CHAPTER-II

2.1 Performance Audit on Industrial Development Activities of Tamil Nadu Industrial Investment Corporation Limited

Executive Summary

Tamil Nadu Industrial Investment Corporation Limited (Company), is a deemed State Financial Corporation under the State Financial Corporation Act, 1951. Its share capital of ₹321 crore was contributed by Government of Tamil Nadu (GoTN) and Small Industries Development Bank of India (SIDBI) to the extent of 94.56 per cent and 5.30 per cent respectively. Audit took up the Performance Audit of this Company covering its activities from 2011-16 to evaluate the system for planning, mobilisation of funds, sanction and disbursement of loans, monitoring of the assisted units, recovery performance and effectiveness of internal control.

Planning

The Company did not prepare corporate plan setting up long term goals and strategy as directed (April 1989) by the GoTN. The annual plans also suffered due to fixation of adhoc targets, belated approval by the Board of Directors (BOD) etc.

Mobilisation of Funds

Short comings noticed in mobilisation of funds were (i) non receipt of equity from two State PSUs as committed by GoTN, (ii) lack of plan for disinvestment of shares from assisted units, which had market value of ₹173.87 crore and loss of ₹36.17 crore due to non availing of exit offers from three companies (iii) not floating the public bonds at the market rate of interest, resulting in additional interest commitment of ₹9.56 crore.

Sanction and disbursement of loan

Deficiencies in the sanctions included assistance to incapable promoters, sanction of loans inspite of non fulfillment of conditions, sanction to unviable projects, sanction with inadequate collateral securities, sanction based on unrealistic projection etc. These failures led to accumulation of overdues amounting to ₹47.44 crore in respect of 22 cases test checked.

Monitoring of assisted units

There was shortfall ranging between 10 and 53 per cent during 2011-16 in carrying out mandatory inspection of the assisted units. The deficient inspections led to accumulation of overdues amounting to ₹35.53 crore in 15 cases test checked. The Company also failed to obtain the audited financial statements and monthly stock statements from the assisted units as required.

Recovery performance

The Company fixed the targets for recovery ranging from 25 to 85 per cent of total dues during 2011-16, which were equivalent to or less than the current dues. Due to deficiencies in recovery, the Company could not recover ₹56.37 crore in 13 cases test checked.

Though the Company agreed with SIDBI to maintain Non Performing Assets (NPA) within 10 per cent, its NPA increased from 10.27 in 2011-12 to 13.64 per cent in 2015-16, resulting in non-accrual of internal source of funds to the extent of ₹83.23 crore.

During 2011-16, the Company took possession of 111 units out of 169 defaulting units. The shortfall in take-over of defaulting units indicated that the Company had exercised selective approach in take-over of the assets without any recorded justification.

The Company sold assets of 135 units in auction and realised ₹11.88 crore, which constituted only two per cent of the total outstanding amount of ₹677.35 crore in respect of these units.

Internal Control and Internal Audit

Out of the total of 42 Board meetings during 2011-16, the Directors representing MSME and Finance department were absent in 30/28 meetings. The contract for web centric solutions to be completed within two years of award (March 2011) remained incomplete even after five years. The Company had no internal audit manual and the audit committee did not review the internal audit functions.

Conclusion

The performance of the Company would have been better if it had drawn long term strategy plan, mobilised its resources economically and avoided deficiencies in sanctions, monitoring the assisted units and recovery of loans. These deficiencies found in the earlier Performance Audit continued despite COPU's recommendation to improve the system for sanction, disbursement and recovery of loan.

Recommendations

Drawing long-term corporate plan, evaluation of cost of borrowings from various sources to ensure economy, ensuring the viability of the project by independent assessment of the projections, ensuring strict adherence to the procedures for sanction and disbursement, continuously monitoring the assisted units, etc., are some of the Audit's recommendations.

Introduction

2.1.1 Tamil Nadu Industrial Investment Corporation Limited (Company), a deemed[21] State Financial Corporation (SFC), was formed in the year 1949. The Company's Share Capital (as on 31 March 2016) of ₹ 321 crore[22] was mainly contributed by the Government of Tamil Nadu (GoTN) and Small Industries Development Bank of India (SIDBI) at 94.56 *per cent* and 5.30 *per cent* respectively.

2.1.2 The Company, which has been mandated to render financial assistance to the industrial units within the State, extends term loan for setting up industrial units and their expansion, Working Capital Term Loan and discounting of bills. Besides, the Company is the implementing agency of the GoTN for disbursement of loan to sugar mills at concessional rates.

Organisational Setup

2.1.3 The Management of the Company is vested with a Board of Directors (BOD) comprising of 10 Directors including the Chairman and Managing Director (CMD), who is assisted by eight[23] functional heads. The Company's business is carried out through a network of six Regional Offices (ROs) headed by the Regional Managers and 25 Branch Offices (BO) in different places headed by Branch Managers.

Scope and Audit Methodology

2.1.4 The performance of the Company was last reviewed and included in the Report of the Comptroller and Auditor General of India (Commercial) for the year 2003-04 – Government of Tamil Nadu. In this review, Audit reported that loans were sanctioned in several cases despite adverse factors brought out in appraisal notes and without adhering to the terms and conditions of sanctions. The Committee on Public Undertakings (COPU), which discussed the review in December 2009, had recommended to the Company to take recovery action in respect of held up dues on account of deficient sanctions, disbursements and follow-up of loans.

The current Performance Audit (PA) of the Company was conducted between April and August 2016 covering its activities for the five years from 2011-12 to 2015-16 to assess the improvement in the system for sanction, disbursement and recovery of loans, monitoring of assisted units, possession and disposal of the assets taken over from the defaulted units in the light of the earlier Audit as well as COPU's recommendations.

The scope and objectives of the PA were shared with the management by way of an entry conference held on 13 June 2016. During the conduct of

---

[21] As per Section 46 of the State Financial Corporation Act,1951 (SFC Act), the Central Government may notify any institution established by the State Government as deemed SFC which will derive powers as per the provisions of the SFC Act.

[22] The balance 0.14 *per cent* was contributed by Co-operative banks, Insurance Companies and Government of Puducherry

[23] Two General Managers, two Deputy General Managers, three Assistant General Managers and a Company Secretary.

Performance Audit, records of 10[24] out of 25 branches, three out of six Regional Offices and the Company's Corporate Office at Chennai were test checked. The draft PA report was forwarded to the GoTN/Company in October 2016 and the audit finding were discussed in an exit conference held on 14 November 2016 with the Principal Secretary to the GoTN, Industries Department and the CMD of the Company. The views expressed by the GoTN/Company in the exit conference as well as in the replies furnished (November 2016) by the Company have been considered and incorporated where ever found appropriate.

Audit Objectives

2.1.5 The objectives of the PA were to ascertain whether:

- the Company had framed long/short term plans for improving its overall performance.
- the Company had mobilised the required financial resources efficiently and economically.
- there was an efficient system in place for sanction and disbursement of loans.
- the Company had effectively monitored the assisted units for recovery of dues; and
- an effective internal control system, including internal audit, was in place to manage and improve upon mistakes/lapses.

Audit Criteria

2.1.6 The audit criteria adopted were:

- Provisions of the SFC Act, 1951, Micro Small Medium Enterprises (MSME) Act, 2006 and Companies Act, 1956 and 2013.
- Guidelines of Small Industries Development Bank of India (SIDBI)/Reserve Bank of India (RBI) and GoTN.
- Industrial policy of GoTN.
- Terms and Conditions of sanctions, disbursements and recovery of loan assistance.

Audit Findings

Audit findings are discussed below:

[24] Branch Offices at Chennai, Thiruvallur, Tambaram, Coimbatore, Kurichy, Pudukottai, Erode, Tiruppur, Vellore and Villupuram. The Branch offices as well as files for sanction of loans were selected based on stratified sampling method.

Planning

Long-term planning

2.1.7 The GoTN directed (April 1989) all PSUs to draw up corporate plan setting out goals and strategy for achieving their goals. The Company, however, did not prepare such a long term plan suggesting strategy for better performance. Thus, the Company had not only lacked long term strategy but also did not comply with the Government's directives.

The Company replied that it would explore performance oriented long term strategy as suggested by Audit.

Short-term planning

2.1.8 The Company prepared short term plans in the form of annual budgets. The budgets and the actuals of the Company for the five years ending 2015-16 are detailed in **Annexure-3**. Audit observed the following:

- Though annual budgets are to be finalised before the commencement of the financial year, the Company submitted the budgets to the BOD in the first quarter of each year during 2011-16 (except 2012-13), which forced it to achieve the target of 12 months in nine to ten months every year.
- Audit could not verify the rationale for fixing targets for sanctions, disbursements of loan. The Company neither offered any justification nor fixed any benchmarks for such targets.
- After approval of the budget, BOD did not review the actual performance and the reasons for variations to guide the Company for improving its performance. Instead, the BOD issued only a general advice to the Company to achieve the targets and to contain the NPAs.

The Company replied that the provisional targets were communicated to the branch offices from the very beginning of the financial year. However, Audit could not find such instructions to the branches in any of the financial years during 2011-16.

Mobilisation of funds

2.1.9 The financial position and working results of the Company for the five years upto 2015-16 are as given in **Annexure-4 and 5.**

The resource-mix used by the Company for disbursement of loans and repayments to financial institutions, during the five years upto 31 March 2016 are detailed in the following table:

Table 2.1.1 Mobilisation of funds

(₹ in crore)

Particulars	2011-12		2012-13		2013-14		2014-15		2015-16	
	Target	Actuals	Target	Actuals	Target	Actuals	Target	Actuals	Target	Actuals
Total Cash outflow	1280.41	1134.54	1416.32	1358.70	1577.10	1560.93	2034.16	1813.86	2184.17	1775.20
Resources:										

Particulars	2011-12		2012-13		2013-14		2014-15		2015-16	
	Target	Actuals	Target	Actuals	Target	Actuals	Target	Actuals	Target	Actuals
Share capital/Ways and means	---	---	---	---	---	37.50	---	---	---	---
Refinance/ Borrowings	375.00	164.57	240.00	146.65	209.00	105.76	250.00	182.65	220.00	200.80
Bonds	---	---	150.00	---	150.00	150.00	200.00	---	200.00	---
Call Deposits	45.00	81.88	150.00	188.52	230.00	128.50	250.00	245.60	255.00	105.22
Plough back	860.41	888.09	876.32	1023.53	988.10	1139.17	1334.16	1385.61	1509.17	1469.18
TOTAL	1280.41	1134.54	1416.32	1358.70	1577.10	1560.93	2034.16	1813.86	2184.17	1775.20

Source: Data collected from annual accounts of the Company.

From the table, it could be seen that the Company resorted to borrowings ranging from ₹ 246.45 crore (₹ 164.57 crore *plus* ₹ 81.88 crore) and ₹ 306.02 crore (₹ 200.80 crore *plus* ₹ 105.22 crore) in 2011-16, which entailed additional burden of interest payments. The deficiencies noticed in mobilisation of funds are discussed below:

Non-receipt of capital contributions

2.1.10 The Company requested (June 2015) to the Government, to release capital of ₹ 200 crore to strengthen its capital base. Audit noticed that though the Government had concurred (September 2015) to give such share capital assistance through two PSUs, *viz*., State Industries Promotion Corporation of Tamil Nadu Limited (SIPCOT) and Tamil Nadu Industrial Development Corporation Limited (TIDCO), the assistance was not received by the Company as the modalities of release of the share capital assistance by these two PSUs was not finalised by the Government till date (November 2016). Consequently, the Company continued to avail loan from banks resulting in extra interest burden of ₹ 4.83 crore[25].

Blocking up of funds in investments

2.1.11 The Company held investments valuing ₹ 53.99 crore in 53 companies as on March 2016. A review of the investments by Audit revealed that:

- Though the State Government had issued (April 1990) instructions to the PSUs to review the investments in assisted companies after three years of their investments, the investments were held by the Company without any time limit and the vintage of this investment ranged way back from 1960 to 1998.
- The book value of investment of ₹ 4.57 crore in 29 companies had become "NIL" as on 31 March 2016 due to poor performance of the companies.
- The Company failed to review possible disinvestments of its shares in 21 companies which had higher market value (₹ 173.87 crore) than book value of ₹ 48.64 crore.
- The monetary limit fixed (May 1988) by the Government for taking disinvestment decisions by the Company was only ₹ 50 lakh. When the

25 Interest calculated at the rate of 9.66 *per cent* being the average cost of capital for the year 2015-16.

Company received (between December 2007 and June 2011) offers from three promoters for buyback of the shares (with monetary value above ₹ 50 lakh), it could not decide on these offers and referred (between November 2010 and May 2014) the matter to the Government for its decisions, which was not received till date (October 2016). Consequently, it lost potential revenue of ₹ 36.17 crore.[26]

The Principal Secretary stated in the exit conference that the recommendations given by the Committee formed in 2012 by the Government were under consideration.

Mobilisation of funds from issue of bonds

2.1.12 Based on the Government's approval (October 2012) to issue Bonds to public with repayment guaranteed by it, the Company issued (January/Feburary 2014) bonds for a value of ₹ 150 crore with effective cost of borrowings at 9.85 *per cent per annum.*

Audit observed that before arranging for mobilisation of bonds, the Company did not compare the rates of interest offered with the rates of similar credit rated organisations. Audit verification revealed that during June 2013/October 2014, Kerala Financial Corporation (KFC) which had similar credit rating had issued bonds at the rate of 9.15 *per cent per annum*. Due to issue of bonds with interest rates more than the prevailing market rates, the Company had to bear avoidable commitment of ₹ 9.56 crore towards interest on bond.

The Company replied that the interest rates are dependent on many factors like quantum of issue, maturity period, rating of guarantor *etc*. The reply was not convincing because KFC and the Company had same credit rating, but KFC was able to obtain public bonds at a cheaper rate of interest.

Borrowings from banks

2.1.13 The Company had been operating its activities through five[27] principal bankers. The Company requested (June 2010) all the banks to consider sanction of loan at a fixed rate of seven *per cent per annum* with a repayment period of seven years. None of the banks accepted the above condition. The CMD in the second instance approached (August 2010) only Indian Bank for sanction a loan of ₹ 200 crore without indicating the acceptable rate of interest. Indian Bank offered the loan at *nine per cent per annum*, which was availed by the Company between September 2010 and March 2011.

In this connection, Audit observed that the Company did not approach the Government for obtaining guarantee for term loan from banks as was done in respect of the public deposit and bonds. This would have enabled the Company to obtain loan from any of the banks based on Government guarantee. A comparison of the interest rates of State Bank of India (SBI) with that of the Indian Bank for the three years upto 2013-14 revealed that SBI's interest rate (eight *per cent*) was cheaper than the rate of Indian Bank (nine *per*

[26] Madras Aluminum Company Ltd -₹ 18.42 crore, Chettinad Cement Corporation Ltd - ₹ 17.50 crore and India Forge and Drop Stamping Ltd -₹ 0.25 crore

[27] Indian Bank, Indian Overseas Bank, State Bank of India, Canara Bank and Union Bank of India.

cent). However, the Company could not obtain the loan at a competitive rate resulting in avoidable extra interest of ₹ 4.75 crore, for the period from September 2010 to March 2016.

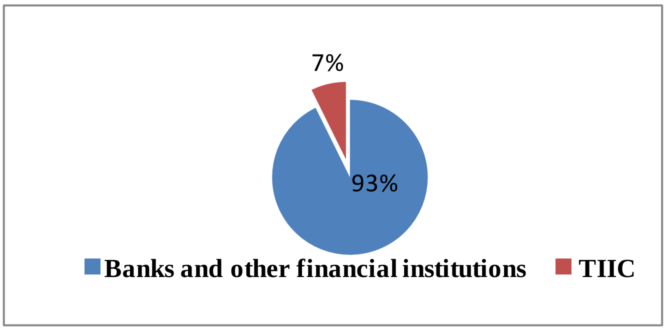
The Company replied that SBI was not willing to sanction loans with a repayment period of seven years. The reply was not convincing because Company neither approached Government for its guarantee nor tried to get loan with a lesser repayment period from SBI to obtain the loan at a cheaper rate.

Sanction and disbursement of loan

Role of the Company in MSME sector

2.1.14 The State Level Bankers' Committee (SLBC)[28], Tamil Nadu reported (April 2016) that total outstanding advances provided to the MSME sector as on March 2016 by banks and other financial institutions amounted to ₹ 63,372.75 crore against which the outstanding loan assistance provided by the Company was ₹ 4,975.80 crore. The diagram below shows the share of the Company's assistance to the MSME sector.

Role of the Company in MSME sector



The market share of assistance to MSME sector by the Company was meagre (7 *per cent*) compared to the assistance provided by the banks and SIDBI. The reasons for marginal role of the Company were as under:

- The Company is having 25 branches spread throughout the State. But, upto 48 *per cent* of the beneficiaries were covered only by four[29] branches and the individual coverage by other 21 branches was less than five *per cent* during 2011-2016. Thus, the coverage of loan assistance to the beneficiaries was not wide spread throughout the State because the sanction of loan was made by four out of 25 branches.
- The Government sanctioned (September 2012) three *per cent* interest subsidy from 2012-13 onwards to the Company to facilitate competitive

[28] A committee formed by RBI in the year 1969 to ensure co-ordination between the State Government and Banks on the matters pertaining to banking development within the State.

[29] Chennai, Thiruvallur, Kancheepuram and Coimbatore.

business. But the Company's lending rates ranging from 10.5 to 11.5 *per cent*[30] were not competitive compared to the lending rates of commercial banks, which ranged between 8.5 and 11 *per cent* during the period 2011-2016. Consequently, the Company could not substantially provide loan assistance for the industrial units of MSME sector.

- Out of 697 sanctioned loans test checked by Audit, 270 (38.7 *per cent*) loans were sanctioned with delays ranging from 50 to 200 days against the time limit of 35 days. This was attributable to procedural delays as the Company registers the application of the loanees only after ensuring that the application was received in complete shape with required enclosures.

Procedure for giving financial assistance

2.1.15 The Company provides financial assistance for setting up of new industrial units as well as for expansion of MSME units. After receipt of the application, the Company conducts technical and financial appraisals and sanctions the loan after verifying the genuineness and adequacy of securities provided by the borrower.

Sanction of loan

2.1.16 The details of achievement against targets for sanction of loan fixed by the Company for the last five years upto 2015-16 were as under:

Table-2.1.2 Sanction and disbursement of loan

(₹ in crore)

Year	Sanction of Loan				Disbur-sement	Shortfall with reference to Sanction	Percentage of shortfall of disbursement to Sanction
	Target	Achieve-ment	Short-fall	Per cent			
1	**2**	**3**	**4=2-3**	**5=4/2*100**	**6**	**7=3-6**	**8=7/3*100**
2011-12	1350	768.25	581.75	43.09	702.94	65.31	8.50
2012-13	1025	954.89	70.11	6.84	790.19	164.70	17.25
2013-14	1165	1207.75	-42.75	-3.67	1021.66	186.09	15.41
2014-15	1600	1436.13	163.87	10.24	1220.18	215.95	15.04
2015-16	1800	1448.70	351.30	19.52	1240.83	207.87	14.35
Total	**6940**	**5815.72**	**1124.28**		**4975.80**		

Source: Data furnished by the Company

Note : The variations between actual sanction and disbursement of loans for all the five years were due to release of disbursements in subsequent year and cancellation/ withdrawal of loans.

Audit observed that the Company was not able to achieve its target in four out of five years. The shortfall was high in 2011-12 which was due to upward revision (129 *per cent* of the proposed level) of the target by the BOD. Further, there was wide variation between the actual sanction and disbursement ranging from 8.50 to 17.25 *per cent*. However, the Company had not analysed the reasons for drop out of beneficiaries after sanction of loan.

---

30 After factoring the interest subsidy of three *per cent* allowable to the prompt paying loanees.

Irregularities in sanction of loans

2.1.17 The credit manual of the Company stipulated that the Company has to insist on furnishing of documents such as project report, audited financial statements, market tie-up letter, arrangement letters for working capital from the commercial banks, IT and wealth tax returns by the promoter, *etc.*, before and after sanction of loans. Audit examined the records relating to 697 out of 7,906 assisted units during the test check of 10 branch offices. The Audit examination revealed that there were inadequate pre-sanction appraisal or post sanction failures as summarised below:

Table-2.1.3 Deficiencies in pre-sanction and post sanction appraisals

Sl.No.		No. of units
A	**Procedural deficiencies in pre-sanction stage**	
(i)	Not insisting Project reports along with applications/Acceptance of Project Reports without critical study	256
(ii)	Not insisting audited financial statements of applicant units	157
(iii)	Not insisting audited financial statements of Associated units	69
B.	**Procedural deficiencies in Post sanction stage**	
(i)	Non-verification of assets	72
(ii)	Collateral Security Inflated	22
(iii)	Inadequacy of working capital	135
(iv)	Non insisting of IT/ Wealth Tax returns	317
(v)	Non verification of compliance with statutory provisions/regulations	192

Source: Audit observation based on check list furnished by the Company

Audit observed that inspite of the recommendation of the COPU in December 2009 to adhere to the laid down procedures for sanction and disbursement of loans, the Company deviated from the procedures for sanction which resulted in upsurge in NPAs and 14 such cases involving total overdue amount of ₹ 7.79 crore are given in **Annexure-6.**

The Company replied that loan application itself was structured in a manner to collect all the information required for project appraisals. The reply was not tenable because the credit manual of the Company demanded furnishing of separate documents in support of the data furnished in the loan applications. But, the same was not insisted by the branch offices of the Company in the instant cases noticed by Audit.

Sanction of loan to incapable promoters

2.1.18 As per the credit manual, the Company was required to disburse the loan after ensuring that the assisted units had actually arranged/brought in their portion of working capital. A case of violation of this provision is given below:

M/s Mahan Textiles (Private) Limited (MTPL) proposed to set up a knitted fabrics unit at a project cost of ₹ 26.30 crore. The project cost was to be met by term loan from the Company (₹ 12 crore), promoters contribution including working capital loan from bank (₹ 9.30 crore), loan from SIDBI (₹ 5 crore[31]). The loan amount of ₹ 11.94 crore was disbursed in August 2008/September 2009. As per the project report, the unit was to commence the commercial production in January 2009. But the commercial production started only in October 2010. Even after commercial production, the unit suffered due to inadequate working capital, as the promoter failed to contribute their capital and working capital loan from bank. Therefore, the Company allowed (July 2010) rescheduling of the loan upto October 2011. As MTPL paid (July 2012) only ₹ 38.87 lakh as against total overdue of ₹ 1.98 crore, the Company foreclosed (September 2012) the loan account. The Company took over the assets only in January 2014, *i.e.*, after a delay of 15 months, but the same were not disposed off till date (October 2016) due to lack of response in the auction. The total overdue amount in October 2016 was ₹ 23.04 crore (principal: ₹ 11.64 crore and interest: ₹ 11.40 crore).

Audit observed that the Company failed to take note of inadequate capital contribution made by the promoter and non-availability of working capital as required in the credit manual, but disbursed the major portion of the loan of ₹ 11.37 crore in July 2010 itself *i.e*., prior to the date of project implementation, which resulted in non-recovery of the overdues forcing the Company to write off the dues in 2015-16.

The Company replied that the failure of project was due to power cuts and problems relating to pollution and that it was taking steps for recovery of the dues. The reply was not convincing because project failed mainly due to inability of the promoter to bring in the required working capital, which the Company failed to take note of before release of the loan.

Sanction of loan despite non fulfillment of conditions

2.1.19 As per the credit manual, the Company has to ensure that the amount already disbursed was actually utilised by the loanee for the intended purpose before releasing subsequent instalments, which was not followed in the case detailed below:

The Company sanctioned and disbursed three[32] term loans amounting to ₹ 18.02 crore to Amaravathi Sri Venkateswara Paper Mills Limited (Amaravathi). These loans were disbursed for following purposes:

---

[31] Against the sanction, SIDBI disbursed ₹ 4.90 crore.

[32] First loan of ₹ 5.70 crore in June 2007, the second loan of ₹ 6.50 crore in January 2010 and the third loan of ₹ 5.82 crore in January 2011.

Loan No	Month of disbursement	Amount (₹ in crore)	Purpose
1.	November 2007	5.70	Import of second hand de-inking machinery.
2.	March 2010	6.50	Takeover of loan given by India Overseas Bank for expansion of the plant capacity.
3.	November 2011	5.82	Construction of a factory building and erection of machinery.
	Total	**18.02**	

The assisted unit defaulted in repayments from 2013-14 onwards due to operational loss and non-implementation of the expansion unit and consequently, the amount overdue as on April 2016 was ₹ 4.80 crore including the interest overdue of ₹ 1.49 crore. As the loanee became defaulter, loan was classified as NPA. However, the Company was yet (October 2016) to takeover the assets of the defaulted unit.

Audit observed that the expansion program was not implemented by the loanee and imported machinery was kept in open yard. Consequently, Indian Overseas Bank (IOB), which initially funded the project foreclosed its loan, citing that the assisted units had delayed the implementation of the expansion programme. But, the Company took over the loan from IOB, which was not warranted because the promoter had not implemented the expansion programme. The Company also paid the third loan for construction of factory building despite being aware of the fact as a result of a joint inspection carried out with another PSU in January 2011, that the loanee had not utilised the loan of ₹ 6.50 crore paid for erecting the plant and machinery in the expanded unit. Thus, the loanee had not utilised the loan disbursed by the Company for erection of machinery and construction of the factory and continued to keep the machinery idle in the open yard. The Company failed to ensure that the loan disbursed was utilised by the loanee for the intended purpose, which led to the loan becoming NPA but the Company had not fixed any responsibility on the erring officials.

The Company replied that failure of the project was due to slow down of the market condition. But, the Company's reply was silent about Audit points about sanction of loan on unjustified grounds.

Sanction of loan to an unviable project

2.1.20 As stipulated in the credit manual, the Company has to independently verify the viability of the project and ensure the capability of the promoters.

The Company sanctioned (October 2008) a term loan of ₹ 2.00 crore to M/s Prapanjas for establishment of a resort at a location 23 Kms away from Madurai city. After disbursing (December 2008) ₹ 1.96 crore, the Company sanctioned and disbursed (September 2010) additional term loan of ₹ 2.55 crore for construction of building and purchase of machinery. The Company also granted (September 2010) a moratorium of four years against the normal moratorium of two years. Due to low occupancy, the assisted unit did not repay any amount towards principal from January 2013 till date.

Consequently, the total overdues increased to ₹ 7.32 crore (principal: ₹ 4.42 crore and interest: ₹ 2.90 crore). The loan was foreclosed in February 2016.

Audit observed that the Company failed to take note of the locational disadvantage of the project. The Company also failed to note that the promoter did not have business tie-up with tourist agents, travel companies, *etc*., but relied on the projected occupancy of 70 *per cent* from the third year of business operation. It is pertinent to note that two hotels belonging to a State PSU and located within Madurai had occupancy upto 50 *per cent* only. Further, the partners of the firm had no previous experience in the hotel industry. Thus, extension of loan to inexperienced promoter without assessing the market scenario and locational disadvantage led to non-recovery of ₹ 7.32 crore.

The Company replied that legal action has been initiated for recovery of dues.

Sanction of loan without justification

2.1.21 The Company sanctioned and disbursed (February/March 2013) a term loan of ₹ 1.93 crore to Sri Periyandavar Exports (SPE) for purchase of imported machinery for expansion of its capacity of manufacturing of cotton/knitted gloves. The Company was not regular in repayment of principal and interest from February 2015 onwards and the total overdue amount increased to ₹ 79.83 lakh in May 2016 (principal: ₹ 47.90 lakh and interest: ₹ 31.93 lakh).

Audit observed that:

- The existing capacity utilisation of the loanee was 61 *per cent* but the Company extended financial assistance for additional machinery without considering the spare capacity available.
- The Company failed to notice that the promoter had not arranged for working capital requirement amounting to ₹ 1.15 crore for the proposed expansion of the unit.
- The Company's branch office at Tambaram found during inspection (January 2015) that 17 stitching machines hypothecated to the Company were missing. But, the same branch office disbursed additional loan of ₹ 32.47 lakh in February 2015, which was irregular.

Thus, deficient sanction of loan without verification of spare capacity and working capital arrangement coupled with undue favour extended to the loanee at the branch office level led to accumulation of overdue of ₹ 79.83 lakh as on May 2016. None of the officials were held responsible for these serious lapses.

The Company replied that the project failed due to non-receipt of dues from foreign customers by the loanee. The reply was not tenable because the loan for expansion of the unit was given when the existing unit was operating with lesser capacity and subsequent disbursement was made despite missing machinery. The non-recovery of the loan was mainly due to these reasons and not due to the reasons stated by the Company.

Sanction of loan against inadequate collateral security

2.1.22 The Company sanctioned (July 2013) a term loan of ₹ 6.50 crore and disbursed (November 2013) ₹ 6.44 crore to Real Links Engineering India Private Limited (RLE), for setting up a new steel foundry in Coimbatore at a cost of ₹ 9.78 crore. Based on the loanee's request (November 2014), the repayment of the loan was postponed to commence from July 2015 and was to be completed by June 2022. Prior to rescheduling, the assisted unit paid meagre amount of ₹ 8.24 lakh upto July 2015, but started defaulting from August 2015 onwards. The loan extended to RLE became NPA in May 2016 with total overdue of ₹ 1.22 crore.

Audit observed that:

- Against the norm of obtaining 50 *per cent* of the loan amount as collateral security (₹ 3.25 crore), the Company obtained collateral security of ₹ 1.83 crore from RLE. Neither the justification for obtaining lesser security was available in the files, nor the Company fixed responsibility for the lapse.
- The BOD ignored the comments (July 2013) of the Chief Risk Officer (CRO) of the Company regarding the slow growth in foundry business in the State and the inability of the unit to arrange for working capital assistance from the banks for additional loan of ₹ 3.27 crore.

The Company replied that the sudden decline in the business was not expected at the time of sanction. The reply was not tenable because the associated risk in the foundry business was known to the Company from the remarks of CRO, but the loan was sanctioned ignoring the remarks of the CRO resulting in doubtful recovery of dues.

Sanction based on unrealistic projection

2.1.23 Mobest Associates (MA), a proprietary concern, was engaged in the manufacture of modular furniture items in Chennai since 2000. The Company sanctioned (July 2012) and disbursed (between July 2012 and January 2013) a term loan of ₹ 52 lakh for expansion of the furniture unit. Since the unit defaulted in repayment of loan from June 2014, the Company foreclosed loan in December 2014. The overdue amount loan was ₹ 69.57 lakh as on May 2016. The Company was yet (October 2016) to take physical possession of the primary and collateral security.

Audit observed that against the existing turnover of ₹ 0.96 crore for the year 2011-12, the turnover projected by the promoter was ₹ 3.52 crore for the year 2012-13. This projection was unrealistic because the promoter had achieved cumulative increase of only 40 *per cent* in the turnover in the last four years upto 2011-12. Therefore, sanction of loan on the basis of unrealistic projections with sudden increase in the turnover to the extent of 367 *per cent* within a year without any concrete evidence led to non-recovery of the dues.

The Company replied that they have decided to take possession of the unit.

2.1.24 The Company sanctioned and disbursed three[33] Working Capital Term Loans (WCTL) amounting to ₹ 1.04 crore to Andavar Modern Rice Mill (AMR) at Villupuram for building up of inventory. Immediately after disbursement of the third loan, AMR started (November 2011) to default in payment of dues and total overdue from AMR stood at ₹ 1 crore in June 2016.

Similarly, the Company disbursed (May/June 2011) WCTL of ₹ 50 lakh to Sri Panduranga Modern Rice Mill (PMR), Gingee. Since the loanee did not repay the loan from November 2011 onwards due to mismanagement of the unit by the promoter, the overdue increased to ₹ 77.38 lakh in June 2016. However, the Company was yet to takeover the defaulted unit.

Audit observed that the branch office failed to analyse the financial statements submitted by AMR and PMR before sanction of WCTL. This was evident from the fact that the cash profits of AMR were only ₹ 3.96 lakh, ₹ 3.29 lakh and ₹ 3.57 lakh in 2007-08, 2008-09 and 2009-10 respectively, but the loan was sanctioned, accepting the projected profit of ₹ 39.03 lakh, ₹ 43.65 lakh and ₹ 48.29 lakh in the first three years of operation after availing WCTL of ₹ 50 lakh in August 2010. The incorrect projection was proved by the fact that the unit earned only ₹ 4.86 lakh for 2010-11. The branch office had also not collected the financial statements for the subsequent years from 2011-12 till date.

Similarly, the financial statements furnished by PMR indicated its operating profit between ₹ 5.68 lakh and ₹ 6.70 lakh during the three years upto 2010-11. But, the branch office relied on the projections of operating profit ranging from ₹ 48.37 lakh to ₹ 60.59 lakh for three years upto 2013-14 without any evidence.

These actions were violative of the directions issued by the Company to the branch offices to independently verify the projections made by the loanee regarding viability of the project. Thus, sanction of loan by the branch office relying upon inflated estimates of profit and failure to take cognizance of the actual profit, resulted in non-recovery of ₹ 1.77 crore. The Company had not fixed any responsibility for these lapses.

The Company replied that AMR had approached the High Court, Chennai restraining its legal action. In respect of PMR, it stated that despite conducting two auctions after takeover of the assets, there were no offers. But, the reply was silent on failures of the branch offices as observed by Audit.

Non-disbursement of Government assistance

2.1.25 The Company was appointed (August 2004) as a nodal agency to provide loan assistance to sugar mills. The GoTN extended (August 2004/February 2005) loan of ₹ 113.67 crore and credited the same in the non-interest bearing RBI's public deposit account (PD Account) in the name of the Company. Out of this amount, the Company released (April 2005) only ₹ 31.00 crore to a sugar mill and the remaining balance (₹ 82.67 crore) was kept in the PD account till 2012 as the Company could not find other sugar mills, which were in need of loan between 2005-2012. Even though the

[33] First loan of ₹ 50 lakh was disbursed in August 2010, second loan of ₹ 19 lakh was disbursed in January 2011 and third loan of ₹ 35 lakh was disbursed in October 2011.

idleness of the amount in PD account was pointed out in the Audit Report (Civil) for the year 2007-08, the Company remitted back the amount to GoTN only in October 2012. Due to blocking of funds from April 2005 to October 2012 by the Company, there was avoidable interest burden to the Government to the extent of ₹ 30.62 crore.[34]

The Company replied that the delay in remitting of amount to GoTN was due to lack of directions from the Government about utilisation of the balance amount. The reply was not convincing because idleness of the amount was known to the Company and the Government from April 2005 to October 2012. But, they did not take action in a timely manner for surrender of the unspent amount resulting in loss of interest.

Monitoring of assisted units

2.1.26 As per the Company's Manual on Credit Management and Recovery, the Company was required to carry out inspection of all the assisted units on quarterly basis. The details of inspections carried out during 2011-16 are tabulated below:

Table-2.1.4 Short fall in inspection of assisted units

Sl. No	Details	2011-12	2012-13	2013-14	2014-15	2015-16
1	Total number of units	826	974	868	983	1062
2	Total number of units inspected during the year	619	855	411	582	955
3	Shortfall in inspection (Units)	207	119	457	401	107
4	Shortfall in inspection (Percentage)	25.06	12.21	52.64	40.79	10.07

Source: Data furnished by the Company

The number of units not inspected ranging between 107 in 2015-16 and 457 in 2013-14 indicated that the Company failed to carry out the mandatory inspection. The other deficiencies noticed in monitoring of the units are detailed below:

- The audited financial statements of borrower concerns/associate concerns were not obtained within six months of the closure of every financial year as required by terms of sanction in all 697 cases test checked by Audit during inspection of ten selected branch offices.
- The 697 loans test checked by Audit included 133 cases of Working Capital Term Loan (WCTL) sanctioned by the Company. The terms and conditions of WCTL stipulated that loanees had to submit monthly stock statements to the Company which would ensure that the loan was utilised only for Working Capital requirements. However, Audit noticed after disbursement of WCTL in all 133 cases, the monthly stock statements

[34] Calculated at the borrowing rate of 5.7 *per cent per annum* for six years and six months.

were not received as the Company failed to insist upon submission of stock statement from the loanees.

- The deficiencies mentioned above were against the COPU's recommendation to evaluate a system to obtain the periodical reports to assess the performance of the assisted units.

Though, the Company replied that the branch office inspected the units regularly, Audit could not verify that inspections were carried out regularly in respect of cases test checked in branch office.

The implications of deficiencies in monitoring the defaulted units are illustrated in the following cases:

2.1.27 The Company sanctioned and disbursed (between October 2005 and September 2006) a term loan of ₹ 19.37 crore to Srinidhi Fabrics Private Limited (SFPL) engaged in weaving business for expansion of its activity to bleaching, dyeing and printing of woven fabrics. After availing these loans, the borrower continued to incur losses from 2008-09 onwards due to problems related to effluent discharge and TNPCB's orders for closure of the unit upto June 2009. Consequently, the loanee did not clear the dues even after rescheduling of the loan in January 2009. Finally, the Company foreclosed the loan in February 2012, but SFPL registered (September 2012) its case with Board for Industrial and Financial Reconstruction (BIFR)[35]. As on June 2016, total overdue amount was ₹ 28.47 crore, which included principal and interest.

Audit observed that:

- Despite the borrower failing to repay the loans as per its commitment since May 2010, the Company permitted (April 2011) to sell part of the business unit without proper study on the capability of the promoter to repay the loan with reduced business prospects. Coupled with this, the delay in takeover of the defaulted unit allowed the borrower to make a reference to BIFR in July 2012 with an accumulated loss of ₹ 14.11 crore that eroded its net worth. Thus, non-compliance with proper recovery action led to non-recovery of ₹ 28.47 crore (principal overdue of ₹ 13.82 crore and interest overdue of ₹ 14.65 crore).

The Company replied that the overdue amount could not be recovered because the loanee unit was referred to BIFR in July 2012. The reply was not tenable because after TNPCB's order for closure of unit in June 2009, the loan was foreclosed only in February 2012 and there was no further action for takeover of assets till July 2012 which allowed the loanee to make reference to BIFR.

2.1.28 The Company extended five term loans and a WCTL aggregating to ₹ 1.33 crore to Sri Elumalayan Rice Mill (SERM) between October 2009 and August 2011. SERM started defaulting payment of dues from March 2012 onwards and loanee unit became defunct since May 2014. The Pudukottai Branch office of the Company inspected the unit in March 2015 and found that major machinery worth ₹ 34.40 lakh financed by it was missing.

[35] Board for Industrial and Financial Reconstruction (BIFR) is an authority formed by Ministry of Finance , GoI to declare any industrial unit as a sick industrial unit as per Sick Industrial Companies (Special Provisions) Act,1985 and offer rehabilitation packages for revival of sick Industrial units.

Therefore, the Company filed (June 2015) a criminal complaint for the missing machinery and initiated possession of the collateral properties.

Audit observed that though the manual prescribed that Branch office was to inspect defunct unit on monthly basis, the Company neither took possession of the machinery nor inspected the defunct unit as prescribed to ensure availability of the assets. The total overdues from SERM stood (July 2016) at ₹ 1.35 crore including principal of ₹ 86.59 lakh. Thus, lack of inspection allowed the loanee to remove the machinery resulting in non-recovery of the overdues.

2.1.29 The Company disbursed (January and August 2011) a term loan and WCTL amounting to ₹ 1.03 crore to an existing loanee *viz*., Southern Rubber and Company (SRC), Vellore. The borrower started defaulting in payment of dues of total loan (including earlier loan) from April 2012 onwards. The borrower submitted (October 2012) financial statements for the years 2010-11 and 2011-12 with a request for rescheduling of loans. From these financial statements, Audit observed that the promoters had withdrawn ₹ 56.88 lakh from the business after sanction of the loan in January 2011. However, the Company while rescheduling (November 2012) the loan, failed to take notice of this withdrawal. The total overdue from SRC stood (May 2016) at ₹ 2.02 crore which included principal of ₹ 1.28 crore. Such a situation could have been avoided with proper review of the financial statements of the unit which was not done by the Company.

The Company replied that withdrawal of capital was generally permitted when there were no outstanding dues. The reply was not convincing because the withdrawal of ₹ 56.88 lakh during 2010-11 by the partners was main reason for the unit becoming NPA which the Company failed to notice while examining loanee's financial statements.

In addition to the above, Audit found deficiencies in monitoring by the Company in 12 cases involving an overdue amount of ₹ 3.69 crore, as detailed in **Annexure-7.**

Recovery performance

2.1.30 Recovery of loans and advances at optimum levels provides funds for furtherance of business of a financial Company. The Recovery performance of the Company during the years 2011-12 to 2015-16 is given in **Annexure-8.**

Audit observed that the Company had fixed target equivalent to/or less than the current year's due in all the five years upto 2015-16. Moreover, no separate targets for recovery of old and current dues were fixed. In the absence of details of recovery of overdue and current demand, the Company did not have control on recovery of overdue amount.

The Company replied that recovery targets are fixed on case to case basis. The fact, however, remains that the targets were not equal even to the current year's dues and hence, was not adequate.

Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) was a scheme jointly initiated (2000) by the GoI and SIDBI to provide guarantees in respect of credit extended to MSME entrepreneurs. The Company which availed guarantee facility under this scheme was required to lodge its claim for reimbursement within one year from date of NPA. Audit noticed that the Company made a claim between June 2012 and March 2016 with CGTMSE for reimbursement of the NPA amounting to ₹ 6.85 crore in respect of 665 defaulted cases. However, these claims were disallowed by CGTMSE stating that the claims were time barred. In this connection, Audit observed that the delay was mainly attributable to the Company's failure to collect the details from the branches in respect of the cases, which had become NPA within the period of one year. Consequently, it lost an opportunity of getting reimbursement of the NPA amounting to ₹ 6.85 crore in respect of these cases.

The Company replied that the branches had been advised to explore the possibility of recovering the claims, which were rejected by CGTMSE from the loanees, who had defaulted the payments in respect of the cases. The reply was not tenable because these loans had already been NPA and the Company had lost an opportunity of recovering this amount from the CGTMSE because of its failure to adhere to the time limit.

In respect of 13 cases involving ₹ 56.37 crore, the recovery was not made due to deficiencies in the recovery system of the Company as detailed in **Annexure-9.**

Non-performing assets

2.1.31 In terms of SIDBI guidelines of November 2005 as modified from time to time, an asset becomes a NPA, when it ceases to generate income for the Company or the interest remained due for a period exceeding 90 days. The following table gives the details of NPA as at the end of last five years.

Table-2.1.5 Details of standard and non-performing assets

(₹ in crore)

Sl. No	Type of assets	2011-12	2012-13	2013-14	2014-15	2015-16
1	Total asset/loan balance	1,392,98	1,458.35	1,555.27	1,660.59	1,729.55
2	LESS: Standard assets	1,300.08	1,327.13	1,404.61	1,505.94	1,530.91
3	Non-performing assets	92.90	131.22	150.66	154.65	198.64
4	Written Off #	50.18	17.24	18.44	11.73	37.25
5	Total Non-performing Assets and Write off (3+4)	143.08	148.46	169.10	166.38	235.89
6	**Percentage of NPA to total assets as worked out by the Company**	**6.7**	**9.0**	**9.7**	**9.3**	**11.48**
7	**Percentage of NPA worked out by Audit (including write off)**	**10.27**	**10.18**	**10.87**	**10.01**	**13.64**

Source: Data furnished by the Company

Note:# Though these amounts were written off by the Company, action would be continued for recovery like other categories of NPA.

Audit observed that:

The prevailing percentage of NPA of the Company was high compared to 5.80 *per cent* (MSME 7.45 *per cent*) in the case of other Financial Institutions and Nationalised Banks in Tamil Nadu.

The Company had already agreed (December 2010) in the MOU with SIDBI that it would bring down NPA within 10 *per cent*. The excess level of NPA indicated the inability of the Company to recover the dues from the defaulters as is evident from the fact that the NPA cases increased from 285 to 1,346 and the amount increased from ₹ 92.90 crore to ₹ 198.65 crore in the last five years ending 31 March 2016. If only the Company had contained its NPA at 10 *per cent* as committed, the same would have generated internal source of ₹ 83.23 crore and would have earned an additional revenue of ₹ 8.32 crore (calculated at minimum interest of 10 *per cent).*

In all the 63 cases (₹ 14.43 crore) of NPA test checked, the Company had not invoked the personal guarantee of the promoters.

The Company which had a data of 5,329 live borrowers, data relating to 2,463 borrowers only were updated (31 October 2015) with Credit Information Bureau (India) Limited (CIBIL). This was against RBI's guidelines to update and enlist periodically the willful defaulters of ₹ 25 lakh and above to CIBIL. The shortfall in updation of the data was attributed to non-completion of the software solutions compatible to CIBIL.

Nineteen cases involving ₹ 57.77 crore which had been written off during 2011-16 had revealed various deficiencies in the recovery mechanism as detailed in **Annexure-10.** In these cases, the collateral value of the property held by the Company was ₹ 30.42 crore. However, the respective branch offices of the Company failed to take possession of these collateral securities and auction them for adjustment of the recovery of overdues.

Extension of One Time Settlement scheme (OTS)

2.1.32 All doubtful loans and loss assets[36] are eligible for settlement under one time settlement scheme provided the default was due to genuine reasons and not wilful and the borrowers were not involved in any fraudulent practices. Thus, the benefit of OTS was meant for *bonafide* defaulters only. The following table indicates the OTS cases under various categories:

Table-2.1.6 Settlement of cases under OTS

(₹ in crore)

Sl. No.	Category	Number of cases	OTS amount collected	Amount waived
1	Settlement of loss and written off category without any asset back up	94	0.74	79.99
2	Settlement of loans disbursed upto ₹ 10 lakh with asset back up and in the category of doubtful and below (including written off)	308	4.64	103.22

[36] The loans, which are identified as non-recoverable but not written off are classified as loss assets.

Sl. No.	Category	Number of cases	OTS amount collected	Amount waived
3	Settlement of loans under compromise and negotiated settlement scheme	67	10.64	385.65
	TOTAL	**469**	**16.02**	**568.86**

Source: Data furnished by the Company

Audit observed as under:

- As per the Credit Manual, the amount recovered through OTS should include principal and simple interest. In respect of 469 cases mentioned above, the amount waived was ₹ 568.86 crore, which worked out to 97 *per cent* of the total dues. It is pertinent to mention that the Company had neither valued the collateral security in hand nor invoked the same before extending the OTS scheme to the defaulters. Thus, this action of the Company was not in its financial interest.

- As per the instructions issued by the RBI from time to time, the OTS was not to be extended to the wilful[37] defaulters. However, the Company did not classify the defaulters as *bona fide* and wilful defaulters at the unit level. An independent verification by Audit of the three[38] branch offices revealed that OTS was extended to 11 wilful defaulters by collecting ₹ 0.13 crore and by waiving ₹ 15.99 crore, which resulted in extension of undue benefit to wilful defaulters.

- As per RBI guidelines and the Company's Credit Manual governing the OTS scheme, only interest is to be waived and not principal. But, Audit noticed that the BOD approved waiver of principal amounting to ₹ 14.42 crore. Even though the Company justified wavier of principal on the ground that the cases were very old, Audit found that mandatory pre-audit before extending OTS was not carried out in respect of all the 469 cases.

The above deficiencies indicated that the recovery action was not timely and OTS was extended to willful defaulters which led to increase in NPA.

The Company replied that the extension of OTS and waiver of the principal was with approval of the BOD. Notwithstanding the approval of the BOD, the concessions were extended against the RBI guidelines and without following legal process, recovery of dues from the collateral securities and guarantors, *etc*., resulting in undue benefits to the ineligible defaulters.

Possession of assisted units

2.1.33 Section 29 of the State Financial Corporation (SFC) Act empowers the Company to take possession of the assisted units and dispose of their assets to recover the dues in case of default. The details of units taken possession as on 31 March 2016 are given in **Annexure-11**

Audit observed as under:

[37] A loanee would be classified as willful defaulter if he defaulted the loan repayment despite having capacity to pay, diverted the working capital, sold or transferred the assets of the units without the approval of the financial institution.

[38] Thiruvallur (five cases), Kurichi (five cases) and Erode (one case).

- During 2011-16, the Company had taken possession of 111 units even though it had categorised 169 units for the purpose of doubtful and loss assets for which it had already made provision for 100 *per cent* of the outstanding dues. Even though the Company's Credit Manual stipulated that the assets of the defaulting units were to be taken over after 21 days of issue of notice foreclosing the loan, the shortfall in takeover indicated that the Company had exercised selective approach in takeover of the assets without any recorded justification.
- The Company did not fix any annual targets to dispose of assets. Consequently, there were 69 out of 132 units under possession for more than five years as on March 2016. Due to holding of these assets over longer period, the Company had to incur maintenance of security charges, which worked out to ₹ 4.94 crore for the period 2011-15.
- The Company conducted auctions and sold assets of 135 units and realised ₹ 11.88 crore as against the price of assets fixed by the Company amounting to ₹ 14.53 crore. Audit noticed that these amounts constituted only two *per cent* of total outstanding amount of ₹ 677.35 crore in respect of these units. It is pertinent to mention that COPU had already recommended for forming a strategy for timely disposal of assets. The continuation of delays in takeover of the assets and disposal leading to deterioration of value of assets and consequent loss implied that the Company had not implemented COPU's recommendation.

The Company replied that the takeover of units was considered as a last resort. The reply was not correct as the takeover was carried out by the Company without fixing any time limit or criteria.

Internal Control and Internal Audit

2.1.34 The following deficiencies were noticed in the corporate governance and Internal Control System of the Company:

- The Company conducted 42 board meetings during 2011-16. The Directors representing the MSME and Finance Department were absent in 30 and 28 meetings respectively. The absence of these Directors deprived the guidance of two vital departments on various issues on policy of disinvestment, mobilisation of resources including capital bonds *etc*.
- The Company decided (December 2010) to create a centralised data base to facilitate the corporate office to monitor and analyse the performance of the branch offices through web centric solution. The contract for web based solution was awarded (March 2011) for a value of ₹ 1.04 crore to Electronics Corporation of Tamil Nadu Limited (ELCOT). Though the work was scheduled to be completed in December 2012 for which the Company had already paid part amount of ₹ 66.34 lakh, the work remained incomplete due to delay in finalising the user requirement by the sub-contractor of ELCOT. Consequently, the web based data base was not implemented by the Company even after lapse of five years of the award of work order.

The Company replied that the rollout of the project was expected to complete by December 2016. The fact remains that there were unduly long delays in taking care of the above work, which was important for informed decision making by the management.

- Though the Company's existing credit policy stipulated (July 2008) that the policy was to be reviewed on annual basis, the same was not complied with for the last eight years upto March 2016. It is pertinent to mention that this lapse was also pointed out by SIDBI in their inspection report of April 2016. The Company replied that the revision of the credit policy was under consideration by the BOD.
- The BOD did not analyse the investments made by the Company in the shares of assisted units to propose to the Government for possible disinvestments at the appropriate time.

2.1.35 The Company had not prepared the internal audit manual till date, which would have outlined the standards of performance of the internal audit wing. The internal audit did not cover the planning, finance and resources management sections of the corporate office. Similarly, they did not cover the OTS scheme of the branch offices. The audit committee did not review the adequacy of the internal audit functions, as the Company placed before the audit committee meeting only the status report of internal audit with no reference to the observations. The internal audit report did not report any of the sanction failures, monitoring lapses, *etc.*, during the entire period of 2011-16 to the BOD. Thus, the internal control system in the Company was inadequate to periodically review the systems for efficient performance, as it did not help the management for taking informed decisions.

During the exit conference, the Company stated that updated internal audit manual would be submitted to BOD for approval.

Acknowledgement

Audit acknowledges the co-operation and assistance extended by the staff and management of the Company at various stages of conducting the Performance Audit.

Conclusion

The Company established to provide financial assistance to MSME sector had been rendering such assistance marginally, while the coverage by banks and others was significant. The performance could have been better if the Company had drawn a long term strategic plan addressing its weaknesses such as non-competitive interest rate and not carrying out wide spread coverage throughout the State. Though the Company earned profits in all the five years of 2011-16 and wiped off its entire accumulated loss, the profit could have been better if the Company had mobilised its resources economically and avoided the deficiencies in Sanction and disbursement of loan, Monitoring the assisted units and Recovery of loans and advances noticed by Audit during 2011-16. These deficiencies found in the earlier review and found to be continued during current PA, led to huge write off of NPA and an overall increase in NPA. There were also deficiencies in implementation of OTS as well as in disposal of the assets taken over.

Recommendations

The Company needs to:

- draw a long-term corporate plan setting out its goals and strategy for achieving them as per the directions of GoTN.
- avail the external borrowings after evaluating the cost of borrowings from various sources.
- ensure viability of the assisted project based on independent assessment before extending financial assistance.
- ensure strict adherence to the laid down procedures for sanction and disbursement of loan.
- continuously monitor the assisted units by obtaining and reviewing the financial reports and by periodical inspection.
- fix the target for recovery at 100 *per cent* of the amount due, to minimise the shortfall in recovery and NPA.
- promptly enforce legal process for recovery of overdues from collateral securities and guarantees before extending OTS facility.
- implement project of web-centric data base without further delay.

2.2 Follow up IT audit on the Computerisation of Tamil Nadu State Marketing Corporation Limited

Executive Summary

Tamil Nadu State Marketing Corporation Limited (Company) has the exclusive privilege of wholesale supply and retail vending of Indian Made Foreign Liquor (IMFL) in the State. IMFL is procured and distributed through its 43 depots and 6,200 Retail Vending Shops (RV shops) across Tamil Nadu. The Company had computerised its operations in 1998. The Company decided to upgrade the hardware and software to Oracle platform in three phases. The third phase commenced in 2009.

Previous Audit Coverage

An IT Review on the Computerisation of TASMAC was included in the Audit Report (Commercial) 2008-09 with seven recommendations which were accepted by the Company.

The present audit was taken up, as a follow-up, to assess whether the recommendations were implemented.

Recommendation 1- Uniform software in all depots

Uniform software has been implemented in 43 depots. However, due to poor management of contracts, the implementation of third phase of upgradation of software got delayed by 6 years.

Recommendation 2-Computerisation of SRM, DM offices and RV shops

The SRM and DM offices were linked with neither Godown Monitoring System (GMS) nor Integrated Information Management System (IMS) leading to duplication of works. Though 2,204 RV shops were installed with Electronic Billing Machines (EBMs), the data generated could not be used for decision making due to lack of reliability as invoices were not captured during the course of actual sales.

Recommendation 3- Input and validation checks

The deficiencies pointed out in the earlier Report such as non-availability of provision to capture multiple batch numbers, missing continuity in system generated numbers, sales to customers without verifying licenses, deficiencies in issue of transport permit, flaws in mapping tax laws and manual intervention in system generated numbers continue to remain till date (November 2016).

Recommendation 4- Development of in-house expertise for maintenance of the system

The Company did not have an IT wing supported by qualified personnel. The Company continued to employ outsourced programmers to maintain the systems.

Recommendation 5 –Protect validity and confidentiality of transfer of data

The Company continued to transfer data from depots to Corporate Office (CO) through private e-mail servers and over telephone, reducing the reliability and confidentiality of the data.

Recommendation 6 - Lay down Business Continuity and Disaster Recovery Planning

There was no access control policy to regulate access to the system. A documented backup policy involving storage both at on-site and off-site and regular restoration of backup data did not exist even now at the Company.

Introduction

2.2.1 Tamil Nadu State Marketing Corporation Limited (Company) was incorporated in 1983 as a State Public Sector Undertaking (PSU). The Company has been granted the exclusive privilege of vending Indian Made Foreign Liquor (IMFL) for the entire State of Tamil Nadu on wholesale basis in May 1983 and retail basis in November 2003. The Company procures IMFL from various manufacturers, within and outside the State and distributes through 43 depots and 6,200 Retail Vending shops (RV shops) situated in different parts of the State. The procurement of IMFL is done centrally at Corporate Office (CO) and delivered at depots which, in turn, distribute to the RV shops and directly sell to the clubs and hotels.

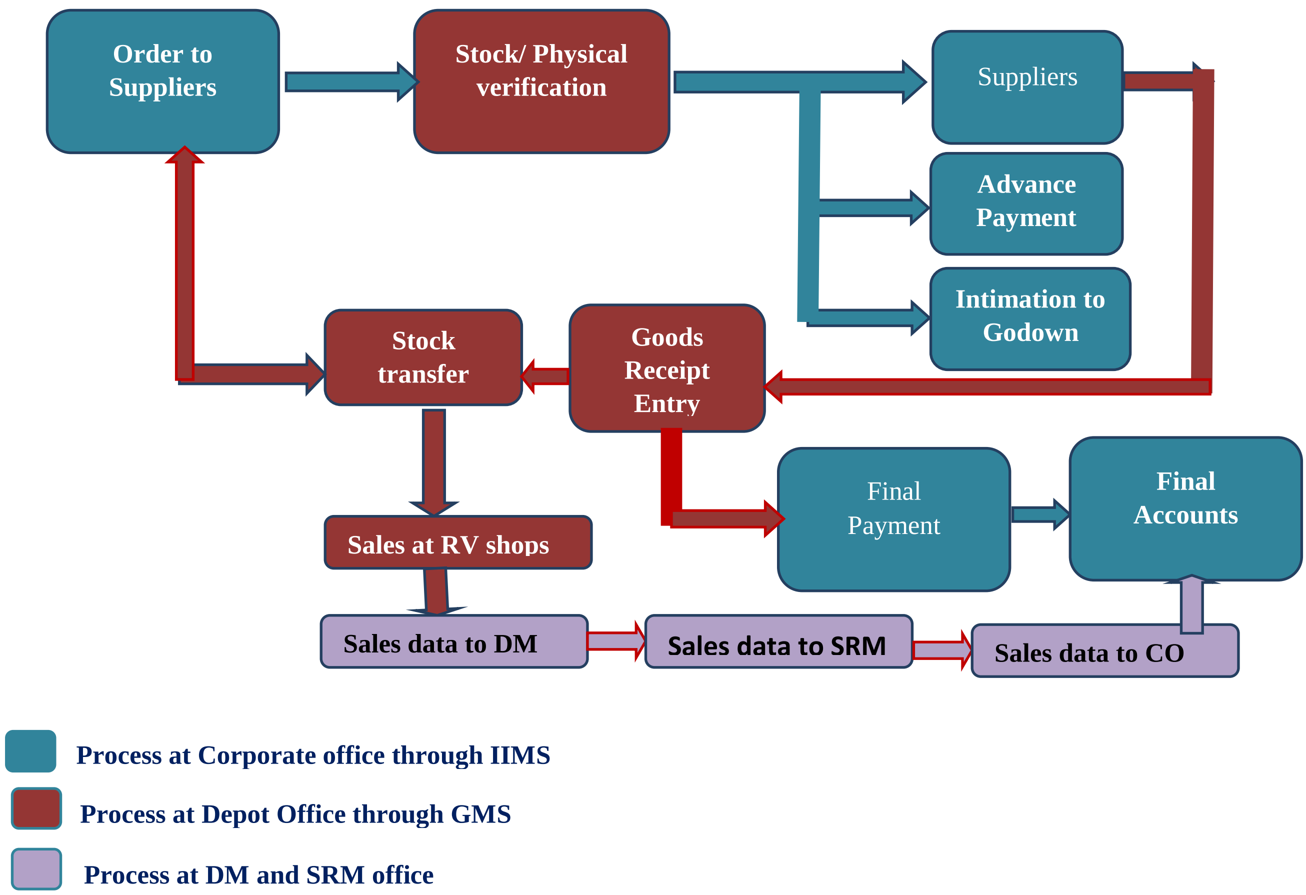
Organisational Setup and business process

2.2.2 The Managing Director (MD), assisted by three functional Chief General Managers/General Managers at CO, is the Chief Executive of the Company. In the field, there are five Senior Regional Managers (SRM) assisted by 33 District Managers (DM).

Computerisation

2.2.3 To have better inventory control, disseminate timely information to the management, supply chain management and ensure safety of the data at depots, the Company carried out (1998) computerisation of its operations such as order placement, bill processing and payment, stock monitoring, financial accounting at CO and SRM office and depot level. The above work was completed with Oracle as back end at CO and FoxPro as backend at Depots. The application used in CO was Integrated Information Management System (IMS). At depot level, the Stock Monitoring System was operated as standalone software called Godown Monitoring System (GMS). Later, the Company decided (September 2001) to upgrade the existing hardware and software at the Depots to Oracle in a phased manner. The activities of the Company are depicted in the following diagram.

Process flow diagram



Previous Audit Coverage

2.2.4 An IT audit on the Computerisaton of the Company was included in the Audit Report (Commercial) 2008-09 and was placed in the State Legislature in May 2010. During this audit, it was found that the Company failed to evolve long term strategy for up-gradation of computerisation programme resulting in incompleteness of the existing system. Deficient input controls and validation checks made the data incomplete, incorrect and unreliable. Absence of computerisation of SRM offices and RV shops led to manual interventions in assimilation of required data. Therefore, Audit had made the following seven recommendations and the Company, accepting all the recommendations, assured to take the required corrective action.

Recommendations of the earlier review

2.2.5 The accepted recommendations of the previous IT Audit were**:**

- Implementation of uniform software in all Depots
- Computerising the SRM and DM Offices and RVshops
- Building necessary input and validation checks to extract complete, correct and reliable data
- Develop in-house expertise to maintain the system

- To protect the privacy and confidentiality of transfer of data
- Lay down well documented Business Continuity and Disaster Recovery Management plan and
- Consider an integrated system for the Company's IT environment.

Scope and Methodology

2.2.6 The present audit was taken up between March and June 2016 to assess whether the recommendations made in the earlier IT audit, which had been accepted by the Company, were implemented. Audit Methodology included issue of questionnaire to the Company to elicit action taken to implement the accepted recommendations. The Company's response was analysed and verified through data analysis of records of the Company for the period 2009-16, to ascertain the extent of implementation at CO, SRM offices, DM offices, Depots and RV shops. An exit conference was held on 16 November 2016 with the Commissioner of Prohibition and Excise cum MD of the Company to discuss the follow-up audit findings. The views expressed in the exit conference and the reply received (November 2016) from the Government were considered and incorporated, wherever found necessary. The audit findings are discussed below:

Audit findings

Recommendation No.1

Implementation of uniform software in all Depots

2.2.7 One of the main recommendations of the previous Audit was to implement uniform software in all depots. However, it was noticed during the present Audit that:

Following the up-gradation of 25 depots with Oracle in the two phases between 2004 and 2008, the Company decided (February 2009) to upgrade the remaining depots in the third phase. After finalising the system requirements for the third phase, the Company issued (August 2010) Purchase Order (PO) for procurement of 16 servers at a cost of ₹ 21.21 lakh, which were delivered between December 2010 and February 2011. Subsequently, the Company decided (August 2011) to procure the desktops, operating systems, Oracle software license and database conversion job and requested (November 2011) M/s ELCOT to supply the required hardware and software by making (January 2012) an advance payment of ₹ 39.91 lakh. Though M/s ELCOT supplied (February to April 2012) desktops and operating software, it could not deliver the Oracle software because of non-finalisation of tender for supply of Oracle software due to which data base conversion was not possible. After prolonged correspondence, M/s ELCOT refunded (August 2013) ₹ 17.54 lakh, being the cost of Oracle software. In the meantime, the 16 servers already procured were utilised as replacement for the servers commissioned in the first and second phase of conversion.

The Company again placed (July 2014) order with M/s ELCOT for 17 servers at a cost of ₹ 74.68 lakh and received the same during October 2014. The

Company also procured (April 2015) 90[39] Oracle software licences from M/s ELCOT at a cost of ₹ 28.45 lakh. The database conversion work at 18 depots (16 old and 2 new) was awarded (April 2015) to M/s Broadline Computers at a rate of ₹ 45,000 per depot and work was completed in September 2016.

In this connection, audit observed the following:

- As per the PO placed with M/s ELCOT, the supply of Oracle license should be completed within one month from the date of PO, *i.e.*, by February 2012. However, ELCOT did not supply the Oracle license even after a delay of 16 months (from March 2012 to August 2013) due to its failure to finalise the rate contract for supply of the license from the outsourced agencies. Audit further noticed that the Company could not levy any liquidated damages for the non-fulfillment of the PO condition, which was due to non-inclusion of penalty clause, which mainly contributed for delayed implementation of third phase to that extent.
- The PO issued to M/s Broadline Computers also did not specify any time frame for Oracle conversion or penalty clause. Consequently, the work which was started in April 2015, could be completed only in September 2016, but the Company could not levy penalty. Hence, the depots continued to operate with dual databases.
- The work was awarded to ELCOT for Oracle conversion without mentioning any time frame, which led to abnormal delay of six years in completion of the work.

The Government replied (November 2016) that all depots of the Company have switched over to Oracle, and from 01.09.2016 onwards all depots transactions have been carried out in uniform programme. However, the reply was silent about the poor planning for implementation of the third phase of computerisation which got delayed by 6 years.

Recommendation No.2

Computerisation at SRM, DM offices and RV Shops

2.2.8 In the earlier IT Audit, we had commented that implementation of software in Depots and SRM offices in FoxPro platform was envisaged (October 1997), but no such software was being used in the SRM Offices and there was no connectivity between depots and SRM offices. During the present Audit, we noticed the following deficiencies in computerisation of SRM, DM offices and RV shops.

(a) Computerisation at SRM Offices

Though the Company had assured (November 2009) that SRM offices would be equipped with the Regional Office Information System Module (RMIS) during the III phase of conversion of 16 Depots, it was noticed during follow-up audit that the work order issued for conversion of depots under III phase did not include conversion of/installation of RMIS at SRM offices due to not analysing the user requirement by the Company. Thus, the SRM

[39] Five licenses each for 18 depots.

offices which act as a link between the depots and CO did not have access to either GMS or IMS. Due to this, data was continued to be collected through e-mail from the Depots and forwarding the processed data to CO again through e-mail, which otherwise would have been carried out automatically at SRM office. Further, this process necessitated the Depots to process the required data in MS-Excel format, which resulted in waste of time and effort at the Depot level.

The Government replied (November 2016) that computerisation of SRM offices will be taken up during the installation of integrated software like SAP/ERP software. However, we are of the opinion that before going to SAP/ERP software, the installation of existing IMS at SRM office with the access restrictions to their jurisdiction, as an immediate step would reduce the duplication work.

(b) Computerisation at DM offices

During the present audit, the following were noticed in DM offices:

- Depots collect indents from the RV shops, generate stock transfer invoice using GMS and the hard copy of invoice is sent to DM office. In DM office, the stock transfer invoice is again prepared in MS-Excel and uploaded to Electronic Billing Machines (EBM) web server. Thus, the Company failed to auto upload the GMS data in EBM, resulting in duplication of work at DM office. Further, this failure had risk of errors in data feeding manually.
- Further, to ascertain the actual sales and arrive at the amount to be remitted to the bank by RV shops, DM office collects data on opening stock, stock transfer from depots, stock returns, closing stock and bank remittance from the RV shops, in writing and feed the data into MS-Excel. Though all these information is available in GMS, EBM server and the SMS server[40], they are once again collected from the RV shops in printed forms due to lack of inter-connectivity between RV shops and DM office, resulting in duplication of work and having a risk of errors in data feeding manually.

The Government replied (November 2016) that till the EBM is installed in all the shops, the existing system will continue as it is very effective. However, the Company could have connected the already working EBMs, SMS server with GMS server and tested their effectiveness.

(c) Computerisation at RV shops

In the previous audit, it was observed that the sales figures from RV shops were passed through telephone to CO affecting the reliability and confidentiality of facts. During the present audit, it was observed that:

- The Company invited tender for procurement of 2,500 EBMs for usage at RV shops. The Company started receiving 2,500 EBMs from October 2013 in 5 lots, however, it initiated action to set up the cloud server[41] after

[40] It is a web server containing the daily sales details of individual RV Shops sent by the shop Supervisors using mobile SMSs.

[41] The cloud server is an internet based computing that provides shared computer processing resources and data to other computers and devices on demand.

three months only, *i.e.*, with effect from December 2013. Thus, the second phase of installation of 4,335 EBMs, as announced (May 2013) by the Government was yet to be taken up.

- Further, the EBM supplier had not supplied 90 EBMs in addition to the 2,500 as agreed to by him during the price negotiation, which was not insisted upon by the Company.
- Audit test checked 41 out of 2,204 RV shops EBMs data, selected randomly covering all the five regions, which revealed that on 21 March 2016 and 28 March 2016, in all the shops, invoices were prepared not in the course of actual sales but after working hours and in batches. Thus, the very purpose of EBMs *viz*., real time capture of sales details was defeated.
- Comparison of both sales details generated through SMS and EBM of Chennai North, on 29 February 2016 and 31 March 2016 revealed that there was discrepancy in both sale details. EBM values were overstated in 30 shops to the extent of ₹ 17.29 lakh and understated in 45 shops to the extent of ₹ 49.86 lakh. Since the data generated by EBM are not matching with the data collected through SMS system of collecting sales details, the same was not accurate.

Audit observed that the information captured through EBMs were not utilised for collecting daily sales details of RV shops. This indicated that an amount of ₹ 7.14 crore[42] spent for the purchase of EBMs and rental cost of cloud server, did not serve its intended purpose. The MD stated in the exit conference that a system study was under progress to integrate the EBM data with GMS and the existing EBMs will be linked in the first phase.

Recommendation No.3

Build input and validation checks to ensure completeness, correctness and reliability of data

2.2.9 The previous audit had commented on various deficiencies in input controls and validation checks.

During follow-up of earlier audit, the test check of six depots[43] revealed the following:

(a) Non-availability of provision for capturing multiple batch numbers

To ensure inventory management on first in first out (FIFO) basis as per the accounting policy of the Company, the batch number and date of manufacture must be entered at the receipt point in Goods Receipt Acknowledgement (GRA) and at the selling point. However, the GRA module had provision to capture details of only one batch for an item and not for items which have multiple batches. Similarly, sale invoices did not have provision to capture the batch details and GRA numbers. Hence, goods despatched from depots could not be linked with their receipt in the depot. Further, the age-wise inventory, sediment stock, if any, *etc*., at the depot level, were not ascertainable.

[42] ₹ 6.70 crore on procurement of EBMs and ₹ 0.44 crore on hiring of cloud servers.

[43] Ambattur I, II and III, Thirumazhisai I, II and III.

On this being pointed out, Government accepted (November 2016) that the batch details were not captured in the system, instead FIFO method was being ensured through manual control. This indicated that the deficiencies pointed during earlier audit continued without rectification till date (November 2016).

(b) Continuity in system generated numbers

GRA numbers and Invoice numbers were generated through the system automatically in GMS and hence, the numbers should be continuous. In the previous audit, as well as during the follow-up audit, it was noticed that there was no continuity in such numbers. The gaps found in documents verified by Audit are tabulated below:

Name of the document	Number of gaps	Missing numbers
GRA	**5,576**	**78,240**
Invoice	**9,817**	**4,42,148**

Audit scrutiny revealed that missing GRA/Invoices reflect cancelled ones. However, Audit trail to verify the reasons for such cancellations was not available in the software. Therefore, the justification for such cancellations could not be verified by Audit. The Government stated (November 2016) that, instructions were given to the Company to see that there were no such missing/cancellation *etc*. If at all there were any missing/cancellation, details should be recorded for future reference.

(c) Linking of Master Stock Register with Physical Verification module

The Master Stock Register (MSR) is linked with Physical Verification Excess Entry Module (PVEEM). The PVEEM has an edit option, whereby the excess stock, if any, found on physical verification, during previous day could be accounted for directly in the MSR. Though the excess/shortage of stock found during physical verification had to be adjusted in MSR only after verifying its justification by the competent authority, automatic adjustment of stock in MSR defeats the basic objective of physical verification and not having any control over persons responsible for such shortage/excess of stock. An attempt by audit to overwrite the opening stock through PVEEM was accepted by the system, indicating the continued deficiency in the system design. The Government replied (November 2016) that now the Depot Managers had been instructed to maintain excess/shortage stock in a separate file. However, the possibility of changing the stock position through the module is still prevalent.

(d) Sales to the customers without verifying validity of licenses

Invoices to customers were generated through the Retail Invoice Module by linking with the customer details. This was envisaged in the system to have internal control over the sales. During data analysis, it was observed that 25,548 invoices were issued during 2015-16 to 152 FL2/FL3 Licensees,[44]

[44] These customers represent Clubs and Hotels who are given annual licences for holding the stock of IMFL.

whose licenses had expired as on 31 March 2015. This implied that the software did not have the provision to check the validity of the licenses and refusal to generate invoices in case of expired licenses. Further, analysis showed that the details of renewal of licenses had not been updated in the system. The Government replied (November 2016) that instructions have been given to update the system through programmers.

(e) Transport Permit

As per the extant rules, liquor cannot be transported without proper transport permit. Further, as per the procedure in vogue, only one invoice should be raised per customer per day. Hence, the software was designed to generate only one transport permit for one shop against one invoice on the same day. It was, however, observed that the system allowed generation of more than one invoice per RV shop on a given day.

In view of this, if more than one invoice was prepared, the quantities relating to second invoice were being written manually in the transport permit already generated by the system. During data analysis for the year 2015-16, it was found that 534 invoices were issued with no separate transport permit through the system for goods sent from the depots to RV shops, which indicated that the business rules were not mapped in the system development even though it was pointed out in the previous Audit Report. The Government replied (November 2016) that necessary instructions have been issued to modify the programme.

(f) Non-capturing of Lab report

As a part of quality management system, the software was designed to capture the details of quality report obtained from the manufacturer's laboratory. Moreover, as per the software specification requirements, system based quality monitoring was essential to process the Bills for payment. On analysis of data, it was noticed that these details of quality checking were still not captured in the system. The Government replied (November 2016) that necessary instructions have been issued to capture the lab results.

(g) Mapping of Tax Laws

As per Section 206 C read with section 288 B of Income Tax Act, the Company has to collect tax on sale of liquor to clubs and hotels and any amount payable under this Act should be rounded off to the nearest multiple of ten rupees. It was, however, observed that the software rounded off the tax component to the next higher rupee instead of to the nearest multiple of ten rupees indicating incorrect mapping of tax laws in the software. This may result in excess/short collection. Data analysis for the period 2009-15, revealed that tax collected on sales were wrong for 17,725 sales, which resulted in excess/short collection of ₹ 40,420 / ₹ 18,518.

Though the Government replied (November 2016) that software has been modified accordingly, the data analysis at depot, however, revealed the existence of the same issue in mapping of tax laws.

(h) Manual Interventions in system generated invoice numbers

The invoice numbers were generated automatically in chronological order by the system along with system date and time. On a further scrutiny, it was found that the system dates were changed through manual intervention. Thus, the data was vulnerable to manipulation.

Data analysis revealed that in 14,820 cases, the chronological order with reference to the time and dates was missing. On this being pointed out, the Government replied (November 2016) that FL2/FL3 licensees give indents on a particular day with an assurance to lift the stock on the next day. Based on this, the invoices are prepared for the next day by changing the date in the system. However, the change in the data at the back end would amount to tampering of data and may lead to financial irregularities and possible fraud.

Recommendation No.4

Development of in-house expertise for maintenance of the system

2.2.10 Though the Company had initiated computerisation of its activities in 1998 itself, it did not have an IT wing supported by qualified personnel. Further, it was noticed that the Company continued to employ eight outsourced programmers to maintain the GMS, IMS and EBM software.

The Government replied (November 2016) that the software related services were being availed on outsourcing basis to have continuity on maintenance and updating the existing software since September 2009. The fact, however, remains that even after lapse of seven years, the programmers were continued from the same software Company. Thus, the deficiencies pointed out in the previous Report were still persisting.

Recommendation No.5

To take necessary steps to protect validity and confidentiality of transfer of data

2.2.11 GMS data available in the depot offices was not uploaded automatically to the Central server, which was located at CO. The data from depots is transmitted every day to the CO as text files/zip files through internet using private e-mail IDs, which would result in data being stored in foreign server and thus, possibility of external threats to data would increase. Further, the daily sales figures from the RV Shops, through SRM and DM offices, were passed over the telephone to the CO, thus reliability and confidentiality of the facts could not be taken care of. Thus, the Company was yet to ensure validity and protect confidentiality of transfer of data.

While accepting the audit observation, the Government stated (November 2016) that as the Company did not have an independent holistic system having own servers, integrated IT system covering all aspects, it was dependent upon private e-mails. The non-existence of integrated IT system has been commented vide Recommendation 7.

Recommendation No.6

To lay down well documented Business Continuity and Disaster Recovery Planning

2.2.12 During the previous audit, it was pointed out as under:

(a) Physical and Logical Controls:

- that there was no password policy to regulate access to the system. The access to the system was not controlled by user authentication procedures with proper access rights and authority levels.
- that there was no System Administrator to regulate access to the system and there was no audit trail in the system of corrections/modifications carried out in the system.
- that same user names and passwords were being used in all depots by all users.
- that no fire-walls, intrusion detection system was installed.
- that since the maintenance of GMS was outsourced, the vital data stored in computers was accessible to outsiders, which increased the risk to the data security.

(b) Business continuity and disaster recovery planning:

- A documented backup policy involving storage both at on-site and off-site and regular restoration of backup data did not exist at the Company.

Audit observed that all the above deficiencies were still prevalent in the depots/CO (November 2016).

The Government replied (November 2016) that computers were being used under the strict supervision of DMs, Depot Managers, who were Deputy Collectors, Tahsildars on deputation from Government. Hence, there would not be any wrong doing by the computer operators. The fact, however, remains that the system deficiencies pointed out in the previous audit continued to exist till date (November 2016).

Recommendation No.7

Considering an integrated system

2.2.13 During the previous audit, it was recommended that an integrated system for IT environment was essential, considering the volume and value of the transactions involved. However, during follow-up audit, it was noticed that such an integrated system was yet to be implemented, as detailed below:

- At present, the Company was having IMS only at its CO without stock monitoring system and RMIS modules.
- The Stock Monitoring System was operated as stand alone software (GMS) at depot level. The SRM offices were not supplied with the RMIS module.
- Since GMS are not integrated with the IMS, Depot data such as GRA, stock transfer to RV and Invoice generation are transferred to CO, in MS-Excel format through e-mails and are verified and uploaded to IMS database at CO and used for the decision making processes like need

analysis, order placement, indent placement, and for making payment to suppliers.

- In order to place indent for materials based on the actual stock position of Depots, CO collects particulars like, stock of materials, supplier-wise, brand-wise, size-wise sale and stock in transit through e-mails on daily basis.
- The Financial Accounting System module, which is part of IMS was available in CO only.
- Depots, DM and SRM offices prepare the monthly accounts in MS-Excel and forward to CO through e-mail. The CO consolidates the accounts through IMS after ensuring correctness. Had the Company linked Depots, DM and SRM offices with IMS, the monthly accounts could have been prepared automatically.

In the absence of an integrated system, the following deficiencies were noticed:

(a) Order processing

Orders to be placed on the various suppliers are arrived at by calculating weighted average sales of each brand. For this purpose, Company collects item-wise sales details of IMFL and Beer, both in quantity (cases and bottles) and value, in a text file exported from GMS, from all the depots so as to arrive at the sale per day (case-wise). Audit compared the original records of Ambattur (I-III) and Thirumazhisai (I-III) depots with the uploaded IMS sales per day records of the CO during the period 2009-16 and observed as under:

- In 1,975 instances, the depot and CO records showed differences in both quantity and value.
- A total of 3,44,569 cases of bottles with a value of ₹ 108.24 crore were shown in excess in CO records than the depot records.

The above instances indicated that corrections were made to the depot data after transmission to the CO leading to decision taken based on manually intervened sales data.

The Government replied (November 2016) that the difference was due to correction subsequently done in depot in respect of invoices and same was not updated/replaced in CO system, *i.e.*, due to non-receipt of/not uploading final data in the system at CO. The reply confirmed the audit observation.

(b) ***Payment of approximate VAT***

The Company is required to collect sales details from 6,200 retail shops regarding 87 IMFS and 16 Beer brands with 3 and 2 pack sizes. Each brand/pack size has different selling price and sales tax rate in respect of each item is also different. Considering the difficulty in ascertaining the actual total sales, for the purpose of payment of VAT, the Company adopted a formula, wherein the total collections remitted in bank of each Branch is apportioned towards Beer as well as various brands/sizes of IMFS on the proportion of stock transferred from Depots to RV shops during the month.

In the subsequent month, the correct amount of sales is calculated and the difference is adjusted/paid.

Audit scrutiny revealed that though EBM software has facility to generate brand-wise/pack-wise sales details but the data could not be utilised for payment of VAT as the Company considered the data as unreliable/incorrect. Hence, the Company was paying sales tax at approximate sale value and subsequently adjusting/paying the dues along with penalty/interest. As per the demand notice (July 2015) of Commercial Taxes Authorities, the amount of penalty for short payment of tax during 2014-15 was ₹ 2.55 crore. Audit further noticed that during 2015-16, the Company made excess payment of VAT in seven months ranging from ₹ 4.23 lakh to ₹ 87.40 lakh and short payment in five months ranging from ₹ 19.51 lakh to ₹ 3.25 crore, indicating that the penalty for the year 2015-16 was also not ruled out. The necessity for payment of penalty was due to non-implementation of EBMs in all the RV shops and non-integration of the installed EBMs with the IMS, which would have enabled the Company to generate accurate sales figures.

The Government stated (November 2016) that the Company was taking corrective measures for smooth flow of data to EBMs to computer nodes in CO, DM office through external means. Once all EBMs start working without any hindrance, the payment of VAT would be done based on the EBM figures.

(c) Accounts issue

Though the GMS could generate stock statement at the close of the accounting year, the Company has not used the same for valuation of closing stock. Instead, it considers only the physical verification report submitted by other Depots/District Managers, indicating unreliability of GMS.

The Government replied (November 2016) that the valuation of closing stock was to be done based on the physical verification report, as per the requirement of the Companies Act and Accounting Standards (AS-2: Valuation of inventories). However, the system lacks provision to record the authority and justification to modify the MSR.

Conclusion

The Company having an annual turnover of more than ₹ 30,200 crore could not integrate its activities at CO, depots, SRM and DM offices as well as RV shops through the computerised environment even after the lapse of 15 years. Such non-integration was mainly due to absence of IT policy and strategic plan and execution of computerisation in a piece-meal manner without covering SRM offices, DM offices and RV shops. Further, the present levels of computerisation lacked adequate controls, validation checks resulting in the data generated becoming unreliable. Though these deficiencies were pointed out by Audit in 2008-09 and the Company also accepting to overcome the deficiencies, persistence of the same deficiencies even in 2015-16 revealed that the lackadaisical approach to bring in computer based decision making to manage its massive activities. Thus, there was an urgent need for the Company to

frame an IT policy and reorient its activities for installing uniform software at CO, SRM, DM, Depots and RV shops.