective date of the asset being downgraded. Further, a special credit monitoring cell at the apex level and at the zones had been set up (2016) to ensure the asset classification of these accounts, as per the regulatory norms.

However, despite having a system level asset classification, special credit monitoring cell at apex level and at the zones, there was huge divergence in asset classification and provisioning as reported/ noticed by the RBI/ statutory auditors.

Thus, the Bank's credit control system and financial reporting system failed to identify the NPA accounts in time which is indicative of the fact that the Audit Committee of the Board did not exercise proper oversight over the Bank's financial reporting process. The Bank needs to review the current asset classification system to identify and rectify the gaps leading to under reporting of NPA accounts.

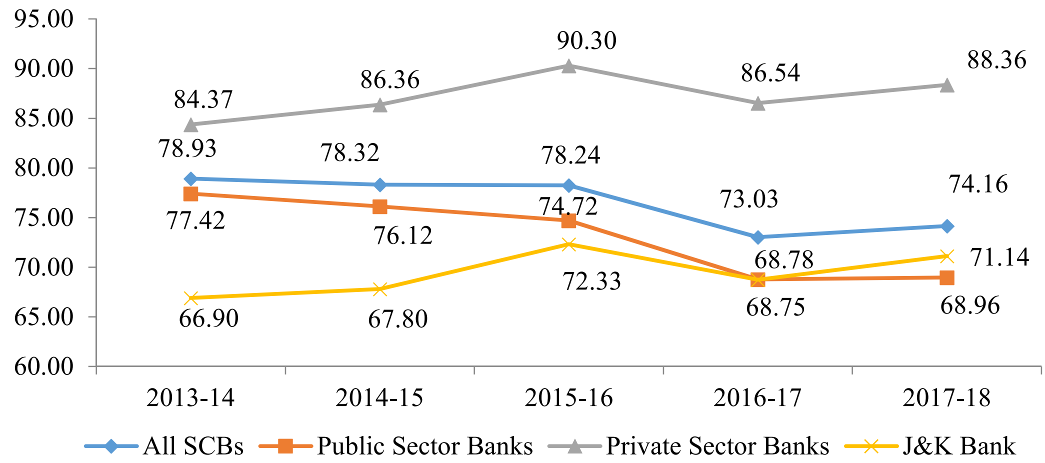
4.7 Banking operations

One of the important functions of the Bank is to accept deposits from the public for the purpose of lending. The Bank accepts deposit from customers through various forms viz., term deposits, savings bank deposits, current account deposits, etc. Interest payments are made by the Bank to the customers on their deposits. Advances granted by commercial banks take various forms such as term loans, cash credit, overdrafts, purchase or discounting of bills, etc. Interest on Advances is major source of income for a banking Company.

4.7.1 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. CD Ratio of the Bank during 2013-14 to 2017-18 detailed in **Chart-4.4** below remained below the overall National average of Scheduled Commercial Banks (SCBs).

Chart-4.4: Credit Deposit Ratio-Comparison



(Source: Reports of Reserve Bank of India)

Zone-wise analysis of data revealed that during 2017-18, the CD Ratio in Jammu Central-I and Kashmir Central-I remained as low as 25.28 *per cent* and 52.40 *per cent*, respectively. In comparison, CD Ratio remained as high as 350.19 *per cent* in Bangalore Zone, 844.21 *per cent* in Mumbai Zone and 230.78 *per cent* in Delhi Zone during 2017-18.

As depicted in Table-4.5, the deposits within the State had grown from ₹45,193.38 crore in March 2014 to ₹71,472.00 crore in March 2018. However, poor CD ratio within the State indicated that the Bank had not been able to advance the funds within the State commensurate to the deposits raised within the State. Instead, the funds were raised from within the State and advances were made outside the State. With this approach, the Bank may not succeed in fulfilling its vision to engender and catalyse economic transformation of Jammu and Kashmir.

The Management attributed (December 2018) the low CD ratio in the State zones during 2016-17 to inflow of large deposits during the implementation of demonetisation in Q3 of the financial year.

The reply of management is not tenable as the effect of demonetization in the year 2016-17 was evident for all SCBs. The fact remained that the CD ratio of J&K Bank remained the lowest in four out of the five years among all the categories compared.

The deposits and advances are discussed in detail in the succeeding paragraphs.

4.7.2 Deposits

The position of Deposits of the Bank and targets achieved during 2013-14 to 2017-18 is given in **Table-4.4** and **Table-4.5**.

Table-4.4: Year-wise growth of deposits

(₹ in crore)

31 March of Year	Deposits	Year over Year Growth	Growth rate (*per cent*) of the deposits of		Break up of deposits of the Bank	
			J&K Bank	All SCBs[19]	Within State	Outside State
2013-14	69,335.86	5,115.24[20]	7.97	14.85	45,193.38 (65.18)	24,142.48 (34.82)
2014-15	65,756.19	(-) 3,579.67	(-) 5.16	10.55	48,724.60 (74.10)	17,031.59 (25.90)
2015-16	69,390.25	3,634.06	5.53	6.98	52,762.34 (76.04)	16,627.91 (23.96)
2016-17	72,463.10	3,072.84	4.43	10.12	61,416.95 (84.76)	11,046.15 (15.24)
2017-18	80,006.00	7,542.91	10.41	6.12	71,472.00 (89.33)	8,534.00 (10.67)
Growth during 2013-2018		**15,785.38**	**24.58**			

(Source: Information provided by the Bank)
Figures in parenthesis denote percentage of deposits made within/ outside the State to total deposits

Table-4.5: Target and achievement of Deposits

(₹ in crore)

Year	Geographical	Targets	Achievements	Shortfall	Shortfall (*per cent*)
2013-14	Within the State	48,431.00	45,193.38	3,237.62	6.69
	Outside the State	26,706.00	24,142.48	2,563.52	9.60
	Total	**75,137.00**	**69,335.86**	**5,801.14**	**7.72**
2014-15	Within the State	52,882.00	48,724.60	4,157.40	7.86
	Outside the State	27,199.00	17,031.59	10,167.41	37.38
	Total	**80,081.00**	**65,756.19**	**14,324.81**	**17.89**
2015-16	Within the State	57,761.00	52,762.34	4,998.66	8.65
	Outside the State	19,902.00	16,627.91	3,274.09	16.45
	Total	**77,663.00**	**69,390.25**	**8,272.75**	**10.65**
2016-17	Within the State	60,728.00	61,416.95	@	--
	Outside the State	18,546.00	11,046.15	7,499.85	40.44
	Total	**79,274.00**	**72,463.10**	**6,810.90**	**8.59**
2017-18	Within the State	70,572.00	71,472.00	@	--
	Outside the State	12,701.00	8,534.00	4,167.00	32.81
	Total	**83,273.00**	**80,006.00**	**3,267.00**	**3.92**

(Source: Information provided by the Bank) @ - targets achieved

The deposits of Bank grew by 24.58 *per cent* during the period 2013-18. However, the growth rate of deposits of Bank remained below the National average of Scheduled Commercial Banks during 2013-17.

- The growth rate of deposits of Bank remained below the National average of Scheduled Commercial Banks during 2013-17.
- The overall targets for deposits was not achieved in any of the years covered, especially from outside the State.

Analysis showed that deposits outside the State had come down from ₹24,142.48 crore at the end of March 2014 to ₹8,534 crore by the end of March 2018. Further, the percentage of deposits outside the State which constituted 34.82 *per cent* of its total deposits at the end of March 2014 had decreased to 10.67 *per cent* by the end of March 2018.

19 All Scheduled Commercial Banks (Source: Reports of Reserve Bank of India)
20 Calculated on Deposits as on 31 March 2013: ₹64,220.62 crore

The Bank achieved its targets of mobilization of deposits in the period 2016-18 within the State. However, there was shortfall in achievement of targets of deposits from outside State ranging between 9.60 *per cent* and 40.44 *per cent* during 2014-18.

The shortfall in achievement of targets in Mumbai Zone was 59.97 *per cent* during 2014-15. The position at the end of March 2018 had not improved, as the shortfall during 2017-18 was 58.66 *per cent*. In Delhi and Bangalore Zones, shortfall during 2016-17 was 40.81 *per cent* and 69.50 *per cent*, respectively.

The growth rate of deposits in 2017-18 over 2016-17 was 10.41 *per cent* as compared to 6.12 *per cent* of all scheduled commercial banks. The Government deposits in the Bank grew by ₹1,929.58 crore (34.61 *per cent*) and deposits from Corporate Sector by ₹3,401.91 crore (15.70 *per cent*) in the year 2017-18 over 2016-17.

We further observed that during the period 2013-14 to 2016-17 the Bank focused on maximising low cost deposits and did not rollover high-cost bulk deposits which had mainly been raised from outside the J&K State, bringing down the percentage share of deposits from outside the state vis-à-vis J&K State.

However, the Bank was reducing the targets of raising deposits from outside the State in successive years but could not achieve even the reduced targets of deposits. Further, the Bank was unable to attain the overall targets of deposits in any of the years during 2014-18.

4.7.2.1 Saving Bank accounts of Government departments in violation of RBI directives

As per the 'RBI (Interest Rate on Deposits) Directions, 2016', Scheduled Commercial Banks were prohibited (March 2016) to open a saving account in the name of entities other than individuals, Karta of Hindu Undivided Family and organisations/ agencies. Further, the Banks were allowed to open saving account of Government departments/ bodies/ agencies in respect of grants/ subsidies released for implementation of various programs/ schemes sponsored by Central Government/ State Government.

Records, however, showed that the Bank had allowed operations of saving accounts maintained by departments of GoJK with Moving Secretariat Branch of the Bank in contravention of the RBI directions of March 2016 as these accounts were not operated for management of grants/ subsidies released for implementation of any program/ scheme sponsored by Government. Instead, the accounts were operated for collection of revenue.

The Management replied (December 2018) that as of 31 March 2018, the Bank had complied with the guidelines of the RBI.

However, two[21] saving accounts as highlighted above were operational till December 2018, despite directions of RBI in March 2016. Further, the Bank had credited interest of ₹3.06 crore to these accounts between March 2016 and December 2018.

[21] Saving Bank Accounts maintained by Finance Department and PHE Department of Government of J&K

4.7.3 Advances

Position of Advances (Gross) of the Bank during the 2013-14 to 2017-18 and their annual growth vis-a-vis Private, Public and SCBs is given in **Table-4.6**:

Table-4.6: Year-wise position of advances

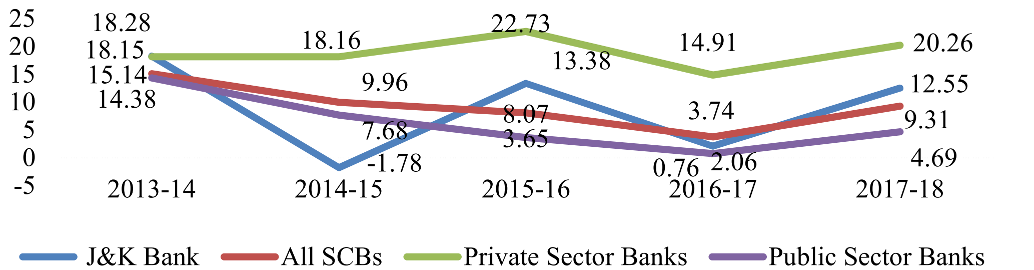
(₹ in crore)

Year	Advances (Gross)	Year over Year Growth	Growth (*per cent*) of advances of J&K Bank	Growth (*per cent*) of advances[22] of		
				All SCBs	Private Sector Banks	Public Sector Banks
2013-14	47,137.54	7,283.84[23]	18.28	15.14	18.15	14.38
2014-15	46,300.54	-837.00	-1.78	9.96	18.16	7.68
2015-16	52,493.74	6,193.20	13.38	8.07	22.73	3.65
2016-17	53,573.45	1,079.71	2.06	3.74	14.91	0.76
2017-18	60,298.28	6,724.83	12.55	9.31	20.26	4.69

(Source: Information provided by the Bank and information obtained from reports of RBI)

The Bank recorded an increase of 51.30 *per cent* in advances during 2013-14 to 2017-18 with the Year over Year (YoY) growth fluctuating between (-) 1.78 *per cent* and 18.28 *per cent* as shown in **Chart 4.5**.

Chart-4.5: Growth of Advances of the Bank vis-a-vis Other Banks (*Per cent*)



Advances within the State recorded growth of 82.38 *per cent* during 2013-14 to 2017-18. However, advances outside the State showed a decrease of 11.72 *per cent* during 2013-14 to 2017-18. Negative growth in advances of 29.02 *per cent* and 16.26 *per cent* was observed in Bangalore and Mumbai zones respectively during the period 2013-14 to 2017-18. Further, growth of advances of the Bank during 2014-15 and 2016-17 remained below the overall National average of all SCBs.

Management attributed (December 2018) the lower credit off take during 2014-15 and 2016-17 to floods in September 2014 and social disturbances in 2016 in the State. They added that the Bank continued its low-ticket high-volume credit dispensation in J&K State and selective big-ticket lending in the rest of the country.

Audit also observed that the shortfall in achievement of targets of advances during 2014-2018 ranged between 5.89 *per cent* and 19.73 *per cent* as detailed in **Table-4.7**:

[22] Source: Reserve Bank of India
[23] Calculated on advances at the end of March 2013: ₹39,853.70 crore

Table-4.7: Position of targets vis-à-vis achievements in respect of advances

(₹ in crore)

Year	Targets (Gross)	Achievements	Shortfall	
			Amount	*(In per cent)*
2013-14	50,304.00	47,137.54	3,166.46	6.29
2014-15	57,679.00	46,300.54	11,378.46	19.73
2015-16	55,778.00	52,493.74	3,284.26	5.89
2016-17	62,117.00	53,573.45	8,543.55	13.75
2017-18	70,822.00	60,298.28	10,523.72	14.86

(Source: Information provided by the Bank)

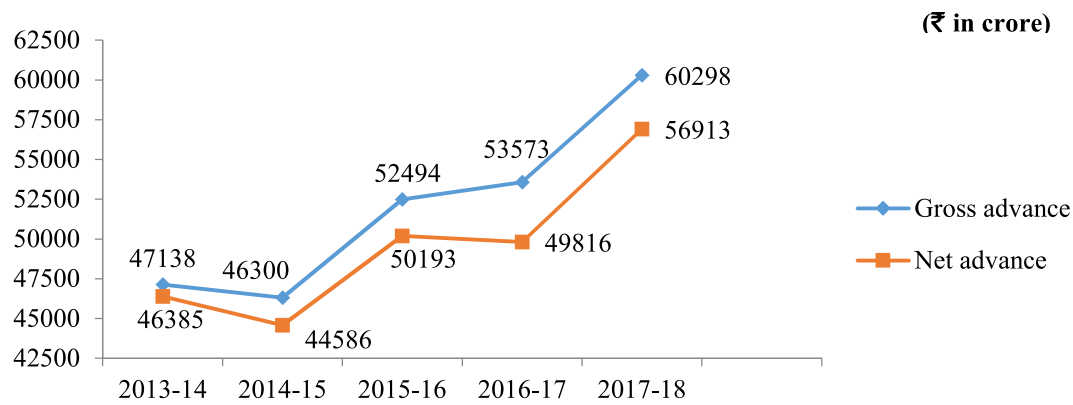
Shortfall in advances of 39.15 *per cent* in Bangalore zone during 2014-15, 28.84 *per cent* in Mumbai Zone during 2017-18, 37.26 *per cent* in Delhi Zone during 2017-18, 16.36 *per cent* in Jammu Central-I during 2015-16 and 16.25 *per cent* in Kashmir Central-I during 2016-17 was observed. The non-achievement of targets of advances had resulted in the funds remaining idle to the extent of shortfall.

The Management replied (December 2018) that low growth in advances resulted in shortfall in achievement of targets and focus was on retail lending outside the State.

i) Quality of advances

Audit observed that gross advances increased by 51.30 *per cent*[24] during 2013-14 to 2017-18 and corresponding increase in the net advances[25] as depicted in **Chart-4.6** was 45.18 *per cent*[26].

Chart-4.6: Growth of Gross Advances vis-à-vis Net Advances



The increasing gap between gross advances and net advances is indicative of the deteriorating quality of advances during the review period as the Bank had to make more provisions for doubtful advances. The Management replied (December 2018) that Bank had to face business disruptions due to floods in September 2014 and social disturbances in 2016. The reply of the Management is not tenable as floods and social disturbances affected the business within the State whereas during the period covered in audit, Bank's gross NPA ratio outside the State remained much higher as compared to within the State which indicates deteriorating quality of Bank's advances.

24 Calculated on gross advances at the end of March 2013: ₹39,853.70 crore
25 Net Advance is equal to Gross Advance less Provisions
26 Calculated on net advances at the end of March 2013: ₹39,200.41 crore

ii) Position of unsecured advances

The position of unsecured advances for the last five years ended 31 March 2018 is given in **Table-4.8** below:

Table-4.8: Position of Unsecured Advances

(₹ in crore)

Category of Net Advances	2013-14	2014-15	2015-16	2016-17	2017-18
Secured by Tangible Assets	36,983	34,130	37,922	36,584	40,453
Covered by Bank/ Government Guarantees	51	342	583	596	582
Unsecured	9,351	10,114	11,688	12,636	15,878
Total Net Advances	**46,385**	**44,586**	**50,193**	**49,816**	**56,913**
Percentage of Unsecured to total advances	*20.16*	*22.68*	*23.29*	*25.37*	*27.90*

(Source: Information provided by the Bank)

The percentage of unsecured advances to total net advances had increased from 20.16 per cent at the end of March 2014 to 27.90 per cent at the end of March 2018 which was in excess of the ceiling of 20 per cent fixed by the Bank for advancing under unsecured exposure. The increase indicates that the Bank had increased its exposure to unsecured advances, without safeguarding itself against the risk of non-recovery of advances in case of loans turning NPA.

Management attributed the growth in unsecured advances to the fact that it prefers to give advances to PSUs in the rest of India, rather than the risky advances (collaterally secured). The Management contention is not borne out of facts as unsecured advances to PSUs constituted a mere 9.62 *per cent* of the total unsecured advances by end of March 2014 and came down to 6.23 *per cent* as on 31 March 2018.

4.7.4 Risk Management Framework

Banks in the process of financial intermediation are confronted with various kinds of financial and non-financial risks viz., credit, market, liquidity, legal, regulatory, reputational, operational, etc. These risks are highly interdependent and events that affect one area of risk can have ramifications for a range of other risk categories. Thus, top management of banks should attach considerable importance to improve the ability to identify, measure, monitor and control the overall level of risks undertaken.

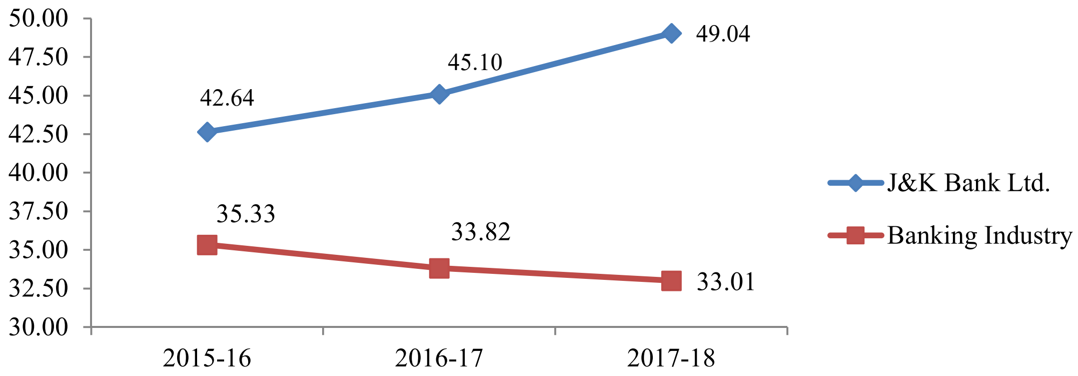
i) Credit concentration Risk

In accordance with the RBI guidelines, the Bank carries out a detailed concentration risk analysis of its credit portfolio. The objective of the analysis is to draw the picture of concentration in various segments for assessing limit position and devising further lending strategies.

The Bank's concentration risk for industry-wise exposure as on 31 March 2016 was categorized as 'moderate', as advances to infrastructure industry constituted 42.64 *per cent* of the total industry exposure. It was categorized as 'high' during 2016-17 and 2017-18 due to infrastructure advances rising to 45.10 *per cent* ending March 2017 and 49.04 *per cent,* ending March 2018.

The Bank's concentration risk for industry-wise exposure was on higher side when compared to the average of overall banking industry as shown in the **Chart-4.7** below:

Chart-4.7: Percentage of Infrastructure Advance to Total Industrial Advances



Despite increase in exposure in Infrastructure sector, the Bank did not initiate any steps to keep a check on further lending in the sector. Further, the Bank did not carry out analysis of industry-wise growth of NPAs.

Management stated (August 2019) that the concentration risk in infrastructure sector was being monitored closely by the bank and the percentage of Infrastructure advances to industry exposure as on 31 March 2019 had come down to 42.02 *per cent*.

ii) Appointment of Chief Risk Officer

The role of Chief Risk Officer (CRO) in a bank is to review and manage potential risks which may arise from regulatory changes/ or changes in economic/ political environment, to facilitate the analysis of risks and interrelationships of risks across market, credit and operational risks, to review the risk profile and to prioritize action to mitigate the potential risks.

In order to align the risk management system with the best practices, the RBI advised (April 2017) all the banks to appoint a CRO for a fixed tenure, with the approval of the Board. Further, the Banks were advised to lay down a Board-approved policy clearly defining the role and responsibilities of the CRO.

However, it was noticed in audit that the post of CRO remained vacant between April 2017 and May 2018 as there was no Board-approved policy on roles and responsibilities of CRO till May 2018.

The Management stated (August 2019) that during the period from April 2017 to May 2018, the function was looked after by President, Risk Management.

iii) Policy on Risk Based Internal Audit

The RBI issued (December 2002) guidance note on Risk Based Internal Audit (RBIA) in banks and advised all the banks to develop a well-defined policy, duly approved by the Board, for undertaking risk-based internal audit. The policy was required to include the risk assessment methodology for identifying the risk areas based on which the audit plan would be formulated.

The Bank did not have a Board-approved RBIA policy during 2013-14 to 2018-19 despite the fact that the Audit Committee of the Board, in its meeting held on 08 December 2013, recommended that steps for framing RBIA policy should be initiated. However, the RBIA policy was approved by the Board only in March 2019, indicating poor compliance framework.

In absence of RBIA policy, allocation of audit resources could not be prioritized and risk sensitivity amongst field staff could not be created.

iv) Preventive Vigilance Framework

The RBI issued (May 2011) detailed guidelines for private sector banks on internal vigilance. As per the guidelines, the Bank was required to appoint an officer of suitable seniority as Chief of Internal Vigilance (CIV) who will head the Internal Vigilance Division of the bank. However, CIV should not be a party to processing and decision-making processes or be involved in other administrative transactions, which are likely to have clear vigilance sensitivity.

The officer designated as CIV of the Bank, during the period between October 2016 and May 2017, also looked after the Advances and Asset Planning (J&K State) portfolio and Asset Monitoring and Information Department during the same period which was in violation of *ibid* guidelines.

Further, as per guidelines, CIV was required to furnish a report on the vigilance activities in the bank to the Board on a periodic basis. However, CIV of the Bank failed to submit any reports to the Board during 2013-14 to 2017-18. The Bank formulated a policy document on Preventive Vigilance Framework only in November 2018.

The Management admitted that the reports on working of vigilance were not placed before the Board during the period under audit scrutiny and stated (August 2019) that the same are now being submitted on periodic basis.

v) Appointment of Chief Technology Officer

In order to strengthen the Bank's risk governance framework in the area of technology, the RBI advised (May 2017) all scheduled commercial banks to appoint Chief Technology Officer (CTO) in banks. The Regulator prescribed that the minimum qualification for appointment as CTO should be engineering Graduate or MCA or equivalent qualification from a recognized university/ Institution.

However, the Presidents who held the charge of Technology Department of the Bank during the period between May 2017 and June 2019 did not meet the qualification criteria fixed by the regulator.

The Management attributed (August 2019) the same to non-availability of IT Professionals at the Vice President level.

4.7.5 Non-Performing Assets

The movement of gross NPAs of the Bank during the years from 2013-14 to 2017-18 is given in **Table-4.9** below:

Table-4.9: Movement of Non-Performing Assets

(₹ in crore)

Sl. No.	Particulars	2013-14	2014-15	2015-16	2016-17	2017-18
1.	**NPA at the beginning of the year**	643.77	783.42	2,764.08	4,368.62	6,000.01
2.	**Addition during the year**	410.60	2,525.80	2,383.23	3,278.41	3,104.69
3.	**Total NPAs during the year**	**1,054.37**	**3,309.22**	**5,147.31**	**7,647.03**	**9,104.70**
	Less					
4.	Upgraded accounts[27]	117.70	343.77	188.92	154.76	185.64
5.	Recovery made	146.16	197.53	272.07	664.34	1,300.63
6.	Written off	7.09	3.84	317.70	827.92	1,611.73
7.	**Total reduction in NPA (Row 4 +5+6)**	**270.95**	**545.14**	**778.69**	**1647.02**	**3,098.00**
8.	NPA at the end of each year	783.42	2,764.08	4,368.62	6,000.01	6,006.70
9.	Gross Advances	47,137.54	46,300.54	52,493.74	53,573.45	60,298.28
10.	NPA to Gross Advance (*Percentage*)	1.66	5.97	8.32	11.20	9.96

(Source: Information provided by the Bank and annual accounts of the bank)

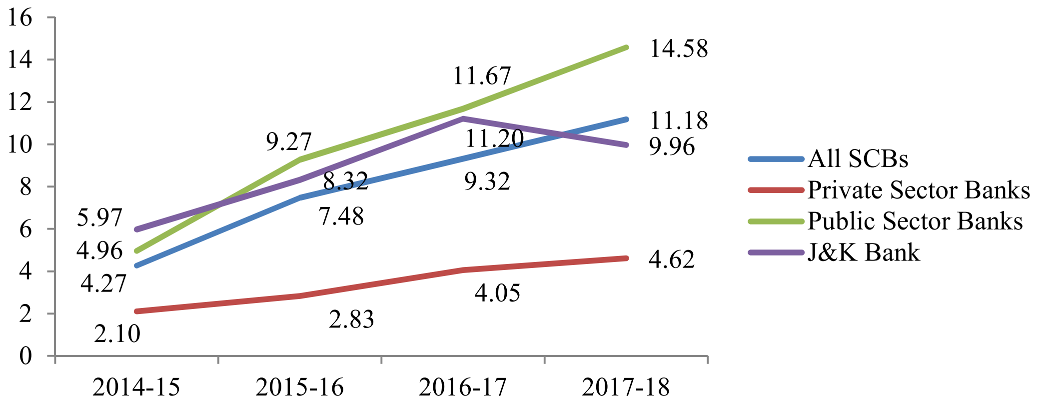
Audit analysis revealed that Gross NPAs of the Bank increased by ₹5,362.93 crore (833.05 *per cent*) from ₹643.77 crore as on 01 April 2013 to ₹6,006.70 crore as on 31 March 2018. The Bank had classified advances of ₹11,702.73 crore as NPAs during the period 2014-2018. Of this NPA, ₹7,164.98 crore (61.22 *per cent*) were contributed by three Zones[28] during 2014-2017. The overall reduction of ₹6,339.80 crore in NPAs during 2013-14 to 2017-18 was on account of actual recovery of ₹2,580.73 crore (40.71 *per cent*), up-gradation of accounts of ₹990.79 crore (15.63 *per cent*) and write-off of ₹2,768.28 crore (43.66 *per cent*).

The percentage of NPAs to Gross Advances had increased from 1.66 *per cent* at the end of March 2014 to 9.96 *per cent* at the end of March 2018.

The Gross NPA ratio of bank was above that of average of Private Sector Banks and all Scheduled Commercial Banks (except 2017-18) in the Country as depicted in **Chart-4.8** below:

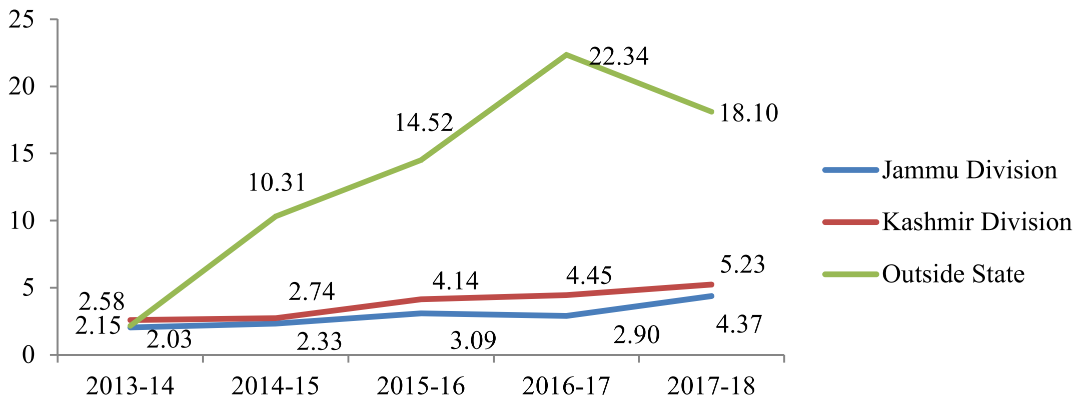
27 Once the past dues are paid, the account will be regularized and converted from NPA to standard asset
28 Delhi Zone: ₹3,544 crore; Mumbai Zone: ₹2,718.15 crore; Kashmir Central-I Zone: ₹902.83 crore

Chart-4.8: Comparison of Gross NPA ratio of the Bank with Industry (*per cent*)



Analysis of division-wise data revealed that percentage of Gross NPAs to total advances as on 31 March 2018 was lower within the State in comparison to those advanced to customers outside the State. It was 4.37 *per cent* in Jammu Division, 5.23 *per cent* in Kashmir Division and 18.10 *per cent* outside the State as depicted in **Chart-4.9** below:

Chart-4.9: Division-wise Gross NPAs (*per cent*)



This indicated that the Bank failed to effectively check the slippage of advances to NPAs outside the State.

Consortium financing

Credit Policy authorizes the Bank to make advances under Consortium arrangements to share credit risk. While extending credit under consortium, the Bank also has to make independent appraisal of project besides that made by the lead bank.

- Advances under this segment ranged between 10.78 *per cent* and 16.86 *per cent* of the total advances during 2014-15 to 2017-18.
- The outstanding balance of advances under Consortium at the end of March 2018 was ₹6,502.60 crore which included NPAs of ₹3,312.69 crore. As against the overall Gross NPA ratio of 9.96 *per cent* as on 31 March 2018, the NPAs under Consortium advances were 50.94 *per cent*.

- Despite the fact that NPAs under Consortium advances reached an alarming level, the Bank had not fixed any prudential limit/ ceiling for advancing loans under the consortium lending.

The Management attributed (December 2018) the higher percentage of NPAs in advances extended outside the State to stress in Infrastructure/ steel/ power sectors. The Bank asserted that it mostly lent funds as part of consortium finance and owing to the economic slowdown in the country, it came under stress as a result of which the accounts slipped to NPA and added that due to decisions taken, the Gross and Net NPAs as percentage to Gross and Net Advances as on March 2018 have been brought down to 9.96 *per cent* and 4.90 *per cent* from 11.20 *per cent* and 4.87 *per cent* a year ago. For advances extended within the State, it attributed the high NPA ratio to natural calamity and social unrest.

It was, however, observed that during 2014-15 to 2016-17, J&K Bank's NPA ratio had exceeded the average gross NPA ratio of both private sector and all Scheduled Commercial Banks in the Country. The Bank's gross NPA ratio was recorded at 11.20 *per cent* at the end of March 2017 whereas the gross NPA of all SCBs as on 31 March 2017 was 9.32 *per cent.* Also Bank's contention that disruptions on account of floods and disturbances contributed to higher NPA ratio is also not tenable as the Bank's Gross NPA ratio within the State increased from 2.41 *per cent* as on 31 March 2014 to 3.90 *per cent* at the end of 31 March 2017, whereas Gross NPA outside the State had increased from 2.15 *per cent* to 22.34 *per cent* during this period.

> The percentage of NPAs came down in March 2018 mainly due to write-off of ₹1,611.73 crore.

The Bank's gross NPA ratio came down from 11.20 *per cent* by end of March 2017 to 9.96 *per cent* by end of March 2018 only after writing off ₹1,611.73 crore of NPAs during 2017-18.

4.7.5.1 Failure to effect recoveries leading to doubtful recoveries and losses

The position of NPA under three categories viz. sub-standard, doubtful and loss assets at the close of financial year during 2013-14 to 2017-18 is given in **Table-4.10** below:

Table-4.10: Classification of NPAs

(₹ in crore)

Classification	31.03.2014		31.03.2015		31.03.2016		31.03.2017		31.03.2018	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
Sub-standard	2,909	171.29 (21.86)	11,743	1,317.27 (47.66)	9,655	2,052.08 (46.97)	7,748	614.27 (10.24)	4,721	1,092.53 (18.19)
Doubtful	8,751	533.03 (68.04)	8,227	1,215.21 (43.96)	13,112	1,473.84 (33.74)	17,693	5,062.57 (84.38)	18,212	4,864.59 (80.99)
Loss	5,382	79.10 (10.10)	5,365	231.60 (8.38)	4,548	842.70 (19.29)	4,091	323.17 (5.38)	3,327	49.58 (0.82)
Total	**17,042**	**783.42**	**25,335**	**2,764.08**	**27,315**	**4,368.62**	**29,532**	**6,000.01**	**26,260**	**6,006.70**

(Source: Information provided by the Bank)
Figures in parenthesis are percentage under each category to total NPAs as on respective dates

The Bank had failed to effect recoveries in case of chronic NPA cases, as a result of which the NPAs under doubtful and loss assets category increased from ₹612.13 crore (78.14 *per cent* of total NPAs) at the end of March 2014 to ₹5,385.74 crore (89.76 *per cent* of total NPAs) at the end of March 2017. However, the same had come down to ₹4,914.17 crore (81.81 *per cent* of total NPAs) at the end of March 2018, mainly due to write-off of ₹1,611.73 crore of NPAs during 2017-18.

The Management replied (December 2018) that most of these accounts are under consortium banking arrangement and the Bank's share in the total advances in these accounts ranged from one *per cent* to five *per cent*, so the Bank has to follow the consortium decision for recovery of dues in these accounts.

The reply of the management is not tenable as out of NPAs of ₹4,914.17 crore under doubtful and loss assets category at the end of March 2018, the NPAs under consortium segment was ₹2,627.16 crore and the Bank could not effect recovery in respect of ₹2,287.01 crore of NPAs under multi-banking and sole-banking arrangement.

4.7.5.2 Case Studies-Non-Performing Assets

Test-check of NPA cases[29] revealed that loan and credit facilities were extended overlooking Bank's interest. There was loss/ non-recovery of ₹197.98 crore, doubtful recovery of ₹1,599.14 crore and excess payment of ₹14.10 crore in the 29 cases[30] detailed in ***Appendix-4.1.2*** on account of non-enforcement of internal control procedures, inadequate security cover, improper credit appraisal, non-adherence to the pre or post-disbursement conditions of the sanctions, irregular monitoring etc. These causes contributed to advances turning into NPAs enforcement of which would have sent warning to Bank to take rectificatory measures. The following cases are highlighted:

Sl. No.	NPA Case	Brief facts and observations
1.	M/s. Chhaparia Industries Private Limited	• The Bank extended credit facility of ₹41.95 crore (up to February 2011) including Cash Credit (CC), Term Loans (TL) and Inland Letter of Credit (ILC) secured by charge on assets, stock and debtors. • Bank sanctioned (October 2011) another ILC of ₹three crore which was dishonoured. • Bank restructured (July 2012) the facilities on default of Company in servicing the credit and accepted the projected Debt Service Coverage Ratio (DSCR[31]) of 1.23 (average) of the Company which was lower than minimum acceptable ratio[32] reflecting weak credit

29 312 NPA cases in five selected zones were test-checked where the outstanding balance as on 31 December 2017 was more than ₹five crore

30 Includes M/s Go Fresh which took over the credit facility of M/s Kehwah Square Pvt. Limited

31 DSCR refers to the amount of cash flow available to meet annual interest and principal payments on debt

32 As per credit policy minimum DSCR should be 1.30 with average of 1.50

		risk controls. Further, the Bank did not ensure adequate security cover despite the external rating[33] of high/ very high risk assigned to the long term/ short term debts of the Company. • The Bank also enhanced (June 2013) credit exposure by ₹five crore. • Bank, despite non-servicing of the credit facilities, sanctioned (May 2014) *adhoc* cash credit facility of ₹six crore and also allowed the borrower company to sell off one of its properties mortgaged with the Bank thereby reducing its security cover. • Company failed to service its loan and Bank classified (December 2014) the same as NPA. • Against a principal and unapplied interest of ₹47.20 crore, the Bank held a security of ₹22.15 crore (September 2016). • The assets were sold (February 2017) to an Asset Reconstruction Company for ₹19 crore. • Extending of credit facilities in deviation to Bank's credit policy coupled with inadequate security cover resulted in loss of ₹28.20 crore[34].
2.	M/s REI Agro Limited	• The Bank sanctioned three crop loans (between December 2012 and August 2013) aggregating ₹400 crore[35] to 80 Joint Liability Groups (JLGs)[36] of farmers. The Company, engaged in marketing of basmati paddy was required to repay the Company in three structured instalments. • The credit was secured by corporate guarantee of the Company, receivables generated by JLGs against basmati paddy supplied to Company and post-dated cheques. • The Company failed to repay the interest and principal as a result of which loan was classified (June 2014) as NPA. • The Bank did not obtain undertakings from farmers/ JLGs that the funds availed would be utilised for intended purpose although this was one of the conditions of the sanction. • The Bank relied exclusively on certification by Chartered Accountants regarding end use of funds. These were found to be deficient as the certification was only with regard to transfer of funds by the leader of JLGs to farmers and the end use of funds by the farmers was not ensured. This was despite RBI directives to Banks to strengthen and conduct post-sanction supervision to ensure end use of credit reflecting poor compliance of regulator's directives.

33 External rating by Credit Analysis and Research (CARE), a credit rating agency
34 ₹47.20 crore – ₹19.00 crore
35 Crop Loan of ₹200 crore in December 2012, ₹100 crore in February 2013 and ₹100 crore in August 2013
36 Joint Liability Group (JLG) is a lending model that enables a group of individuals to avail loans for income generating activity by forming a group

		• Disbursement conditions of loan stipulated for transfer of loan amount to savings accounts of farmers/ JLGs to be opened with J&K Bank but they were transferred to accounts of leaders of JLGs held in other banks and hence were outside the control of bank indicating poor compliance culture at operational level. • Bank did not obtain the details of land holdings of the farmers and their financial position. No specific policy of extension of credit to such JLGs was in place. KYC details of farmers were not obtained and duplicity of farmers' names in different JLGs was observed (***Appendix 4.1.3***). • The Bank, in deviation to its credit policy, had not rated 80 JLGs accounts of ₹five crore each through risk score application and extended credit merely on the corporate guarantee of the Company indicating weak credit risk controls. • Non-exercising of due diligence in sanctioning/ disbursing of crop loans coupled with non-obtaining of tangible security to safeguard the Bank's interest led to doubtful recovery of ₹639.42 crore[37].
3.	M/s REI Agro Limited	• The Bank sanctioned (May 2011) bill discounting (BD) facility of ₹100 crore secured against collateral security, corporate guarantee of the Company and post-dated cheques. • Company was to procure basmati paddy from identified suppliers and Bank was to discount the bill drawn by these suppliers. • The BD facility was renewed (October 2013) even though the current ratio of the Company (1.27) was below the minimum acceptable level of Bank which stood at 1.33 indicating weak credit risk controls. • *Adhoc* BD of ₹15 crore was extended (January 2014) without competent authority's approval and despite the existing facility being overdue for more than 90 days which had already rendered the account as NPA indicating weak internal controls. • Company failed to adjust the overdue discounted bills and account was classified (June 2014) as NPA. • The collateral security obtained was already charged to term loans availed by the Company from other branches of the Bank which had also turned NPAs in June 2014. Charged properties which were valued at ₹305.38 crore against a book value ₹149.82 crore and on being taken over (November 2015/ March 2016) were assessed at ₹168 crore and could not be sold at reserve price of even ₹60 crore. • Non-safeguarding of Bank's financial interest in discounting of supplier bills resulted in doubtful recovery of ₹172.45 crore[38].

[37] NPA of ₹400 crore and unapplied interest of ₹239.42 crore
[38] NPA balance of ₹111.27 crore and unapplied interest of ₹61.18 crore

4.	M/s Aanjaneya Life Care Limited	• The Company availed (September 2011) Short Term Loan (STL) of ₹20 crore from Bank against primary security of four lakh promoters equity shares and collateral security by way of second charge on fixed assets and post-dated cheques. • Bank sanctioned (December 2011) ILC/ FLC of ₹15 crore and took over existing term loans of ₹10.66 crore from another Bank. • The Company defaulted in servicing of STL of ₹20 crore and the Bank restructured (November 2012) the account and its repayment was rescheduled from September 2012 to June 2014. • The loan was assessed as sub-standard in September 2013. However, the Bank further sanctioned (December 2013) ILC of ₹8.71 crore and one time Packing Credit[39] (PC) of ₹18.38 crore without ensuring adequate security cover for facility extended reflecting weak credit risk controls. • The export shipment for which facility was disbursed was not shipped and the PC facility disbursed by the Bank was utilised by the Company to service the interest and instalments of overdue amount in various other accounts (STL of ₹20 crore and term loans of ₹10.66 crore)[40] by routing the transactions through another firm which indicates that post-disbursement monitoring was inadequate. • Company failed to meet its obligations and was declared (March 2014) as NPA. • Sanctioning/ disbursing of credit facilities without safeguarding the Bank's interest led to doubtful recovery of ₹40.32 crore[41].
5.	M/s Paradise Avenue, a partnership firm (firm), for construction of residential township at Narwal Bala, Jammu	• The Bank[42] sanctioned four Term Loans (TL-I: ₹74.27 crore in January 2012; TL-II: ₹68.91 crore in May 2014; TL-III: ₹20 crore in June 2015 and TL-IV: ₹14.50 crore in February 2017) aggregating to ₹177.68 crore against which disbursement of ₹175.60 crore was made. • As per Bank's credit policy, credit exposure to partnership firm was to be restricted to ₹50 crore and in exceptional cases of borrowers having good track record, the Board may consider relaxation. However, the Bank made disbursement of TL-1 of ₹74.27 crore in departure to its credit policy and without obtaining prior approval of the Board. • The credit was extended without obtaining any collateral security thereby exposing to risk of loss in case of default. Necessary credit rating of debt portfolio was not obtained from an independent external agency thereby deviating Bank's credit policy.

39 Packing credit is a loan provided to exporters to finance the goods' procurement before shipment

40 Advanced by the J&K Bank Limited

41 Against outstanding balance of ₹40.96 crore (Principal amount: ₹27.96 crore and Unapplied Interest: ₹13 crore), the securities were valued at ₹0.64 crore

42 Business Unit, New University Campus, Jammu

		• The Bank obtained Board's approval in May 2014 for extending TL-II of ₹68.91 crore. However, it had not apprised (May 2014) the BODs that the firm failed to infuse requisite promoter's contribution[43]. Further, the firm was allowed (March/ April 2014) by the Chairman to withdraw ₹6.59 crore for payment to suppliers, out of the Escrow account, designated for repayment of term loan only. However, the action of the Chairman was accorded post-facto approval by the Board in May 2014. • The Bank accepted (May 2014) Debt-Equity ratio of 2.75:1 against benchmark of 2:1 and also did not conduct credit audit of the firm on quarterly basis though required as per its credit policy. • The Bank, time and again, rescheduled the repayment of Term Loans from October 2014 to June 2017 citing change in scope and size of the project from ₹96.36 crore to ₹209.90 crore. • The Bank disbursed ₹128.79 crore[44] up to May 2017, and the firm was required to employ the margin of ₹46.72 crore, thereby making total funding of ₹175.51 crore (loan plus margin). However, the project was valued (January 2018) at ₹118.16 crore[45] which indicated that margin money was not employed by the firm. • Mismatch between reports of chartered engineers and chartered accountants were overlooked which indicates that monitoring was not adequate. • The firm did not make any repayment and its failure to service the account led to classification (December 2017) of account as NPA. • Against the outstanding principal of ₹156.47 crore and unapplied interest of ₹28.19 crore, the account was settled for ₹130.00 crore. • The Bank sacrificed principal of ₹26.47 crore and unapplied interest of ₹28.19 crore.
6 (i)	M/s Kehwah Square Private Limited	• The Bank[46] sanctioned (August 2013) a term loan of ₹42.76 crore for setting up controlled atmosphere storage facilities and a CC limit of ₹7.50 crore for meeting working capital requirement. • As per disbursement conditions of sanction, the CC was to be released only after commissioning of plant. However, the Bank released (July 2014 and October 2014) ₹5.91 crore under CC limit before commissioning of plant (November 2014), indicating poor compliance culture at operational level. • Funds of ₹3.02 crore were diverted (March 2016) from CC account of M/s KSPL to its sister concern engaged in business of silk products. The Bank also released the funds in excess of the available drawing power reflecting inadequate monitoring.

43 Against the term loan of ₹74.27 crore fully released by the Bank up to February 2014, the promoter's contribution should have been ₹22.09 crore whereas the firm infused only ₹6.96 crore

44 Excluding Interest of ₹46.81 crore during construction

45 Including the cost of land: ₹21.96 crore

46 Business Unit, Air Cargo, Srinagar

		• Cash withdrawals of ₹2.30 crore[47] were allowed in CC account of the Company without ensuring end use of funds and cash deposits of ₹2.45 crore[48] were also accepted in CC account. • Temporary overdrafts amounting to ₹six crore sanctioned (December 2015) to associate entities[49] for meeting their working capital requirements were diverted to M/s KSPL which is indicative of lack of monitoring of account at operational level. • The Company defaulted in repayment of interest/ instalment as a result of which the Bank classified (June 2016) the accounts as NPA. • The storage facility project implemented by M/s KSPL was eligible under capital investment subsidy scheme of National Horticulture Board (NHB). • As per the scheme guidelines, subsidy of ₹16.50 crore was released by NHB to the Bank which was to be kept in the separate 'Subsidy Reserve Fund' and the subsidy amount in the borrower's TL account was to be adjusted only as recovery of last instalment. However, the Bank transferred (₹four crore in March 2016 and ₹12.50 crore in March 2017) subsidy amount to adjust term loan of M/s KSPL in contravention of the NHB guidelines. • Total outstanding balance against M/s KSPL on 31 March 2017 was ₹58.61 crore[50] before adjustment of subsidy of ₹12.50 crore. • The Bank sanctioned (31 March 2017) a term loan ₹40.10 crore in favour of M/s Go Fresh for acquiring the project of the Company. • As per terms of sanction, the loan amount sanctioned in favour of M/s Go Fresh was to be credited directly to the existing term loan account of M/s KSPL. The loan amount to M/s Go Fresh was disbursed through an accounting adjustment by crediting accounts (TL: ₹25.64 crore and CC: ₹10.30 crore) of M/s KSPL and debiting equal amount to M/s Go Fresh. • Adjustment of ₹10.30 crore to CC limit of M/s KSPL was in violation of conditions of sanction of term loan. • In the process of adjustment of credit facilities of M/s KSPL, the Bank also waived off interest of ₹6.58 crore in TL account and ₹1.69 crore in CC account of M/s KSPL thereby resulting in loss of ₹8.27 crore. • The account of M/s Go Fresh turned NPA in April 2019 with outstanding amount of ₹39.56 crore.
6(ii)	M/s Kehwah Wheels Private Limited	• The Bank sanctioned (February 2013) a TL of ₹30.89 crore in favour of M/s Kehwah Wheels Private Limited (KWPL) for setting up and providing bus services in the State.

47 28 July 2014: ₹0.80 crore; 01 September 2014: ₹1.50 crore
48 01 September 2014: ₹2.00 crore; 29 June 2015: ₹0.45 crore
49 Mr. Adil Shokat, Mr. Abdul Aziz and M/s Hotel Grand Mahal
50 TL: ₹46.62 crore (NPA of ₹40.04 crore and unapplied interest of ₹6.58 crore) and CC: ₹11.99 crore (NPA of ₹10.30 crore and unapplied interest of ₹1.69 crore)

		• In February 2015, the Bank restructured the existing TL and also sanctioned a fresh TL of ₹1.76 crore in favour of M/s KWPL under 'Rehabilitation Package of 2014'. • Owing to non-servicing of instalments of credit facilities by the Company, the Bank classified the accounts as NPA in March 2016[51]. • The Bank did not obtain credit rating of Company's debt portfolio from any external agency thereby departing from its credit policy reflecting weak credit risk controls. • The Bank did not obtain lease deed of shops (kept as primary security against the credit facility) resulting in non-creation of charge on the property. • The disbursement of loan amount was made without ensuring infusing of margin money by promoters. Funds of ₹4.68 crore were transferred between April and June 2013 from TL to Current Account of the Company resulting in diversion of funds which reflects poor compliance culture and inadequate monitoring at operational level.
6 (iii)	Kehwah Group of Companies	• In addition to the credit facilities availed by M/s KSPL and M/s KWPL, the Kehwah Group of companies viz. M/s Kehwah Xpress Services Private Limited (KXSPL), M/s Kashmir Sunsilk Industries Pvt. Ltd. (KSIPL), M/s Silk Enterprises, M/s Kehwah Food & Retail, M/s Kashmir Threads & Color Mills and M/s Bangalore Silk House were also availing various credit facilities from the Bank. • Owing to non-servicing of instalments of credit facilities by Kehwah Group, the Bank classified the accounts as NPA in March 2016[52]. • The Bank did not file legal suit against the group for recovery thereby departing from its recovery policy. • The Bank sanctioned (March 2017) One Time Settlement (OTS) in favour of the Kehwah Group for ₹105.00 crore against the outstanding amount of ₹159.84 crore[53]. As per the OTS, the group was required to deposit ₹50.00 crore by March 2017 and remaining ₹55.00 crore by June 2017. • The group did not pay the settlement amount as per agreed terms and the scheme was terminated (October 2017) by the Bank. Meanwhile, the Group deposited (March 2019) ₹11 crore in its various loan accounts (NPAs) out of which amount of ₹two crore was deposited in cash.

51 Effective date 30 September 2014

52 Effective date of NPA was taken as 30 September 2014/ March 2015

53 NPA of ₹138.79 crore and unapplied interest of ₹21.05 crore as of February 2017 (before taking over of accounts of M/s KSPL by M/s Go Fresh)

		• Non-adhering to disbursement conditions, exercise post-sanction monitoring and ensure the end use of funds resulted in loss of ₹8.27 crore, and recovery of ₹124.06 crore[54] from Kehwah group and ₹39.56 crore[55] from M/s Go Fresh became doubtful. Bank also irregularly released subsidy of ₹16.50 crore to the Company.
7.	M/s Haldia Coke and Chemicals Private Limited	• Bank sanctioned (March 2011) Cash Credit limit (CC) of ₹12 crore and ILC/ FLC of ₹48 crore and renewed (February 2013 and June 2014) the facilities. • The Bank did not obtain any collateral security and extended facilities against primary security by way of first *pari passu* charge on current assets, stores and stocks. • CRISIL indicated (March 2012 and April 2013) moderate to high risk to debt portfolio of the Company, Bank renewed (February 2013 and June 2014) the credit facilities by overlooking CRISIL ratings indicating deficiencies in credit appraisal process. • Funds were released beyond drawing powers and mandatory credit audit was not conducted indicating inadequate monitoring mechanism. • The account due to non-servicing was declared (July 2016) as NPA and total outstanding was ₹84.77 crore[56]. • Company approached the National Company Law Tribunal for resolution under Insolvency and Bankruptcy Code from which Bank received (April 2018) ₹21.39 crore. • Due to non-obtaining of adequate securities and weak post-sanction monitoring, the Bank lost ₹63.38 crore[57].
8.	M/s. AGL Televentures and M/s Trunks & Roots	• Bank sanctioned (December 2010 to November 2013) cumulative credit facilities of ₹57.40 crore to M/s AGL and to M/s Trunk and Roots. • Funds were released without ensuring receipt of required margin money. MOUs of the firms with purchasers of their products were not obtained. • Funds were released under cash credit limits beyond the drawing powers which were framed incorrectly. Regular credit and stock audit were not conducted. Diversion of funds by the firms was undertaken indicating poor compliance culture and inadequate monitoring mechanism. • The facilities were defaulted by both the firms and were classified (December 2014 and June 2015) as NPAs.

54 NPA balance of ₹71.64 crore and unapplied interest of ₹52.42 crore as of June 2019

55 NPA balance of ₹39.18 crore and unapplied interest of ₹0.38 crore

56 NPA balance of ₹53.54 crore (CC: ₹12.00 crore; ILC/ FLC: ₹41.54 crore) and unapplied interest of ₹31.23 crore

57 Principal of ₹32.15 crore and unapplied interest of ₹31.23 crore

		• Bank took self-possession (December 2017) of one of the properties for ₹23 crore. • Outstanding balance against both the firms after adjusting the above amount was ₹51.09 crore[58]. • Non-adherence to disbursement conditions, to exercise post-sanction monitoring and to ensure end use of funds led to doubtful recovery of ₹30.53[59] crore.
9.	M/s. Cranes Software International Limited	• Bank sanctioned (September 2010) restructuring of existing credit facilities[60] and two Working Capital Term Loans (WCTL) of ₹25 crore and ₹19.58 crore. A Term Loan (TL) of ₹5.58 crore and Funded Interest Term Loan (FITL)[61] of ₹4.55 crore were also sanctioned. • The credit facilities were secured by way of hypothecation of stocks, book debts and fixed assets of the Company on *pari passu* basis with other lenders besides immovable properties and personal guarantee of promoters. • Restructured loans were repayable from October 2011 in quarterly instalments. • Bank recovered instalments till June 2014 through sale of mortgaged securities at ₹32.11 crore. • Bank sanctioned Temporary Overdrafts (TODs) of ₹10.46 crore in favour of group firms without any additional security cover despite the fact that the Company did not adhere to the repayment schedule of existing facilities. • TODs were released without prior approval of competent authority indicating weak internal controls. • Withdrawal of funds in cash was allowed from TODs reflecting poor monitoring. • Inability to service the loan resulted (September 2014) in downgrading of loan account. • Company approached (August 2017) the Bank for One Time Settlement and was sanctioned (September 2017) for ₹23 crore. • Against outstanding amount (July 2017) ₹41.60 crore[62], the Bank settled the accounts at ₹23 crore by sacrificing principal of ₹3.92 crore and unapplied interest of ₹14.68 crore.

As discussed in above paragraphs, significant deviations from the terms and conditions of sanction orders, credit policies, RBI directives etc. were noticed. The major lapses noticed were disbursement of loans without complying with terms of sanctions, departure from bank's credit policy with regard to minimum acceptable

58 NPA of ₹24.92 crore and unapplied interest of ₹26.17 crore
59 ₹51.09 crore - ₹20.56 crore (being realizable value of property)
60 Cash Credit, Term loan and post-shipment limit
61 A loan extended to the borrower for making repayment of interest component of an existing loan
62 NPA of ₹26.92 crore and unapplied interest of ₹14.68 crore

ratios, non-conducting of fresh valuation of mortgaged properties in accordance with Bank's credit policy, non-classification of accounts as NPA in line with the prudential norms of RBI, non-obtaining of credit rating of the borrower's debt portfolio from any external agency as required under credit policy of the Bank, non-conducting of credit audit and stock audit at regular intervals, releasing of funds in excess of available drawing powers, diversion of funds for purpose other than that specified in the sanction orders, non-creation of charge on mortgaged properties, non-maintenance of Drawing Powers Register and disbursements without ensuring matching contribution by promoter.

We also observed that Audit Committee of the Board while reviewing the top NPAs of the Bank on quarterly basis had also reviewed the NPA cases highlighted in this report. However, the agenda notes placed before the Audit Committee did not analyse and highlight the lapses noticed in these accounts viz., non-adherence to disbursement conditions, poor monitoring, deviation from bank's credit policy, non-classification of accounts as NPA, non-conducting of credit audit/ stock audit, irregular release/ diversion of funds, non-creation of charge on mortgaged properties, non-obtaining of adequate security etc. In absence of analysed information, the Audit Committee could not review these accounts properly and could not utilize the opportunity to issue directions to eradicate the weaknesses in the Bank's credit process as one of the prime roles of audit committee is to provide oversight of Company's system of internal controls.

Audit observations where advances made by the Bank have not yielded returns and recovery is doubtful had featured in Reports of C&AG of India in earlier years[63] also. However, the Bank had failed to eradicate weaknesses in its credit process as evident from the NPA cases discussed above.

4.7.6 Information Technology Systems

As Information Technology (IT) becomes more pervasive, technology-based solutions are increasingly used for business operations. In order to ensure smooth functioning of IT systems, effective design and operation of automated internal controls are also becoming more and more important. In order to automate its operations through Core Banking Solution (CBS), the Bank employed 'Finacle' application in the year 2003. Following deficiencies were noticed with regard to IT systems of the Bank:

i) Incorrect linking/ Non-linking of PANs

Bank's policy on Know Your Customer (KYC) norms and Anti Money Laundering standards stipulates that Business Unit should verify the genuineness of Permanent Account Number (PAN) Card submitted by customer by authenticating the same on the income tax web portal enabled through bank's intranet. Further, the RBI advised (November 2016) all the banks to ensure quoting of PAN while accepting deposit of more than ₹50,000 in cash.

[63] Para No. 5.2 of Report No. 1 of the year 2018; Para No. 5.1 of Report No. 3 of 2015, Para 3.1 of Report No. 2 of 2016 of Government of Jammu and Kashmir

PAN is a ten-digit unique alphanumeric number issued by the Income Tax Department. The fourth character of PAN represents the status of the PAN holder[64]. Data analysis showed that bogus PANs were entered in case of 3,944 accounts. Further, a test-check of accounts[65] showed that cash deposits in excess of the threshold limit of ₹50,000 were accepted in case of 21 such accounts, indicating that mechanism was not in place to counter high cash deposits in accounts linked with bogus PANs. We also observed that there was no inbuilt feature in Bank's IT system to ensure authentication of PAN while entering it in the Finacle, which resulted in non-linking/ incorrect linking of PAN with Customer Identification Numbers (CIDs).

The following deficiencies were also noticed:

- A test check of 36 CIDs[66] revealed that PANs of Individuals were linked in case of CIDs of three registered companies[67]. Further, PANs were not linked in case of CIDs of six registered companies[68].
- Out of six CIDs where PANs were not linked, high value cash transactions (credits) ranging between ₹2.50 lakh and ₹15.00 lakh were allowed in case of M/s Green Land Cements Private Limited during the period from October 2017 to January 2019, thereby violating advisory of the regulator.
- Cash transactions (credits) ranging between ₹1.00 lakh and ₹5.82 lakh were also allowed in accounts of two customers[69] during the period from November 2016 to March 2019, despite the fact that PANs were not tagged with the CIDs.
- Test-check of 43 CIDs of borrowers who were provided benefit under Interest subvention scheme further revealed that in case of five customers[70] registered as Private limited companies, PANs of individual/ firms were linked. Out of these five customers, cash deposits ranging between ₹37 lakh and ₹50 lakh were made in March/ April 2019 in current deposit account of M/s Kehwah Xpress Services Pvt. Limited.
- In case of two CIDs[71], bogus PANs (with fourth character as 'D') were linked. Both these customers were advanced consumption loans of ₹10 lakh each during April/ May 2017.

64 'P' stands for Individual, 'C' stands for Company, 'H' stands for Hindu Undivided Family, 'A' stands for Association of Persons, 'B' stands for Body of Individuals, 'G' stands for Government Agency, 'J' stands for Artificial Juridical Person, 'L' stands for Local Authority, 'F' stands for Firm/ Limited Liability Partnership and 'T' stands for Trust

65 Out of 3944 accounts, 138 accounts were test-checked

66 Pertaining to NPA cases of registered Companies

67 CIDs-002762993 (M/s Meera Motors Pvt. Limited), 006167698 (M/s Jammu Chemicals Pvt. Limited) and 001962191 (M/s Sultan Agro Tech Pvt. Ltd.)

68 CIDs-003169820(M/s Astra Asia Therapeutics Pvt. Limited), 003169831 (M/s Tanwell Tanneries Pvt. Limited), 042916165 (M/s Green Land Cements Pvt. Limited), 004139797 (M/s Samash Technology Pvt. Limited), 000732052 (M/s Tanwell Tanneries Pvt. Limited) and 001893604 (M/s Baba Anmol Food Pvt. Limited)

69 CIDs-011425809 (M/s Dream Travel) and 003816346 (Mr. Mohd. Ramzan Dar)

70 M/s Shuhul Automobiles Pvt. Limited, M/s Halycon Builders Developers and Construction Pvt. Limited, M/s Himalayan Rolling Steel Industries Pvt. Limited, M/s Kehwah Xpress Services Pvt. Limited and M/s Shuhul Roller Flour Mills Pvt. Limited

71 CIDs-013511049 (Mr. Amit Wanchoo) and 013635494 (Mr. Ramesh Kaul)

Non-linking or incorrect linking of PAN may result in tax evasion by individuals and entities as all financial transactions made by a particular individual or entity could not be tracked. Besides, acceptance of deposits in excess of ₹50,000 without obtaining PAN details violated RBI's advisory of November 2016.

The Management replied (August 2019) that most of the accounts were seeded with PAN/ Form 60. However, the accounts which could not be seeded with PAN/ Form 60 were centrally frozen except the Government Offices, small and other accounts. Further, a separate application for PAN/ TAN verification has been made available to business units for ascertaining the authenticity of PAN of a customer. With respect to bogus PANs, the Management stated that accounts are being rectified.

However, there was no inbuilt feature in Bank's IT system to ensure authentication of PAN while entering it in the Finacle as a result of which bogus PANs were entered in the system and incorrect PANs were linked with CIDs.

ii) High Value Transactions in small accounts under PMJDY

The RBI issued (August 2014) a press release wherein it clarified that persons who do not have any of the 'officially valid documents' can open 'small accounts' with banks under Prime Minister Jan Dhan Yojna (PMJDY). A 'small account' can be opened on the basis of a self-attested photograph and putting her/ his signature or thumb print in the presence of an official of the bank. Further, the Regulator clarified that the aggregate credits in such accounts should not exceed Rupees one lakh in a year.

Audit analysis of data revealed that no check was put in place and high value transactions were allowed in these small accounts. In 2,271 Jan Dhan accounts, 2,538 high value credit transactions exceeding ₹one lakh and ranging up to ₹ten lakh were noticed during the months of March 2018 and March 2019, thereby violating RBI guidelines.

The Management replied (August 2019) that in case of PMJDY accounts there were adequate checks in place in the system for disallowing high value transactions in such accounts. However, on fulfilling the full KYC requirements, transaction limits shall not be applicable to such PMJDY accounts, as allowed by the regulator.

The reply is not acceptable as high value transactions were noticed in 397 PMJDY accounts where full KYC was pending as of June 2019.

iii) Non-closure of small accounts pending KYC

The RBI (August 2014) clarified that the 'small accounts' would be valid normally for a period of twelve months. Such accounts would be allowed to continue for a further period of twelve more months, if the account holder provides a document showing that she/ he has applied for any of the Officially Valid Document (OVD), within twelve months of opening the small account.

Audit, however, observed that the Bank had allowed operations in 1,64,816 small accounts where KYC was pending for more than two years, as the IT systems of the Bank were not programmed to deactivate or stop operations in these accounts.

Age-wise analysis of data further showed that out of 1,64,816 small accounts, KYC in case of 1,15,428 accounts were pending for more than four years.

Non-closure of small accounts where KYC is pending for more than two years resulted in exposure to the risk of being used by criminal elements for money laundering activities, besides violating the guidelines of the Regulator.

The Management replied (August 2019) that most of the small accounts pertained to beneficiaries of social welfare schemes and customers belonging to lower economic strata of the society.

The reply is not tenable as the cases highlighted above were operational small accounts where KYC was pending for more than two years.

iv) Non-strengthening of SWIFT related controls

The RBI asked (February 2018) all the scheduled commercial banks to implement and strengthen SWIFT[72] related operational controls in a time-bound manner. Records showed that the Bank failed to ensure that the users entering/ passing/ authorizing the transactions in CBS[73] are different from those operating in SWIFT. Further, the Bank failed to ensure that the logs generated from SWIFT were fully reconciled for financial and non-financial messages independently on a daily basis by either the internal audit or concurrent audit. As the Bank failed to implement SWIFT related controls within the timelines set by the Regulator, penalty of ₹two crore was imposed (February 2019) on the Bank by the regulator.

The Management replied (August 2019) that the RBI direction stands complied as the integration of CBS with SWIFT has been completed and the SWIFT messages are getting generated from CBS (Finacle) itself.

However, the Bank failed to comply with directions within the timelines set by the Regulator as a result of which it had to pay a penalty of ₹two crore.

v) Punching of Date of Birth in Finacle System

The date of birth as part of the customer's profile helps the bank to identify a prospective customer of legal age to open an account with the bank. Further, when the minor attains the age of majority he has to comply with certain rules before he is allowed to operate the account. The date of birth also helps the Bank to identify the senior citizens once the account holder reaches the age, as the bank offer special privileges to senior citizens.

Data analysis revealed that 'Date of Birth' in case of 14,51,988 Customer IDs (CIDs)[74] had not been entered in the Finacle system, in absence of which the age of the customer could not be ascertained and the applicability of correct interest rate could not be ensured.

[72] Society for Worldwide Interbank Financial Telecommunication system
[73] Core Banking Service
[74] Out of 1,17,97,142 CIDs

Considering the importance of date of birth in identification of customer, the 'Date of Birth' field should be made mandatory.

vi) Non-uploading of scanned signatures

The Corporate Office of the Bank advised (June 2017) all operating levels to ensure that signatures are scanned and uploaded into the system immediately on opening of the new customer accounts in the eligible schemes of the bank, besides also ensuring that scanning of signatures in all pending legacy accounts is taken up on war footing to complete the process in minimum possible time.

Data analysis revealed that scanned signatures had not been uploaded in the system in case of 17,85,455 accounts. As such, instant verification of signature through IT system was not possible in respect of these accounts which may result in customer inconvenience, particularly while handling inter-branch transactions.

We further observed that out of these accounts, the Bank had issued cheque books in case of 22,197 accounts, thereby exposing itself to the risk of fraud.

The Management stated (August 2019) that the scanning and uploading of signatures has been undertaken on a war footing.

vii) Multiple Customer Identification Numbers allotted to one customer

The increased complexity and volume of financial transactions necessitated that customers do not have multiple identities within a bank. The RBI advised (June 2012) all the scheduled commercial banks to introduce a unique identification code for each customer which would help banks to identify customers, track the facilities availed, monitor financial transactions in a holistic manner and enable banks to have a better approach to risk profiling of customers, besides smoothening banking operations for the customers.

Audit, however, observed that multiple customer identification numbers (CIDs) have been allotted to single customer. Data analysis revealed that 9,209 customers, identified on the basis of Permanent Account Numbers (PAN) issued by Income Tax Department, had been allotted multiple CIDs ranging between two and 172 CIDs.

This defeated the very purpose of creating unique customer identification, besides rendering the database unreliable.

The Bank stated (August 2019) that it is pursuing the matter with the concerned business units.

viii) Non-capturing of details of RCs in case of vehicle loans

In order to meet the twin objectives of obtaining of Registration Certificates (RC), viz. proof of purchase of the vehicle out of the bank finance and its hypothecation to the bank, the Corporate Office of the Bank advised (January 2009) that all business units shall invariably obtain the copies of RCs in all vehicle loans soon after their disbursement.

Audit, however, observed that the IT system of the Bank had not been capturing details of RCs in case of vehicle loans[75] in absence of which the Bank Management could not exercise control through Management Information System (MIS) over the business units to ensure obtaining of RCs by them.

ix) Insurance details in case of Vehicle Loans

In order to safeguard the bank's interest, the copy of insurance cover is obtained from the borrowers in case of vehicle loans. Further, the corporate office of the Bank advised (January 2019) all the business units to ensure that the vehicles financed by them remain comprehensively insured during the course of finance, in order to safeguard the interests of the Bank.

Data analysis, however, showed that field 'POLICY-AMT' in the IT system of the Bank had not been filled in 1,464 vehicle loan accounts. Further, bogus data like '0' (28 cases), '1' (4,551 cases), '2 to 100' (173 cases) and '100000000000000' (215 cases) had been entered in field 'POLICY-AMT' of the database, thereby rendering the database unreliable.

x) Punching of value of securities in Finacle System

The data captured in the Finacle system is of paramount importance as the Bank relies heavily on this data to comply with the regulatory guidelines and also for financial reporting. The operative levels of the Bank were advised (November 2017) to cross check the security value as well as other details punched in the Finacle in respect of existing credit facilities with the records available with them and make necessary changes in CBS.

Data analysis[76] revealed that values of primary securities had not been entered in the Finacle system in case of 44 Cash Credit (CC) accounts despite the fact that the CC limits were primarily secured by way of hypothecation of stock/ debtors. It was also observed that in case of 23 accounts, the value of primary security entered ranged between 1,038 *per cent* and 1,90,533 *per cent* of the sanctioned limit.

Entering of incorrect data in the Finacle system had rendered the data base unreliable.

xi) Non-updation of KYC of high-risk customers

The RBI instructed (July 2013) all the scheduled commercial banks to carry out full 'Know Your Customer' (KYC) exercise at least every two years for high risk individuals and entities[77].

Data analysis, however, revealed that KYC of 11,901 high risk customers had not been updated so far (May 2019). Age-wise analysis of data showed that out of 11,901 customers, KYC updation in case of 2,006 customers was pending for more than three years.

75 95,385 vehicle loans were outstanding as of May 2019

76 2,933 accounts having sanctioned limit between ₹one crore and ₹five crore

77 As per guidelines of RBI, every bank is required to categorize the customers into low, medium and high risk considering parameters of risk perception like nature of business activity, location of customer, mode of payments, volume of turnover, social and financial status etc.

In absence of KYC updation of high-risk customers, the objective of KYC guidelines to prevent the bank from being used, intentionally or unintentionally, by criminal elements for money laundering activities could not be achieved.

In reply, the Management stated (August 2019) that the matter is being pursued with the business units.

xii) Non-application of preferential rate of interest on auto-renewal of term deposits of Senior Citizens

As per the Bank's policy, domestic Term Deposits of Senior Citizens of over 60 years of age shall earn 0.50 *per cent* additional rate over and above the normal rate as applicable to other term deposits.

Audit, however, observed that term deposits which were auto renewed had not been applied additional rate of interest of 0.50 *per cent,* despite the fact that the customers had attained the age of 60 years.

The Management stated (August 2019) that the matter has been taken up with the Finacle vendor.

xiii) Non-punching of date of valuation of security in Finacle System

In terms of prudential norms of RBI on Income Recognition, Asset Classification and Provisioning pertaining to Advances, collateral securities charged in favour of the bank should be got valued once in three years. Further, Bank's credit policy stipulates that fresh valuation of the property mortgaged to the bank as primary or collateral security should be made after every three years.

Audit observed that the actual dates of valuation of securities had not been punched in the Finacle system in absence of which the Management could not exercise control through MIS over the security valuations.

This may be viewed in light of the fact that values of securities captured in the Finacle system in case of 14 NPA accounts[78] have not been updated even after lapse of more than three years from the date of their entry in the Finacle system thereby contravening regulator's norms.

4.7.7 Restructuring/ Rescheduling of loan accounts

RBI guidelines allow rescheduling of repayment terms of loans in cases where borrowers face difficulties in meeting obligations due to internal and external factors. The guidelines are aimed at enabling the revival of loans and have to be considered after assessing viability of units and ascertaining certainty of repayment. The Bank regularly reviews the financial position of its borrowers through examination of their financial statements, progress of the projects for which loan have been advanced, etc. Similarly, customers who have been advanced loans, being part of consortium of lenders, are pursued through lead bankers. The credit policy of the bank prescribes

[78] Out of 37 NPA accounts test-checked

that in case of restructuring of loan assets, the sanctioning authority has to submit its proposal of restructuring to the next higher authority in the Bank hierarchy.

During 2014-18 the Bank restructured 32,893 loan accounts involving ₹5,765.64 crore. Of these, 1,780 accounts involving ₹1,906.62 crore (33 *per cent*) were downgraded to non-performing assets and eventually 79 restructured accounts were written off, involving ₹344.85 crore.

The Management replied (December 2018) that it had to restructure a large quantum of its credit portfolio in the State on account of natural calamities in September 2014 and disturbances in July 2016. They added that some accounts rehabilitated in 2014 slipped to NPA category as a result of mismatch of cash flows due to social disturbances in July 2016 and that Bank is pursuing NPA loan accounts.

The Bank's reply is not tenable as the accounts affected in July 2016 were again restructured as per Special Rehabilitation Package of 2016 and their cash flow mismatch was offset as discussed in succeeding paragraphs.

4.7.7.1 Rehabilitation Package to the borrowers hit by riots/ disturbance

Government of J&K declared (November 2016) the State as 'disturbance hit' from 08 July 2016 to 15 November 2016. In order to provide relief to borrowers affected due to turmoil/ disturbances, the RBI advised (December 2016) that all borrowal accounts as on 07 July 2016, except those which were overdue[79], should be considered for restructuring. Consequently, the Bank rehabilitated/ restructured 36,132 borrowal accounts to the tune of ₹3,265.83 crore between January and March 2017 under the Rehabilitation Package. Audit checked all 64 cases of borrowers with outstanding balances of ₹five crore and above which were rehabilitated. They included ten ineligible borrowal accounts[80] amounting to ₹333.24 crore, which were overdue as on 07 July 2016 but were included under this rehabilitation package.

> The downgrading and writing off of restructured loans showed that the purpose of revival of the loans through restructuring was not achieved.

The Management replied (December 2018) that in order to provide relief to borrowers, the Bank undertook the rehabilitation package in accordance with RBI Master Direction on Natural Calamities. As such, the Bank ensured that all dues up to 07 July 2016 were cleared and only those accounts were rehabilitated.

The Bank did not offer its comments to the specific ten ineligible borrowers pointed out by Audit which were also considered for rehabilitation.

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79 Any amount due to the Bank under any credit facility is overdue if it is not paid on the due date fixed by the Bank

80 M/s Himalayan Rolling Steel Industries Pvt. Ltd. (two Accounts), M/s HK Cement Industries (two Accounts), M/s Magpie Hydel Construction Operation Industries Pvt. Ltd., M/s Valley Fresh Cold Chain Pvt. Ltd., M/s Kashmir Premium Apples Pvt. Ltd., M/s Pinnacle Resorts Pvt. Ltd. (two Accounts) and M/s Alpine Fresh Pvt. Limited

4.7.8 Interest subvention to restructured accounts under Prime Minister's Development Package

In order to provide financial assistance for restoration of livelihood of traders/ self-employed/ business establishments etc. affected during September 2014 floods in Jammu and Kashmir State, the Scheme for Interest Subvention (Scheme) was announced by the Hon'ble Prime Minister on 07 November 2015 under 'Prime Minister's Development Package'. Accordingly, the Government of India released (25 April 2016) ₹800 crore under the Scheme. Since Jammu and Kashmir Bank Limited is convenor of Jammu and Kashmir State Level Banker's Committee (JKSLBC), the scheme was to be implemented and monitored by the State Government through the Bank. Further, the State Government accorded (29 April 2016) sanction for:

i. subsidizing interest to the extent of 50 *per cent* for the period from 01 September 2014 to 31 December 2015 in case of accounts restructured under Special Rehabilitation Package after floods of September 2014, with a cap of ₹five lakh per unit; and

ii. grant of five *per cent* interest subvention to these restructured accounts with effect from 01 January 2016 to 31 December 2019, with a cap of ₹five lakh per business unit, per annum.

Providing of interest subvention to restructured accounts

Audit observed that the Bank provided subvention to the extent of 50 *per cent* of interest charged between 01 September 2014 and 31 December 2015 to 11,449 accounts which were restructured after floods of September 2014. Scrutiny of records, however, revealed that accounts of nine ineligible borrowers which were sub-standard as on 30 June 2014 were also restructured under Special Rehabilitation Package after floods of September 2014. Subsequently, these accounts were provided interest subvention of 50 *per cent* of the interest charged during 01 September 2014 to 31 December 2015 amounting to ₹0.16 crore. Further, the Bank also provided five *per cent* of interest subvention from 01 January 2016 to 30 September 2018 amounting to ₹0.37 crore to these nine borrowers' accounts.

Since these accounts were not to be restructured as per Special Rehabilitation Package, providing of interest subvention to the extent of ₹0.53 crore was not in order.

4.7.9 One Time Settlement

The Bank had formulated a policy[81] for recovery of NPAs by way of compromise/ negotiated settlement and write-off under the guidelines of the RBI for reducing its NPA level. The position of cases settled under OTS, recovery effected and amount

[81] OTS requests received as per policy are awarded marks on various parameters and ultimate settlement amount is dependent on the quantum of marks received by the requests. The minimum settlement amount can vary from 100 *per cent* of the principal amount of NPA to any amount that may be possible to recover

waived off (Principal and Interest) during 2014-2018 is indicated in **Table-4.11** below:

Table-4.11: One Time Settlements

(₹ in crore)

Year	No of cases settled	Balance outstanding		Settlement amount		Amount waived off	
		NPA	Un-applied interest	NPA	Un-applied interest	NPA	Un-applied interest
2013-14	1,456	70.02	24.73	59.12	3.64	10.90	21.09
2014-15	1,008	47.89	27.63	44.33	3.39	3.56	24.24
2015-16	1,362	95.47	40.17	75.38	5.44	20.09	34.73
2016-17	1,326	619.95	298.66	547.00	16.26	72.95	282.40
2017-18	2,989	547.35	405.76	388.44	8.78	158.91	396.97
Total	**8,141**	**1,380.68**	**796.95**	**1,114.27**	**37.51**	**266.41**	**759.43**

(Source: Information provided by the Bank)

From the table above, it could be seen that the Bank settled 8,141 NPA cases involving outstanding balance of ₹2,177.63 crore (NPA: ₹1,380.68 crore; Unapplied interest: ₹796.95 crore) during 2014-2018 under One Time Settlement (OTS) Scheme and recovered ₹1,151.78 crore (NPA: ₹1,114.27 crore; Unapplied interest: ₹37.51 crore) through compromise/ negotiated settlements and sacrificed ₹1,025.84 crore (principal amount: ₹266.41 crore; un-applied interest: ₹759.43 crore) constituting 47.11 *per cent* of the outstanding balances of principal (19.30 *per cent*) and un-applied interest (95.29 *per cent*), respectively.

4.7.9.1 Case studies-One Time Settlement

Audit scrutiny of 21 One Time Settlement (OTS) cases (where the outstanding amount exceeded ₹one crore) revealed that in following four cases OTS was sanctioned in deviation of Bank's recovery policy which resulted in sacrificing of principal amount of ₹17.97 crore.

Sl. No.	OTS Case	Brief observations
1.	M/s Oriental Trimex Limited	• The Bank sanctioned (December 2000) a CC limit of ₹11.60 crore in favour of M/s Oriental Trimex Limited (Company) which was further enhanced (December 2012) to ₹25.00 crore. The Bank also sanctioned ILC/ FLC of ₹1.60 crore, BG of ₹1.00 crore and a term loan of ₹3.40 crore in favour of the Company. • The Company defaulted in repayment of credit facilities and the Bank declared (March 2016) accounts as NPA. The outstanding balance at the end of August 2017 against the Company was ₹33.56 crore (NPA of ₹27.22 crore and unapplied interest of ₹6.34 crore). • The Company approached (August 2017) the Bank for OTS with a total sum of ₹12.00 crore which was accepted by the Bank. • As per Bank's recovery policy, minimum recovery of ₹20.41 crore[82] was to be made under OTS. However, the Bank settled the case by accepting ₹12.00 crore and got the OTS approved from the Board.

[82] 75 *per cent* of ₹27.22 crore

		The Bank justified the deviation on the plea that its share in realizable value of security available was ₹9.69 crore. • Realizable value of Plant and Machinery (having book value of ₹12.58 crore as on 31 March 2017) was not considered at the time of settlement despite the same being hypothecated to Bank. • As per the Bank's recovery policy, huge variation in valuation of properties at the time of considering the OTS as compared to its valuation at the time of advance was to be critically examined. • However, the Bank had not examined the variation in valuation of properties despite the fact that the value of securities at the time of advance was ₹42.55 crore[83] which had come down to ₹19.38 crore[84] at the time of settlement. • Thus, sanctioning of one time settlement in deviation of Bank's recovery policy resulted in sacrificing of principal amount of ₹8.41 crore.
2.	M/s Zain Autocrafts Private Limited	• The Bank sanctioned (May 2013) a CC limit of ₹5.61 crore and a term loan of ₹0.50 crore in favour of M/s Zain Autocrafts Private Limited (Company) against primary security of hypothecation of plant and machinery, tools and equipments etc. and collateral security of mortgage of four immoveable properties valued (March 2013) at ₹6.26 crore. Besides, the personal guarantee of Directors and third party guarantee of four persons were also obtained. • The Company defaulted in repayment and the Bank classified (March 2017) the accounts of the Company as NPA. The outstanding balance at the end of October 2017 against the Company was ₹9.17 crore (NPA of ₹8.19 crore and unapplied interest of ₹0.98 crore). • The Bank settled (December 2017) the account at ₹6.15 crore under OTS. • As per Bank's recovery policy, minimum ₹8.19 crore[85] was to be recovered. • The Bank settled the case by accepting ₹6.15 crore and got the OTS approved from the Board of Directors. The Bank justified the deviation on the plea that realizable value of security available was ₹5.87 crore. However, the personal guarantees were not considered despite the fact that guarantors were having net worth of ₹five crore at the time of settlement. • Thus, sanctioning of one time settlement in contravention of Bank's recovery policy resulted in sacrificing of principal amount of ₹2.04 crore.

83 As per valuation report of June 2012/ January 2013
84 Valuation report of January 2017
85 100 *per cent* of NPA balance

3.	M/s Hind Industries Limited	• The Bank sanctioned (July 2011) a term loan of ₹40.00 crore in favour of M/s Hind Industries Limited against equitable mortgage of immoveable property, situated at Okhla Industrial Area, valued (June 2011) at ₹43.62 crore, corporate guarantee of M/s Hind Agro Industries Limited and personal guarantee of promoter Directors of the borrower company. • The Bank also sanctioned a term loan of ₹10.60 crore in favour of M/s Hind Air Links Private Limited[86] against the primary security by way of equitable mortgage of immoveable property, situated at Nariman Point Mumbai, valued (June 2010) at ₹20.13 crore and collaterally secured by way of hypothecation of current assets of the Company, corporate guarantee of the Company and personal guarantee of promoter Directors. • Further, the Bank sanctioned (July 2012) a Cash Credit limit of ₹15.60 crore in favour of M/s Integrated Livestock Village Farm Private Limited[87]. The facility was extended against primary security by way of hypothecation of stock and other current assets and collaterally secured by way of mortgage of agricultural land, situated in Aligarh, valued (January 2011) at ₹6.20 crore. • Owing to non-servicing of accounts, the Bank classified (September 2015) the accounts of all the three Companies as NPA. The outstanding balance at the end of February 2017 against the group companies was ₹59.73 crore (NPA of ₹45.90 crore and unapplied interest of ₹13.83 crore). • The Bank settled (March 2017) the accounts of all the three companies under OTS at ₹35.00 crore by considering all the three companies as one consolidated entity. • As per the recovery policy, the Bank was required to recover NPA balance of ₹4.13 crore[88] in case of Hind Air Links Private Limited, NPA balance of ₹26.17 crore[89] in case of M/s Hind Industries Limited and 75 *per cent* of NPA balance equivalent to ₹11.69 crore[90] in case of M/s Integrated Livestock Farms Private Limited. • The Bank accepted amount of ₹35.00 crore against the minimum amount of ₹41.99 crore required to be recovered from the group companies thereby departing from its recovery policy. • The Bank had not examined the variation in valuation of properties despite the fact that the value of securities at the time of advance was ₹57.38 crore[91] which had come down to ₹28.09 crore[92] at the time of

86 Sister Concern of M/s Hind Industries Limited

87 Sister Concern of M/s Hind Industries Limited

88 100 *per cent* of NPA balance

89 100 *per cent* of NPA balance

90 75 *per cent* of NPA balance

91 Immoveable property at Okhla Industrial Area with realizable value (June 2011) of ₹39.26 crore and Immoveable property situated at Nariman Point Mumabi with realizable value (June 2010) of ₹18.12 crore. It does not include value of agricultural land at Aligarh as the same was not revalued at the time of settlement

92 Valuation report of June 2016/ January 2017

		settlement, thus recording 51 *per cent* decline in value over the period of six years. • Thus, sanctioning of OTS in deviation to Bank's recovery policy resulted in sacrificing of principal amount of ₹6.99 crore.
4.	M/s Rajendra Exports	• The Bank sanctioned (February 2012) a CC facility of ₹0.90 crore in favour of M/s Rajendra Exports (firm) which was further enhanced (November 2012) to ₹two crore. The facility was extended against primary security by way of hypothecation of stocks and books debts and collaterally secured by way of equitable mortgage of property having value of ₹2.24 crore. • Owing to non-servicing of account, the Bank declared (September 2014) the accounts as NPA. • The outstanding balance at the end of February 2017 against the firm was ₹3.23 crore (NPA of ₹2.18 crore and unapplied interest of ₹1.05 crore). • As per the recovery policy, the Bank was required to recover minimum ₹2.18 crore[93] under OTS. • The Bank settled (April 2017) the account at ₹1.65 crore thereby departing from its recovery policy. • The Bank had not examined the variation in valuation of property despite the fact that value of mortgaged property had shown a decline of 33 *per cent*[94] over the period of time. • Thus, sanctioning of OTS in contravention of Bank's recovery policy resulted in sacrificing of principal amount of ₹0.53 crore[95].
	Total	**Sacrifice of Principal amount of ₹17.97 crore**

(Source: Calculations based on the information provided by the Bank)

4.7.10 Assignment of rights to Assets Reconstruction Companies

The SARFAESI Act, 2002 provides for acquisition by any Securitisation Company or Reconstruction Company of any right or interest of any Bank or Financial Institution in any financial assistance for the purpose of realisation of such financial assistance. The Bank had a policy for sale of financial assets to Securitisation Companies/ Reconstruction Companies under the SARFAESI Act, 2002 as also to other Banks/ FIs/ NBFCs etc.

92 Valuation report of June 2016/ January 2017
93 100 *per cent* of NPA balance
94 Property valued at ₹2.24 crore at the time of advance (November 2012) was valued at ₹1.50 crore at the time of settlement (January 2017)
95 ₹2.18 crore less ₹1.65 crore

The Bank sold ten NPAs to Asset Reconstruction Companies (ARCs) during the period 2014-18 by sacrificing principal amount of ₹671.10 crore and unapplied interest of ₹504 crore as detailed in **Table-4.12** below:

Table-4.12: Assignment of rights to Assets Reconstruction Companies

(₹ in crore)

Year	No. of cases sold	Balance Outstanding		Settlement Amount		Sacrificed Amount	
		NPA	Unapplied interest	NPA	Unapplied interest	NPA	Unapplied Interest
2015-16	01	38.27	1.87	38.27	1.87	0	0
2016-17	03	139.03	35.60	125.83	0	13.20	35.60
2017-18	06	1,606.35	468.40	948.45	0	657.90	468.40
Total	**10**	**1,783.65**	**505.87**	**1,112.55**	**1.87**	**671.10**	**504.00**

(Source: Information provided by the Bank)

Audit findings in respect of one of the test-checked cases sold by Bank to ARC are discussed below:

4.7.10.1 Sale of financial assets to ARC below the reserve price resulted in loss of ₹21.89 crore

The Corporate office of the Bank identified (October 2016) the account of M/s Eurobond Industries Private Limited (Company) for sale in response to which the Sale Initiating Committee recommended (January 2017) to fix the reserve price at ₹36.89 crore on 25:75 basis (Cash: Security Receipts). The outstanding balance against the Company at the end of November 2016 was ₹73.83 crore[96] against the available securities of ₹53.43 crore. The Bank management accorded (October 2017) approval for sale/ assignment of financial asset at the reserve price of ₹36.89 crore. The Bank invited (October 2017) bids, in response to which only one bid was received for ₹12 crore. After negotiations with the bidder, the Bank sold (March 2018) the financial assets of the Company to CFM Asset Reconstruction Private Limited (bidder) at a price of ₹15 crore, on Cash (25 *per cent*) and SR (75 *per cent*) basis.

Bank's policy on sale of stressed assets stipulated that realisation on sale of asset to ARC should not be less than Net Present Realisable Value (NPRV)/ Reserve Price. However, the Bank accepted the bid for the financial assets of the Company at a sale price of ₹15 crore, against the reserve price of ₹36.89 crore and departed from its policy, resulting in loss of ₹21.89 crore.

The Management replied (December 2018) that CFM (ARC) offered ₹12 crore, who had already taken over the account of the UCO Bank at 20 *per cent* which was holding 49.26 *per cent* stake in the consortium. Since the J&K Bank was holding 32.36 *per cent* stake in the consortium, it was considered fit to accept offer of CFM at 25 *per cent* of the NPA balance. Further, the account was fully provided and there was no negative impact on P&L of the bank with the deal.

96 NPA of ₹59.22 crore and unapplied interest of ₹14.61 crore

However, the sale of financial asset to ARC below the reserve price resulted in loss of ₹21.89 crore and the Bank's plea that the account was fully provided and there was no negative impact on P&L of the Bank may be seen in light of the fact that the provision was made in the accounts by charging the P&L of the Bank for the earlier years. Further, the Bank was not under any obligation to sell financial assets at a price lower than the reserve price.

4.7.11 Investments

The investment portfolio of the Bank comprised Statutory Liquidity Ratio (SLR) securities[97] and non-SLR Investments[98]. The position of investments during 2014-2018 is detailed in ***Appendix-4.1.4.***

> The Bank had to invest funds under RIDF/ NABARD/ SIDBI as it failed to meet priority sector lending targets.

- As on 31 March 2018, total Investments (SLR and Non-SLR) was ₹22,036.41 crore against ₹25,770.83 crore as on 31 March 2013.
- SLR investments increased from ₹14,067.43 crore at the end of March 2013 to ₹17,201.97 crore at the end of March 2018, registering a 22.28 *per cent* increase. The annual return on SLR investments during 2014-18 ranged between 7.57 *per cent* and 8.60 *per cent*.
- Non-SLR investment decreased from ₹11,703.40 crore at the end of March 2013 to ₹4,834.44 crore at the end of March 2018 registering a 58.69 *per cent* decrease. The annual return from Non-SLR investments was 8.87 *per cent* in 2013-14, which declined to 6.09 *per cent* during 2017-18.
- The Bank placed ₹10,971.30 crore under Rural Infrastructure Development Fund (RIDF)/ National Bank for Agriculture and Rural Development (NABARD)/ Small Industries Development Bank of India (SIDBI) during 2014-2018 at rate of return ranging between 4.45 *per cent* and 5.43 *per cent*.
- Overall annual yield on investment had decreased from 8.06 *per cent* in 2013-14 to 7.26 *per cent* in 2017-18.

4.7.11.1 Non-Performing Investments

A non-performing investment (NPI) is one where interest/ instalment (including maturity proceeds) is due and remains unpaid for more than 90 days. The movement of NPIs during 2013-14 to 2017-18 is depicted in **Table-4.13** below:

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97 Investment in securities of the Government of India issued under Market Borrowing Programme and the Market Stabilisation Scheme, Treasury Bills of the Government of India, State Development Loans of the State Governments issued under the Market Borrowing Programme

98 Non-SLR securities comprise of PSU Bonds, Corporate Debentures, Commercial papers (CP), Certificate of Deposits (CD) etc.

Table-4.13: Movement of Non-Performing Investments

(₹ in crore)

Particulars	2013-14	2014-15	2015-16	2016-17	2017-18
1. Total NPIs at the beginning of each year	95.96	144.61	251.24	369.53	569.67
2. Additions during the year	48.80	108.33	209.11	227.95	167.69
3. Total	**144.76**	**252.94**	**460.35**	**597.48**	**737.36**
4. NPIs written off	0.00	0.00	0.00	0.00	0.00
5. Recovery Made					
(a) In full	0.00	1.70	90.82	27.81	0.00
(b) By way of settlement/ sale	0.15	0.00	0.00	0.00	84.14
(c) Amount waived off under OTS	0.00	0.00	0.00	0.00	0.00
6. Total Adjustment (4+5)	**0.15**	**1.70**	**90.82**	**27.81**	**84.14**
7. Total NPIs at the end of each year (3-6)	144.61	251.24	369.53	569.67	653.22
8. Gross Investment at the end of each year	26215.85	25126.14	22882.80	23553.88	22036.41

(Source: Information provided by the Bank)

During 2013-14 to 2017-18, NPIs had increased from ₹95.96 crore at the end of March 2013 to ₹653.22 crore at the end of March 2018 whereas investment had decreased to ₹22,036.41 crore at the end of March 2018 from ₹26,215.85 crore at the end of March 2014. The Bank had recovered ₹204.62 crore during 2014-2018. The recovery of NPI as a percentage of total NPI during 2014-2018 ranged between 0.10 *per cent* and 19.73 *per cent*.

4.7.11.2 Case studies-Non-Performing Investments

Audit scrutiny of NPI cases revealed imprudent investment decisions, non-invoking of State Government's guarantee in a case and non-safeguarding of Bank's interest, which led to doubtful recovery/ loss of ₹180.43 crore in four[99] test-checked cases out of 28 NPI cases as below.

Sl. No.	NPI case	Facts
1.	Investment (December 2010) of ₹20 crore in Secured Redeemable Non-Convertible Debentures (NCDs) of M/s Elder Pharmaceuticals Limited at interest rate of 10.75 *per cent* payable half yearly and the principal amount was to be repaid in 12 quarterly instalments.	• Investment secured by first charge on immovable properties of the borrower. • The Company did not pay first three quarterly instalments of principal due on 23 March 2013, 23 June 2013 and 23 September 2013. • The half yearly interest payment due on 23 June 2013 was defaulted and the investment was declared (September 2013) as NPI. • External rating agency (M/s CARE) assigned safety rating 'A+' signifying adequate safety of investment. • The Bank's internal rating was not correct as a result of which the higher score (adequate safety) was awarded instead of lower score of moderate safety.

99 Includes case study on investment of ₹48.37 crore in Commercial Papers (CP) of M/s Deccan Chronicle Holdings Limited (Company), already commented in para 5.1 of the Report of the Comptroller and Auditor General of India for the year ended 31 March 2017

		• As per the investment policy, entry level minimum rating for debentures by external agency should be A(+) and above. Further, the proposal for investment was subject to bank's internal rating system. • The Bank could not ensure parity of internal rating with external rating.
2.	Investment in SLR Bonds of Jammu and Kashmir State Financial Corporation (a State Government of Jammu and Kashmir undertaking) of ₹seven crore[100].	• The Bonds were secured by way of guarantee of Government of Jammu and Kashmir (GoJK). • The interest payments were to be made by the Corporation on half yearly basis and principal was to be repaid on date of maturity. • The Corporation failed to make repayments as a result of which the Bank (September 2012) declared investment as NPI. • The total outstanding was ₹9.14 crore (Principal: ₹seven crore and Interest: ₹2.14 crore) by end of June 2016. • Bank did not invoke the guarantee of State Government for repayment of full principal and accrued interest thereon. • The account was settled by accepting ₹seven crore as full and final settlement against the total outstanding of ₹9.14 crore. • Interest due of ₹2.14 crore sacrificed.
3.	Investment (May 2010) in ₹100 crore[101] Deep Discount Convertible Debentures (DDCDs) of M/S Lavasa Corporation Limited.	• External rating agency (M/s CARE) assigned adequate safety rating – 'A+'[102] based on promise of 'put option' on promoter Company, M/s Hindustan Construction Company Limited. • Investment of ₹100 crore was secured by mortgage over one acre of land valuing ₹0.50 crore only. • The Bank had no specific policy/ guidelines in place for investments in unsecured financial instruments. • The DDCDs were converted (August 2010) into non-convertible debentures (NCDs) at rate of interest of 10.75 *per cent* per annum redeemable on 12 May 2015. • Bank had right to exercise 'put option' for repayment of principal at the end of 39th, 48th and 60th month from closing date of offer or on a material breach of contract if breach not cured within 60 days.

[100] Investment in Bonds of face value ₹three crore at interest rate 8.30 *per cent* with date of maturity as 20 February 2012, Bonds of face value ₹two crore at interest rate 7.92 *per cent* with date of maturity as 26 July 2012 and Bonds of face value ₹ two crore at interest rate of 6.50 *per cent* with date of maturity as 12 March 2013

[101] At a discount of ₹six crore

[102] Instrument with this rating offer adequate safety for timely servicing of debt obligations

		• Company made interest payments up to August 2011 and expressing inability to pay further interest requested non-exercise of 'put option'. • In lieu of non-exercising of put option – rate of interest raised from 10.75 *per cent* per annum to 12.50 *per cent*. • Company could not make interest payment due on February 2015 and Bank exercised put option available at 60th month. • Company expressing inability to honour repayment of NCDs, Bank declared (June 2015) the NCDs as NPI. • The investment was sold (October 2018) to an ARC for ₹13.50 crore. • The Bank lost ₹130.87 crore (Principal: ₹82.89 crore and Interest: ₹47.98 crore) in the sale.
4.	Investment of ₹48.37 crore in Commercial Papers (CP) of M/s Deccan Chronicle Holdings Limited (Company)	• Investment was made (27 March 2012) in deviation to RBI guidelines as internal credit analysis of CP was not carried out by the Bank and it relied on external rating of 'A1+'[103] by M/s Credit Analysis & Research Limited (CARE). • The CP were due (26 June 2012) for redemption with maturity value of ₹50 crore. • The Company failed to pay the redemption amount and the Bank declared (September 2012) the investment as a Non-Performing Investment (NPI). • The Bank filed (November/ December 2012) an application for recovery of dues in Debt Recovery Tribunal-1 (DRT), Mumbai and winding up petition at National Company Law Tribunal (NCLT). As per the approved resolution plan, the Bank's share was ₹0.95 crore. However, the implementation of the Resolution Plan was pending (October 2019). • The Bank overlooked the constraints[104] highlighted by M/s CARE while assigning the rating of A1+. • The Bank did not take cognizance of decline of 73.87 *per cent* in Company's profit for period ending December 2011 vis-à-vis profit for the period ending December 2010. • The Bank also ignored the fact that the stocks of the Company which were trading at ₹180 in Mumbai Stock Exchange during April 2010, fell to ₹49.20 in December 2011.

[103] Instrument with this rating offer very strong degree of safety for timely servicing of debt obligations

[104] Higher collection days leading to stretched working capital cycle, decline in the profitability margins and inherent industry risk, political uncertainty in Andhra Pradesh for its publication business, current ratio and quick ratio declined between March 2010 and March 2011 and the Company posted decline of 11.15 *per cent* in 2010-11 in Publication Division which was the core business of the Company

		• There was an issue of CP of the same value i.e. of ₹50 crore by the Company, subscribed by the Bank, which carried a settlement date of 27 March 2012 which is the commencement date of the current CP, i.e. roll over, that met with default. This indicated that the fresh issue of CP was a renewal or means of providing funds to the Company to honour its repayment commitment in the earlier CP. • Thus, investment in CP in violation of the RBI guidelines and by placing complete reliance on the ratings of CARE led to doubtful recovery of ₹47.42 crore[105].
	Total	**Doubtful recovery/ loss: ₹180.43 crore**

(Source: Calculations based on the information provided by the Bank)

4.7.12 Priority Sector Lending

All the Commercial Banks are advised by RBI to lend to priority sector[106] at 40 *per cent* of Adjusted Net Bank Credit (ANBC)[107] on the rate of interest, as determined from time to time. The advances extended to Priority Sector are detailed in ***Appendix-4.1.5***.

There had been shortfall in all the years during 2014-2018 in lending to the Agriculture Sector. The highest shortfall was ₹4,601.56 crore (in 2016-17) and least shortfall was ₹1,815.63 crore (in 2017-18). Under Micro & Small and Other Enterprises sector, the shortfall was ₹828.72 crore (14.57 *per cent* of target) during 2013-14. The lending to weaker sections sector saw a shortfall of ₹756.20 crore (13.81 *per cent* of target) during 2016-17.

The Bank had not fixed any targets for recovery and has not maintained data pertaining to movement of NPAs under Priority Sector during 2013-2018. The NPA ratio for advances to this sector was 2.28 *per cent* at the end of March 2014 and 4.77 *per cent* at the end of March 2018.

The Management stated (December 2018) that the Bank has been making efforts to achieve targets of loan disbursements under priority sector. The Bank had to face disturbances/ calamities which culminated in targets under priority sector not being achieved.

The Management's contention of targets under priority sector lending not being achieved due to disturbances/ calamities in the home state is not acceptable as there was shortfall of 44.06 *per cent* and 31.66 *per cent* during 2013-14 and 2015-16 respectively under Agriculture Sector which was before the difficult business period quoted.

105 ₹48.37 crore less ₹0.95 crore
106 Agriculture sector, Weaker sections of society and Micro, small and other enterprises
107 Net Bank Credit (Gross advance less provisions) *plus* investments made by banks in non-SLR bonds held in 'Held to Maturity' category

4.8 Compliance framework

The activities of the Bank are subject to and controlled by various regulatory and statutory bodies besides its own internal control procedures. The broad internal controls in the Bank are its:

- **Stock audit** wherein the Bank periodically reviews borrower's credit availing capacity through physical verification of stocks against which Bank has extended credit;
- **Credit audit** wherein Bank reviews the compliance of the terms and conditions prescribed while extending loan;
- **Concurrent audit** of its branch level operations and **Risk Based Internal Audit (RBIA)** of activities to ensure operational risk levels are within acceptable limits**.**

The external controls on the Bank are exercised by operation of various Acts and policy frameworks[108] made thereunder by the regulator viz., the RBI. Besides, the Bank is subject to audit by its Statutory Auditors who are appointed by the C&AG. Further, C&AG also conducts supplementary audit of the accounts of the Bank under section 143 of the Companies Act, 2013.

The C&AG also conducts compliance audit of the Bank and significant issues of interest noticed during audit are reported to the State Legislature through its Audit Reports.

4.8.1 Post-sanction follow-up of Advances

Bank undertakes review of its advances portfolio on regular basis as a part of internal control. Credit Policy of the Bank stipulates close supervision and post disbursal follow up of advances for timely detection of warning signals and taking preventive measures for avoiding possible slippage into NPAs. The procedures for review of advances are discussed below:

4.8.1.1 Non-periodic review of Working Capital Limits

The Bank procedures stipulate renewal/ review of all working capital credit limits sanctioned and outstanding at least once in a year. All renewal of sanctioned working capital shall be ensured within due dates and not later than three months after due date in accounts, where it was not possible due to specific reasons.

The Bank had not reviewed/ renewed all the Working Capital (WC) limit accounts, as laid in Credit Policy. The shortfall in review/ renewal of accounts during 2013-14 to 2017-18 ranged between 3,612 (2.33 *per cent*) and 37,126 (7.42 *per cent*). Age-wise analysis of accounts revealed that 3,143 out of 5,00,403 accounts remained un-reviewed/ un-renewed as of March 2018, for more than three months, thereby enhancing the chances of slippage of these accounts to NPA.

The Management attributed (December 2018) the major portion of pendency in the renewal of working capital limits to Kissan Credit Card (KCC) Scheme where review is on annual basis but the renewal of the facilities is to be conducted after five years.

[108] Prudential norms on Income Recognition, Asset Classification (IRAC) and Provisioning pertaining to Advances, Know Your Customer (KYC) norms, RBIA etc.

The Bank added that follow-up mechanism for review/ renewal of accounts has been strengthened.

The reply of the Management is not tenable as the KCC accounts remaining un-reviewed/ un-renewed for more than three months constituted 21.96 *per cent,* 36.53 *per cent* and 30.26 *per cent* of the total working capital accounts remaining un-reviewed/ un-renewed for more than three months during 2015-16, 2016-17 and 2017-18, respectively.

Non-review/ renewal of working capital limits of the loans beyond three months after the due date had resulted in inadequate monitoring of the 3,143 accounts and indicated inadequate internal control.

4.8.1.2 Stock Audit

Credit policy of the Bank (2013) stipulates annual stock audit[109] of all accounts availing fund-based working capital limit of ₹one crore and above. In accounts where working capital limit is ₹0.50 crore and above, but designated as high risk, annual stock audit is done.

Table-4.14 indicates the position of stock audits planned and conducted during 2013-18 with working capital limit of ₹one crore and above:

Table-4.14: Stock Audit

Year	Targets/planned	Actually conducted	Shortfall	Percentage of shortfall
2013-14	838	777	61	7.28
2014-15	687	610	77	11.21
2015-16	765	697	68	8.89
2016-17	500	354	146	29.20
2017-18	810	731	79	9.75

The Management assured (December 2018) for completion of stock audit of eligible accounts on time.

In absence of timely stock audit, the Bank management could not review the performance of accounts and ensure the end use of funds. Audit also observed, in cases where deficiencies were pointed out by stock auditors, corrective measures were taken by the Bank before renewing working capital credit facilities.

4.8.1.3 Credit Audit

Credit Policy of the Bank also stipulates that all borrower accounts where Bank has exposure of ₹one crore will be subject to internal credit audit annually. Audit noticed that the Bank neither planned credit audit of all the eligible accounts during 2013-2018 nor conducted credit audit of all the accounts planned for coverage during this period. The shortfalls ranged between 50.78 *per cent* and 70.80 *per cent*, as detailed in **Table-4.15**:

[109] Including Book Debts

Table-4.15: Credit Audit

Year	Number of accounts having exposure of more than ₹one crore and above (A)	Targets/ planned (B)	Actually conducted (C)	Shortfall (A-C)	Percentage of shortfall
2013-14	3,264	1,615	953	2,311	70.80
2014-15	3,159	1,831	1,516	1,643	52.01
2015-16	3,471	1,818	1,585	1,886	54.34
2016-17	3,692	1,749	1,332	2,360	63.92
2017-18	4,145	2,571	2,040	2,105	50.78

Analysis showed as many as 109 observations relating to deficiencies in documentation and securities, non-conducting of external credit rating, infirmities in insurance covers, non-obtaining of fresh valuation of properties etc. were pending for compliance, as of February 2018.

The Management replied (December 2018) that care is taken to cover all the accounts during the particular year but there were some deficiencies in timely completion. They added that of the 109 observations raised in the credit audit, more than 50 *per cent* observations stand rectified by the concerned units and rest are under process.

The point stays that the Bank had not been able to complete the credit audit of targeted accounts within the scheduled time period. Observations raised in credit audit still remained un-attended, periodicity of which could not be ascertained in Audit as age-wise data of observations was not available.

The non-conducting of credit audit on regular basis deprived the Bank Management an opportunity of picking up early warning signals and initiating timely corrective action. Test check also showed that out of 29 NPA cases highlighted in the report, credit audit was not conducted regularly in 13 NPA cases.

4.8.2 Legal Audit and Status of cases under litigation

Credit policy of the Bank stipulates (April 2013) that the title deeds and other documents received in respect of all credit exposures of ₹five crore will be subject to annual legal audit. Re-verification of title deeds with relevant authorities was to form part of regular audit exercise till the loan stood fully repaid. However, legal audit department was established only by April 2016 and the Bank had not fixed any targets for legal audit during 2016-17 and 2017-18. Further, the Bank did not have any approved legal audit policy until July 2018 when the first ever policy on legal audit was approved by the Board of the Bank.

The Management stated (August 2018) that the Bank had initially fixed target of auditing legal documents for all loan accounts with credit exposure of ₹50 crore which was achieved as of 31 March 2018. They added (December 2018) that legal audit policy of the Bank was approved by the Board of Directors in July 2018 and now, the legal audit of all accounts exceeding exposure of ₹five crore would be covered.

Thus, the control requirement as stipulated in credit policy of regular verification of legal documents had not been fulfilled.

4.8.2.1 Position of NPA cases under litigation

As of March 2018, 1,686 cases involving ₹2,117.61 crore were under litigation. Pending litigation cases included 378 cases involving ₹194.71 crore filed more than five years back, where final decisions from competent courts were awaited. The Bank could not execute orders passed in its favour in 518 cases involving ₹26.84 crore. It could not effect recovery or dispose-off assets of borrowers in 620 cases involving ₹241.91 crore, where decrees in favour of the Bank had been executed.

The Management attributed (December 2018) the delays to non-taking over of mortgaged properties in absence of the borrowers/ guarantors to execute the orders and procedural delays in disposal of mortgaged properties.

4.9 Lead Bank Scheme

As per the directives of the RBI, the Lead Bank Scheme came into existence with objectives of improvement in branch expansion, financial inclusion, deposit mobilisation and lending to the priority sectors, especially in rural/ semi-urban areas.

i) Financial Literacy Camps

In terms of RBI guidelines (June 2013) the rural branches were required to hold at least one financial literacy programme every month and the banks were also advised (January 2016) to organise special camps for five target groups[110] during 2016-17.

Details of Financial Literacy camps conducted by the Bank during last four years ending March 2018 are given in **Table-4.16** below:

Table-4.16: Financial Literacy camps

Particulars	2014-15	2015-16	2016-17	2017-18
Targets	5,070	5,295	33,264	5,676
Achievements	2,750	2,759	2,182	3,745
Shortfall	2,320	2,536	31,082	1,931
Per cent	45.76	47.89	93.44	34.02

(Source: Information provided by the Bank)

The Management attributed (December 2018) the shortfall to natural calamity and social causes. The Management may make efforts to improve Bank's social outreach.

ii) Finance to Joint Liability Farming Groups of 'Bhoomiheen Kissan'

Government of India launched (October 2014) a scheme for landless farmers called 'Joint Liability Farming Groups of Bhoomiheen Kissan' to be implemented through NABARD. The Bank could not achieve targets set by NABARD for formation of Joint Liability Groups (JLGs) during 2016-2018. The shortfall ranged between 12.02 *per cent* and a high of 81.82 *per cent*, as detailed in **Table-4.17** below:

[110] Farmers, SHGs, Micro & Small Entrepreneurs, Senior Citizens and School children

Table-4.17: Finance to JLGs under Bhoomiheen Kissan Scheme

(₹ in crore)

Year	Target	No. of JLGs formed	Shortfall	*Percentage* of Shortfall	Accounts of JLGs credit linked	Amount of Credit
2015-16	641	304	337	52.57	207	3.14
2016-17	749	659	90	12.02	546	10.21
2017-18	2,112	384	1,728	81.82	310	3.71

The Management attributed (December 2018) low take-off of JLG scheme to the social causes which had adversely affected the credit dispensation.

iii) Financial Inclusion plan of J&K State

RBI advised (December 2015) the State Level Bankers Committee (SLBC) convenor banks to identify villages having population of more than 5000 but without any branch of scheduled commercial banks and allot these to banks for opening of branches by 31 March 2017. In J&K State, 104 such villages were identified by J&KSLBC and 48 villages were allocated to the Bank. RBI allowed (May 2017) to provide banking services cover in these villages by opening 'CBS-enabled Banking Outlets'[111]. Records showed that the Bank had covered only nine such villages by the end of May 2018.

The Management stated (December 2018) that the Bank had expedited the process of coverage of these locations and has further covered 12 more locations, thus taking the total number of villages to 21. The opening of banking outlets in other uncovered villages is under process.

4.10 Human Resources Management

As per Bank's recruitment policy, the posts of Probationary Officers (POs), Relationship Executives (REs) and Banking Associates (BAs) are required to be filled through a written examination conducted by Institute of Banking Personnel Selection (IBPS) or by any other agency, as decided from time to time. The written examination shall be followed by interview to be conducted by selection committee of the Bank. Further, as per the practice in vogue, the Chairman of the Bank had made need-based appointment of attendants/ sub-staff. Since the records relating to appointment of attendants/ sub-staff had been seized by Anti-Corruption Bureau, Kashmir, the same were not made available to audit for scrutiny.

The details of Bank's business and manpower for the last five years ending 31 March 2018 are given in **Table-4.18** below:

[111] Core Banking Solution (CBS) enabled Banking Outlet is a fixed point service delivery unit, manned by either bank's staff or its Business Correspondent where services of acceptance of deposits, encashment of cheques/ cash withdrawal, lending, transfer of money are provided for a minimum of 4 hours per day for at least five days a week

Table-4.18: Bank's Business and Human Resources

Particulars	March 2014	March 2015	March 2016	March 2017	March 2018
Number of Employees[112]	10,418	10,281	10,161	10,022	11,422
Total Business[113] (₹ in crore)	1,09,913.17	1,06,061.64	1,15,252.88	1,21,725.15	1,37,870.78
Business per Employee (₹ in crore)	**10.55**	**10.32**	**11.34**	**12.15**	**12.07**
Number of Business Units	777	817	857	865	904
Employees per Business Unit	13.41	12.58	11.86	11.59	12.63
Employee Cost (₹ in crore)	743.91	894.03	1,057.4	1,122.54	1,286.88
Cost per Employee (₹ in crore)	**0.07**	**0.09**	**0.10**	**0.11**	**0.11**

(Source: Data provided by the Bank and Bank's Annual Report for the respective years)

Analysis showed that number of employees of the Bank had increased from 10,418 by end of March 2014 to 11,422 by end of March 2018 and business per employee had also increased from ₹10.55 crore by end of March 2014 to ₹12.07 crore by end of March 2018. The cost per employee which was ₹0.07 crore in March 2014 had increased to ₹0.11 crore in March 2018.

4.10.1 Irregularities in recruitment process

In order to meet its manpower requirement, the BODs of the Bank resolved (December 2014) to recruit 1,014 Relationship Executives (REs) and 554 Banking Associates (BAs). The Bank invited (March 2015) online application for the post of REs. However, posts of BAs were not advertised. The written examination of REs consisted of three tests viz., English Language (30 marks), Reasoning (35 marks) and Quantitative Aptitude (35 marks) aggregating 100 marks and were conducted in September 2015 through Institute of Banking Personnel Selection (IBPS). Out of 38,000 candidates who appeared for the examination, IBPS shortlisted (September 2015) 6,155 candidates by applying test-wise criteria[114].

The Bank, however, revised (December 2015) the requirement for the post of REs to 1,327 on district-wise basis, out of which 760 vacancies (57 *per cent*) were allotted to Kashmir Division, 520 (39 *per cent*) to Jammu Division and 47 (four *per cent*) to Ladakh Division, on the basis of total business handled by each division.

However, the Bank applying fresh criteria decided to interview candidates with minimum 30 marks (overall)[115] in the written examination and called (December 2015) 3,107 candidates for interview. Interviews of 2,851 shortlisted candidates[116] were conducted between June 2016 and September 2016.

Meanwhile, the BODs accorded (March 2017) approval for creation cum appointment of 350 REs and 1,250 BAs citing huge time gap between the two assessments (December 2014/ 2015 and March 2017).

The Bank declared (March 2017) the final result for the post of 350 REs. 1,250 candidates were offered (March 2017) the post of BAs, against which only 872 joined. The Bank offered post of BAs to 378 more candidates in order of merit,

112 Including contractual employees
113 Advances plus Deposits (Net-off Inter-bank deposits)
114 Minimum marks to be obtained in each test
115 Without any minimum marks criteria for each test
116 256 candidates did not appear for interview

after BODs approval for filling up the unfilled posts in the cadre, out of 2,851 interviewed candidates.

Further, the BODs accorded (September 2018) approval for initiating recruitment process of 1,200 BAs and 250 Probationary Officers (POs). The Bank advertised the recruitment notification for said vacancies in October 2018. The BODs also accorded (October 2018) approval to appoint 582 leftover candidates as BAs, out of 2,851 interviewed candidates.

Audit observed the following:

- The Bank had an Officers Service Manual 2000 which was the policy document for Human Resources (HR) related issues. The Manual *inter alia* included J&K Bank Ltd. Officer Recruitment, Discipline, Conduct and Appeal Rules 2000. However, the Manual was not reviewed during the period between July 2000 and August 2018. Resultantly, recruitment of officers/ employees during this period were made on the basis of rules which were not updated, as discussed in succeeding paragraph.
- The Bank advertised (March 2015) the post of REs without disclosing the number of vacancies to be filled, as the same was not required to be disclosed as per Recruitment Rules in vogue. The requirement of notifying the number of vacancies was incorporated only in September 2018.
- The Bank prepared district-wise merit list of 3,107 candidates. The fact that the recruitment would be district-wise was not mentioned in the advertisement notification. Bank's recruitment policy did not specify preparation of merit list on district-wise basis and the decision was taken by the Chairman without approval of the BODs.
- The District-wise preparation of merit list allowed the Bank to call 1,377 candidates (44 *per cent*) from Jammu Division, 1,614 candidates (52 *per cent*) from Kashmir Division and 116 candidates (four *per cent*) from Ladakh Division, whereas as per short listing by IBPS on the basis of marks obtained in individual tests, 57.60 *per cent* successful candidates were from Jammu Division, 39.80 *per cent* from Kashmir Division and 2.60 *per cent* from Ladakh Division.
- The Bank did not have any defined criteria approved by the BODs for selection of candidates for interview, thereby leaving scope for flexibility in shortlisting the candidates. This was evident from the fact that the IBPS initially shortlisted (September 2015) 6,155 candidates[117] which was revised to 3,107 after deciding to call district-wise candidates with minimum of 30 marks in the written examination. Further, the short listing of candidates by applying the fresh criteria was approved by the Chairman without placing the same before the BODs.
- The Bank did not place (March 2017) any agenda papers before the BODs for seeking its approval for creation cum appointment of 350 REs and 1,250 BAs, against recruitment of 1,014 REs and 554 BAs, as approved earlier by the BODs in

[117] After applying test-wise and category-wise criteria as per Bank's requirement

December 2014. The same was got approved from the BODs without detailed analysis of manpower requirement. The Bank also did not apprise the BODs that it had advertised (March 2015) only for post of REs and the appointment of 1,250 BAs would be out of the shortlisted candidates who appeared for post of REs.

- The BODs desired (20 March 2017) that there shall be no waiting list in respect of those vacancies which remained unfilled due to non-joining of selected candidates. The Board further directed that recruitment process should be completed in a time bound manner. However, the BODs overturned its earlier decision and accorded (September 2017) approval for filling up of 378 vacancies in BAs cadre from the available shortlisted candidates.
- The Bank initiated (6 October 2018) the recruitment process for filling of posts of 1,200 BAs. However, the Bank appointed (16 October 2018) 582 leftover candidates as BAs, out of 2,851 selected on the basis of written exam conducted in September 2015.
- The Bank advertised (March 2015) the posts of REs, whereas the shortlisted candidates were offered the posts of BAs, indicating Bank's extemporary approach in recruitment of employees. This may be viewed in light of different roles, responsibilities, qualification etc. attached to the posts of REs and BAs.
- As per the Bank's recruitment policy, the minimum qualification for the post of clerical staff (Banking Associate) was graduation from any recognized university. However, the Bank invited (March 2015) applications for post of REs with minimum qualification as 55 *per cent* marks in graduation or 50 *per cent* in post-graduation. The Bank's offer of posts of BAs to candidates shortlisted against the posts of REs without advertising these posts had deprived the graduates of the State with required eligibility criteria from participating in the selection process**.**

Thus, number of posts was not disclosed in the advertisement and was kept open-ended as a result of which the Bank revised the manpower requirement from time to time without detailed analysis. There was no Board-approved policy with regard to shortlisting of candidates on district-wise/ test-wise basis. The Bank offered appointments to 2,560 candidates to the post of RE/ BA in multiple tranches[118] during March 2017 to October 2018 by shortlisting the candidates on the basis of written examination conducted for the post of REs and held way back in September 2015. The purpose of conducting the interview was also defeated as 90 *per cent*[119] of the interviewed candidates were offered appointment for the post of RE/ BA.

The Management admitted that the number of posts for RE was not mentioned in the advertisement notification and stated (November 2019) that Recruitment Policy 2018 has now provided for notifying the number of vacancies in the advertisement notification. They also added that the Bank shall review Recruitment Rules on annual

118 350 candidates were offered post of RE and 1,250 candidates were offered post of BA in March 2017, 378 candidates were offered post of BA in September 2017 and 582 candidates were offered post of BA in October 2018

119 2,560 out of 2,851 interviewed candidates

basis. Further, the advertisement notification did not mention any selection procedure to be followed by the Bank. However, the selection of REs/ BAs was done on the basis of requirement as per Board Resolution. The Management further stated that the candidates who were not considered for post of RE were offered post of BA to fill the vacancies in BAs, as recruitment process is a costly and time consuming affair.

Since there was no Board-approved policy with regard to shortlisting of candidates on district-wise/ test-wise basis, the criteria applied for shortlisting of candidates should have been approved by the BODs. Further, appointment of 350 REs and 1,250 BAs, against recruitment of 1,014 REs and 554 BAs, as approved earlier by the BODs in December 2014, was got approved from the BODs without detailed analysis of manpower requirement. The Bank's offer of posts of BAs to candidates shortlisted against the advertised posts of REs had deprived opportunity to the graduates of the State with less than 55 *per cent* marks, thereby restricting the competition.

4.11 Corporate Social Responsibility (CSR)

As per the provisions of Companies Act, 2013 read with Companies (Corporate Social Responsibility Policy) Rules, 2014, the Bank formulated CSR Policy for incurring expenditure under CSR activities. The main objective of the Bank's CSR Policy envisaged continuous commitment to operate in an economically, socially and environmentally sustainable manner, so as to ensure upliftment of the marginalized and under-privileged sections of the society.

The Bank spent, directly or through various implementing agencies, ₹95.80 crore on the projects/ activities under CSR during 2014-15 to 2017-18. CSR Policy of the Bank stipulates that it shall spend a maximum of 15 *per cent* of the prescribed CSR budget for a single activity/ project and not more than 35 *per cent* in a single segment. Audit, however, observed, that in contravention to its CSR Policy, the Bank had spent 53.09 *per cent* and 83.82 *per cent* on a single activity/ project (Kashmir Golf Course Development) during 2016-17 and 2017-18, respectively**.** Further, the Bank had spent 49.33 *per cent,* 75.99 *per cent* and 95.27 *per cent* under a single segment (Ecology and Environment) during 2015-16, 2016-17 and 2017-18, respectively.

> Bank spent ₹39.17 crore during 2015-16 to 2017-18 on re-development of Kashmir Golf Course owned by GoJK, ₹6.28 crore on Amusement Park at Pahalgam, ₹1.51 crore on printing of Ration Cards (RCs) issued by State Government during 2015-16 in contravention of the Bank's CSR policy.

The Management replied (December 2018) that CSR is a Board level activity and all the decisions regarding CSR activities/ programs remain in the knowledge of the Board. Accordingly, deviations for segment/ project approvals are exercised by the Board within the purview of its powers.

The reply of the Management is not tenable as the Board was not apprised of the fact that the expenditure on the particular activity/ program exceeded the threshold fixed under the CSR policy.

Following deficiencies were noticed in spending of CSR fund by the Bank:

i) Expenditure on re-development of Kashmir Golf Course out of CSR fund

The Bank incurred an expenditure amounting to ₹39.17 crore during 2015-16 to 2017-18 on re-development of Kashmir Golf Course, owned by GoJK, in contravention of the Bank's CSR policy, which focuses on upliftment of the marginalized and under-privileged sections of the society. We also observed that redevelopment of golf course under CSR activities was approved by the Board without the same being placed before the CSR Committee of the Board, thereby deviating from Bank's CSR policy.

The Management stated (December 2018) that floods in 2014 damaged the Golf Course and the Bank as a conscious corporate took up its re-development under CSR.

We are of the opinion that as Bank's CSR policy focuses on upliftment of the marginalized and under-privileged sections of the society, the expenditure on re-development of golf course, which is a preserve of the elite, was not in order. Further, the expenditure on Golf Course during 2016-18 constituted 47.73 *per cent* of the total funds spent under CSR activities by the Bank during this period.

ii) Expenditure on Amusement Park, Pahalgam

The Bank incurred an expenditure of ₹6.28 crore on Amusement Park, Pahalgam under the segment 'Ecology/ Environment' during 2015-16 to 2017-18. The amusement park is an entertainment spot and expenditure thereon was not related with ecology & environment activities.

iii) Expenditure on printing of Ration Cards issued by State Government

The Bank incurred an expenditure of ₹1.51 crore out of CSR funds, on printing of Ration Cards (RCs) issued by State Government during 2015-16, despite the same being responsibility of State Government, for which cost was charged from beneficiaries. The Management replied (December 2018) that the issue will be taken up with the concerned departments.

iv) Monitoring of CSR projects

Rule 5(2) of CSR Rules, 2014 stipulates that the CSR Committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the Company. Audit observed that an adequate and transparent monitoring mechanism commensurate to the size and nature of expenditure incurred by the Bank was not in place.

The Management stated (December 2018) that the monitoring system shall be strengthened further.

4.12 Conclusion and Recommendations

- The Bank had not complied with the SEBI Regulations and some of the provisions of Companies Act, 2013 relating to corporate governance. The Bank may adopt the best practices to ensure good corporate governance;
- Overlooking and non-enforcement of internal control procedures, inadequate security cover, improper credit appraisal, non-adherence to the pre or post-disbursement conditions of the sanctions, irregular monitoring etc. were observed which contributed to advances turning into NPAs. There was loss/ non-recovery of ₹197.98 crore, doubtful recovery of ₹1,599.14 crore and excess payment of ₹14.10 crore in the 29 cases. The Bank may exercise due diligence while extending credit facilities, so as to safeguard its interests;
- The Bank's credit control system and financial reporting system was deficient. The Bank may improve the monitoring system of advances to ensure that high risk accounts are identified in time and corrective steps taken to prevent slippage to NPA;
- Deficiencies were noticed in IT systems of the Bank. The Bank may take steps to strengthen controls of its Information Technology Systems;
- The Bank sanctioned OTS in deviation of its recovery policy resulting in sacrifice of principal amount of ₹17.97 crore in test-checked cases. The Bank may settle the OTS cases strictly in accordance with the policy guidelines and ensure realisation of principal amount in full;
- Imprudent decision-making, non-invoking of guarantee and non-safeguarding of Bank's interest led to doubtful recovery/ loss of ₹180.43 crore in test-checked NPI cases;
- The Bank could not achieve targets under priority sector lending. The Bank may make efforts to achieve the targets under Priority sector lending;
- Irregularities in recruitment process were noticed. The Bank may take steps to streamline its recruitment process; and
- The Bank incurred irregular expenditure on activities in violation of its CSR policy. The Bank may spend money under CSR activities strictly in accordance with its CSR policy.

The cases pointed out are based on test check conducted by Audit. The Bank may initiate action to comprehensively examine similar cases and take necessary corrective action.

लोकहितार्थ सत्यनिष्ठा

Dedicated to Truth in Public Interest

This Paragraph is an excerpt from the Audit Report No. 1 of 2020 - Revenue Sector and Public Sector Undertakings (Social, General and Economic Sectors), Government of Jammu & Kashmir. The full Report can be accessed through https://cag.gov.in/ag/jammu-kashmir/en/audit-report/details/111857