REPORTS OF THE COMMITTEE TO ENQUIRE INTO SECURITIES TRANSACTIONS OF BANKS AND FINANCIAL INSTITUTIONS

(JANAKIRAMAN COMMITTEE
APPOINTED BY THE RESERVE BANK OF INDIA)

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BOMBAY
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General

1. On the basis of the information received that some banks were undertaking large-scale transactions in Government securities through the medium of brokers in the course of which they were violating the Reserve Bank of India (RBI)'s detailed guidelines issued to them in July 1991, RBI had started making enquiries into the securities transactions of some of the banks since January 1992. Towards the end of March, information was also received that State Bank of India (SBI) had purchased a large quantity of Government securities on a ready forward basis one day prior to the date on which the coupon rate of Government of India securities was raised. Therefore, the securities transactions of SBI were also taken up for scrutiny immediately. The bank was advised on 2 April 1992 to furnish to RBI a statement of the investments held by it as on 31 March 1992. The bank's response was that only the statement as at the end of January 1992 was available and that it would furnish the particulars as on 31 March 1992 as soon as the statement was compiled. It was observed that the bank was unable to furnish the statement as it had not reconciled the balance of securities held by it as shown in its books with the actual balance held in the Subsidiary General Ledger (SGL) Account with the RBI beyond November 1991. SBI was urged to reconcile the figures. On 23 April 1992, a news item in the Times of India made mention of a shortfall in Government securities held by the SBI. Even while the scrutiny was in progress, the Governor, RBI set up a Committee on 30 April 1992 to investigate into the possible irregularities in funds management by commercial banks and financial institutions, and in particular, in relation to thier dealings in Government securities, public sector bonds and similar instruments. The Committee was required to investigate various aspects of the transactions of SBI and other commercial banks as well as financial institutions in this regard. The Committee is headed by Shri R.Janakiraman, Deputy Governor with Shri Y.H. Malegam, Chartered Accountant and Shri V.G. Hegde, Principal Legal Adviser, RBI as members and Kum.V.Visvanathan, Executive Director as Member-Secretary. The Committee decided to invite a representative each from the Income Tax Department and the Central Bureau of Investigation (CBI) to join the Committee and accordingly Shri C.P.Ramaswamy, Deputy Director of Income Tax (Investigation), and Shri E.N. Renison, Additional Director (Retd.), CBI were nominated as members.

2. Terms of Reference :

The Committee is required to specifically

a) enquire into the extent of non-compliance by banks and financial institutions with the guidelines of the RBI regarding securities transactions including transactions in PSU bonds, units, etc.,

b) enquire into the inadequacies in systems and procedures in force in these institutions generally and the extent of use of Bank Receipts (BRs) which have been in vogue in regard to the transactions in Government securities and other instruments;

c) suggest such corrective steps as may be necessary to have a more efficient and accountable system in the future;

d) examine and determine the extent of malpractices, if any, indulged in by officials of banks and financial institutions, where their funds have been allowed to be used for speculative transactions by brokers and other intermediaries, and whether undue benefits have been thereby derived by brokers and others through unauthorised access to borrowed funds of the banks/financial institutions and fix responsibility therefor and recommend the action to be taken; and

e) scrutinise the procedure adopted by Public Debt Offices (PDOs) of the RBI in regard to the maintenance of SGL accounts and other related matters and suggest remedial measures to tone up the responsiveness of the system.

3. Basis for the Committee's preliminary report.

The Committee has had several meetings. The Committee noted that the RBI has ordered a detailed examination to be carried out by its officials into the securities transactions entered into by banks and other financial institutions with particular emphasis on the aspects which form the Committee's terms of reference. The Committee has had the benefit of the preliminary Reports received from the officials of RBI carrying out the examination of books of banks and financial institutions with regard to their transactions in securities and have also had discussions with a number of concerned officials. The Committee has given directions to the inspecting officers regarding the further investigations to be made and it has also framed a detailed questionnaire to be answered by them after carrying out the examination. The Committee recognises that since all transactions entered into by banks and other financial institutions in securities including completed transactions since 1 April 1991 are to be examined by the officials and the transactions of a particular bank/financial institution are to be verified with the transactions and the relative entries appearing in the books of counterparty banks, it will take some time for the scrutiny to be completed. The Interim Report of the Committee is thus based on the preliminary reports of the RBI inspecting officials, the discussions the Committee has had with them and other material presently available to the Committee. The Committee is continuing its investigations and will submit a further report.

4. RBI Instructions relating to Investment Portfolio of banks

The investment portfolio of banks in the normal course (given the low yield on them as compared to their opportunity cost) is basically intended to comply with the SLR requirements and accordingly expected to comprise of approved trustee securities. Since the bulk of the portfolio consists of Government securities, a major portion of the transactions in securities among banks were expected to be put through their respective SGL Accounts maintained with the PDOs of RBI. However, since the PDOs of RBI maintain SGL accounts only for Government securities, these accounts cannot be operated by banks for their dealings in PSU bonds, Units and similar instruments. Accordingly, the transactions through the mechanism of BR were expected to take care of exceptional circumstances wherein the seller bank of a non-SGL security was not in a position to give physical delivery of the security to the buyer bank either because scrips were yet to be received from the issuer of the security or the security was held at a different place. Except in cases of such exceptional circumstances, the transactions between banks in non-SGL securities were expected to take place on physical delivery basis.

On the basis of information received by the RBI in March 1992, inspection/scrutiny of investment portfolios of banks was undertaken and it was confirmed that the banks were freely putting through transactions in all types of securities, including SGL securities, through the mechanism of BRs, and that they were not only issuing BRs on the basis of BRs of other banks held by them covering their own Investment Account but also issuing their own BRs covering transactions of their broker clients. In July 1991, therefore, while cautioning the banks in general about the undesirable methods followed by some banks while undertaking transactions in securities, RBI advised the banks to frame and implement a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices and while evolving the policy with the approval of their respective Boards, to keep in view the guidelines prescribed by it. The RBI guidelines inter-alia stipulated that under no circumstances the banks should hold an oversold position in any security, transactions between banks should not be put through brokers' accounts, banks should adopt the format and strictly follow the guidelines prescribed by the Indian Banks' Association (IBA) for issue of BRs (which inter-alia prescribed that normally BRs should not be issued for SGL securities), banks should issue BRs covering their own sale transactions only and should not issue BRs on behalf of their constituents including brokers, and that banks should be circumspect while acting as agents of their broker clients for carrying out transactions in securities on their behalf. The Committee is informed by the RBI that a large number of banks had confirmed that an investment policy had been formulated and approved by their respective Boards.

Earlier, from time to time, the RBI had issued detailed guidelines to banks for undertaking underwriting and other commitments in respect of public issues of corporate shares and debentures and public sector bonds, advances against corporate shares and debentures to different types of borrowers, prohibiting their undertaking buy-back deals (ready-forward) with non-bank clients specifically in public sector bonds and units of UTI, and providing portfolio management services to their clients. Details of various types of transactions in securities undertaken by banks, guidelines/instructions issued to banks particularly the RBI guidelines issued in July 1991 and IBA guidelines of May 1991 on issue of BRs, are furnished in the Annexure (page 20).

5. Preliminary Findings

On the basis of the preliminary examination made by the RBI officials, it has been found that:-

(a) The following banks, subsidiaries of banks and institutions have made payments for purchase of investments for which they do not hold either securities, SGL forms or BRs to the extent indicated below :-

		(Rs. in crores)
National Housing Bank (NHB)	1199.39	
State Bank of Saurashtra	175.04	
SBI Capital Market Ltd.	121.23	(including a BR for (SBI Caps) Rs.67.83 crores for which the transaction is denied)
Standard Chartered Bank	300.00	
	1795.66	

(b) Banks, subsidiaries of banks and institutions are holding BRs/SGLs issued by the Bank of Karad Ltd. and the Metropolitan Co-operative Bank for which the issuing banks do not appear to have sufficient backing to the extent indicated below :-

	(Rs. in crores)
Standard Chartered Bank	755.00
Canbank Financial Services Ltd. (Canfina)	425.00
Canbank Mutual Fund	102.97
	1282.97

(c) The transactions put through the intermediation of NHB and which are outstanding are, prima facie, connected with the broker, Shri Harshad S.Mehta and/or his associate concern Growmore Research and Assets Management Ltd. This is evident from the fact that almost all the payments made by NHB by means of A/c. payee cheques drawn on the RBI and issued in favour of the counterparty banks have been collected and credited to the current accounts of Shri Harshad Mehta maintained with SBI and ANZ Grindlays Bank. A large number of transactions undertaken by SBI on its own investment account (about Rs.17000 crores during 1 July 1991 to 6 April 1992) have been put through Shri Harshad Mehta. Besides, in the current account of Shri Harshad Mehta with SBI several of his transactions appear to have been put through in an irregular manner. The transactions put through State Bank of Saurashtra and SBI Caps have also a link with the broker Shri Harshad Mehta. The transactions at Standard Chartered Bank and Canfina have been put through the broker Shri Hiten Dalal. The Bank of Karad Ltd. has issued BRs in the account of the broker Shri A.D. Narottam. The BRs issued by Metropolitan Co-operative Bank are on behalf of Dhanraj Mills Private Ltd. and Excel & Co. A large number of transactions of Standard Chartered, Canfina and Canbank Mutual Fund have been put through Shri Hiten Dalal with the help of BRs issued by Bank of Karad Ltd. and Metropolitan Co-operative Bank.

(d) The reconciliation of investment accounts in some of the individual banks is still in progress and the full picture will emerge only after the reconciliations are completed. However, the preliminary examination seems to suggest that the irregularities are confined to only a few banks.

(e) There has been a systematic diversion of funds from the banking system to the individual accounts of certain brokers and this diversion is presumably represented by the transactions for which the banks and subsidiaries are not holding BRs or are holding BRs of doubtful value.

(f) This diversion of funds has been mainly through three devices, namely

(i) purchases have been made by banks and subsidiaries of securities and other instruments where the counter-party is ostensibly another bank but in reality the proceeds have been directly or indirectly credited to brokers' accounts;

(ii) ready-forward transactions have been entered into by banks either on their own account or on constituents' accounts with brokers which have provided funds to brokers at rates which presumably were lower than the ruling "vyaj-badla" rates in the stock market; and

(iii) brokers have been directly financed by banks through the discounting of bills not supported by genuinetransactions or by purchase of shares by the bank under "ready-forward" terms.

(g) Some of the "ready-forward" deals by banks have not been completed and in consequence the banks may be holding investments whose market value may be considerably lower than the amount paid for the purchase of the investments.

(h) In the case of UCO Bank, bills aggregating Rs.50.40 crores were discounted by the bank. These bills were presumably covering the sale of shares by the broker Mrs.Jyothi H. Mehta (wife of Shri Harshad Mehta) to associate concerns of Shri Harshad Mehta. The manner in which this transacton was effected makes it clear that this was in the nature of a clean advance to the assoicate concerns. On maturity, these concerns appear to have been put in funds to retire the bills through the purchase by UCO Bank from Shri Harshad Mehta of shares of an aggregate cost of Rs.49.50 crores. The UCO Bank had earlier, on 8 April 1992 also, purchased shares of an aggregate cost of Rs.12.25 crores from his holdings. As against the aggregate cost of Rs.61.75 crores, the present market value is only around Rs.40 crores.

(i) The major device by which the transference of funds to brokers' accounts has been achieved has been through the issue of BRs which were not supported by underlying securities and by payments being diverted to brokers' accounts either directly or through counter-parties named in the transactions. This appears to have been made possible by a significant lack of internal control in the banks and presumably by collusion between the concerned officials and the concerned brokers. There is prima facie evidence of fraudulent misrepresentation.

(j) The diversion has also been made possible by a number of other factors which are summarised below :-

(i) There has been a significant increase in the volume of transactions in securities and capital market instruments since July 1991. Thus, in the SBI alone, the volume of transactions increased from about Rs.1000 crores in April 1991 to about Rs.8700 crores in March 1992.

(ii) These transactions have mainly been for "ready forward" deals between banks, between banks and brokers, and under portfolio management schemes. These are purely financing transactions though they take the form of purchase and sale of investments and appear to be an attempt to bypass RBI directives to banks governing direct advances by banks to brokers. They suffer from the further disadvantage that a broker gets access to bank funds without complying with margin requirements as would be the case when direct loans are given.

(iii) Since the transactions have been on a "ready-forward" basis, there is no need to permanently transfer the underlying securities and therefore under several excuses, banks have been resorting to the indiscriminate issue of BRs. On reversal of the transaction these BRs would be returned. There have also been cases where SGLs issued have been returned without being deposited with the PDOs.

(iv) The use of BRs has been justified on the grounds that there is delay in the recording of transactions at the PDOs and also that there is undue delay in the issue of scrips after allotment by PSUs. However, a large number of BRs have also been issued for

Units.

(v) Cheques issued in the names of banks by the purchasing banks have been collected and credited to the individual accounts of brokers without any such instructions by the issuing banks. This has enabled brokers to collect monies from purchasing banks under contracts which are ostensibly with banking counterparts.

(vi) Banks have lent their names to transactions which are not on their own account. Thus, banks have issued BRs at the request of brokers against BRs received or to be received in their favour in respect of transactions where they are neither purchasing or selling investments. These facilities have been provided to earn a fee but without disclosing to the counterparties that the concerned bank is not entering into the transaction on its own account.

(vii) Special facilities have been made available to select brokers whereby banker's cheques drawn in favour of the bank have been credited to brokers' accounts and against these cheques the bank has issued its own banker's cheques in favour of parties nominated by the broker. These have helped hide the true nature of transactions from counterparties.

(viii) In a number of cases there has been total lack or a breakdown of essential discipline regarding the issue and recording of BRs, the scrutiny for genuineness of signatures, the receipt and delivery of securities and the receipt and payment for settlement of transactions.

(ix) There has been no periodical reconciliation by banks of the investment accounts with the SGL accounts maintained by the PDO and in several cases this reconciliation was in arrears for long periods. If such reconciliation had been regularly done and he investments periodically verified by the internal auditors, the non-availability of BRs would have been immediately detected.

(x) In the PDO, the records are not computerised. Separate manual accounts are maintained for each scrip held by each bank and a minimum of information is available in the ledger where these accounts are maintained. It has, therefore, not been the practice, nor does it appear feasible (in the absence of computerisation) for a statement of transactions in the individual bank's account to be sent to the bank. If such a statement was available with the bank, it would have the means of regularly reconciling its investment account. Balance confirmation certificates are also not issued periodically but only on request and copies of such certificates are available with the PDO.

(xi) Through the portfolio management scheme, corporate funds have been used to finance brokers in the manner of "vyaj badla" but at much lower rates than the prevailing "vyaj badla" rates.

(xii) Merchant banking subsidiaries have accepted substantial amounts by way of inter-corporate deposits at high rates of interest and have been under compulsion to earn higher returns. These have been obtained through "ready forward" transactions.

(xiii) In the case of some merchant banking subsidiaries of banks, the deals are made by the subsidiaries but the actual transactions for receipt/delivery of scrips, BRs, etc., and receipt/payment of monies payable/due are arranged by the parent bank. The subsidiary, therefore, is not able to effectively monitor the transaction.

(k) Banks, in respect of their transactions with their customers, do issue BRs on account of sales of Units, PSU bonds, etc. This matter is being examined.

(l) The transactions have been effected by using a large number of banks' accounts in different names in different banks and to establish the trail is a difficult and laborious operation. Therefore, the unraveling of these transactions will necessarily involve considerable time and effort.

(m) The diversion of funds as reflected in the outstanding contracts has been mainly in respect of PSU bonds, Units and similar instruments and to a much lesser extent in respect of transactions in Government securities.

(n) The records of the PDO in the RBI show that :

   (i) a large number of transfer forms (ranging from 9.9 per cent to 18.2 per cent between March and May 1992) have been returned by the PDO under objection for insufficiency of balance. Almost all the
   been guilty of issuing SGL forms when there is insufficiency of balance. This is often due to the fact that banks over-sell at the beginning of the day and even though they square their position by the end of the day, the actual SGL forms for the purchase may not have been received by the end of the day.

   (ii) The entries in the PDO have normally been recorded on the day the SGL transfer forms are lodged in the PDO but delays upto 10 days have occurred on days following reporting Fridays and when half-yearly interest is due.

   (iii) There are a number of corrections for errors in the records.

   (iv) Objection memos have generally been prepared on the day of lodgement of the SGL forms or the next day though there are a few cases of apparent delay which need to be examined further. There is no delay in communicating these memos when delivery of the objection memos is made over the counter or by hand delivery but there is considerable delay when the memos are despatched by post.

   (v) There is delay of about 10 to 12 days in preparing credit advices.

   (vi) There is no copy of confirmation certificates issued by the PDO to the banks.

Some of the preliminary findings are detailed in subsequent paragraphs.

6. Extent of the problem :

The Committee as a first step, suggested that BRs held by banks for purchases and those issued by them for sales and outstanding may be matched so that the extent of transactions which are not backed by BRs could become available and in the process the problem exposures of banks and financial institutions could be assessed. The second step (which is in progress) was to examine the genuineness of the BRs, existence of the securities covered by the BRs, and the capacity of the issuers of BRs to honour the commitments. The findings to date, of the exercise are detailed below.

The matching exercise has revealed that, by and large, banks and financial institutions hold BRs in respect of the outstanding transactions except in a few cases. The BRs held have also been confirmed by the counter-party banks. The aggregate quantum of transactions for which no BRs are held by banks/ financial institutions is as under :

(Rs.in crores)

Name of the bank/ institution	Number of transactions	Security covered	Value of the transactions	Remarks
1. National Housing Bank	a) 4	Govt. Securities	302.05	—
	b) 22	Units and PSU bonds	857.47	
	c) 4	PSU bonds	39.87*	*No BRs held but the concerned counterparty has accepted the transactions which are overdue.
			1199.39	
2. State Bank of Saurashtra	4	Units & PSU bonds	175.04	—
3. SBI Caps	a) 7	Units	53.40	—
	b) 1	Units	67.83@	@Though BR of NHB is held the latter has denied the transaction.
			121.23	
4. Standard Chartered Bank	a) 1	Govt. securities	250.00	—
	b) 1	Units	50.00#	#The bank has a discharged BR.
			300.00	
	GRAND TOTAL		1795.66	

It will thus be seen that the aggregate exposure on account of banks not having BRs or securities is significant. Out of the total exposure of Rs.1795.66 crores, contracts in respect of transactions in Government securities amount to Rs.552.05 crores and the rest are in respect of Units and PSU bonds.

However, analysing the backing on the basis of which BRs have been issued and the capacity of the issuer of BRs to honour the commitments, the position is even more serious. It is observed that a number of BRs have been issued which are not backed by security or BRs held. BRs have also been issued on the basis of BRs held, where the capacity of the issuer to honour the BRs is in doubt. A summary position is indicated below :

(Rs.in crores)

Name of the institution holding the BRs		Name of the institution whose BRs are held	No.of BRs	Security covered	Amount	Remarks
Standard Chartered Bank	(a)	Metropolitan Co-op.Bank	6	Units & PSU bonds	530.00	A very small sized urban co-op. bank (Board since superseded)
	(b)	Bank of Karad Ltd.	6	Units & PSU bonds	225.00	Since taken to liquidation
					755.00	
Canfina		Bank of Karad Ltd.	3	Units & Govt. securities	425.00	Since taken into liquidation
Canbank Mutual Fund		Bank of Karad Ltd.	1	Govt. securities	102.97	SGL dated 27.5.1991 has bounced.
				GRAND TOTAL	1282.97	

The BRs issued by Bank of Karad Ltd. have either no backing or backing of doubtful quality. The BRs issued by Metropolitan Co-operative Bank, an urban co-operative bank with less than Rs.10 crores of assets are also of doubtful value.

Thus, taking into account what is stated above, the amount of exposures which banks may find it difficult to realise aggregates to Rs.3078.63 crores. This does not take into account any claims towards interest, etc., which may arise on settlement.

7. Preliminary findings of the scrutiny of certain banks/institutions.

The preliminary findings of the scrutiny of the investment transactions at certain banks/institutions carried out by the officials of the RBI are given in the following paragraphs :

I. State Bank of India

The scrutiny of the securities transactions of the SBI was taken up towards the end of March 1992 in the circumstances explained in paragraph 1 of this Report. During the course of this scrutiny, the SBI was asked to reconcile the balance of securities held by it as shown in its books with the actual balance held in the SGL account with the RBI.

2. During the course of this reconciliation, it was noticed that the securities balances in the SBI books exceeded that shown in the SGL account at the end of March 1992 by Rs.1022 crores. It was also observed that the SGL statement as on 29 February 1992 obtained from the PDO of RBI bore an alteration in the amount of securities shown against 11.5 per cent - 2010 Central Government Loan whereby the figure of Rs.1170.95 crores was shown altered to Rs.1670.95 crores. On reconciliation with the books of SBI, the latter showed an excess of Rs.74 crores (Rs.1744.95

crores as per SBI books less Rs.1670.95 crores as per the SGL altered account balance). As the correct figure of SGL account balance in this security was Rs.1170.95 crores, the excess as per SBI books was Rs.574 crores in that scrips. The excess revealed in the SBI books over that shown in the SGL account balance meant that SGL transfer forms for credit to SBI's SGL account with PDO had not been lodged with the PDO to the extent of the difference.

3. As far as the reconciliation of the overall difference of Rs.1022 crores in the figures of SBI and PDO as on 31 March 1992 was concerned, it was observed that an amount of Rs.699 crores in 11.5 per cent - 2010 Central Government Loan and an amount of Rs.230 crores in 11.5 per cent - 2007 Central Government Loan were shortcredited in the SGL account. Of the former, Rs.200 crores were attributable to the broker Shri N.K. Aggarwala for which SGL/resale was accounted for. The balance viz. Rs.499 crores was attributable to Shri Harshad S. Mehta (HSM). Regarding the second loan, an amount of Rs.60 crores comprised SGL form issued by Standard Chartered Bank for its sale to SBI and the balance of Rs.170 crores was purchased by SBI through HSM. Thus, an amount of Rs.669 crores in all, covering both the loans, represented the value of the securities transactions put through HSM for which no SGL transfer forms had been lodged with the PDO. The net amount after an adjustment of Rs.20 crores in respect of an internal transfer from another SGL account of SBI, representing transactions routed through HSM amounted to Rs.649 crores. Against this, SBI received 9 payment orders of Grindlays Bank aggregating Rs.574.76 crores and one banker's cheque from Syndicate Bank for Rs.47.76 crores from HSM. Adding a further amount of interest on 182 days Treasury Bills from HSM for Rs.0.20 crore, the aggregate payment received from him amounted to Rs.622.72 crores. The amounts were received on various dates between 13 April and 24 April 1992. SBI is reported to be pursuing the recovery of the balance amount of Rs.26 crores receivable by it from HSM. The reconciliation of the Investment Account is still in progress.

4. The sales/purchase transactions undertaken by State Bank of India (SBI) in Government and other approved securities have been entered into by the bank through several brokers including Shri Harshad S. Mehta (HSM). During the period 1 April 1991 to 31 March 1992 the transactions entered into by SBI in Government securities aggregated Rs.48562 crores, of which the contracts put through HSM accounted for Rs.17300 crores (35.6 per cent of the total). The details are furnished below :

(Amounts in crores of Rs.)

Type of transactions	Purchases	Sales
Government Securities		
Ready forward	20368	20007
Outright	3996	932
Switch	1600	1659
	25964	22598
Others		
PSU bonds	150	172
Units	82	46
	232	218
GRAND TOTAL	26196	22816

The transactions have been generally of three types - (i) outright purchase/sale, (ii) ready forward and (iii) double ready forward. The transaction-by-transaction examination is currently on, including verification of the records in SBI relating to the transactions and the entries in the relative books, as also verification of the transactions at the PDO of RBI. Besides, to the extent necessary, the transactions as recorded in the counter-party banks are also being scrutinised.

5. While the individual transactions put through in the Investment Account of SBI are being examined, as mentioned earlier a large number of contracts for sale/purchase of Government securities have been put through HSM as a broker. Besides, the Bombay (Main) branch of the bank also maintains a current account of HSM. This account is used to route transactions entered into by other banks through HSM.

6. The findings which have emerged so far are briefly as under:

i) Prima facie, the accounting and passing of entries for the transactions in respect of contracts put through HSM is entirely different from the accounting and passing of entries in the books of SBI in respect of contracts put through other brokers. Basically, in respect of contracts put through other brokers, the Investment Account maintained in the Bombay (Main) branch of SBI is either debited or credited as the case may be, and bankers' cheques are issued to, or payments are received by means of bankers' cheques from, counter-party banks in respect of the transactions. The relative debits and credits to the Investment Account get also duly in the books of the PDO either on the basis of transfer forms issued by SBI or on the basis of SGL transfer forms issued by other banks in favour of SBI. To the extent it has been possible to verify the transactions, the SGL transfer forms were issued to or received from the counter-party banks named in the contracts entered into through other brokers. In other words, these contracts have been put through in the normal course of business.

ii) As regards contracts entered through HSM, an entirely different set of procedures has been followed and there are certain significant departures in respect of such contracts. These are briefly mentioned below :

a) To the extent verification has been done, the counter-party banks named in the contracts generally seem to be only in name as the relative contracts do not generally appear in the books of these banks. In other words, the counter-party bank has just been named in the contract.

b) HSM has been given the facility of collection and credit of the bankers' cheques issued in favour of SBI and issue of bankers' cheques by SBI as per his instructions. This has facilitated the irregular operations of HSM.

c) The debits and credits in respect of he transactions appear in the Investment Account maintained at the Bombay (Main) branch. However, in a large number of cases the relative debits and credits do not appear in the SGL account of the bank maintained at PDO. There is no separate record available at the Bombay (Main) branch of the bank to indicate whether the relative SGL forms, if any, have been received and similarly, whether any SGL transfer forms have been issued by the SBI. However, computer print-out copies can be obtained to ascertain whether the Bombay (Main) branch has issued SGL transfer forms in favour of he counter-party banks as mentioned in the contracts. From the computer print-outs obtained, it appears that SGL transfer forms have been prepared but the fate of this SGL forms cannot be ascertained.

d) There is no evidence to indicate that bankers' cheques have been issued or received in respect of these contracts.

e) In the current account of HSM, receipts and payments relating to contracts entered into by the other banks through him are put through. A verification of the entries put through the current account of HSM on different dates reveals the following.

(i) The entries do not relate to the contracts entered into by the bank on its own Investment Account through the broker. The entries relate to certain other contracts entered through HSM by other banks. Certain receipts and payments are reflected in the relative vouchers pertaining to the entries put through the current account of HSM. But the vouchers do not indicate, prima facie, that they relate to any sale or purchase transactions.

(ii) While in respect of some of the contracts the counterparty banks named do not seem to be the real counter-party banks, in certain other cases, the bank's name in the contract appear to be genuine. For example, there are contracts entered into by other banks for sale/purchase of Government securi ties through HSM where the counterparty bank is named as SBI. The counterparty purchasing banks have received SGL forms from SBI and issued bankers' cheques to it. The counterparty selling banks have issued SGL forms to SBI but received bankers' cheques from it. The SGL forms have been refelcted in SBI's account with the PDO but these transactions do not appear in the Investment Account in SBI's books but the cheques received and issued by SBI are credited and debited in HSM's account with SBI. Thus, officials of SBI have unauthorisedly operated the SGL account of SBI with PDO without any backing transactions entered into by SBI. In other words, while the SGL account maintained at PDO does not reflect credits or debits relating to the contracts put through by SBI in its Investment Account through HSM, the said account reflects debits and credits in respect of transactions of other banks not put through by SBI. In sum, the SGL account of SBI maintained at PDO, Bombay appears to have been operated as if it is HSM's investment account in PDO.

(iii) A very serious implication of this is that on any one particular day the aggregate balance in respect of Government loans as appearing in the SBI's Investment ledger maintained at the Bombay (Main) branch will not necessarily tally with the relative balances appearing in the PDO's books even after adjustments are made for items in transit. Prima facie, there has been collusion between the officials of SBI and HSM.

(iv) Certain aspects of the issue and receipt of SGL transfer forms by SBI need to be noted. SGL transfer forms involving securities worth crores of rupees are signed by a single official of the junior-most level at the SBI. Generally, it is observed that SGL ransfer forms are signed in the case of other banks by two authorised officials. Apart from this, there is no reliable record available at the Bombay (Main) branch to indicate the issue of SGL transfer forms or receipt of SGL transfer forms in respect of contracts. The SGLtransfer forms are not issued in a uniform manner. The SGL transfer forms have been issued variously by SBI in computer print-out form, in stencil form, in typed form or in photocopy form with, however, the signature of the juniormost official appearing in ink. Some serial numbers are given which are not according to any system or pattern.

II. National Housing Bank (NHB)

A scrutiny was undertaken by the inspecting officials of the RBI of the current account of Shri Harshad S. Mehta (HSM) maintained with ANZ Grindlays Bank which had issued payment orders to the extent of Rs.574.76 crores to SBI, in part repayment of the amount of Rs.649 crores owed by him (as set out in the preceding section on the SBI), with a view to ascertaining the manner in which the current account was funded. The scrutiny revealed that a number of cheques drawn by the NHB on its account maintained with the RBI favouring ANZ Grindlays Bank had been credited to HSM's account. During the period immediately prior to the issue of the aforesaid 9 payment orders, 5 cheques amounting to Rs.405.67 crores drawn by NHB on its account with the RBI favouring ANZ Grindlays Bank had been credited to HSM's account in the latter bank. Consequently, the scrutiny of the books of NHB was undertaken to verify the nature of transactions underlying these payments to ANZ Grindlays Bank.

It was reported by NHB to the RBI that from June 1991 onwards it had been undertaking securities transactions not involving deployment of NHB's own funds but acting as an intermediary on back-to-back basis between the banks or financial services subsidiaries of banks. These transactions had increased in magnitude from October 1991 onwards and had peaked in March-April 1992. While the size of NHB's own surplus investible funds and consequently the size of its transactions on its own investment account were not large, its dealings by way of purchase/sale of securities, PSU bonds and Units on direct, back-to-back, ready-forward, etc. basis were on a very large scale. The total number of transactions in PSU bonds and Units during the half-year ended 31 December 1991 was 223. The turnover increased manifold during the first 4 months of 1992, particularly in PSU bonds and Units, the total number of deals being 165 each; however, the amount of turnover was not available readily.

The preliminary scrutiny undertaken in NHB reveals the following :

The NHB has been undertaking a large number of back-to-back deals. There is no policy note on record giving approval for undertaking such transactions. However, vouchers relating to all such deals were signed by the then General Manager (GM) (now CGM) for some time upto September 1991. Due to his frequent non-availability, the system of signing each voucher was discontinued and instead, a daily statement of deals was put up for sometime and that was also stopped since January 1992. Besides, weekly statements as on Fridays were put up, up to December 1991, which inter alia, included the back-to-back deals without any specific mention in regard thereto and the outstandings thereunder. In addition, a statement was put up to the top management on 18 December 1991, which indicated all the outstanding deals as at that time with a specific mention about the back-to-back deals. There has been no system of reporting to top management after December 1991. Although NHB had mentioned in its report to the RBI that the relative back-to-back deals have not been put through brokers, the diary maintained by the dealing officer does indicate that the deals have been put through brokers. As mentioned earlier, there are 30 transactions presently outstanding, aggregating Rs.1199.39 crores. The NHB has issued BRs to the banks/institutions purchasing the assets from it, but it does not have the backing of any BRs issued by the banks/ institutions which are supposed to have sold these assets to NHB. There are also no contracts available on record. The deals are stated to have been put through on telephonic conversations with the officials of the purchasing banks. The NHB has issued cheques drawn on its account with the RBI marked "account payee", the payees being the purchasing banks. The purchasing banks have credited the amounts to the account of Shri Harshad Mehta maintained with them after collecting the proceeds of the cheques. There are no specific instructions from the NHB to the banks to credit the amounts to the account of Shri Harshad Mehta.

There are no proper and systematic records maintained in NHB with reference to these transactions. No proper records are available of BRs, if any, received by NHB and the BRs issued. The BRs are not serially numbered.

Apart from dealing with banks and their subsidiaries, NHB has also entered into sale/purchase transactions in Units with certain limited companies. NHB also seems to have entered into certain bills transactions on a back-to-back basis.

The investigation into these transactions and other related matters in NHB is continuing.

III. SBI Capital Markets Ltd.

As part of deployment of the resources raised by SBI Capital Markets Ltd. (SBI Caps) in the form of Certificates of Deposit and inter-corporate deposits mainly from public limited companies and PSUs, the company has been making investments in PSU bonds and Units and has also been entering into ready-forward transactions in public sector bonds, Government securities and Units. While in respect of transactions in Government securities it does not maintain a position (the sales and purchases match on any particular day), it has been maintaining a position in PSU bonds and Units. The scrutiny of the securities transactions entered into by the SBI Caps has revealed the following features.

The transactions have been put through by the dealer after verbal discussions with the General

Manager (Corporate Operations and Leasing). These are subsequently put up to the ED and MD of the company. A deal ticket is serially prepared giving the details of the security, broker's name, counter party/ selling bank's name and date of reversal, etc. However, the broker's contract subsequently received does not mention the counter-party's name. The company has, during the period from 1 December 1991 to 31 March 1992 entered into 643 contracts, of which 152 contracts have been put through Shri Harshad Mehta. The deals are entered in a transaction ledger. The company maintains a current account at the Bombay (Main) branch of SBI through which the securities transactions entered into by it are put through. The Securities Department at the Main branch of SBI receives from the broker (in the case of purchases) the securities either physically or in the form of BRs from the counter-party banks addressed to SBI Caps, and in turn hands over the banker's cheques favouring the counter-party (selling) banks. The current account of the company is accordingly debited and a daily statement is forwarded to SBI Caps. On receipt of the statement of account from the SBI Bombay (Main) branch the debits are verified to ensure that they are backed by bank advices/deal tickets. On the due date, i.e., the date of reversal, the dealer raises another deal ticket recording the sale to the same counter-party through the same broker and advice is sent to SBI Bombay (Main) branch after recording the transaction in the books. The Securities Department at SBI Bombay (Main) branch then receives the payment by banker's cheque and credits the proceeds to the company's current account. The SBI Bombay (Main) branch is expected to discharge the BR and return the same to the broker for handing over to the counter-party.

The scrutiny of the transactions put through Shri Harshad Mehta has revealed the following :

(i) In several transactions it is observed that the counter-party mentioned in the contract is only in name and the transactions do not appear in the counter-party's books. In several of the contracts the counter-party named is Canfina but the relative transactions do not appear in Canfina's books.

(ii) In respect of several such contracts the relative credits have been given to the current account of Shri Harshad Mehta in the books of the Bombay (Main) branch of the SBI. There have also been instances of netting of the contracts of SBI Caps with certain other contracts entered into through Shri Harshad Mehta and net entries appear in the current account of Shri Harshad Mehta with Bombay (Main) branch of SBI.

(iii) In respect of some of these transactions there is no evidence to indicate that the SBI's Bombay (Main) branch, acting on behalf of SBI Caps, had in fact obtained and/or released BRs.

(iv) So far as SBI Caps is concerned, since the parent bank is acting as its agent, it did not verify the actual holding of BRs with the outstanding transactions. As a result, SBI Caps possibly did not know the adjustments made by the Bombay (Main) branch of the SBI in its books in respect of the contracts put through by SBI Caps.

However, certain shortcomings were observed.

a) The management of SBI Caps had not framed a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices.

b) The company had undertaken a number of buy-back deals of public sector bonds and Units though strictly prohibited under RBI guidelines.

c) The format of the BR adopted was not as per standardised format recommended by IBA. The BRs issued were not signed by two authorised signatories.

d) The demarcation line between dealing room and back-up office was not maintained. Several BRs issued were signed by the dealer instead of by the back-up officials.

An examination of outstanding contracts, reveals that the undernoted contracts pertaining to deals through Shri Harshad Mehta may devolve on the company.

(Rs. in crores)

Sr No.	Date	Security	Transaction amount	Counter party	Remarks
1.	29.7.91	Units 0.25 cr.	3.38	Standard Chartered Bank	No BR held. Deal ticket missing. Counter-party doubtful and their confirmation of transaction not received. Delivery long overdue.
2.	2.9.91	Units 5.00 cr.	67.83	NHB	Though BR of NHB is held, counter-party has denied the transaction.
3.	31.3.91	Units 1.25 cr.	18.75	Canfina	No BR held. Canfina has denied the transaction.
4.	6.4.92	Units 1.00 cr.	15.15	Canfina	No BR held. Canfina has denied transaction and receipt of any payment.
5.	30.3.92) 3.4.92) 21.4.92) 20.4.92)	Units 1.08 cr.	16.12	Private parties	All contracts are overdue for reversal but no delivery/ payment is forthcoming.
		TOTAL	121.23		

The examination of the transactions at SBI Caps is continuing.

IV. UCO Bank

While the enquiry into the investment transactions of UCO Bank had already commenced, there was a report in a section of the press on 1 May 1992 regarding a bills discounting transaction at UCO Bank. Thereupon a scrutiny of the records at the Bombay (Nariman Point and Hamam Street) branches of the bank was taken up on 2 May 1992. The scrutiny revealed the following facts.

Discounting of bills

(i) On 24 March 1992, the branch discounted two bills for one month - both drawn by M/s. J.H. Mehta (JHM), one on Growmore Research and Assets Management Ltd. (GRM) for Rs.14,44,41,000 and the other on Mazda Industries and Leasing Ltd. (MIL) for Rs.35,95,20,000, both of which are associated concerns of JHM.

(ii) The proceeds at Rs.49.42 crores were credited to the current account of JHM and thereafter transferred on the same day to the current accounts of GRM and

MIL. All the three current accounts were opened on 24 March 1992 (i.e. the date on which the bills were discounted) with nominal amounts.

(iii) On 24 March itself the proceeds were withdrawn by means of pay orders, issued by UCO Bank for the credit of GRM and MIL with ANZ Grindlays Bank.

(iv) The bank earned a net income of Rs.21.35 lakhs in the transaction.

(v) The bill discount facilities were extended by the Assistant General Manager of the branch without any specific sanction from Head Office. In his letter dated 26 March 1992 to Head Office he has mentioned that "as instructed by the Chairman and Managing Director during his last visit to Bombay, we have discounted both the above bills of exchange at a rate of 22.5 per cent on 24 March 1992".

(vi) The parties were not having any dealing with the bank prior to 24 March 1992. Nor did the bank receive any written application from JHM for the discounting facility.

(vii) The underlying transactions of the bills discounted relate to sale of shares of various companies by JHM to GRM amd MIL. The bills were clean.

Adjustment of bills discounted

(i) The bills discounted were adjusted on 27 April 1992 by means of cheques issued by GRM and MIL on their accounts with ANZ Grindlays Bank.

(ii) It is, however, observed that the bank had on the same day (i.e. 27 April 1992) purchased in its investment account the following shares - (a) 8 lakh shares of Gujarat Ambuja Cement Ltd. and (b) 77,150 shares of Castrol Ltd. Originally the shares to be purchased were 11 lakh shares of Gujarat Ambuja Cement Ltd. The broker M/s.V.B. Desai, however, could not give delivery of the entire lot of Gujarat Ambuja shares and instead delivered 8 lakh shares of Gujarat Ambuja Cement Co. Ltd. Instead of the balance of 3 lakh shares of Gujarat Ambuja Cement Co. Ltd. 77,150 shares of Castrol Ltd. were delivered by the broker only on 2 May 1992. The total purchase consideration of Rs.49.50 crores was paid by the bank by means of a banker's cheque dated 27 April 1992 in favour of ANZ Grindlays Bank - Account JHM. This was done as per instructions of the broker, M/s. V.B. Desai. Thus, the proceeds of the shares purchased by the bank on its investment account had gone to the account of JHM. The amount of Rs.49.50 crores credited to JHM's account with ANZ Grindlays Bank was transferred to the accounts of MIL and GRM with that bank. This credit enabled ANZ Grindlays Bank to meet on 27 April 1992 the cheques drawn by GRM and MIL towards payment of the bills discounted by UCO Bank for JHM.

It is evident that the bills discounted by UCO Bank were purely accommodation bills. This is clear from the fact that the drawer and the drawees belonged to the same group and the proceeds of these bills were immediately credited to the current accounts of the drawees. Moreover, on the due date for adjustment of the bills the bank found a way out to adjust the outstanding bills and accordingly made the investment by purchasing the shares standing in the name of the members of HSM family. Incidentally, the value of the shares held in the bank's investment account has also depreciated considerably.

The scrutiny of the securities transactions in the bank is continuing.

V. Bank of Karad Ltd.

The scrutiny of the investment transactions put through the bank is continuing. There have been very few transactions undertaken by the bank on its own Investment account. However, it maintains accounts of 19 brokers of whom only a few are active accounts. A large number of transactions have been put through in the accounts of M/s.Bhupen Champaklal Devidas and Abhay D. Narottam. It may be mentioned that Abhay D. Narottam was until recently a Director of the bank. Prima facie, the bank has issued on brokers' accounts BRs without any backing or against non-existent securities. It is also observed that BRs were issued in anticipation of the broker procuring as backing, BRs of other banks representing purchase of relative securities from those banks. In certain cases, BRs have been issued by Metropolitan Co-operative Bank, a small sized urban co-operative bank. Prima facie, BRs issued by that bank did not have any backing. The funds raised against these BRs have been credited to the account of the broker. The BRs have been used mainly to put through transactions with

Standard Chartered Bank, Canfina and Canbank Mutual Fund. By and large, the relative transactions in the banks/institutions mentioned above have been put through M/s.Hiten Dalal, as broker. The BRs issued by Bank of Karad Ltd. and presumably outstanding of the value of about Rs.750 crores are those issued in the the account of A.D. Narottam. Apart from verifying the linkages, the scrutiny will also trace the use to which the funds raised on the BRs of Bank of Karad Ltd. have been put.

8. Functioning of the Public Debt Office (PDO)

The Inspection Department of the RBI took up a scrutiny of the working of the SGL Section of the PDO at Bombay during the period July 1991 to 15 May 1992, soon after the reconciliation of the balances in the Investment Account of SBI with the SGL balances of the SBI in the PDO books in different loan accounts was commenced by that bank.

The Inspection Department has observed as under:-

(i) Under the reorganised set-up of PDO, which came into effect in 1987, the SGL Section which was a sub section of Accounts Section was given an independent status as a separate section by centralising all transactions connected with SGL Accounts with a view to ensuring better customer service to the investors. The main activities of the section relate to:

(a) opening and maintaining of SGL Accounts in the names of banks, financial institutions, corporate bodies, provident funds, brokers, trusts, etc.,

(b) examination of securities tendered for credit to SGL Account, issue of scrips by debit to SGL Account and transfer of SGL balances from one account to another on the basis of transfer deeds submitted by SGL Account holders (intra PDO transfers);

(c) preparation of advices/accounting vouchers;

(d) effecting inter PDO transfer of balances as per advices of holders;

(e) payment of half-yearly interest on balances held in SGL Accounts on the due dates;

(f) payment of amount to SGL Accounts pertaining to loans notified for repayment;

(g) furnishing of balance statements to the account holders periodically.

(ii) Due to the policy of restricting the issue of scrips only in the form of stock certificates and SGL and dispensing with the issue of scrips in the form of GP notes, and liberalisation and extension of SGL facilities to provident funds, trusts, etc., bulk of the transactions in Government securities is accounted for in SGL Accounts resulting in increase in the number of SGL Accounts and the volume of work. Thus, the number of accounts which stood at 228 as at the end of June 1989 increased to 332 as at the end of June 1990 followed by an increase upto 394 by the end of June 1991. As at the end of April 1992, the number of operative SGL Accounts stood at 438, the particulars of which are as under :

(a) SGL Account of banks (including Bank's investment a/c.)	-	116
(b) Financial Institutions like LIC, GIC, NABARD, DFHI, etc.	-	25
(c) Others, i.e.Provident Funds, trusts, etc.	-	297

The figure at item (c) above includes accounts of three brokers viz., Narandas & Sons, J.G. Shah and Co. and M/s.V.B. Desai. The transactions in these accounts are, however, meagre.

(iii) The objection memos have been prepared on the same day/next day but there has been delay in the preparation of credit advices ranging upto 10 - 12 days. There has also been considerable delay in some case in the despatch of advices and objetion memos.

(iv) There have been several instances of wrong postings which have been corrected subsequently, indicating that due care has not been exercised in the postings. It is also observed that some of the banks have been executing SGL transfer forms although adequate balance is not available in their accounts. The Chairmen of some of the banks in whose case the transfer forms had to be returned under objection frequently had been advised by means of a D.O. letterm from the Manager of the Bombay Office of the RBI in August 1991 to ensure that banks do not execute SGL transfer forms for amounts in excess of the actual balance available in the relative SGL accounts. Despite this, the percentage of SGL forms returned under objection to total receipt was very high during the months of March, April and May 1992.

The three non-RBI members of the Committee viz. Sarvashri Y.H. Malegam, C.P. Ramaswami and E.N. Renison, visited the PDO at Bombay on 25 May 1992 to familiarise themselves with the functioning of the PDO. The officers in-charge of PDO apprised them of the procedures followed in PDO. The members went round the SGL Section and made a sample scrutiny of various registers and files.

The preliminary findings of such scrutiny are

(a) The functioning of the SGL Section in the PDO in general is satisfactory. All the SGL accounts are maintained manually.

(b) SGL transfer forms received on a given day are generally disposed of on the same day.

(c) Particularly, where there is adequate balance in the SGL account and there is no technical irregularities in respect of an SGL transfer form, all the relevant ledger entries are posted on the date of its receipt itself.

(d) Where there is an objection due to some defect in the SGL transfer form (on account of signature, nature of loan, etc.) or there is inadequate balance in the account, the objection memo is prepared on the same day and delivered either on the same day or within a week. In some cases, where there has been undue delay in the preparation and despatch of objection memos, the RBI officials concerned have been asked to look into its causes for the delay and furnish reasons for the same.

(e) No statements of SGL Account transactions are furnished to the banks.

(f) Half-yearly statements of balances are sent. Besides, as and when any bank asks for balances on any given date, such balances are furnished, without keeping any office copy.

(g) Personnel from constituent banks are not allowed to see their SGL accounts.

(h) Scroll number given at the receipt counter to the SGL transfer form is not referred to either in the ledger or in the day-book.

(i) In a given SGL ledger account debit entry is made by one official and credit entry, by another.

The Committee would undertake a detailed study of the procedures in the PDO. While certain recommendations have been made on the basis of the preliminary study, additional measures to the extent necessary will be suggested after the detailed study is completed.

9. Recommendations

Based on the Committee's preliminary findings it would like to make the following recommendations.

1. The diversion of funds has been largely facilitated by the practice of banks executing a large number of "ready-forward" and "double ready-forward" transactions. Since there is no permanent sale or transfer of investments in such cases, there is no real need to effect transfer of actual scrips or SGL forms or to deposit SGL forms, when issued, with the PDO. These transactions have, therefore, presumably been supported by BRs or SGL forms not intended to be deposited with the PDO. As the transactions effectively get reversed on the due date, it is also possible that the transactions were effected without the issue of BRs or SGL forms, or by the issue of unauthorised BRs or SGL forms. A "ready-forward" transaction in substance could also be a mere lending of funds for the period of the contract in the guise of a purchase/ sale of investments. The Committee would recommend that -

a) the practice of banks entering into "ready-forward" and "double ready-forward" deals with other banks be restricted to Government securities only (as permitted by the RBI and referred to in the Deputy Governor's letter dated 26 July 1991 to the Chairmen of banks) and guidelines be laid down specifying the circumstances in which such transactions would be permitted;

b) banks be prohibited from entering into "ready-forward" and "double ready-forward" deals in other securities including PSU bonds, Units and shares;

c) the prohibition regarding banks entering into "buy-back" deals with non-bank clients (already imposed by the RBI) be strictly enforced and action be taken against banks which have violated this direction;

d) banks be prohibited from entering into "ready-forward" and "double ready-forward" deals on behalf of customers under portfolio management schemes (PMS).

2. The internal control procedures of banks regarding their treasury functions be immediately reviewed by the RBI, inter alia, with regard to -

a) the segregation of duties between (i) persons responsible for entering into deals, (ii) persons having custody of investments and (iii) persons responsible for recording the transactions in the books of accounts and other records;

b) the periodic reconciliation of investment account and the independent verification thereof;

c) controls over the issue of SGL forms and BRs and record keeping in respect thereof;

d) controls for verification of the authenticity of BRs and SGL forms and confirmation of authorised signatories;

e) procedures for confirmation with counterparties of brokers' contracts as also of overdue BRs;

f) the segregation of responsibilities of persons handling the bank's own investments and those dealing on client's accounts.

3. Banks should be required to formulate and get approved internal exposure limits for transactions. These should include limits which ensure that there is no undue reliance on a few brokers. These limits should also cover the maximum amount of outstanding BRs or SGLs issued by other banks which can be accepted by the bank.

4. Brokers contract notes should be required to indicate the counterparty so that direct communication with such parties is possible. The notes should also indicate separately the brokerage charged on the transaction.

5. When banks act as custodian of brokers' or other parties' securities, all transactions effected for such customers (including all documentation) must clearly disclose that the bank is acting as a custodian and not as a principal.

6. The existing prohibition on banks issuing cheques drawn on their account with the RBI for third party transactions should be strictly enforced. Such payments should be made through normal instruments like bankers' cheques, drafts or a transfer advice which clearly discloses the identity of the person on whose behalf the transfer is made.

7. When banks exercise custodian functions on behalf of their merchant banking subsidiaries, these functions should be subject to the same procedures and safeguards as would be applicable to other constituents. Therefore, full details should be available with the subsidiaries of the manner in which the transactions have been executed.

8. The issuance of a large number of BRs in respect of transactions in PSU bonds may have been justified by the banks on the ground that there has been undue delay in the issue of scrips by the PSUs and therefore trading in such bonds has been possible only through BRs. The issue of a large number of BRs in respect of Units may also have been justified by the banks on the ground that the transfer of the Units in the name of the buyer involves stanmp duty and therefore transfers need to be effected only when the Units need to be lodged with the UTI for payment of dividend. These are no doubt valid assertions but the practice of issuance of BRs in respect of these instruments has been largely responsible for the divergence of funds to the brokers. The Committee would, therefore, recommend that banks may be required to conduct all their transactions in PSU bonds, Units and similar securities through a separate institution like the Stock Holding Corporation which can be established. This would obviate the need to issue BRs in respect of such securities.

9. The issuance of BRs in respect of Government securities as also the apparent short-trading has been sought to be justified by the banks on the grounds of the inability of the PDOs in the RBI to speedily record the transactions effected and to communicate the credit advices in time to banks. Banks, therefore, do not know the fate of SGL forms lodged when they in turn issue SGL forms. The Committee is not convinced that this justification is valid particularly since objection memos have generally been communicated in time. However, the work of the PDOs needs to be considerably speeded up and more relevant information furnished to banks. This information should include -

a) immediate advice of all objection memos. Unless a bank makes arrangements on a regular basis to collect objection memos over the PDO counter, the advices should be by courier for which acknowledgement would be available with the PDO and the courier cost should be debited to the account of the concerned bank;

b) a weekly statement of all transactions in individual ledger accounts together with the balance thereof.

It is also necessary that there is a daily verification of all securities held in the SGL accounts of all banks in the aggregate and that on a weekly basis the PDO submit to the Department of Banking Operations & Development (DBOD) of the RBI a report giving bank-wise details of all SGLs returned for want of sufficient balance.

The Committee believes that given the large number of accounts, the large number of individual securities and the number of transactions, the work of the PDO cannot be done manually and needs to be immediately computerised.

10. The Committee recognises that with 80 banks having over 60,000 branches it is virtually impossible for the RBI's inspection procedures to examine individual transactions of banks. At present, the RBI carries out an Annual Financial Review (AFR) and a Financial Inspection once in four years. Even the financial inspection is largely concerned with the advances portfolio of the banks and the adequacy of provisions. The Committee understands that the inspection system and procedures of the DBOD have been recently reviewed by a Committee appointed by the Governor, and that its recommendations are in the process of being implemented. However, the primary responsibility in this regard must remain with the bank managements which must ensure that there are adequate internal controls (including internal audit) procedures. The Committee would, therefore, recommend that :-

a) On-site inspection by the RBI should be supplemented by reporting of compliance by banks with prudential and other guidelines. To lend authenticity to this compliance reporting, banks should be required to get compliance in key areas certified by the statutory auditors of the banks.

b) The scope of the RBI inspection should be widened to include greater emphasis on the treasury function.

c) The RBI should review the adequacy of the Internal Audit departments of the banks and the scope of their operations.

d) The portfolio management operations of banks should be subjected to a separate audit by the banks' statutory auditors as these operations are in the nature of trusteeship functions.

e) The RBI should strengthen its organisation responsible for market intelligence so that early action can be taken when there are market rumours of irregularities.

11. Though the National Housing Bank is a wholly owned subsidiary of the RBI there are not at present any institutional arrangements for the inspection of its operations. It is necessary that these arrangements be made at an early date.

R.Janakiraman
Chairman

Y.H. Malegam **V.G. Hegde**

C.P. Ramaswami **E.N. Renison**

Vimala Visvanathan
Member-Secretary

BOMBAY
31 MAY 1992

ANNEXURE

Banks have been undertaking transactions in securities (i) on their own Investment Account (ii) on account of PMS Clients" Account in their fiduciary capacity and (iii) on behalf of their other constituents including brokers purely as an agency function.

The Investment portfolio of banks (In respect of their own Investment Account) primarily comprises Government and other Trustee securities (except a very small fraction consisting of PSU bonds, shares and debentures which would have devolved on them on account of their underwriting commitments) which are intended to comply with the SLR requirements. Therefore, in the normal course banks' transactions in securities on their own Investment Accounts are expected to be in Government and other Trustee securities. Further, since bulk of the portfolio comprises Central Government securities, a major portion of the securities transactions among banks is expected to be put through their respective SGL Accounts maintained with PDO of the RBI.

However, composition of the portfolio in respect of PMS Clients' Account is expected to generally consist of high coupon bearing capital market instruments like PSU bonds, corporate debentures and shares. Accordingly, the transactions on account of PMS Clients' Account are expected to be primarily in the above securities and in the absence of SGL Account facility for them, the transactions are expected to be on actual delivery basis.

The transactions in securities on behalf of their other constituents like brokers undertaken as an agency function would be both in trustee securities and other corporate bonds, debentures and shares because the broker client may be dealing in both Trustee securities as well as corporate bonds, debentures and shares.

Banks' transactions in Trustee securities are generally on outright basis and ready-forward basis. The outright deals would also be in the nature of switch deals. Outright sales are undertaken generally when the bank has surplus SLR security and it wants to get rid of the security because of its low yield and its opportunity cost is higher than the yield and it is in a position to book the loss arising therefrom. Similarly, when a bank is short of SLR security and it has long-term funds, it prefers to buy a security on an outright basis, whereas when the bank does not have any surplus SLR security, as a long-term strategy of improving the overall yield from its SLR securities held in is investment portfolio, by deliberately booking a loss at the short-end , the bank may undertake a switch deal by selling a low coupon security and buying a high coupon security, provided it is in a position to book the loss arising out of the sale. However, given the maturity pattern of their resources and uncertainty about their future requirement of SLR securities, the banks have been generally managing their short-term cash requirements either for maintenance of CRR or for other purposes and SLR requirements, by entering into ready-forward (buy-back or repose) deals in SLR securities. In this type of transaction, a bank buys/sells a SLR security ready with the undertaking to sell back/buy back the same security on the specified future date (normally a fortnight and rolled over from fortnight to fortnight) at a mutually agreed pre-determined rate. The rates agreed upon (ready and forward rates) have no relevance to the market rates of the security but are related to the call money rate prevailing on the date of putting through the first leg of the transaction, as this type of transaction is basically a fund management/ SLR management exercise (i.e. raising funds against a SLR security which is in excess of the SLR requirement or temporary borrowing a SLR security for a cost). Thus, the difference between the ready and forward rates in a ready forward deal is supposed to represent the cost of funds. Thus, by this method, a bank which has a surplus security but wants cash prefers to borrow temporarily because it would be cheaper as compared to call-money borrowing as it has an additional cost of maintenance of CRR thereon. It may not like to sell the security outright because it may not be sure about its future SLR requirements and in such a situation, if it is required to buy outright later on to comply with future SLR requirements, it may have to pay a higher price. In so far as buying the security ready is concerned, it may be short for complying with SLR requirements and it may have no long-term resources to buy outright or it may not be sure about its future requirements and therefore, it prefers to buy short and roll over. Further, raising funds in the call-money for purchasing a security on outright basis may be costlier than buying it on a ready forward basis. Earlier, as there was no short-term maturity SLR securities available to banks to enable them to use such securities for short-term management of their cash/SLR securities requirements, (before the introduction of 182 days Treasury Bills), the banks have been permitted by the Rbi to undertake ready-forward deals in Trustee securities among themselves. However, deals with their non-bank clients. In fact, as far back as in 1988, the RBI had instructed the banks that ready-forward deals should be undertaken only among banks and that too only in approved Trustee securities and that no ready-forward deals should be undertaken in public sector bonds and Units of Unit Trust of India (UTI). The RBI had also clarified to the banks that they should not enter into any ready-forward deals even with financial institutions and bank subsidiaries. Normally, all the deals in securities are expected to be settled between the parties to the deal either through their SGL Accounts maintained with PDO (where SGL Account facility is available) or by physical delivery of securities. Even the ready-forward deals which are very short-term in nature are expected to the settled through their respective SGL Accounts with PDO because normally these are only among banks and that too in Government securities. Use of BRs (which represent a certificate issued by the selling bank to the effect that it has been holding the relevant securities on behalf of the buyer bank for value received and would be delivering the same within a very short period) is expected to be in exceptional circumstances when the seller bank is not in a position to give physical delivery of the security either on account of delay on the part of the issuer of security to issue the scrips or because the security is held by the selling bank at a place other than the place at which the transaction has taken place and it is likely to take some time to transfer the security from the place where it is held to the place where delivery is to be given. In any case, BRs are expected to be used only in such exceptional circumstances and that too only in the case of such securities for which no SGL Account facility is available and the BRs issued are expected to be liquidated within a very short time by physical delivery of securities.

Banks while undertaking the business of their clients including brokers as an agency function are expected to collect the instruments on behalf of their broker clients to the account of the brokers maintained with them and receive or give physical delivery of securities kept with them for safe custody against payment, strictly as per their specific instructions, and are not expected to commit themselves on behalf of their broker clients by issuing their own BRs/SGL forms.

During the course of inspection/scrutiny of securities transactions of some banks it came to the notice of the RBI that some banks had been freely issuing BRs in respect of their sale transactions in securities irrespective of whether SGL Account facility was available in respect of that particular security, some banks had been issuing their own BRs against the BRs of other banks held by them and that some of the banks were unnecessarily committing themselves on behalf of their broker clients by issuing their own BRs covering broker transactions. With a view to cautioning the banks in general about the undesirable systems followed by some banks while undertaking transactions in securities, particularly issue of BRs and undertaking of broker business, in July 1991, vied then Deputy Governor, Shri A. Ghosh's D.O. letter DBOD. No. FSC. 46 / C. 469-91/92 dated 26 July 1991 addressed to all the Chairmen/ Chief Executives of commercial banks (copy appended), the RBI had advised the banks to frame and implement a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices and while evolving the investment policy with the approvals of their respective Boards, to keep in view the following guidelines :

(i) Under no circumstances, position in any security, that is to say, that no sale transactions should be put through without actually holding the security in its investment account.

(ii) All the transactions put through by the banks either on outright basis or on ready-forward basis and whether through the mechanism of SGL Account or BR should be reflected on the same day in their investment accounts and accordingly for SLR purposes, wherever applicable.

(iii) Transactions between banks should not be put through the brokers' accounts.

(iv) For issue of BRs, the banks should adopt the format prescribed by the Indian Banks, Association (IBA) and strictly follow the guidelines prescribed by them in this regard (copy appended) and banks should issue BRs covering their own sale transactions only and should not issue BRs on behalf of their constituents including brokers.

(v) Banks should be circumspect while acting as agents of their broker clients for carrying out transactions in securities on behalf of brokers.

(vi) Any instance of return of SGL form from the PDO of the RBI for want of sufficient balance in the account should be immediately brought to the notice of RBI with the details of the transactions.

The IBA Rules on BRs mentioned earlier, inter-alia provided as under :

(a) the BR should be issued in the prescribed format only. Receipt issued in any other format should not be accepted.

(b) Normally, no BR should be issued where SGL facility is available.

(c) A separate BR should be issued for each type of security.

(d) BR is non-transferable.

(e) BRs should be issued serially numbered on security paper.

(f) BR must be exchanged with actual scrips as early as possible and in any case within 90 days of issue.

(g) BR should be signed by two authorised signatories whose signatures should be registered with the buyer-bank to verify the signatures.

(h) BR can be accepted from any of the following institutions :

i) All member banks of the IBA.

ii) Financial institutions like IDBI, IFCI, ICICI, NABARD, UTI, GIC, LIC.

iii) Public Sector Undertakings.

iv) Any other institution specified by the IBA/ RBI.

The RBI had also issued guidelines and prudential exposure limits to be followed by banks for undertaking underwriting of corporate shares, debentures and PSU bonds and other commitments in the nature of safety net for public issues of convertible debentures and shares and developments arising therefrom, advising them to make periodical review of such business and apprise their respective Boards. As far back as in October 1986, the RBI had issued a Memorandum setting out guidelines/safeguards to be followed by banks in granting advances against corporate shares and debentures to different types of borrowers and the maximum advance that could be granted to different types of borrowers. In 1989, the RBI had instructed the banks that they and their subsidiaries should not finance beadle transactions. In the light of the steep rise in the prices of corporate shares during the second half of 1991, the RBI Governor during his Credit Policy meeting with the Chairmen/Chief Executives of banks had instructed that banks should limit their aggregate advances against corporate shares and debentures to the level which prevailed as on 7 October 1991. Subsequently, in the light of the unprecedented rise in the prices of shares during March/April 1992, the RBI Governor during his Credit Policy meeting with Chairmen/Chief Executives of banks held on 22 April 1992 had instructed the banks that while they should continue with the earlier cap on aggregate lendings against shares and debentures, in the case of advances against shares and debentures to individuals, they should hike the margin requirements to 75 per cent.

The RBI had also issued detailed guidelines to banks and subsidiaries for providing Portfolio Management Services (PMS) to their clients which inter-alia stipulate that PMS should in the nature of investment consultancy for a definite pre-determined fee not related to actual yield on the portfolio, purely at customers' risk, without guaranteeing any pre-determined minimum return on the portfolio. As per RBI guidelines only such banks which have the necessary expertise to provide the PMS on their own should undertake the activity, maintain client-wise record of portfolios, and should furnish the clients periodical statements of their portfolio. Any transactions between the banks' Investment Account and PMS Clients' Account should be at market rates.

DEPUTY GOVERNOR

RESERVE BANK OF INDIA
CENTRAL OFFICE
BOMBAY

D.O. DBOD No. FSC 46/C 469-91/92
SECRET

26th July 1992
4 Sravana 1913 (Saka)

Dear Shri

Investment portfolio of banks
-Transactions in securities

It is a matter for great concern for us that certain banks are engaged in types of transactions in securities which they should not be undertaking. A list of such transactions is appended.

(i) Ready forward (buy-back) deals at rates which have no relevance to the market rates, inter-alia, with a view to window dressing their balance sheet/compliance of SLR requirements,

(ii) Double ready forward deals with a view to covering their oversold position in a specific security.

(iii) Sale transactions by issue of Bank Receipts (BRs)/SGL forms without actually holding the securities/without having sufficient balance in their SGL accounts.

(iv) Issuing BRs/SGL forms on behalf on their broker clients without safeguarding banks' interest.

2. You may be aware that with a view to helping the banks to overcome various deficiencies in the long-term securities market and to enable them to manage their short-term securities market and to enable them to manage their short-term cash deficit/surpluses more efficiently, we have permitted banks to enter into buy-back deals in Government securities among themselves (and not with their non-bank clients). It was our expectation that such deals will be undertaken by the selling bank, only if it holds sufficient securities (either in the physical form or in SGL account), at market related rates and such deals will be properly reflected in their books of account. However, we observe that certain banks have been resorting to this type of transactions, without actually holding sufficient securities either in physical form or in their SGL account (resulting in substitution of BRs/return of SGL forms for want of sufficient balance), at rates which have no relevance to market, with a view to window-dressing their profitability/maintenance of SLR requirement with the tacit understanding with the counter party banks. Some of the banks appear to be taking outright oversold position in securities and in their desperate bid to cover the oversold position in a particular security/ies enter into double ready forward deals and other banks oblige them in the matter.

3. Another disquieting feature observed is the extensive use of BRs by banks. It has been our intention to ensure that the banks do not undertake sale transactions in securities without actually holding them and do not issue BRs unless they are in a position to deliver the securities within a reasonable time. Contrary to our above expectation, banks have been issuing BRs freely (without regard to whether they will be in a position to deliver the securities there against within a reasonable time) and against an initial outstanding BR, a series of transaction are put through by further issue of BRs and in the final analysis only the BRs are exchanged and no security is delivered. Some of the banks have also been issuing BRs on behalf of their broker clients, without verifying whether their broker clients hold the securities covered by the relative BRs.

4. It will be absolutely essential for your bank to frame and implement a suitable investment policy

to frame and implement a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices. While evolving the policy you are requested to keep in view the following guidelines :

(i) Under no circumstances, the bank should hold a oversold position in any security, that is to say that no sale transactions should be put through without acutely holding the security in its investment account.

(ii) All the transactions put through by bank either on outright basis or ready forward basis and whether through the mechanism of/SGL Account or Bank receipt should be reflected on the same day in its investment Account and accordingly for SLR purpose, wherever applicable.

(iii) Transactions between your bank and another bank should not be put through the brokers' accounts. The brokerage on the deal payable to the broker, if any, (if the deal is put through with the help of a broker) should be clearly indicated on the notes/memorandum put up to the top management seeking approval for putting through the transaction and operate amount of brokerage paid, broke-wise, should be maintained.

(iv) For issue of BRs, the banks should adopt the format prescribed by the IBA and should strictly follow the guidelines prescribed by them in this regard. Subject to above, the banks should issue BRs covering their own sale transactions only and should not issue BRs on behalf of their constituents including brokers.

(v) The banks should be circumspect while acting as agents of their broker clients for carrying out transactions in securities on behalf of brokers.

(vi) Any instance of return of SGL form , from the Public Debt Office of the Reserve Bank for want of sufficient balance in the account should be immediately brought to our notice with the details of the transactions.

5. We shall also be glad if a copy of the policy framework for undertaking transactions in securities approved by your bank's Board, is forwarded to us.

6. Please acknowledge receipt.

Yours sincerely,

(A. Ghosh)

INDIAN BANKS' ASSOCIATION

Stadium House, 6th Floor, Block 3, Veer Nariman Road, Bombay-400 020.

Phone Office: 22 23 65 ● Grams: BANKSLINK ● Telex No. 011-5146, 011-2373

No. OPR.C/52-20/1039

6th May, 1991.

Chief Executives of All Member Banks

Dear Sirs,

STANDARDISED FORMAT OF BANK RECEIPT (BR)

In the inter-bank market, large number of transactions in securities are concluded by means of BR deliveries, particularly when the selling bank is not is a position to effect physical delivery of scrips for various reasons. It is common practice among banks to issue BRs which acknowledge receipt of funds for the securities sold and undertake to hold the same in trust, until these are physically delivered. There is, however, no uniformity the format of the BR being used by the banks at present.

It was considered necessary to devise a standard format of BR and frame rules therefor for uniform adoption by member banks, financial institutions, public sector undertakings and other IBA/RBI specified institutions. Accordingly, the standardised formats etc. for the above evolved by Investment Dealers' Club and reviewed by the IBA Committee on funds and Investments (COFI) were placed before the Managing Committee of the IBA in its meeting on 23rd April, 1991 for approval.

The Managing Committee approved the standard format of the SR, BR Rules and monthly statement of BRs held and issued and recommended these for uniform adoption by member banks, financial institution like IDBI/IFCI/ICICI/NABARD/UTI/GIC/LIC, public sector undertakings and other IBA/RBI specified institutions.

At present, different BR formats are being accepted by the IBA non-member institutions; there should therefore, be no difficulty in their accepting the uniform BR format which is being recommended now. The RBI is being informed and requested to consider the eligible institutions from its end also.

Member banks may adopt standard format of BR, BR Rules and monthly statement of BRs held and issued, the specimen of which are enclosed.

Yours faithfully,

(A. K BAKHSHY)
SECRETARY

PROFORMA

BANK RECEIPT

NON TRANSFERABLE

B.R.No. 1 DATE :

Name of the Bank ______________________________

Issuing Office Address ______________________________

____

____

We confirm having this day sold, out of our holding, the following security on outright basis/buy back basis to be repurchased after____________ days, i e., on______________________(date)*.

Name of Security	Interest Date	Face Value	Rate : p.a.	Sold to
________	________	________	________	________

The delivery of above security connot be effected due to ______________________________

______________________________.

In consideration of the above, we confirm having received Rs. ______________________ (Rupees ______________________________) by cheque.

Scrips relating to the said security will be delivered within ________________ days on surrender of this receipt duly discharged and in the meanwhile the security sold would be held by us in trust for ______________________________(buyer). This receipt is issued in terms of rules framed by the IBA and subject to realization of cheque.

*Delete which is not applicable.

Revenue Stamp

For _____________(Seller Bank)

1. 2.

(Authorised Signatories)

BANK RECEIPT RULES

1. The Bank Receipt should be issued in the prescribed format only. Receipt issued in any other format will not be accepted.

2. Normally no BR should be issued where SGL facility is available. In all other cases, the scrips shall be delivered to the buyer as soon as possible. except for R/F transactions.

3. A separate BR should be issued for each type of security.

4. BR is non-transferable.

5. Banks should issue BRs serially numbered on Security Paper.

6. BR must be exchanged with actual scrips as early as possible, and in any case within 90 days of issue. However, it would be open for banks to issue fresh receipt in the event BRs are not discharged within 90 days and the reason for the same should be mentioned in the renewed BR.

7. BR should be signed by two authorised signatories whose signatures should be registered with the buyer-bank to verify the signatures.

8. BR can be accepted from any of the following institutions.

    a) All member banks of the IBA

    b) Financial institutions like IDBI, IFCI, ICICI, NABARD, UTI, GIC, LIC

    c) Public Sector Undertakings

    d) Any other institution specified by the IBA/RBI.

MONTHLY STATEMENT OF BANK RECEIPTS FOR____________ Branch____________

BR No.	Date of BR	Particulars of Security	Face value (Rs. lacs)	Rate % p.a.	Name of bank	Broker

A : BRs held & Outstanding

For Purchases

i) On outright basis

ii) On buy-back basis

B : BRs issued & Outstanding

For Sales

i) On outright basis

ii) on buy-back basis

C : BRs held but returned during the month

Date of Reversal	BR No.	Date of BR	Particulars of security	Face Value (Rs. lacs)	Whether SGL received or scrips received or reversal of buy back	To whom returned (Bank)

D : BRs issued but received back during the month

Date of reversal	BR No.	Date of BR	Particulars of Security	Face value (Rs. lacs)	Whether SGL given or scrips delivered or reversal of buy-back	From whom received (Bank)

Second Interim Report

July 1992

I. Introductory

The Committee has submitted an Interim Report to the Governor, Reserve Bank of India on 31 May 1992. The Committee in the said Report had, based on the preliminary examination of the securities transactions entered into by banks and financial institutions, made a preliminary determination of the quantum of problem exposures, the manner in which diversion of funds had taken place from the banking system, and other general irregularities in the manner in which securities transactions had been undertaken by banks and financial institutions. The Committee had also made certain recommendations with a view to ensuring orderly securities transactions and the actions which individual banks should take to ensure that they are not exposed to any undue risk in the securities transactions.

2. The Committee had desired that certain information mainly - (i) particulars of all securities transactions undertaken by banks and financial institutions from 1 April 1991 to 23 May 1992, (ii) position of reconciliation of Investment Accounts as well as investments held on Portfolio Management Schemes(PMS) and other clients' accounts, and (iii) details of transactions relating to bill discount/ rediscount for large amounts, may be called for from banks. These have since been received from most of the banks/institutions and the transactions in securities are being scrutinised by the officials of the Reserve Bank of India (RBI) apart from verification of the reconciliation statements. The scrutiny is continuing. This Report details the further findings based on the scrutiny conducted so far.

II. Findings

In its first Interim Report, the Committee had given its preliminary findings as revealed by the scrutiny of the investment transactions at certain banks/institutions carried out by the officials of the RBI. The findings as revealed by further scrutiny are given in the following paragraphs.

2. The total value of investments made by banks and institutions for which they do not hold either securities, SGL transfer forms or BRs has on further scrutiny been determined to be as under :

(Rs. in crores)

Bank/ Institution	Acquisition cost	Bank/Institution to whom payment was made	Account to which amount received was credited.
1. National Housing Bank (NHB)	1271.20	i) State Bank of India (SBI) - 707.56	Shri Harshad Mehta
		ii) ANZ Grindlays Bank - 506.55	Shri Harshad Mehta
		iii) Standard Chartered Bank (Stanchart) - 55.18	Growmore Research and Asset Management Co.Ltd.
		iv) Canfina - 1.91	Under investigation
		1271.20	
2. State Bank of Saurashtra (SBS)	174.93	i) SBI - 99.11	Shri Harshad Mehta
		ii) NHB - 75.82	Shri Harshad Mehta(through SBI)
		174.93	
3. SBI Caps	121.36	SBI 121.36	Shri Harshad Mehta
4. Stanchart*	400.35	— Under investigation —	
	1967.84		

* As indicated by the bank.

3. The total exposure against BRs/SGL transfer forms issued by Bank of Karad Ltd. (BOK) and the Metropolitan Co-operative Bank Ltd. (MCB) (for which those banks do not appear to have sufficient backing) held by banks/ institutions has on further scrutiny been determined as under :

Bank/Institution	Acquisition cost (Rs. in crores)	BR/SGL issued	Account to which amount received was credited
1. Canfina	435.31	BOK	Shri Abhay D. Narottam
2. Canbank Mutual Fund	102.97	-do-	-do-
3. Stanchart *	355.94	-do-	Under investigation
	575.90	MCB	-do-
	1470.12		

* As indicated by the bank.

4.(a) In the course of an examination of the investment reconciliation of Andhra Bank Financial Services Ltd. (ABFSL) and verification of the investments held by it, it has been determined that three certificates for 9.75 crore Units of the UTI (having a total value @ Rs.15.50 per Unit of Rs.151.12 crores) and deposited by Fairgrowth Financial Services Ltd. (FGFSL) under ready forward transactions were not genuine.

(b) There is also doubt regarding the genuineness of two letters of allotment of HUDCO bonds of the aggregate face value of Rs.45 crores and a letter of allotment of NPTC bonds of the aggregate value of Rs.15 crores also deposited by FGFSL.

(c) On the basis of estimated value of the security held and if the letters of allotment prove to be not genuine, there will be an estimated shortfall in this contract of Rs.206.42 crores. The company has advised that it has obtained additional security from FGFSL for Rs.101.59 crores. This would reduce the shortfall to Rs.104.83 crores.

(d) ABFSL also held a certificate for 1,10,15,500 Units deposited by FGFSL which was returned to FGFSL against payment on 17 June 1992. The concerned certificate which is also admitted to have been not genuine is stated to have been destroyed in FGFSL.

5. In short, the total size of the problem exposure in securities transactions can be arrived at as indicated below:

1.	Total value of investments made by banks and institutions for which they do not hold any securities, SGL transfer forms or BRs (vide paragraph 2)	Rs.1,967.84 crores
2.	Total exposure against BRs/SGL transfer forms issued by Bank of Karad or Metropolitan Co-operative Bank (vide paragraph 3)	Rs.1,470.12 crores
3.	The estimated shortfall in the securities held by ABFSL (vide paragraph 4)	Rs. 104.83 crores
	Total	Rs.3,542.79 crores
	Less: Value of securities reportedly seized by Standard Chartered Bank from M/s.Hiten P. Dalal	Rs.350.00 crores
	Total problem exposure	Rs.3,192.79 crores

6.(a) The investment reconciliation of the SBI as prepared by the bank has revealed a shortfall in investment of the face value of Rs.650 crores. Against this, the bank had recovered Rs.622.52 crores from Shri Harshad Mehta and utilised the same to purchase securities of Rs.624 crores and treasury bills of Rs.21 crores. There is, therefore, an uncovered deficit of Rs.5 crores. The reconciliation prepared by the bank is under investigation.

(b) In the reconciliation prepared by the bank there is a transfer after 31 March 1992 from SGL A/c. No.111 to its own investment account of 11.5% GOI loan 2010 of the face value of Rs.67 crores and 11.5% GOI loan 2008 of the face value of Rs.20 crores. SGL A/c.No.111 is intended to be used for transactions on behalf of clients but has been indiscriminately used even for other transactions. However, on a scrutiny of the PDO records, it was seen that as at 31 March 1992, the total face value of securities held in SGL A/c.No.111 in respect of 11.5% GOI loan 2010 was only Rs.2.02 crores. The transfer shown in the reconciliation can, therefore, only be out of deposits made in the SGL account after that date.

(c) Included in the deposits made in SGL A/c. No.111 after 31 March 1992 is a deposit for Rs.50 crores of 11.5% GOI loan 2010 for which the SGL transfer form dated 6 April 1992 was issued by UCO Bank. This form has been debited in PDO books to the SGL account maintained by UCO Bank for its clients and is on account of Shri Harshad Mehta. SBI has not made any payment to UCO Bank on this account. It would, therefore, appear that this Rs.50 crores was also a shortfall for which recovery has been made from Shri Harshad Mehta.

(d) The issue of the SGL transfer form by UCO Bank was made possible only because of certain purchases in that scrip made by Shri Harshad Mehta and recorded in UCO Bank's books. After the entries for these purchases were entered in Shri Harshad Mehta's current account in UCO Bank, the account showed an overdrawn balance of Rs.39.07 crores. The overdrawing has been adjusted by a receipt of Rs.40 crores from NHB on that day which is recorded in NHB's books as a call loan to UCO Bank whereas in UCO Bank's books the amount has been credited to Shri Harshad Mehta's account.

7. Reconciliation of investments has still not been completed by certain banks/institutions.

8. The preliminary finding that there has been a systematic diversion of funds from the banking system to the individual accounts of certain brokers has been confirmed by the further scrutiny. The Interim Report had detailed three main devices through which this diversion had taken place. These were :

(i) purchases made by banks/institutions where the counterparty was ostensibly another bank but in reality the proceeds were directly or indirectly credited to brokers' accounts;

(ii) ready-forward transactions between banks/institutions and brokers;

(iii) direct financing of brokers through discounting of accommodation bills and purchase of shares on ready forward terms.

9. Further scrutiny has revealed four other devices through which this diversion has taken place. These are as under :

(i) Banks/institutions have shown large payments as call money placed with other banks. However, in the books of the receiving banks there is no record of any call money accepted but instead the amounts have been credited to individual brokers' accounts. On due date, these alleged call loans have been repaid by payment out of the brokers' accounts in the same or other banks;

(ii) Banks/institutions have rediscounted bills of exchange held by other banks/institutions but the proceeds and repayments have been routed through brokers' accounts;

(iii) SBI has issued SGLs on its account with the PDO at the request of Shri Harshad Mehta and has deposited in the same account SGLs delivered by Shri Harshad Mehta. There is no record in the books of SBI for these transactions and the payments received for SGLs issued and the payments made for SGLs received have been credited and debited in Shri Harshad Mehta's account. To this extent, Shri Harshad Mehta appears to have used the SBI's investment (as reflected in its SGL balance with the PDO) to finance ready forward deals with other banks and for the period of the deals used the funds generated thereby. Between 1 April 1991 and 22 June 1992, the total face value of SGL forms delivered from the SGL account and the total face value of SGL forms deposited in the SGL account in this manner aggregated to Rs.7282.89 crores and Rs.6712.67 crores respectively. The shortfall of Rs.570.22 crores presumably forms part of the amount of Rs.622.52 crores recovered by SBI from Shri Harshad Mehta as referred to in paragraph 6.(a) above. The entries in the SGL account are still under investigation;

(iv) Merchant banking subsidiaries of public sector banks have received large sums as inter-corporate deposits and under PMS and similar schemes, and these funds have been made available to brokers under ready forward deals. In many cases these deals are in respect of transactions in shares and often the funds have been made available by public sector companies and public sector corporations. Where the funds are received under PMS, the subsidiary is acting only as an agent and the investment is made by the entity which has placed the funds. It needs to be examined whether in such cases the provisions of the Companies Act, 1956 (and particularly section 372 which puts limits on investments by companies) have been complied with. Where the investment is made out of inter-corporate deposits, the investment is made by the merchant banking subsidiary (which is a company incorporated under the Companies Act, 1956) and it needs to be examined whether the subsidiary has complied with the provisions of the said Act.

10. There are a number of transactions where the rates at which sales of investments have been booked by banks/institutions are at rates which are considerably in excess of the rates at which counterparty banks have booked the purchases. The payments received by the banks/institutions have been at the rates at which purchases have been booked by the counterparty banks/ institutions and the difference often running into crores of rupees has been received from the brokers. It is obvious that sales have been booked at artificial rates to book a profit or avoid a loss. It is also obvious that the broker would not have paid the difference unless he had been compensated in some fashion. The matter is under further investigation.

11. There are a number of instances where with the full knowledge of the management, banks/financial institutions have issued SGL forms against SGL forms brought by brokers. In some cases, these are reflected as purchases/sales of the banks/ financial institutions but in other cases there is no such entry made. For these services rendered to the brokers, the banks/ financial institutions have charged a fee, normally 0.01 per cent of the face value of the securities involved.

12. Banks and their merchant banking subsidiaries have bid for and acquired shares in public sector enterprises on partial disinvestment by the Government. The terms and conditions on which these bids were invited contained a condition that the shares acquired could be off-loaded through normal Stock Exchange transactions. However, in some cases these have been off-loaded through private deals with brokers and at least in one case there is evidence that the sale was negotiated even before the bid was made and the bank acted only as a conduit for the shares being acquired by persons not authorised to bid for the same. It is also possible that since the sales were made at negotiated prices before market rates could be established, the full value of the shares may not have been realised.

13. A statistical study of the total securities contracts entered into by banks(even though the required data has not been received from some banks) shows that :

(i) During a period of about 14 months between 1 April 1991 and 23 May 1992, the contracts entered into by banks exceeded 58,000 in number and Rs.9,00,000 crores in face value of the underlying securities.

(ii) More than two-thirds of these transactions were entered into by only four foreign banks. The same four foreign banks accounted for over 70 per cent of the transactions in Units. Given the deposit base of these banks when compared to the total banking system, it is obvious that the transactions were not entered into for the purpose of funds management but rather for the arbitrage resulting from purchase and sale.

(iii) The securities transactions entered into by the banks have been predominantly on ready forward basis.

(iv) Over sixty per cent of the transactions have been entered into through the intervention of brokers and over forty per cent of the transactions entered into through the intervention of brokers have been through the intervention of only four brokers.

(v) Over twenty per cent in number and thirty per cent in value of the transactions cannot be matched, the transactions not appearing in the books of the counterparty bank named by the reporting bank. This is a matter which needs further investigation.

14. On the basis of a questionnaire issued to the inspecting officers of the RBI and completed by them it is obvious that there are serious deficiencies in the systems of internal control exercised by banks and institutions. Some of the major deficiencies noted in many cases are as under :

(i) dealing tickets are not available;

(ii) scrips/SGL forms/BRs and cheques were delivered to and received through the intervention of brokers and were not directly delivered to or received from counterparties;

(iii) BRs have been issued against BRs on hand;

(iv) there is no record of BRs received and held on hand nor is there evidence of periodical verification of such BRs by persons other than the custodians;

(v) the procedures regarding issue of BRs are weak;

(vi) there is no record or verification of authorised signatories before acceptance of SGL transfer forms, BRs, etc.;

(vii) there is no system of asking for or sending confirmation of contracts;

(viii) where investment records are not computerised, controls are not adequate;

(ix) separate custody is not maintained for own investments and investments held under PMS;

(x) controls regarding ready forward deals with customers are not adequate.

15. Some of the preliminary findings as set out above are detailed in the subsequent paragraphs.

III. Securities transactions in the Banking System - Statistical analysis

The Committee had called for details of securities transactions undertaken by banks during the period from 1 April 1991 to 23 May 1992 and this data is being analysed. The data has not been submitted by a few banks and therefore the study is incomplete. Also, it does not include the figures for institutions other than banks. The results revealed by the study made on the basis of the data received are summarised in the following paragraphs.

2. During this period of about 14 months, the total number of transactions entered into were 57980 for an aggregate value of Rs.9,06,192 crores (face value). The magnitude of the transactions has ranged from a sum of Rs.31,381 crores in June 1991 to a high of Rs.1,04,008 crores in March 1992 and shows a gradual increase from January 1992. The analysis of the transactions as reported has been as follows :

(Rs. in crores)

	Amount (Face value)	Percentage
Ready forward	5,05,482	55.78
Outright	47,681	5.26
Others	3,53,029	38.96
	9,06,192	100.00

In several cases, transactions where the commitments to repurchase or resell the securities have not been documented but are matters of "understanding" have been reported by the banks as "others" and not as ready forward. Therefore the percentage of ready forward transactions is actually much more than indicated above. What is however significant is that transactions reported as outright purchases or sales amount for only 5.26 per cent of the total transactions.

3. The total number of transactions reported to be in respect of Units of the UTI amount to 6,708 with an aggregate value of Rs.72,760 crores, accounting for about 8.03 per cent of the total. However, four foreign banks alone account for transactions of an aggregate value of Rs.51,633 crores, i.e. 70.96 per cent of the total transactions in Units.

4. Broker-wise analysis of the transactions is as under :

(Rs. in crores)

Broker	Amount (Face Value)	Percentage
Direct	3,50,270	38.65
M/s.Bhupen Champaklal Devidas	61,045	6.74
M/s.Harshad Mehta	48,331	5.33
M/s.H.P. Dalal	55,185	6.09
M/s.V.B. Desai	30,954	3.42
Other brokers	3,60,407	39.77
	9,06,192	100.00

5. Bank-wise analysis of the transactions is as under :

(Rs. in crores)

Bank	Amount (Face Value)	Percentage
Citibank	2,15,179	23.75
Standard Chartered Bank	1,67,014	18.43
Bank of America	1,51,646	16.73
ANZ Grindlays Bank	79,497	8.77
State Bank of India	54,343	6.00
Andhra Bank	42,135	4.65
UCO Bank	28,906	3.19
Canara Bank	27,879	3.08
Punjab National Bank	20,877	2.30
Others (below Rs.20,000 crores)	1,18,716	13.10
	9,06,192	100.00

6. An attempt was made to match on the computer the transactions reported by a bank as being with a specified counterparty bank with the transactions as reported by the concerned counterparty bank. For this purpose, transactions with banks from whom data has not yet been received have been eliminated. Therefore the number of transactions considered for matching is less than the total number of transactions reported. The number of transactions which have not matched is tabulated below :

(a) As per reporting bank

(Rs. in crores)

Name of bank	No.of transactions	Amount (Face value)	Percentage
Standard Chartered Bank	2022	63,761	23.18
Citibank	2531	45,026	16.37
Bank of America	1419	39,756	14.45
State Bank of India	789	25,556	9.29
UCO Bank	538	18,211	6.62
ANZ Grindlays Bank	943	16,848	6.12
Andhra Bank	584	12,430	4.52
Canara Bank	513	10,244	3.72
Others (below Rs.10,000 crores)	2927	43,276	15.73
	12266	2,75,108	100.00

(b) As per name of counterparty bank appearing in reporting bank's records

(Rs. in crores)

Name of bank	No. of transactions	Amount (Face value)	Percentage
Standard Chartered Bank	2398	46,546	16.92
Citibank	1603	45,232	16.44
Bank of America	859	32,542	11.83
State Bank of India	847	23,371	8.50
Andhra Bank	869	23,216	8.44
ANZ Grindlays Bank	677	16,242	5.90
Punjab National Bank	359	13,226	4.81
Canara Bank	372	10,489	3.81
Others (below Rs.10,000 crores)	4282	64,244	23.35
	12266	2,75,108	100:00

7. Eventhough the data is incomplete and the matter is under investigation, certain preliminary findings emerge.

(a) During a period of about 14 months, the securities transactions entered into by the reporting banks were almost 58,000 for an aggregate value of Rs.9,06,192 crores (face value).

(b) The bank-wise analysis of these transactions shows that a very large proportion of such transactions (67.68 per cent) were entered into by only four foreign banks. As the deposit base of these banks when compared to the total banking system is not very large (3 per cent in 1990/91) it is obvious that the transactions were not entered into for the purpose of funds management but rather for the arbitrage resulting from purchase and sale. This is further confirmed by the fact that the same four foreign banks accounted for over 70 per cent of the transactions in Units of the UTI.

(c) Of the reported transactions, 55.78 per cent was on ready forward basis and only 5.26 per cent of the transactions were for outright purchase or sale. Since as much as 38.96 per cent of the transactions is reported as "others", one can presume that this category includes ready forward transactions where the commitments to repurchase or resell are not documented, as also ready forward transactions on clients' accounts under portfolio management schemes and ready forward transactions on brokers' account. It is therefore obvious that predominantly, the securities transactions entered into by the banks were on ready forward basis.

(d) About 61.35 per cent of the transactions (face value) was entered into through brokers and four brokers alone accounted for over 20 per cent of the total face value of transactions entered into through brokers.

(e) There are as many as 12,266 transactions for an aggregate face value of Rs.2,75,108 crores where the name of the counterparty as appearing in the books of the reporting bank is not confirmed by an entry in the books of the named counterparty bank. This represents 21.16 per cent in number and 30.36 per cent in face value of the reported transactions but the percentages could be even higher because for the purposes of the matching exercise the transactions with banks from whom data has not been received have been eliminated. This is a matter which needs further investigation. However, it is obvious that this could not have occurred if cheques paid and received for transactions in securities and other documents had been directly exchanged between banks and also if bankers' cheques had not been credited to brokers' accounts or had not been issued on brokers' instructions without necessary intimation to the receiving bank.

IV. Deficiencies in Internal Control

With a view to assessing the degree of internal control generally exercised by banks and institutions with regard to transactions in securities, the inspecting officers of the RBI were asked to complete a questionnaire based on their inspection of individual banks and institutions. The findings of the officers are summarised in the following paragraphs.

2. Deal tickets were not available in many banks/institutions. However, other records like cost memos, contract notes, etc., were available.

3. The contract notes generally did not mention the name of the counterparty and this information had to be obtained from other records.

4. While generally scrips/SGL transfer forms/BRs and cheques were stated to be delivered to and received from counterparties directly, in the State Bank of India and its associate banks as also in some of the nationalised banks the deliveries and receipts were through the intervention of brokers.

5. In a number of cases the BRs were not discharged by delivery of scrips but the original BRs were returned on reversal of the transaction. Similarly, SGL transfer forms received for purchases were often not lodged with the PDO but were returned to the counterparty on reversal of transactions. Also BRs were issued against BRs held. This practice was more prevalent in branches of foreign banks but also existed in a few public sector/private sector banks and institutions.

6. In several banks/institutions there are no records of BRs received and on hand, nor is there evidence that these were periodically verified by persons other than the custodians.

7. In a few banks/institutions, the persons preparing cheques for purchases were not different from the persons delivering/receiving the scrips, SGL transfer forms or BRs.

8. The procedures regarding issue of BRs were generally weak. In a number of cases BRs were issued under single signature, there was no serial control over BRs issued, unused BR books and forms were not kept under proper custody, and discharged BRs were not serially filed. In a few cases, BRs were not issued in the form prescribed by the Indian Banks Association (IBA).

9. In a few banks/institutions procedures regarding issue of SGL transfer forms needed improvement and copies of SGL advices were not available.

10. Most banks (except the branches of a few foreign banks) and institutions do not have an uptodate record of authorised signatories for acceptance of SGL transfer forms, BRs etc. Even where such records are available verification of signatures is not often done.

11. Except in the case of the branches of a few foreign banks there was no system of asking for or sending confirmations of contracts.

12. Investment records are generally computerised in branches of foreign banks. Where safeguards are built into the system, they have provided adequate controls regarding acceptance of transactions, avoidance of short sales, reconciliation with accounting records etc. However in the case of most other banks/instiutions, records are manually prepared and similar controls are not enforced.

13. Portfolio Management Schemes (PMS) are operated in the branches of a few foreign banks and a few banks/institutions. In this connection it was observed -

(a) in some banks/institutions the bank's/institution's own investment dealings and investment dealings under the PMS are made by the same persons; and

(b) in most cases the person or group of persons had custody of both the bank's/institution's own investment and investments held under PMS.

14. The branches of a few foreign banks have also entered into ready forward deals with customers. In this connection it was observed that :

(a) investments sold under the deals were in most cases retained by the banks;

(b) the custody of the investments was with the same persons who had custody of the bank's investments;

(c) in some cases there was no record of the investments sold under ready forward deals for which custody was with the bank;

(d) the branches of a few foreign banks have issued BRs to customers instead of delivery of scrips.

15. The completed questionnaires received in respect of individual banks/institutions are under further examination.

V. Public Sector Enterprises - Equity Bids

1. (a)In February 1992, the Ministry of Industry, Department of Public Enterprises of the Government of India issued letters to approved financial/investment institutions, mutual funds and nationalised banks inviting bids for purchase of a part of the shares held by the Government of India in 16 Central Public Sector Enterprises(PSEs). For the purposes of the sale all the PSEs were grouped into 120 bundles of different company combinations.

b) The terms and conditions of the offer specified inter-alia that:

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(14) The shares of all the PSEs offered for sale shall be listed out on all principal Stock Exchanges in the country. CCI has already issued necessary guidelines to all the Stock Exchanges in the country to permit listing of shares of Central PSEs, irrespective of the level of disinvestment by the Government.

(15) The financial institutions/mutual funds/banks shall be free to offload their shareholding in these PSEs through the normal Stock Exchange transactions.

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2. In the course of scrutiny by the RBI officials, it has been seen that Allahabad Bank and SBI Caps have made bids for the bundles and have been successful.

3. (a)In the case of Allahabad Bank, it made a bid for and acquired on 22 February 1992 two bundles for Rs.13.01 crores each and sold the same for Rs.20.25 crores and Rs.20.06 crores respectively on 31 March 1992. It booked a net profit(after expenses) of Rs.14.17 crores.

(b) It was however seen that even before it made the bid, the bank had received quotations from three brokers, namely M/s.Stewart & Co., M/s.C.Mackertich and M/s.Y.S.N. Shares and Securities Pvt.Ltd., for resale of the shares for which it was bidding. The three brokers are believed to have close business connections with one another. The sale was ultimately made on 31 March 1992 to the broker, M/s.Y.S.N.Shares and Securities Pvt.Ltd., which had by its letter dated 19 February 1992 undertaken to conclude the entire business by 31 March 1992. The brokers' letters giving the quotations clearly indicate that the brokers' bids were being made on behalf of their clients. The broker in turn has sold one of the bundles to Citibank.

(c) From a scrutiny of the records of Citibank it is seen that the bundle was acquired by Citibank on 2 April 1992 for the account of one of its fiduciary clients.

4. (a)In the case of SBI Caps, the company made a bid in February 1992 and acquired three bundles for an aggregate cost of Rs.39.62 crores. Payment for the purchase was made on 28 February 1992.

(b) The company sold two of the bundles under package deals to two brokers M/s.C.Mackertich and M/s.Stewart & Co. These sales were made on the basis of confirmatory letters dated 4 March 1992 and 11 March 1992 respectively received from the brokers.

(c) The deal with M/s.C.Mackertich was to sell the bundle at cost Rs.13.12 crores and also sell 13% PSU bonds of an aggregate face value of Rs.202.50 crores at par. Similarly, the deal with M/s.Stewart & Co. was to sell one bundle at cost Rs.13.12 crores and also sell 13% PSU bonds of an aggregate face value of Rs.102.50 crores at par. As mentioned in a memorandum dated 21 April 1992 to the Committee of Directors, the purpose of the sales was to avoid booking a loss on the PSU bonds for which there were no buyers at that time even at 20% discount.

(d) It was seen that 13% PSU bonds of the face value of Rs.202.50 crores have in fact been sold to Bank of America(BOA) and Canfina at par and not to the brokers. BOA has in turn sold most of the bonds at a discount of Rs.15/- per bond(as against the discount of Rs.20/- mentioned in the note to the Committee of Directors). Canfina has recorded the purchase in its books at Rs.90/- per bond and the balance of Rs.10/- per bond has been received by Canfina from the broker, M/s.C.Makertich.

5. Though both Allahabad Bank and SBI Caps have made substantial profits by the purchase and sale of the PSE shares, the following matters need to be noted:

(a) The sales were clearly violative of condition 15 of the terms and conditions on which bids were invited, which required that the off loading of the shareholding shall be through normal Stock Exchange transactions.

(b) In the case of Allahabad Bank at least, it is clear that there was a rior arrangement to sell the shares and that the bank only acted as a conduit for making the bid. It is possible that a similar arrangement existed in the case of SBI Caps also, since the brokers concerned had made similar bids to Allahabad Bank.

(c) By not waiting for the shares to be listed and for a market price to be established, the bank and the company were not in a position to judge whether the negotiated price for the sale was the best price that it could have obtained for the sale of the PSE shares. This has particular significance when it is considered that the brokers involved in the transactions with the bank and the companyh had close business connections and appeared to have shared the business.

VI. National Housing Bank (NHB)

In our Interim Report we have given the findings based on a preliminary scrutiny of the NHB's records made by the officials of the RBI. The findings based on a further scrutiny are given in the following paragraphs.

2. During the period from April 1991 to April 1992, NHB entered into 1332 money market transactions for an aggregate value of over Rs.26400 crores. These are summarised below :-

(Rs. in crores)

Nature of Transaction	No.of transactions	Total Debits	Total Credits
Call Money	434	10033.57	10033.57
Bills Rediscounted	183	2914.29	2914.29
Government securities (including treasury bills)	20	715.32	715.32
Special Rural Housing Debentures (SRHDs) of State Agricultural & Rural Development Banks (ARDBs)	45	529.68	545.68
PSU Bonds	314	6137.28	6177.07
Units (1964 Scheme) of UTI	298	5450.62	5673.03
Sale of Bills (including sale of CDs)	23	630.52	630.52
Certificates of Deposit	15	59.70	31.43
	1332	26470.98	26720.91

Most of the security transactions were back to back transactions on a ready forward basis not involving deployment of NHB's own funds.

3. NHB is a 100 per cent subsidiary of the RBI and was established in July 1988. Until April 1992 it had no Board of Directors but was headed by a full-time Chairman and Managing Director till January 1991 and a part-time Chairman and Managing Director from April 1991 onwards, aided by an Executive Director. Authority for undertaking money market transactions was given to the dealer Shri C.Ravikumar initially for call money operations and later for placement of "very very short-term surplus funds (one/two days) in other money market instruments like treasury bills, purchases of public sector bonds/units on a buy-back basis...". This authority was however permitted to be exercised only as an exception when NHB funds could not be profitably deployed in other avenues like call money or bills rediscounting. In April 1991 Shri Ravikumar requested and was granted authority to enter into ready forward deals as and when required especially around reporting Fridays. This was approved by senior management including the Chairman. In February 1992, Shri C.Ravikumar had prepared a note which stated that "any change in the investment practices have been done in consultation (formal/ informal) with the top management" and that "it is felt that under the circumstances and also as expressed in the note on yield ... the two way trading in assets be regularised and allowed within the overall investment framework of the bank keeping in view low risk, high yield and high profitability". There is no evidence on the note to show that it has been seen by the higher authorities.

4.(a) As on 22 June 1992, NHB has 32 outstanding contracts for purchases for an aggregate value of Rs.1458.73 crores for which it does not hold securities, SGL transfer forms or BRs. A summarised position of these contracts is as under :

(Rs. in crores)

Counterparty	No.of contracts	Amount
State Bank of India (SBI)	10	707.56
ANZ Grindlays Bank (Grindlays)	15	511.66
State Bank of Saurashtra (SBS)	1	95.39
BOI Finance Ltd. (BOIF)	2	58.68
Standard Chartered Bank (Stanchart)	1	55.18
Fairgrowth Financial Services Ltd. (Fairgrowth)	2	20.35
Canbank Financial Services Ltd. (Canfina)	1	9.91
	32	1458.73

(b) In respect of the contracts with SBI and Grindlays, the counterparties have claimed that the payments made were credited to the current accounts of Shri Harshad Mehta and have denied liability except for a contract of Rs.5.11 crores where Grindlays claims that delivery of the securities was effected. Though there is no record of securities having been received by NHB, there is a BR for an equivalent amount issued by NHB to another bank for which there is no claim on NHB. Presumably delivery was effected by the broker to that bank.

(c) In respect of the contract with SBS, NHB had sold the securities to Canfina and issued a BR. Though no delivery was effected by NHB, the BR duly discharged is with NHB.

(d) In respect of the contracts with BOIF, the claim has been accepted by BOIF to be set off against the liability of NHB for a larger amount in another contract.

(e) In respect of the contracts with Stanchart, the matter is under discussion.

(f) In respect of the contracts with Fairgrowth, securities have since been recovered. However, consequent on the notification issued by the Custodian on 3 July 1992 attaching the assets of Fairgrowth under the Special Court (Trial of Offences relating to transactions in securities) Ordinance, 1992, legal issues relating to the passing of ownership of these securities to NHB have to be resolved.

(g) In respect of the contract with Canfina, it is claimed by Canfina that the contract is for DVC bonds of the face value of Rs.10 crores (present estimated value Rs.8 crores) whereas NHB claims the contract is for Units.

(h) The total exposure of NHB in respect of the outstanding purchase contracts can therefore be estimated at Rs.1271.20 crores computed as under :-

		(Rs. in crores)
Total outstanding contracts		1458.73
Less :		
Contract with Grindlays where delivery is claimed to have been effected	5.11	
Contract with SBS for which discharged BR from Canfina is available	95.39	
Contract with BOIF where claim is accepted	58.68	
Contracts with Fairgrowth where securities are subsequently received	20.35 *	
Contract with Canfina where liability for DVC bonds is accepted	8.00	
		187.53
		1271.20*

Note : * If any of the securities delivered by Fairgrowth are not considered as valid delivery, the exposures of NHB will increase by a corresponding amount.

(i) Against the above, SBI has made payment under protest of Rs.707.56 crores.

5. The following transactions in Units and PSU bonds need to be noted :

(a) SBI Capital Markets Ltd. (SBI Caps) has made a claim on NHB in respect of a BR dated 2 September 1991 for Rs.67.95 crores covering a sale of 5 crore Units @ Rs.13.59 per Unit. SBI Caps claims that the payment was made under their instructions by SBI. There is no record in NHB of either a sale of units, issue of the BR or of receipt of any amount from SBI. The amount has been credited by SBI to the account of Shri Harshad Mehta. NHB has repudiated the claim.

(b) (i) On 24 October 1991, as per NHB's records, it purchased 9% IRFC Bonds from SBS for which it paid Rs.76 crores. In the books of SBS this receipt is shown as a call money borrowing. On 25 October 1991, as per NHB's records, it sold the 9% IRFC bonds to SBS for which it received Rs.76.03 crores. In the books of SBS this is shown as a repayment of the call money borrowing with interest.

(ii) On 24 October 1991, as per NHB's records, the 9% IRFC Bonds purchased from SBS were sold to SBI for which it received Rs.0.15 crore from SBI and Rs.75.85 crores from SBS even though the sale was to SBI. In the books of SBS the payment of Rs.75.85 crores has been recorded as a purchase of units of the face value of Rs.55 crores from NHB.

(iii) On 25 October 1991, as per NHB's records, to effect sale of the bonds to SBS, it purchased the bonds from SBI for which it made payment to SBI of Rs.76.03 crores.

(iv) The books of SBI do not show any transactions for the sale of PSU bonds to NHB and the amount of Rs.76.03 crores received from NHB has been credited to Shri Harshad Mehta's account.

(v) The net result of the above transactions is that SBS has according to its records purchased 5 crore units from NHB for Rs.75.85 crores for which it has made payment but for which no delivery has been effected whereas the amount of Rs.76.03 crores paid by NHB to SBI has been credited to Shri Harshad Mehta's account in SBI. In respect of this transaction, SBS has made a claim of Rs.75.85 crores on NHB which in turn has made a claim on SBI for Rs.76.03 crores (included in para 4 above).

(c) (i) On 3 January 1992, as per NHB books, it purchased 9% IRFC bonds of the face value of Rs.100 crores from SBI and sold the same to Canfina. It made payment of Rs.95.40 crores by cheque to SBI but on inspection of the discharged cheque it was noticed that .0.50" the cheque was later altered in favour of SBS.

(ii) The records of SBS show that on 3 January 1992, Shri Harshad Mehta wrote to SBS requesting SBS to receive on his behalf a cheque for Rs.95.40 crores (drawn in favour of SBS) and to issue on his behalf cheques to the undermentioned banks :

	(Rs. in crores)
Canara Bank	79.80
SBI	5.01
Grindlays	6.37
Bank of India	4.10
	95.28

These receipts and payments were to be made by credit and debit to his current account No.2230 with SBS. The bank complied with the above instructions except that the payment to Grindlays was made for Rs.5.37 crores and not Rs.6.37 crores. In the process, the residual amount of Rs.1.12 crores stands automatically credited to his current account.

(iii) The amount received by Canara Bank from SBS was appropriated towards amounts due to Canfina for purchases made by Growmore Research and Assets Management Ltd. (a group concern of Shri Harshad Mehta). In the other three banks, the amounts received from SBS have been credited to Shri Harshad Mehta's account.

(iv) For the sale to Canfina, NHB received Rs.95.44 crores from Canfina and issued its BR. It appears that .lm 0.50" the BR was discharged by Canfina on 31 March 1992 by taking physical delivery of the bonds from Shri Harshad Mehta. For the purchase from SBS, NHB has not received the bonds or a BR and has made a claim (included in paragraph 4 above) which SBS has disputed.

(d) (i) On 14 March 1992, NHB has purportedly made a sale of Units of the face value of Rs.30 crores to State Bank of Patiala (SBP) and since that day was a Saturday when NHB is closed, SBP was formally advised by NHB to make payment of Rs.44.98 crores directly to SBI, from whom presumably the Units were purchased. The amount paid by SBP to SBI has been credited by SBI to Shri Harshad Mehta's account.

(ii) In the books of NHB, there is no entry recording this transaction. However, a cost memo was prepared and a BR was issued. In the dealers' diary the transaction is recorded both on 14 March 1992 and 16 March 1992 but both entries have been cancelled.

(iii) SBP has made a claim on NHB which in turn has made a claim on SBI (included in paragraph 4 above).

(e) There are also a number of transactions appearing in the books of NHB as purchases/sales of Units/PSU bonds for which in the books of the counterparty banks (mainly SBI and Grindlays) there are no corresponding transactions. The amounts paid and received for such transactions have in the counterparty banks' books been debited/credited to Shri Harshad Mehta's account.

6. Between July 1991 and April 1992, NHB entered into twelve ready forward "back to back" deals in Government securities for an aggregate value of Rs.653.06 crores and two similar deals in treasury bills. The following deals need to be noted.

(a) (i) NHB has made payment to SBI for the following purchases :

Date	Security	(Rs.in crores) Amount
21.02.1992	Treasury bills	47.98
21.02.1992	11.5% GOI loans 2007 and 2008	152.12
07.03.1992	11.5% GOI loans 2010	101.89
		301.99

(ii) No securities or SGL transfer forms have been received by NHB and there is no record in SBI of these transactions. The amounts paid by NHB have been credited to Shri Harshad Mehta's account in SBI.

(iii) As these were back-to-back deals, NHB has in turn issued its BRs to the undermentioned banks.

	(Rs.in crores)
State Bank of Patiala	47.98
Bank of Karad	51.57
SBI Capital Markets Ltd	100.62
Standard Chartered Bank	101.89
	302.06

(iv) The purchasing banks have made claims on NHB which in turn has made a claim on SBI (included in paragraph 4 above).

(b) (i) In the records of NHB there is an original undischarged SGL transfer form dated 26 August 1991 for 11.5% GOI loan 2015 for face value Rs.38 crores issued by UCO Bank in favour of NHB.

(ii) There are no entries in the books of NHB for a purchase from UCO Bank. However, there are jottings in the dealers' diary on 26 August 1991 which indicate a purchase of this loan from UCO and a sale to SBI Caps. There is also on record a copy of BR dated 26 August 1991 issued by NHB in favour of SBI, duly discharged by SBI.

(iii) There is also available in the records of NHB a cost memo dated 7 September 1991 for a subsequent sale of the same security by SBI to NHB for Rs.38.97 crores. The broker mentioned in the cost memo is Shri Harshad Mehta.

(iv) In the books of SBI, there is a deal slip which shows a purchase on 26 August 1991 of 11.5% GOI loan 2015 for Rs.38 crores and a resale of the same security on 7 September 1991.

(v) On enquiry, UCO Bank has denied issuing the SGL transfer form which is made out as signed by one of its officers. The matter is under further investigation by CBI.

7(a) NHB has subscribed to the Special Rural Housing Development Debentures (SRHDs) issued by various State Agricultural and Rural Development Banks. NHB has entered into 45 ready forward deals in respect of SRHDs aggregating to Rs.169.00 crores are with SBI.

(b) All the deals with SBI are through broker Shri Harshad Mehta but no BRs appear to have been received or issued for the purchase or sale transactions. For the deals with other banks, the BRs are issued for sale of Units or PSU bonds and the description in the brokers' notes and delivery orders is also for Units and PSU bonds. On reversal of the transactions, the discharged BRs have been received back. However, the entries in the books of NHB, both at the time of entering into the transaction and its reversal, are for SRHDs and recorded in the SRHD register.

(c) It is obvious that for the above transactions there was no actual or even intended delivery of the SRHDs or Units or PSU bonds and these were pure and simple financing transactions. It is also obvious that since SRHDs do not have a secondary market and do not have a wide acceptance, the documentation was made to show a transaction in Units or PSU bonds.

(d) Even as per NHB records, sales were effected of bonds which did not exist. For example, on 26 February 1992, NHB has sold bonds of an aggregate value of Rs.72.45 crores when its total holding on that date was only Rs.62.22 crores.

8(a) NHB has been quite active as a lender in the call money market. However, in a large number of cases, transactions recorded in NHB's books as call money lending to other banks have in fact been a loaning of funds to broker Shri Harshad Mehta routed through SBI, Grindlays, etc Some of these transactions are listed below :

(b) On 6 April 1992, NHB presumably lent Rs.40 crores at call to UCO Bank. In the UCO bank (Hamam Street Branch) the amount is credited to Shri Harshad Mehta's account. It is stated that this was done under instructions from its Head Office and its Zonal Office at Bombay. The funds dealing officer at the D.N. Road (Bombay) branch has stated that there was a letter from NHB enclosing the cheque but this is not traceable either in UCO Bank or in NHB. At the date of the credit the account of Shri Harshad Mehta in UCO Bank showed an overdraft of Rs.39.07 crores. The repayment of the alleged call deposit has been received by NHB through Grindlays which has debited Shri Harshad Mehta's account.

(c) On 20 April 1992 NHB presumably lent Rs.5 crores at call to Grindlays. The amount was credited in Grindlays to Shri Harshad Mehta's account and was repaid on 21 April 1992 by debit to this account.

(d) On 2 April 1992 NHB presumably lent Rs.17 crores at call to SBI. The amount was credited to Shri Harshad Mehta's account in SBI. On 3 April 1992 NHB received in repayment Rs.3.27 crores from Grindlays by debit to Shri Harshad Mehta's account and Rs.13.74 crores was rolled over as a fresh call money loan to SBI. On 6 April 1992, NHB received Rs.13.76 crores in repayment of the alleged call money loan to SBI from UCO Bank. The amount was debited in UCO Bank to Shri Harshad Mehta's account.

(e) On 25 March 1992 NHB presumably lent Rs.15 crores as call money loan to Grindlays which was credited by Grindlays in Shri Harshad Mehta's account. Between 4 May 1992 and 2 June 1992, NHB passed rectification entries treating the payment as being for purchase of Units. This amount is still outstanding in NHB books and is claimed from Grindlays (included in paragraph 4 above).

(f) It may be noted that under the National Housing Bank Act, 1987, NHB cannot make direct loans to brokers. The recording of these transactions as call money transactions appears to be a subterfuge to give loans to broker Shri Harshad Mehta by booking the same as call money loans to other banks.

9. (a) On 27 September 1991, NHB's books record a receipt from SBI of Rs.38.90 crores and a payment on the same day to SBI of an equivalent amount. Though these items appear in NHB's account with RBI, there are no entries for this receipt and payment in the books of NHB except in the RBI scroll.

(b) On scrutiny it was observed that the receipt was from SBS and not from SBI. In the books of SBS, this payment to NHB is recorded as the discounting by SBS of a bill for Rs.40 crores due on 26 November 1991. SBS received Rs.14.00 crores on 26 November 1991 and Rs.26.01 crores on 27 November 1991 from NHB which was recorded as repayment for the bill discounted with interest for 1 day's delay.

(c) In the books of NHB, the repayments of Rs.14 crores on 26 November 1991 and Rs.26.01 crores on 27 November 1991 were financed from the following receipts :

(i) Rs.14 crores received on 26 November 1991 from SBI and credited to Sundry Deposits Account and paid to SBS on the same day by debit to the same account.

(ii) Rs.25.53 crores received from Canara Bank on 27 November 1991 and Rs.0.48 crore received from SBI.

(d) In the books of SBI, the payments of Rs.14 crores and Rs.0.48 crore were debited to Shri Harshad Mehta's account.

(e) In the books of Canara Bank, the payment is shown as being for a reversal of a sale by Canfina of 9% IRFC bonds for Rs.25 crores for which Canfina had issued a BR to NHB and which was received back duly discharged by NHB.

10. On 19 July 1991 NHB sold a bill for Rs.15 crores to SBS for Rs.14.84 crores and on 10 August 1991 made repayments to SBI even though the bill was sold to SBS. On enquiry, it appears that SBS received payment on 27 July 1991 from SBI.

11. NHB is holding certain bonds and other securities and documents related thereto which are not related to its transactions and which purportedly were received from Growmore Research and Assets Management Company Ltd. The matter is under further investigation.

12. As mentioned in our Interim Report, there were serious deficiencies in the control systems regarding the transactions in money market instruments and in the record keeping for the same. Some of these are mentioned below :

(a) All the funds management operations were centralised with Shri C.Ravikumar, Assistant General Manager. He was not only the dealer but was also one of the signatories to the cheques. The back-up functions were with Shri S.Suresh Babu, Assistant Manager who reported to Shri Ravikumar and acted under his instructions. These two officers, between themselves, were responsible for all the functions including (i) making the deal, (ii) recording the same, (iii) preparing the vouchers, (iv) preparing the cheques, (v) signing the cheques (as one of two signatories), (vi) preparing and signing BRs, (vii) custody of BRs received from counterparties, (viii) issuing and receiving SGL transfer forms and lodging the same with the RBI, and (ix) maintaining the account with the RBI and reconciling the same.

(b) Even in the dealing transactions no proper procedures appear to have been laid down. Thus,

(i) no deal tickets were prepared and the only record is a rough diary maintained by Shri Ravikumar;

(ii) no confirmations of deals were called for or issued;

(iii) there is no record of BRs issued or BRs received;

(iv) The BRs issued are only on NHB's letterhead but are not serially numbered.

(c) There are serious deficiencies in the accounting records maintained. Thus,

(i) The writing of day books and General Ledger appears to have been in arrears for several months. There is also evidence of Cash Book entries being posted out of order. It was also noticed that funds transactions for an aggregate value of Rs.171.73 crores pertaining to 19 July 1991 were accounted in the General Ledger and Cash Book only on 27 September 1991.

(ii) No attempt was made to reconcile the balance in the RBI as appearing in the General Ledger with the balance as appearing in the statement received from RBI. In fact in August and September 1991, the balance with RBI as appearing in the General Ledger showed an overdraft running into several crores of rupees.

(d) There does not appear to have been any reporting system prescribed for the transactions entered into by the Funds Management Group. Upto October 1991, vouchers for individual deals were put upto the General Manager (now Chief General Manager). Thereafter, daily statements of deals were put up to the General Manager, but in early January 1992 this was also stopped. A weekly statement was also put up to the General Manager but this was also stopped in December 1991. Occasionally, a statement was put up to the top management including the Chairman but this was not done on a regular basis. In both these statements only the outstanding position of investments was shown and therefore the back-to-back transactions which did not result in any change in the outstanding balance were not reflected in the statements.

13. (a) As NHB is not a bank within the meaning of the Banking Regulation Act, 1949 its operations were not subject to inspection by the Department of Banking Operations and Development of the RBI. NHB had statutory auditors who examined the books of NHB. Its accounting year ends on 30 June in every year. Therefore the last audit was for the year ended 30 June 1991. The bulk of the transactions have been after that date and therefore have not been subject to scrutiny either by the statutory auditors or an independent inspection agency.

(b) At the initiative of the late Chairman, a firm of Chartered Accountants was appointed in July 1991 to conduct an internal audit. The objective of the audit as mentioned in the letter of proposed appointment was to "ensure that the accounting system presently followed in our offices at Bombay and Delhi particularly checks and cross checks are working satisfactorily, changes if any needed in the system and additional safeguards that may be built in to strengthen it further." The internal auditors have submitted two reports.

(c) In the first report dated December 19, 1991, the internal auditors have stated that "a thorough review and change in maintaining call money receipts is called for." The General Manager wrote to the internal auditors on January 30, 1992 for "specific suggestions as to what sort of records/registers you suggest so as to set right the position." No further action appears to have been taken. The second report dated March 30, 1992 makes no mention regarding money market operations.

14. It would therefore appear that there has been a total abdication of responsibility by top management regarding the fund management in NHB. The operations were centralised in an individual, no exposure limits were prescribed, the most elementary control procedures were not imposed nor was there any worthwhile system of reporting. No doubt, internal auditors were appointed to look into some of these aspects but unfortunately they have not brought out any deficiencies to the attention of the management on which basis remedial action could have been taken.

VII. Andhra Bank Financial Services Ltd.

Andhra Bank Financial Services Ltd. (ABFSL) is a wholly-owned subsidiary of Andhra Bank. The Chairman of the bank is also the Chairman of the subsidiary. The company has its Central Office at Hyderabad and has offices in Bombay, Bangalore, Delhi and Madras. As on 20 June 1992, the total amount placed with the company by institutions for investment was Rs.130.23 crores. In addition, the company had received inter-corporate deposits of Rs.368.84 crores. The aggregate funds placed with the company were therefore Rs.499.07 crores.

2. The company used the funds to purchase securities on a ready forward basis. In some cases, these are on the basis of an oral understanding with the counterparty and in certain other cases the counterparty used to give a corresponding re-purchase contract to be executed on the due date. Some of the reversal contracts did not materialise and in effect the contracts became outright purchases. The particulars of the counterparties from whom the purchases were made, the amount of the contracts and the securities held by the company are given below:

(Rs. in crores)

Counterparty	**Amount of re-purchase commitments**	**Value of securities held @@**
Fairgrowth Financial Services Ltd.(FGFSL),Bombay	75.42	50.91
FGFSL, Bangalore	164.60	215.12
	240.02	266.03
Hiten P. Dalal	140.71	156.87
National Housing Bank	24.46	24.46
M/s.V.B. Desai	40.00	40.00
Canfina	8.82*	8.82*
Others	2.90	3.00
Total	456.91	499.18

Notes : @@ The above value has been determined in the books of ABFSL taking bonds at face value and the Units at Rs.15.50 per Unit. However, the actual realisable value will be lower.

* Since adjusted.

3.(a) During the investigation of the reconciliation of investments, a physical verification of the securities held at the company's Bombay and Bangalore offices was carried out. It was observed that the securities held in Bangalore against the dues of FGFSL, included 3 UTI certificates covering 9,75,00,000 Units (having a total value at the rate of Rs.15.50 per Unit, of Rs.151.12 crores) purportedly issued by the Bangalore Office of the UTI. As some doubts arose regarding these certificates, the three certificates were taken into custody and kept with the RBI, Bangalore. The sealed cover containing the certificates was opened on 1 July 1992 in the presence of the Executive Director of Andhra Bank, the concerned officials of ABFSL, the Manager, RBI, and the Manager, UTI, Bangalore with a view to enabling the UTI to scrutinise the certificates and verify their genuineness or otherwise. After scrutiny of the certificates, the Manager, UTI, Bangalore has certified that while the format of the three certificates is according to the format of the Unit certificates issued by UTI, the certificates in question did not appear to have been issued to the parties named therein on the dates given in the certificates and that the number of Units and the names and addresses of the parties given therein appeared to have been over-written by tampering with the original number of Units and the names of the holders. He had come to the conclusion that the contents of the Unit certificates were not genuine.

(b) Incidentally, one Unit certificate covering 1,10,15,500 Units had been returned by the company to FGFSL on 17 June 1992 against payment and therefore the original was not available for scrutiny but a photocopy of the certificate is available. Since the Bangalore office of FGFSL was also under inspection, the officer inspecting that office was asked to enquire about the fate of the returned certificate.

(c) In this connection, an official of FGFSL admitted in writing to the tampering and issuance of 4 tampered Unit certificates. He added that additional physical certificates (not originals) of 9% HUDCO Bonds were given to ABFSL. These are in the form of two letters of allotment of HUDCO bonds for an aggregate face value of Rs.45 crores given to ABFSL as security which are in the possession of ABFSL. According to this official, the formats of different allotment letters of these bonds were faxed to him by the company's Bombay office. (The Bombay office has disputed this). He had added that the tampering was done since the company was under severe pressure from ABFSL to deliver the securities to cover the funding support extended by ABFSL to it. The official also stated that the fourth Unit certificate returned by ABFSL had been destroyed.

(d) The matter has been reported by the RBI to CBI for further investigation and also to the Custodian to consider notifying the company under the relevant Ordinance.

4. The company's Bombay office had released Unit certificates for an aggregate face value of Rs.12.20 crores (valued by the company at Rs.18.91 crores) received from FGFSL. These were released by the company to FGFSL for lodgement at UTI for transfer to FGFSL's name. The relative certificate has been taken by FGFSL from UTI and it has not relodged the certificate with the company.

5. The company is also not assured of the genuineness of NTPC bonds of the face value of Rs.15 crores held at its Bangalore Office.

6. Therefore, the effective security held by the company against its exposure to FGFSL comprises only of bonds of the face value of Rs.42 crores. At an estimated value of Rs.80 per bond of the face value of Rs.100, the realisable value will come to Rs.33.60 crores, thus leaving a shortfall of Rs.206.42 crores. The company has advised that it has obtained additional security of estimated market value of Rs.101.59 crores. This would reduce the shortfall in security to Rs.104.83 crores.

7. The investigation of the security transactions in ABFSL and FGFSL is in progress.

VIII. Canbank Financial Services Ltd.

Canbank Financial Services Ltd. (Canfina) is a wholly owned subsidiary of Canara Bank. Its registered office is at Bangalore but most of its securities transactions are conducted in Bombay. however, the accounts are centralised at its registered office at Bangalore and all original records relating to security transactions like contracts, dealing pads and cost memos are also maintained there.

2. Canfina has reconciled its own investment account as at 31 March 1992. However, it has not so far reconciled, at any point of time, the investments in respect of PMS and Corporate Investment Advisory Services (CIAS) clients.

3. There are a number of open contracts in Government loans as also in PSU bonds and Units appearing in the books of Bank of America where the counterparty bank is shown as Canfina, but for which details do not appear to be available in Canfina records. As Canfina does not maintain a contract register, it is difficult to verify the existence of these open contracts.

4. The following transactions as appearing in Canfina's records may be noted :

(a) (i) On 22 July 1991, Canfina purchased from Bank of Karad Ltd. (BOK) through the broker M/s. Hiten P. Dalal, 16 crore Units of UTI for Rs.212.80 crores for which a BR was received from BOK. This contract was liquidated to the extent of 1.5 crore Units on 15 October 1991 and 7.5 crore Units on 18 October 1991 for Rs.20.85 crores and Rs.100.24 crores respectively. The payment to BOK of Rs.212.80 crores and the receipts of Rs.20.85 crores and Rs.100.24 crores respectively are reflected in BOK as credits and debits in the account of broker Shri A.D. Narottam. To date Canfina has still to receive from BOK 7 crore Units for which it has paid Rs.93.10 crores.

(ii) On 31 July 1991, Canfina purchased from BOK through broker M/s.Hitan P. Dalal, 19 crore Units for Rs.255.44 crores for which BOK issued a BR. The payments was credited in the books of BOK to the account of broker Shri A.D. Narottam. To data Canfina has not received the Units.

(iii) On 6 April 1991, Canfina purchased from BOK through broker M/s.Hiten P. Dalal, 11.5% GOI loan 2008 of a face value of Rs.25 crores for Rs.25.81 crores. The payment was credited in the books of BOK to the account of broker Shri A.D. Narottam. Originally, BOK issued a BR. On 18 April 1992, this was replaced by an SGL transfer form which on lodgement with the PDO was returned due to insufficiency of balance. To date, Canfina has not received the securities.

(iv) All the above transactions were booked by the Chief Dealer, Shri Ashok Kumar. The transactions dated 22 July 1991 and 31 July 1991 were reported to the Managing Director on 30 August 1991 and the transactions dated 6 April 1991 were reported to the Managing Director on 30 May 1991. However, the fact that these BRs remained outstanding was not reported to the Managing Director until 27 April 1992.

(v) As a result of the above transactions, Canfina has in its books, investments aggregating to Rs.374.35 crores for which it has to receive securities from BOK.

(b) On 2 September 1991 Canfina purchased 5 crore Units for Rs.67.75 crores from State Bank of Saurashtra (SBS) through the broker M/s.C.Mackertich, for which it is holding a BR. Delivery of the Units has not been effected to date.

(c) On 23 March 1992 Canfina sold 13% DVC bonds of a face value of Rs.10 crores for Rs.9.90 crores to National Housing Bank (NHB) through the broker Shri Harshad Mehta. Delivery of the bonds has not yet been effected. Nor has a BR been issued. Reference is invited to paragraph 4(g) in the Chapter on NHB in this report.

(d) (i) On 20 January 1992, Canfina sold to Citibank through the broker M/s.Hiten P. Dalal five lots of PSU bonds for which the contracted value as recorded in the dealer's pad aggregated to Rs.31.13 crores. It received from Citibank Rs.25.77 crores as the sale proceeds. It received from the broker an amount of Rs.3.29 crores through State Bank of Travancore. An amount of Rs.2.07 crores is shown in the books of Canfina as receivable from the broker. The details of the rates at which the sales were booked by Canfina and the sale proceeds were received from Citibank are given below :

Particulars of security	Face Value (Rs. in crores)	Contracted rate (as per dealer's pad)	Amount receivable (Rs.)	Rates at which final payment accepted	Amount finally received from Citibank (Rs.)
13 % NPC	10.9365	97.50	111188249.38	80.00	92049374.38
13 % HPF	1.75	97.50	18140787.67	80.00	15078287.67
13 % ITI	4.93	97.50	48418678.08	80.00	39808736.99
13 % NPC	6.00	97.50	60978904.11	80.00	50478904.11
13 % HPF	7.00	97.50	72563150.68	80.00	60313150.68
		Total :	311289769.92		257738453.83

(ii) On 15 January 1992, Canfina sold to Bank of America (BOA) through the broker M/s.Hiten P. Dalal five lots of PSU bonds of a face value of Rs.175.75 crores and the contracted value as recorded in the dealer's pad aggregated to Rs.168.28 crores. It received from BOA Rs.152.38 crores and from Andhra Bank Rs.19.87 crores. The payment made by Andhra Bank is debited in that bank to broker M/s.Hiten P. Dalal's account. As the amount received from Andhra Bank was in excess of the difference between the contracted value and the amount received from BOA, the difference of Rs.3.97 crores has been shown by Canfina as an excess recovery from the broker. The details of the rates at which sales are booked by Canfina and the sale proceeds received from BOA are given below :

Security	Face Value (Rs.in crores)	Contracted rate	Amount receivable (Rs.)
9% IRFCI	45.00	95	42,90,53,424.66
9% IRFCI	50.00	90	45,17,26,027.40
9% IRFCI	60.00	98	60,36,82,191.78
13% NTPC	7.75	92	7,42,25,890.41
13% NTPC	13.00	95	12,41,48,219.18
Total :	175.75		168,28,35,753.43
Amount received from BOA			Rs.152,37,73,253.43
Short recovery			Rs. 15,90,62,500.00

(iii) On 6 February 1992, Canfina sold to Citibank through the broker M/s.Hiten P. Dalal six lots of PSU bonds and other debentures of a face value of Rs.78.83 crores and the contracted value as recorded in the dealer's pad aggregated to Rs.82.85 crores. Canfina has recorded this transactions by showing a receipt of Rs.59.93 crores from Citibank and a recovery of Rs.22.92 crores from the broker. The details of the rates at which the sales are booked by Canfina and the sale proceeds shown as received from Citibank are given below :

Particulars of security	Face Value (Rs. in crores)	Contracted rate (as per dealer's pad)	Amount receivable (Rs.)	Rates at which final payment accepted	Amount receivable as per col.5 (Rs.)
1.	2.	3.	4.	5.	6.
14% Godrej Soaps	5.00	95.67	48525410.96	65.00	33190410.96
14% Insil	10.30	99.3210	107357876.71	62.50	69431876.71
13% CIL	40.00	99.4465	422797506.85	71.50	310931506.85
-do-	15.00	99.5733	158549041.10	71.50	116439041.20
14% Haryana Petro	5.00	99.3364	52122994.52	65.00	34954794.50
15% India Rayon	3.53	105.6598	39154012.58	92.00	34332876.73
Total	78.83		828506842.72		599280506.85

It is however, ascertained that :

1. the payment was made not by Citibank but by American Express Bank and that this payment was made by American Express Bank at the instance of the broker M/s.C. Mackertich;

2. Citibank has purchased the PSU bonds and debentures, not from Canfina but from M/s.C. Mackertich, for which it had paid Rs.59.92 crores. However, this purchase was of bonds and debentures of a face value of Rs.75.30 crores only (as against Rs.78.83 crores as sold by Canfina) though the amount of purchase consideration was almost the same as recorded as sale by Canfina. The details of the purchase as recorded in Citibank books are given below :

Particulars of security	Face Value (Rs.In crores)	Rate	Amount (Rs.)
14% Godrej Soaps	5.00	72.50	3,69,40,410.95
14% INSIL	10.30	72.50	7,97,31,876.71
13% CIL	40.00	74.50	32,27,89,041.10
-do-	15.00	74.50	12,08,85,616.44
14% Haryana Petro	5.00	72.50	3,87,04,794.52
Total	75.30		59,90,51,739.72

(iv) A number of questions arise regarding the above transactions. First, it is obvious that the transactions have been booked at artificial rates in Canfina books either to book a profit or to avoid a loss. Secondly, it has not been explained to us as to why the broker should have agreed to accept debits for the huge amounts of differences between the price paid by the purchasers and the price at which the sales have been booked. Obviously, the broker must have been compensated for these debits in some other transactions. Thirdly, if this compensation has not been made, these transactions could be part of a total deal whereby the losses of Canfina on acquisition of PSU bonds and other debentures have been passed on to some other entity. The matter is under further examination.

5.(a) During 1991-92 Canfina subscribed to the extent of Rs.1982.18 crores in bonds issued by PSUs. In turn, PSUs placed with Canfina Rs.1064 crores under Portfolio Management Scheme (PMS) and Rs.858.80 crores under Corporate Investment Advisory Services (CIAS). The funds placed under PMS were for one year and under CIAS for 51 days to 6 monhts. These funds were largely deployed in ready forward deals, to a large in PSU bonds.

(b) The funds deployed under the PMS and CIAS schemes are likely to show a significant depreciation in value of investment with the fall in the value of PSU bonds and if these losses cannot be passed on to the PSUs who have placed the funds, the loss would have to be borne by Canfina.

IX. State Bank of Saurashtra

The securities transactions of the State Bank of Saurashtra (SBS) are handled by the Funds Management Cell (FMC), which though attached to the Head Office of the bank operates from the Bombay (Fort) branch.

2. The reconciliation of the Investment Account with the balance of the SGL account in the PDO as on 23 May 1992 shows a net difference of Rs.2 crores determined as under:

SGL form to be received from State Bank of India(SBI) for 11.5% GOI loan 2009		Rs.10.00 cr.
SGL forms to be issued to SBI:		
- 11.5% GOI loan 2009	Rs.3.00 cr.	
- 11.5% GOI loan 2007	Rs.5.00 cr.	
		Rs. 8.00 cr.
		Rs. 2.00 cr.

The matter is under discussion with SBI.

3(a) The transactions in respect of which SBS does not hold scrips or BRs are as under:

Date of payment	Particulars of security	Face value (Rs. in crores)	Contract value (Rs. in crores)	Name of counter-party
1.10.91	13% NLC Bonds	5.00	4.55	SBI
2.9.91	Units	50.00	67.74	SBI
10.9.91	Units	20.00	26.82	SBI
23.10.91	Units	55.00	75.82	NHB
		130.00	174.93	

(b) All the above transactions were entered into through broker Shri Harshad Mehta. All the payments made to SBI have been credited to Shri Harshad Mehta's account. The amount paid to NHB has also ultimately been credited to Shri Harshad Mehta's account in SBI. (Reference is invited to paragraph 5(b) of the Chapter on NHB in the report).

4. SBS had entered into ready forward deals with Canbank Mutual Fund and ANZ Grindlays Bank for 13% DVC bonds of the face value of Rs.34.50 crores and RINL bonds of the face value of Rs.21.00 crores, respectively. Both the counterparties have claimed that the purchases were on outright basis. The realisable value of the securities is lower than the prices at which the purchases were made.

5. The following transactions of SBS may be noted:

(a) (i) According to the records of SBS it made call loans of Rs.26 crores and Rs.10.5 crores to UCO Bank on 22 July 1991 and 25 July 1991 respectively and a call loan of Rs.27 crores to Canara Bank on 18 July 1991.

(ii) These loans do not appear in the books of UCO Bank but the amounts received from SBS were credited to Shri Harshad Mehta's account in UCO Bank.

(iii) The amount received by Canara Bank was on account of Canbank Financial Services Ltd (Canfina). In Canfina's books, the transaction is recorded as amount received from SBS for the sale of 13% NTPC bonds of face value Rs.32 crores to SBI Capital Markets Ltd.(SBI Caps). The amount due under this contract was Rs.31.23 crores and the balance amount was received by Canfina from SBI by means of a banker's cheque. In the books of SBI Caps, this purchase transaction is not recorded.

(iv) SBS received the full amount of Rs.63.50 crores on 26 July 1991 by banker's cheque from SBI. In the books of SBI this payment has been debited to Shri Harshad Mehta's account. On the same day, SBI received a banker's cheque from UCO Bank for Rs.63.50 crores. In UCO Bank's books, this amount has been debited to the current account of Shri Harshad Mehta to which the two amounts aggregating to Rs.36.50 crores had been credited earlier (vide item (ii) above).

(b) (i) On 19 September 1991, according to SBS books it made a call loan of Rs.31 crores to Canara Bank through broker Shri Harshad Mehta.

(ii) The repayment of this loan was received the next day from SBI. In the books of SBI the payment was debited to Shri Harshad Mehta's account.

(iii) There is no call borrowing appearing in Canara Bank's books. The payment was in fact to Canfina, in whose books it has been treated as a receipt for the sale of 9% IRFC bonds of the face value of Rs.30 crores to SBS. The broker in this case is Shri Harshad Mehta. The relative BR issued by Canfina for this transaction has been received back by it, after being duly discharged by the Manager, FMC of SBS.

(c) On 19 July 1991, according to SBS books it paid Rs.14.84 crores to NHB for discount of bills under the Bills Rediscounting Scheme. On the due date, ie.27th July 1991, the repayment was received from SBI.

6. There are several cases where securities transactions have been made at the request of brokers using the name of the bank, for which a service fee, normally 0.01 per cent, is received from the broker. Some instances are given below:

(a) On 22 October 1991 SBS received SGL form for 11.5% GOI loan 2009 of the face value of Rs.17 crores from SBI and in turn issued its own SGL form in favour of UCO Bank. A service fee of Rs.0.17 lakh was received from the broker, Shri Harshad Mehta.

(b) On 13 July 1991, SBS purchased 11.5% GOI loan 2009 of the face value of Rs.65 crores from UCO Bank and sold the same to SBI. No exchange of SGL forms took place. A service fee of Rs.0.65 lakh was received from SBI.

(c) On 22 October 1991, SBS received SGL form from SBI for 11.5% GOI loan 2009 for Rs.17 crores and issued SGL form for the same security to UCO Bank. SBS received a cheque for Rs.0.17 lakh from SBI.

(d) On 11 January 1992, SBS purchased from Punjab National Bank 11.5% GOI loan 2008 for face value Rs.50 crores and sold the same to Syndicate Bank. No SGL forms were exchanged between the banks. Service charges of Rs.0.50 lakh were received from the broker Shri Harshad Mehta.

In all the above cases, no entries have been made in the books of SBS except for receipt of the service fees. In all cases the Head Office has been kept informed.

7. The investigation of the security transactions in SBS is in progress.

X. SBI Capital Markets Limited

Reference was made in the first Interim Report to the findings of the preliminary inspection of the securities transactions of SBI Capital Markets Ltd (SBI Caps). The results of a further scrutiny of the transactions are given in the following paragraphs.

2(a) Reconciliation of investments as at 31 March 1992 and 23 May 1992 (as requested by the Committee) has not yet been submitted. The external auditors of the company were asked to produce a list of investments, BRs and SGL transfer forms on hand as at 31 March 1992 as verified by them on that date but this list has also not been made available.

(b) The external auditors had made available from their work papers the reconciliation of investments as at 31 March 1991 which shows that on that date there were on hand BRs for an aggregate value of Rs.186.83 crores and the company had issued at that date BRs of an aggregate value of Rs.286.11 crores which were outstanding. Unfortunately, the reconciliation does not give item-wise details of BRs on hand and outstanding and it is not clear whether the BRs on hand were verified by the auditors or even whether they were in the custody of the company or the State Bank of India(SBI), and whether the existence of these BRs was ceritified by SBI if held by them.

3. The aggregate value of investments made by SBI Caps for which it does not hold BRs or where the counterparty has denied liability has now been determined at Rs.121.36 crores. In all cases, the payment has been credited to Shri Harshad Mehta's current account in SBI. The details of the investments are as under:

Sr.No.	Date	Security	Transaction amt. (Rs.in crores)	Counter-party	Remarks
1.	29.7.91	Units - 0.25 cr.	3.38	UCO Bank	No BR held. Amount credited to Shri Harshad Mehta(HSM)'s current a/c with SBI, Bombay(Main) branch.
2	2.9.91	Units - 5.00 cr.	67.83	National Housing Bank	Though BR of NHB is held, counter-party has denied the transaction. Amount credited to HSM's current a/c with SBI.
3.	31.3.92	Units - 1.25 cr.	18.75	Canfina	No BR held. Amount credited to HSM's current a/c with SBI which issued Pay Order favouring ANZ Grindlays Bank. Amount credited by Grindlays Bank to HSM's current a/c with it.
4.	6.4.92	Units -	15.15 1.00 cr.	Canfina	No BR held. Amount credited to HSM's current a/c with SBI.
5.	30.3.92 3.4.92 20.4.92 21.4.92	Units - 1.08 cr. (Madras office deals)	16.25	Counter-party is not named.	No BR held. Funds were transferred to Bombay Main branch of SBI for credit to HSM's current a/c. Company holds HSM's broker notes evidencing the purchase of Units for SBI Caps.
			121.36		

4(a) The Madras office of SBI Caps collected substantial funds from corporate investors under the portfolio management scheme(PMS) and for short term investment. Since the RBI rules regarding PMS required a minimum lock-in period of one year, funds made available for shorter periods were collected in the guise of advisory services whereby payment was required to be made by the customer directly to the vendor of securities.

(b) The funds collected by the Madras office under both these schemes were deposited in a "Special account" with SBI's Industrial Finance branch in Madras and transferred therefrom to the investing brokers' accounts, presumably under ready-forward deals. On return of the funds, the proceeds were credited to this account. Payment of the principal and assured return was made to the clients from this account and the balance transferred to another account with SBI designated as "collection account". The balance in the latter account represented the earnings of SBI Caps which was transferred to the corporate office.

(c) Therefore even though the funds were collected under PMS or as part of advisory services, the clients have been given only an assured return and the excess earning have been appropriated by SBI Caps as its income.

(d) Even though funds were received by SBI Caps and routed through the Special account with SBI's Industrial Finance Branch, no accounting entries have been passed in SBI Caps' books of account for the funds received and disbursed and only memorandum records have been maintained.

(e) During the period from 1 April 1991 to 21 April 1992, the funds collected in the above manner and credited in the Special account aggregated to Rs.1397.11 crores. These funds were transferred to the following brokers/investing agencies as indicated below:

Broker/Investing Agency	Rs.in crores	Percentage
Growmore Research and Asset Management Ltd(GRAM)/ Shri Harshad Mehta	1,148.61	82.20
Citibank	147.75	10.58
Kotak Mahindra Finance Ltd.	75.25	5.39
Somayajulu & Co	25.50	1.83
	1,397.11	100.00

The above figures represent the aggregate value of transfers but since the funds were rolled over under ready forward deals; the peak outstandings would be lower. While exact figures are not available, these may be roughly estimated at Rs.200 crores.

(f) In most cases, the ready forward deals with GRAM/Shri Harshad Mehta are not supported by BRs or securities though the underlying securities were purported to be PSU bonds or Units of UTI. For all practical purposes, therefore, these appear to be 'clean' loans made available to Shri Harshad Mehta.

(g) As on date, the amount outstanding from GRAM/Shri Harshad Mehta on this account is Rs.16.25 crores for which SBI Caps carries the exposure.

(h) It may also be noted that the clients of Madras office were not included in the list of PMS clients submitted by SBI Caps, and in fact the top management appears to be ignorant regarding the activities of the Madras office in collecting and investing these funds.

5(a)The Bombay corporate office of SBI Caps has entered into the following ready forward deals for bonds for an aggregate face value of Rs.124.50 crores which are outstanding and overdue. The details are as under:

Date	Counter-party	Broker	Security & face value(Rs. in crores)	Contract amt. (Rs.in crores)	Security/ BR held
12.2.92	Canfina	Harshad Mehta	13% NPC 10.00	8.82	Security
12.2.92	Canfina	Harshad Mehta	9% IRFC 12.00	11.20	Security
10.4.92	Stanchart	Harshad Mehta	13% NPC 28.00	25.95	BR held
13.4.92	Grindlays	Harshad Mehta	17% NTPC 10.00	10.25	Security
16.4.92	Grindlays	M/s.V.B.Desai	9% CIL 5.00	4.77	Security
12.2.92	Citibank	M/s.D.S.Pur-bhoodas & Co.	13% NTPC 8.00	7.04	BR held
12.2.92	Citibank	M/s.D.S.Pur-bhoodas & Co.	13% CIL 33.50	29.11	BR held
27.2.92	Citibank	M/s.D.S.Pur-bhoodas & Co.	13% NPC 18.00	15.79	BR held

(b) There is no documentation to establish that the deals were on ready forward basis and if the counterparty does not honour the commitment claimed by SBI Caps there would be a substantial loss, estimated about Rs.7.5 crores, to SBI Caps as the present market value of the underlying securities has depreciated considerably.

6(a) There have been instances noticed where there is a post-facto execution of certain deals. The following two instances may be noted.

(i) Deal ticket No.1580 is dated 13.1.92 while deal ticket No.1578 (for reversal) is dated 14.1.92. The dealer signed deal ticket No.1580 evidencing purchase of 9% IRFC Bonds from SBI through Shri Harshad Mehta on a 1 day ready forward basis on 13 January 1992. The amount was credited by SBI to Shri Harshad Mehta's account with them. This post-facto deal was perhaps made to accommodate Shri Harshad Mehta into whose account the proceeds were credited by SBI Bombay Main branch to enable him to make payments of Rs.91.20 crores for which he was falling short by Rs.5.54 crores. The post-facto execution of the deal is proved by the fact that the said deal for Rs.6.32 crores did not find a place in the inflow/outflow statement put up to the GM/ED/MD for that day. Moreover, the entry appears after the day's total in the receipts/payments register but which was acknowledged by GM(Treasury).

(ii) Deal ticket No.1813 is dated 17.2.92 while Deal ticket No.1815 is dated 15.2.92. The deal ticket No.1813 was prepared by the back-up official (and not by the dealer) for reversing deal of 16.1.92 (deal ticket No.1601) due on 15.2.92. By not reversing the deal on 15.2.92, the earlier deal was in effect extended unauthorisedly by the back-up official. At the same time, i.e.on 15.2.92, dealer entered into a deal(vide deal ticket No.1815) with Canfina through Shri Harshad Mehta for Rs.4.20 crores which amount found its way into Shri Harshad Mehta's account at SBI. This explains why deal ticket No.1813 was extended. Far from meeting his obligation of Rs.27.48 crores to SBI Caps, Shri Harshad Mehta needed Rs.4.20 crores to meet his liabilities to others on that day. There is no broker's contract on record and the deal was not intimated to the GM/ED/MD. The action of the back-up official also entailed a loss for the company inasmuch as the deal was extended at the contracted rate of 10% while the prevailing rate on 15.2.92 charged to Shri Harshad Mehta was 21% for the Rs.4.20 crores deal.

7. There have also been instances noticed by us where BRs have been issued in lieu of earlier ones favouring counterparties with whom no deal had been struck by the company. For example, BR.No.139 favouring NHB was issued on 2 August 1991 in lieu of BR.No.138 dated 1 August 1991 favouring UCO Bank when in fact no sale had been made to NHB on that date.

XI. AllBank Finance Ltd.

AllBank Finance Limited is a wholly-owned subsidiary of Allahabad Bank. The registered office of the company is in Calcutta and it has a branch office in Bombay. The Chairman of the bank is also the Chairman of AllBank Finance Ltd. The company has not raised any public deposits. The main resources of the company are by way of inter-corporate deposits. The main assets of the company are investments in stocks and securities and loans and advances to companies. The loans are mainly by way of bridge loans to companies for whose public issues, AllBank Finance is either the lead manager or co-manager. The main broker of the company is M/s.V.B. Desai. The other broker is M/s.Baijnath Khandelwal & Bros., Calcutta.

2.(a) Besides the inter-corporate deposits, the company has also accepted an amount of Rs.10 crores from a public sector undertaking under PMS for a period of one year from July 1991 to July 1992. The company has been investing this money in various shares and bonds through the broker M/s.V.B. Desai, under ready forward deals which were for periods ranging from 20 days to about 8 months. During the period from 31 July 1991 to 31 March 1992, the company had entered into 29 ready forward deals with M/s.V.B. Desai aggregating Rs.46.82 crores.

(b) The following ready forward deals illustrate the nature of the transactions undertaken:-

Purchases

Sr. No.	Scrip	No.of shares	Purchase rate	Face valu	Date of purchase	Amount (contract value)
1.	2.	3.	4.	5.	6.	7.
1.	Jai Prakash	46,000	65.00	10.00	25.11.91	2,990,000.00
2.	Apollo Tyres	31,000	135.00	10.00	25.11.91	4,185,000.00
3.	Grasim	55,000	331.00	10.00	28.01.92	18,205,000.00

Sales

Sr. No.	Scrip	No.of shares	Sale rate	Sold on (forward)	Actual date of sale	Amount (contract rate)
1.	Jai Prakash	46,000	67.00	27.11.91	06.02.92	3,080,000.00
2.	Apollo Tyres	31,000	138.25	27.11.91	13.01.92	4,285,750.00
3.	Grasim	55,000	337.00	31.01.92	06.05.92	18,535,000.00

These deals partake of the nature of temporary accommodation to the broker for the periods till the forward transactions matured.

(c) As on 15 June 1992, seven ready forward deals in shares and bonds, for which the purchase consideration amounted to Rs.5.89 crores, and which have already become due on 21 May 1992 are outstanding. The company is likely to suffer a loss on the outstanding deals in the event the securities have to be disposed of at lower prices, or the broker is unable to provide the additional margin to cover the shortfall, and the loss is not passed on to the PSU.

3.(a) On 9 April 1992 the company raised an inter-corporate deposit of Rs.100 crores from Housing & Urban Development Corporation (HUDCO) for 46 days (repayable on 25 May 1992) at an interest rate of 21 per cent per annum. The amount of Rs.100 crores was placed at the disposalof M/s.V.B. Desai through ready forward deals. Under the deal, the bank purchased the following shares on 9 April 1992.

Particulars of shares	(Rs.in crores) Amount
60,000 ACC shares at Rs.10,000 per share	60.00
9% IRFC bonds of the face value of Rs.42 crores plus coupon interest, at Rs.92.75	39.98
Total :	99.98

The purchases were authorised by the Chairman. The proceeds of the above purchases were credited to the account of Shri Harshad Mehta with ANZ Grindlays Bank (Rs.60 crores) and his associate concern M/s. Growmore Research and Assets Management Ltd. with Standard Chartered Bank (Rs.39.98 crores)

(b) On 29 April 1992 the company entered into a sale contract for the entire lot of ACC shares at Rs.10,289.75 per share and IRFC bonds at Rs.94.2833 with the same broker viz. M/s.V.B. Desai for delivery on 25 May 1992. On 29 April 1992 the closing rate of ACC shares was Rs.6,358 per share at Bombay. However, the company has explained that since the broker was a reputed firm it would be able to take delivery of the shares at the contracted rate despite the fall in the market value of the shares. On 13 May 1992 the broker offered some additional securities of the face value of Rs.26.80 crores to cover the shortfall in the account due to the steep fall in the prices of the shares. The broker also deposited 1,17,500 shares of M/s.V.B. Desai Financial Services on 6 June 1992.

(c) On 21 May 1992 the broker approached the company with a request to extend the validity period of the sale contract by 30 days, i.e payment by 25 June 1992. On 26 May 1992 the Chairman agreed to extend the period by 15 days, and the broker was to pay interest for the overdue period at 24 per cent per annum. Further, to enable the broker to take delivery of the IRFC bonds to the extent of Rs.40 crores, the company purchased these bonds on 3 June 1992, at the price of Rs.94.20 from the broker and took them in its portfolio as cover for funds amounting to Rs.39.79 crores mobilised from Oil Industries Development Board (OIDB) for a period of one year under PMS. As a result of this transaction OIDB has been put at risk for any loss which may occur on subsequent realisation of the bonds.

(d) On the due date for repayment of the funds obtained from HUDCO i.e, 25 May 1992, the company arranged for payment of the deposit together with interest at Rs.102.72 crores by raising other inter-corporate deposits to the extent of Rs.54.58 crores from other clients and taking a loan of Rs.46 crores from Allahabad Bank at 19 per cent, the balance amount of Rs.2.14 crores being from its own funds. In effect, therefore, since the obligation under the sale contract could not be met, by the broker M/s.V.B. Desai, the company had to repay the deposit of HUDCO by obtaining fresh deposits from other clients and a loan from the parent bank which itself had continuously borrowed from the inter-bank market.

(e) The company has released 25,000 shares of ACC to the broker at Rs.4000 as part payment of its contract on 1 June 1992 and received payment of Rs.10 crores therefor (as against the contracted price of Rs.10,289.75). The company has released on 9 June 1992 a further lot of 1450 ACC shares at Rs.4800 along with some other shares lodged as additional security, for an aggregate payment of Rs.1.38 crores. The company has reported that it has not so far been able to realise two post-dated cheques bearing the date 15 June 1992 for a total value of Rs.14.19 crores lodged by the broker on 9 June 1992, for purchase of further 10,000 ACC shares at Rs.4000 and 15,000 ACC shares at Rs.4100 as also certain other shares, due to suspension of business on the Bombay Stock Exchange and the legal problems relating to delivery of shares by the broker. Thus, the company has so far been able to realise only an amount of Rs.11.38 crores leaving a balance before considering interest, of about Rs.49 crores. Even if the company is able to realise the amount of Rs.14.19 crores for the post-dated cheques held by it and sell the shares remaining with it, there would still remain a deficit without considering interest, of between Rs.9 crores and Rs.10 crores. The company is reportedly trying to obtain further securities from the broker to cover the margin in the value of the security cover held by it including the overdue interest at 24 per cent and the loss incurred in the sale of ACC and other shares at the prevailing low prices. The extent of loss that the company may eventually suffer will depend on the actual prices at which it is able to dispose of the shares presently held by it as also the additional shares, if any, lodged by the broker, after the legal difficulties relating to delivery are resolved.

XII. General

1. The inspecting officers of the RBI have completed a preliminary examination of most of the banks/financial institutions and their interim findings are under consideration of the Committee. On the basis of these findings, the areas for more detailed investigation are being identified.

2. The Committee has also noted that simultaneous investigations are in progress by the Central Bureau of Investigation (CBI) and the Income Tax Department and the RBI has appointed special auditors to examine certain transactions in a number of banks/financial institutions. Internal investigations are also in progress in certain banks/financial institutions.

3. The Committee is continuing its investigations and will submit a further report.

R.Janakiraman
Chairman

Y.H. Malegam **V.G. Hegde**

C.P. Ramaswami **E.N. Renison**

Vimala Visvanathan
Member-Secretary

BOMBAY
5 July 1992.

Third Interim Report

August 1992

I. Introductory

The Committee has submitted two Reports dated 31 May 1992 and 5 July 1992 to the Governor, Reserve Bank of India, based on its examination of the securities transactions of certain banks and findings which could be derived therefrom. This Report is based on the scrutiny made to date by the officials of the Reserve Bank of India in respect of the under-mentioned banks and deals with a few other general matters.

1. Citibank
2. Bank of America
3. Andhra Bank
4. Bank of Karad Ltd. (in liquidation)
5. Metropolitan Co-operative Bank Ltd. (in liquidation)
6. Syndicate Bank
7. Bombay Mercantile Co-operative Bank Ltd.
8. Nedungadi Bank Ltd.

II. Findings

In its second Report, the Committee had reported that over 20 per cent in number and thirty per cent in value of the securities transactions reported by banks/institutions cannot be matched. On a further scrutiny, the possible reasons for the mismatch have been ascertained and are detailed in Chapter III of this Report.

It needs to be clarified that since the transactions as reported tally in totality, there does not appear to be any case where the transactions reported by one bank/institution are not responded by some other bank/institution, though as explained in Chapter III, the actual counterparty bank/institution responding to a transaction may be different from the bank/counterparty as reported.

2. As mentioned in the second Report, there are a number of transactions where purchases and sales have been booked by banks/institutions at what appear to be artificial rates and differences running into crores of rupees have accrued to the accounts of brokers. No satisfactory explanation has been given as to why these huge losses have been borne by the brokers or such huge gains to brokers have been allowed to accrue. It is possible that these losses and gains are compensatory adjustments for other transactions or that the banks/institutions had informal arrangements with brokers whereby the brokers guaranteed to the banks/institutions a specified rate of return on funds deployed through them. A pattern also seems to be emerging in respect of several of the banks referred to in this Report whereby these large differences have occurred in transactions when certain brokers, particularly broker Hiten P. Dalal, are involved and where the ultimate payment for the difference has come out of broker Abhay D. Narottam's account with the Bank of Karad Ltd. This account appears to have been funded by BRs issued by Bank of Karad Ltd. and Metropolitan Co-operative Bank Ltd., not supported by the existence of securities. These transactions and the links between these brokers need further examination.

3. In the second Report the Committee had reported upon the practice of banks/institutions issuing their own SGL forms against SGL forms brought by brokers and charging a fee for these services. This has been confirmed by further scrutiny, particularly in respect of the Bank of Karad Ltd. and Andhra Bank.

4. Data collected from banks/institutions (data from all banks/institutions have not yet been submitted) show that as at 30 June 1992, the total book value of PSU bonds held by the banks/institutions on their own account and on behalf of PMS clients aggregated to Rs.8521 crores which represents over 40% of the total issue of such bonds by PSUs. The aggregate carrying cost of these bonds as reported by the banks/institutions is Rs.7794 crores on "own account" and Rs.727 crores on "PMS account". The market value of the bonds has not been computed but even on the basis of a minimum estimated difference between acquisition cost and market value, of 10 per cent, the shortfall can be about Rs.780 crores in respect of "own" investments and about Rs.73 crores on "PMS account".

5. Part of the shortfall referred to in paragraph 4 above arises from the manner in which "ready forward" transactions are accounted. When a security or Unit or bond is sold under a ready forward deal, the seller credits its investment account with the contract price and books a profit or loss in relation to its holding cost. The purchaser debits its investment account at the contract price. When the reversal is

effected, the original seller repurchases the security or Unit or bond at a price which is higher (to reflect the interest for the period of the deal, the ready forward transaction being in essence a financing arrangement) than the original sale price and debits the repurchase price to its investment account. The carrying cost of the original seller is, therefore, increased by the interest element involved in the deal. However, for the purchaser, the difference between the original purchase price and the resale price is a gain which is reflected in the profit and loss account. Thus, in what is essentially a financing transaction, the original purchaser books an income but the original seller adds the amount to the carrying cost of the investment and does not book the expense. If all investments were to be marked down to market at the year-end, the excess carrying cost would automatically get adjusted. But unfortunately this is not done by all banks and even when this is done, some banks do not mark down PSU bonds and Units on the argument that these are not quoted. The situation is aggravated when the original sale is made not at the market price but at an artificial price. There is, therefore, a risk that ready forward transactions, especially in PSU bonds and Units, may have been used as a device to artificially increase the carrying cost of investments and thereby book profits on initial sale or to avoid debiting to the profit and loss account the expense for the use of funds during the period of the ready-forward transaction.

Portfolio Management and Similar Schemes

6. Banks and their merchant banking subsidiaries were permitted to offer portfolio/fund management services (PMS) in accordance with guidelines issued by RBI in May 1989. These guidelines provided that :

(a) the services were to be provided at the customer's risk, without guaranteeing a pre-determined return;

(b) the services were to be provided to parties in respect of their long term investible funds;

(c) the minimum period for which funds were placed by clients should be one year;

(d) the transactions should be booked at market rates only; and

(e) proper accounting and documentation had to be ensured.

7. In January 1991, these guidelines were further amplified to provide, inter alia, that -

(a) funds accepted for portfolio management should not be entrusted to another bank for management;

(b) a definite fee was to be charged for such services independent of the return to the client;

(c) the funds were expected to be deployed essentially in capital market instruments such as shares, debentures, bonds, securities, etc. and were not to be employed for lending in call money/bill market and lending to/placement with corporate bodies;

(d) transactions between the bank's investment account and portfolio account were to be strictly at market rates;

(e) while putting through transactions on behalf of a portfolio account, a clear indication had to be given that the transactions pertained to the "portfolio account";

(f) the undeployed funds had to be treated as outside borrowings of the bank and CRR/SLR had to be maintained on such funds; and

(g) the bank's liability to its clients in respect of funds accepted for portfolio management had to be properly reflected in the published accounts.

8. In June 1992, as recommended by the Committee in its first Report, RBI has advised banks that PMS clients' accounts should be subjected to a separate audit by external auditors.

9. Large sums of money have been received by the banks and their subsidiaries under the portfolio management schemes. The details of investments made in PSU bonds, corporate shares/ debentures and Units of UTI/Mutual Funds under the scheme as at 30 June 1992 (i.e. excluding undeployed funds) as reported by banks are summarised below :

	PSU Bonds	Shares/Debentures of corporate bodies	Units of UTI and Mutual Funds	(Rs.in crores) Total
SBI Group	18.64	-	4.75	23.39
Nationalised Banks	35.52	404.96	20.35	460.83
Private Sector Banks	0.45	0.27	-	0.72
Foreign Banks	415.70	499.28	471.41	1386.39
Subsidiaries of banks	256.68	201.19	-	457.87
	726.99	1105.70	496.51	2329.20

10. While the above table reflects the position as at 30 June 1992, it is possible that the funds received and invested earlier by subsidiaries of nationalised banks were larger because after the irregularities in the security transactions of banks were detected, a few nationalised banks have purchased substantial amounts of investments made on behalf of PMS clients from their respective subsidiaries. Also, some of the clients are likely to have withdrawn their funds placed under PMS with banks, including foreign banks.

11. As at 30 June 1992, only three banks/institutions accounted for almost 90% of the total investments made out of the funds deployed under the portfolio management schemes as shown below :

Bank/Institution	Amount of investment (Rs. in crores)	% to total
Citibank	1298.12	55.73
Canfina	443.47	19.04
Syndicate Bank	337.34	14.48
	2078.93	89.25

12. As conceived, the portfolio management scheme was intended to provide an opportunity to corporate clients to deploy their long-term investible funds in capital market instruments such as shares, debentures, bonds, securities, etc. and the risk on such investments was to be borne by the clients. In practice however, the scheme appears to have been operated as a "deposit substitute" by banks and clients. While the banks have in their documentation broadly followed the lines of the scheme as envisaged, in practice they appear to have represented to the clients that the funds placed under the scheme would be deposits which enjoyed a higher rate of return than permitted for normal deposits, and a rate of return was indicated, though not guaranteed. Some of the transactions noticed by the Committee and detailed in other chapters of this Report also support the suspicion that artificial rates were used for transactions to ensure that the returns to the client approximate to the indicated rates. The clients' perception of the PMS and other schemes referred to later also seems to support the suspicion that they considered the funds placed under the schemes merely as deployment of short-term funds with banks in the nature of bank deposits enjoying a higher rate of interest and not subject to any risk.

13. The PMS funds had to be placed by the client for a minimum period of one year. As the funds placed by many clients were essentially in the nature of short-term funds, other schemes appear to have been devised by banks to get over this restriction. Thus, several banks have been offering facilities to clients for ready forward transactions whereby securities, bonds and Units are sold to clients on a ready basis and repurchased after the specified period at a pre-determined rate which assured to the client a guaranteed rate of return with no risk. An indication of the magnitude of the funds collected under these schemes is ascertainable from the fact that between 1 April 1991 and 31 May 1992 Citibank entered into ready forward transactions (with parties which had placed funds of an amount of over Rs.5 crores) for an aggregate value of Rs.5972 crores (i.e.an average of Rs.427 crores per month) and Bank of America entered into transactions for an aggregate value of Rs.6954 crores including about 10 per cent on outright basis (i.e. an average of Rs.447 crores per month). Standard Chartered Bank operated a similar scheme styled Corporate Cash Deployment Services and the funds

March 1992 at its Bombay branch alone are estimated to have been around Rs.700 crores.

14. The ready forward transactions entered into by the banks with their clients, particularly in respect of bonds and Units, were clearly in contravention of the RBI guidelines in that regard. It has been argued by Citibank that there was no violation since these transactions were through PMS funds kept by clients and the RBI restrictions on ready forward transactions did not apply to PMS funds. This is a matter which needs to be examined but it does illustrate the dangers involved in the use of PMS funds to bypass RBI guidelines in general. In many cases of ready forward transactions with clients, there is an absence of documentation which suggests that this was only a form used to accept what were in substance deposits.

15. The question of risk to the client also assumes importance in the light of the general fall in realisable values of PSU bonds and shares. As at 30 June 1992, on the basis of returns submitted by banks/institutions to date, the aggregate realisable value of the investments held under portfolio management schemes as estimated by banks is lower than the acquisition cost of the investments by over Rs.100 crores.

16. The Committee has in its second Report (paragraph II.9.[iv]) referred to the need to examine whether under the portfolio management scheme statutory provisions are violated by the clients or the banks/institutions.

17. The guidelines issued by the RBI in January 1991 prescribe that the undeployed funds are to be treated as outside borrowings and CRR/SLR have to be maintained on such funds. However, as the bank is only an agent for the management of these funds, the undeployed funds are held in trust and should not form part of the liabilities or assets of the bank. To treat them otherwise would mean that undeployed funds while increasing the deposits for calculation of CRR/SLR would also increase the cash and bank balances of banks and provide in fact a surplus of cash and bank balances which could be used by banks to meet CRR/SLR requirements on other deposits. In fact there would be an incentive to temporarily liquidate the PMS investments on reporting Fridays to achieve this result.

18. The magnitude of the funds received by banks and institutions from their clients, and the manner in which these funds have been deployed suggest that these funds have had a role to play in financing brokers through ready forward deals. There is also a possibility that in many cases, brokers may have been instrumental in obtaining these funds, particularly from PSUs, mainly motivated by the expectation that the funds would in turn be made available to them by the banks/institutions.

III. Securities transactions in the banking system - Statistical analysis

In the second Report the Committee had summarised the results of a study of details of securities transactions undertaken by banks during the period from 1 April 1991 to 23 May 1992 as submitted by banks/institutions up to the date of that report. Details have been received from some more banks/institutions and the updated figures are given in subsequent paragraphs.

2. The aggregate value of transactions is as under:

	Aggregate face value (Rs.in crores)	Percentage
Ready forward	632,944	51.64
Outright	76,603	6.25
Others	516,175	42.11
	1225,722	100.00

3. The analysis of the above transactions by nature of securities is as under :

	No.of transactions	Aggregate face value (Rs.in crores)	Percentage
Government securities	30,135	5,98,123	48.80
PSU Bonds	32,541	4,54,702	37.10
Units	11,072	1,49,399	12.19
Others	5,773	23,498	1.91
	79,521	12,25,722	100.00

4. The broker-wise analysis of the transactions is as under :

Name of Broker	No.of transactions	Aggregate face value (Rs.in crores)	Percentage
Direct	24,612	463,044	37.78
H.P. Dalal	3,282	75,151	6.13
Bhupen Champaklal Devidas	3,019	67,170	5.48
Harshad Mehta	2,151	61,318	5.00
Somayajulu & Co.	1,778	43,954	3.59
V.B. Desai & Associates	2,339	37,653	3.07
N.K.Aggarwal & Co.	1,487	34,044	2.78
Batliwala & Karani	1,998	29,388	2.40
C.Mackertich	707	18,279	1.49
Darashaw	1,098	17,470	1.42
Asit C. Mehta	703	12,762	1.04
Excel & Co.	729	8,900	0.73
G.N. Hegde	620	8,290	0.68
A.D.Narottam	575	7,519	0.61
Mukesh Babu	543	6,214	0.51
Others (below Rs.5,000 crores)	33,880	3,34,566	27.29
Total	79,521	12,25,722	100.00

5. A bank-wise analysis of the transactions is as under :

Name of the bank	Aggregate face value (Rs.in crores)	Percentage
Citibank	215,179	17.55
Standard Chartered Bank	167,014	13.63
Bank of America	151,646	12.37
Canfina	90,282	7.37
ANZ Grindlays Bank	79,497	6.49
American Express	69,191	5.64
State Bank of India	54,343	4.43
Andhra Bank	42,135	3.44
SBI Caps	32,971	2.69
UCO Bank	28,906	2.36
Canara Bank	27,879	2.27
Bank of Madura Ltd.	25,729	2.10
Canbank Mutual Fund	24,223	1.98
Punjab National Bank	20,877	1.70
National Housing Bank	20,582	1.68
Others (below Rs.20,000 crores)	1,75,268	14.30
	12,25,722	100.00

6. An analysis of transactions on "own account" and on behalf of PMS clients and others is given below.

On account of	No.of transactions	Aggregate face value (Rs.in crores)	Percentage
Own account	47,616	8,53,368	69.62
PMS Clients	27,494	3,15,400	25.73
Others including brokers	4,411	56,954	4.65
	79,521	12,25,722	100.00

7. A further analysis of transactions on behalf of PMS clients and others by major banks is given below :

Name of the bank/ institution	On behalf of PMS clients			On behalf of others		
	No.of trans-actions	Amount (Rs.in crores)	Per-centage	No.of trans-actions	Amount (Rs.in crores)	Per-centage
Citibank	21682	213983	67.84	-	-	-
Canfina	4242	90282	28.63	-	-	-
UCO Bank	486	7459	2.36	-	-	-
ANZ Grindlays Bank	466	2082	0.66	-	-	-
Andhra Bank	-	-	-	1142	26449	46.44
Bank of Karad Ltd.	-	-	-	1671	15423	27.08
Bank of Madura Ltd.	-	-	-	726	7256	12.74
ABFSL	-	-	-	661	5541	9.73
Others	618	1594	0.51	211	2285	4.01
Total	27494	315400	100.00	4411	56954	100.00

8. After a matching of the transactions reported by banks/ institutions after the submission of the second Report, the details of mismatched transactions are as under :

Nature of transaction	Number	Aggregate face value (Rs. in crores)
Purchases	11,918	252,055.16
Sales	12,499	252,739.78

9. The following appear to be the general reasons for the mismatch :

(a) Some of the transactions have been booked individually by one bank/institution but collectively by the counterparty bank/institution.

(b) Some of the transactions have been booked by one bank/institution on one date but by the counterparty bank/institution on the succeeding or preceding day.

(c) Some of the reporting banks have reported the transactions on the date on which the contract was concluded but the counterparty may have reported the transaction on the date on which it was executed.

(d) There may be reporting errors, either by omission or mis-statements of the nature of the security or of the amount.

(e) There are cases where the bank has dealt through brokers and is not aware of the name of the counterparty bank but has shown the name of the bank from which payment was received.

(f) In a large number of cases, the counterparty is shown as a bank whereas the actual counterparty is a broker who is a client of the counterparty bank. For example, in Andhra Bank alone, the value of such contracts is estimated at Rs.26,450 crores.

(g) In a large number of cases, it appears that the name of the counterparty bank/institution given in the transaction is fictitious. This appears to have been done with a view to hide a ready forward transaction in Units or PSU bonds since such a transaction was not permitted under RBI guidelines. Therefore for one leg of the transaction the correct name of the counterparty bank/institution is given but the reverse transaction is booked in the name of a fictitious counterparty and prior to the reverse transaction being completed, the name of the correct counterparty is inserted in the records and the transaction booked with it.

10. The details given in paragraph 8 above show that the mismatched purchases and sales substantially tally and that the sales reported tallied with the purchases reported. This suggests that the mismatched transactions mainly represent transactions where a transaction is responded by a bank/ institution other than the bank/institution shown by the reporting bank/institution.

IV. Citibank

Citibank is one of the major participants in the securities market. During the period from 1 April 1991 to 23 May 1992, the total face value of transactions entered into by the bank aggregated to Rs.215,179.92 crores representing as much as 17.55 per cent of the total face value of transactions entered into by the reporting banks. Of these, "own" investment transactions formed a very small proportion and the bulk of the transactions were on behalf of PMS clients. The main brokers through whom the transactions were effected were Hiten P. Dalal, C.Mackertich and Stewart & Co. A number of transactions were with the Bank of Karad Ltd. and in the books of the latter bank the transactions have been recorded in the account of broker A.D. Narottam. During the period from 1 April 1991 to 30 June 1992, the amounts debited and credited in this account in respect of transactions with Citibank aggregated to Rs.1139 crores and Rs.908 crores respectively.

2.(a) The bank has not complied with certain provisions contained in RBI letter DBOD.No.FSC.46/ C.469-91/92 dated 26 July 1991. For instance the bank issued BRs even where SGL facility is available. It has accepted BRs from other banks which were not in the prescribed format. It has received a single BR covering various State loans; it has not issued BRs on security paper, it has issued BRs signed by only one signatory, many BRs received by the bank were not signed by two authorised signatories, and it had not maintained proper record to verify the signatures of the issuing bank's officials. BRs were not exchanged by the bank within 90 days in several cases. BRs received by the bank were not renewed and no reasons were mentioned in the BR for delay by the issuing bank. Although, accounting entries were passed on the same day in the books, entries relating to exchange of BRs against SGL transfer forms and vice-versa are not recorded promptly in the Computer system.

(b) In a number of cases, the SGL transfer forms issued by Citibank have bounced. In all cases, noticed by the Committee, dishonour of SGL transfer forms issued by Citibank is a result of the dishonour of SGL transfer forms received from other banks, particularly Standard Chartered Bank, which have bounced when lodged with the PDO. In a number of cases SGL transfer forms received from other banks, particularly SBI, have not been lodged with the PDO but have been returned on reversal of the ready forward transactions. There are also a number of cases where BRs have been issued for Government of India securities and SGL transfer forms have not been issued thereagainst, but BRs have been exchanged on the reversal of the ready forward transactions.

3. Citibank is holding 2 BRs dated 30 March 1991 of an aggregate face value of Rs.17.10 crores issued by SBI which have been confirmed by SBI but the securities have not been received. Citibank is also holding 8 BRs of an aggregate face value of Rs.93.57 crores, issued by Standard Chartered Bank which have been confirmed by the latter bank but securities have not been delivered. In turn Citibank has issued 10 BRs of an aggregate face value of Rs.175.70 crores to Standard Chartered Bank for which it has not effected delivery of scrips.

4.(a) The Committee has in its second Report (paragraph VIII - 4[d]) referred to certain transactions between Citibank and Canfina. As shown therein :-

(i) As per Canfina books, it sold to Citibank on 20 January 1992, five lots of PSU bonds of an aggregate face value of Rs.30.62 crores for which the contracted value (as per dealer's pad) was Rs.31.13 crores but for which it received payment from Citibank for only Rs.25.77 crores and the balance of Rs.5.36 crores was recovered from the broker Hiten P. Dalal. The sales as recorded in Citibank books are at the rate at which it made payment.

(ii) As per Canfina books, it sold to Citibank on 6 February 1992, six lots of PSU bonds and other debentures of an aggregate face value of Rs.78.83 crores for which the contracted value (as per dealer's pad) was Rs.82.85 crores but for which it received payment from Citibank for only Rs.59.93 crores and the balance of Rs.22.92 crores was recovered from the broker Hiten P. Dalal. The purchases as recorded in Citibank books are only for five lots of an aggregate face value of Rs.75.30 crores at rates which are different from the rates recorded by Canfina though the aggregate value (Rs.59.90 crores) approximates to the value recorded by Canfina. Moreover, the counterparty for the purchase is recorded as broker C.Mackertich and not Canfina.

(b) Some of the scrips acquired by Citibank on 6 February 1992 from C.Mackertich have been sold back to Canbank Mutual Fund on 11 February 1992 at rates which are considerably higher than the rates at which the scrips were acquired.

(c) The different rates used for the transaction of 6 February 1992 and the subsequent sale by Citibank on 11 February 1992 are tabulated below :

Security	Face value (Rs.in crores)	Contracted Rate as per Canfina Rs.	Actual Rate as per Canfina Rs.	Actual Rate as per Citibank Rs.	Sale Rate of Citibank Rs.
14% Godrej Soaps NCD	5.00	95.67	65.00	72.50	84.00
14% INSILCO NCD	5.00	99.3210	62.50	72.50	84.00
	5.30	99.3210	62.50	72.50	
13% COAL INDIA LTD.	0.00	99.4465	71.50	74.50	
	15.00	99.5733	71.50	74.50	
14% HARYANA PETRO NCD	5.00	99.3364	65.00	72.50	84.00
15% INDIAN RAYON	3.53	105.6598	92.00		

(d) In respect of its purchases, Citibank does not hold delivery orders and in respect of its sales it does not hold contract notes and delivery orders.

(e) Thus there are large differences between (i) the rates recorded in the Canfina dealer's pad and the rate at which the sale is recorded by Canfina (ii) the rate at which the sale is recorded by Canfina and the rate at which the purchase is recorded by Citibank (iii) the rate at which subsequent sale has been made by Citibank. In view of these differences and in view of the absence of contract notes and delivery orders and the fact that in the books of Citibank the purchase is recorded as a purchase from C.Mackertich and not Canfina and the subsequent sale is to Canbank Mutual Fund, the rationale for these transactions as recorded in the books of Canfina and Citibank is open to question.

5.(a) There are a number of other transactions between Citibank and other banks, mostly through broker Hiten P. Dalal and involving the account of broker A.D. Narottam in Bank of Karad Ltd. where large differences have been paid by brokers. Some of these are given in the following paragraphs.

(b) (i) On 29 October 1991, Citibank sold 9% IRFC bonds of face value Rs.25 crores to Bank of Karad Ltd. @Rs.97.25 who sold it on the same day to Standard Chartered Bank @Rs.90.00 thus making a loss of Rs.1.8125 crores.

(ii) On 31 October 1991, Citibank sold 9% IRFC bonds of face value Rs.350 crores @Rs.101 to Bank of Karad Ltd. which issued a banker's cheque for Rs.356.09 crores by debit to overdraft account of A.D. Narottam, who funded the same by sale to Canfina of Bank of Karad Ltd.'s BR No.3462 issued against BR No.015 obtained "free" from Metropolitan Co-operative Bank Ltd. Bank of Karad Ltd. resold the said securities on the same day Rs.150 crores to Citibank @Rs.94, Rs.150 crores to Citibank @Rs.90 and Rs.50 crores to Standard Chartered Bank @Rs.95. The resales to Citibank were only routing transactions as Citibank in turn sold the bonds at the request of Bank of Karad Ltd. through broker Hiten P. Dalal to Bank of America and ANZ Grindlays Bank @Rs.90 and Rs.94 respectively. The loss suffered by Bank of Karad Ltd. in this transaction is Rs.30 crores.

(iii) All the above transactions are recorded in the books of Bank of Karad Ltd. in the account of broker A.D. Narottam and therefore the loss of Rs.31.8125 crores is borne by him.

(iv) It may be noted that for the above transactions. Citibank had, at the time of initial sale, issued BRs which it received back at the time of repurchase. For subsequent sale to Bank of America, it issued BRs which it claimed "were subsequently liquidated against physical delivery of bonds". However, on a further scrutiny at Bank of America and ANZ Grindlays Bank it was seen that in fact no bonds were delivered to Bank of America but BRs were exchanged and in respect of ANZ Grindlays Bank delivery of bonds was only for Rs.65 crores and the balance was against exchange of BRs. There are also no sale contracts between Bank of Karad Ltd. on the one hand and Bank of America and ANZ Grindlays Bank on the other.

(v) Citibank does not hold contract notes and delivery orders in respect of its Rs.350 crores contract with Bank of Karad Ltd.

(c)(i) On 1 June 1991, Citibank entered into a sale contract with Bank of America for sale of 11.5% GOI loan 2010 of the face value of Rs.107 crores at a price, net of brokerage of Rs.100.95 (brokerage being Rs.0.05). The broker was Hiten P. Dalal and the transaction was on behalf of Citibank's fiduciary clients. Therefore an amount of Rs.112.44 crores was the sale proceeds as recorded in Citibank's books.

(ii) In the books of Bank of America, the purchase is recorded at a rate of Rs.98.15 and accordingly it made payment of Rs.109.39 crores.

(iii) The difference of Rs.3.05 crores was received by Citibank from Bank of Karad Ltd. and in the latter bank the amount was debited to the account of broker A.D. Narottam. Bank of Karad Ltd. holds A.D. Narottam's memo instructing it to issue "cheque favouring Citibank for Rs.304,95,000 with a memo on them to adjust this amount towards difference on 107 crores 11.50% 2010 a/c. Hiten P. Dalal". Citibank has claimed that the cheque from Bank of Karad Ltd. was sent by Bank of America but Bank of America has stated that it did not pass on any additional amount to

Citibank other than its own cheque for Rs.109.39 crores.

(d)(i) On 14 December 1991, Citibank entered into a contract through broker Hiten P.Dalal for the sale of 11.5% GOI loan 2010 of face value of Rs.20 crores @Rs.94.82 to Bank of America. Therefore an amount of Rs.18.98 crores was the sale proceeds as recorded in Citibank's books.

(ii) In the books of Bank of America, the purchase is recorded at a rate of Rs.94.5218 through broker N.K. Aggarwal & Co. and accordingly it made payment of Rs.18.92 crores.

(iii) The difference of Rs.0.06 crore was received by Citibank from broker Bimal S. Gandhi even though he is not connected with the transaction.

(e) There is no satisfactory explanation as to why in the above transactions there should be differences in the rates recorded by Citibank and the rates recorded by the counterparty banks and why the large differences should be borne by the broker. It is also seen that all the transactions are through the broker Hiten P. Dalal but the losses are in most cases paid out of broker A.D. Narottam's account with the Bank of Karad Ltd. This raises a suspicion that there was an arrangement whereby the broker Hiten P. Dalal had underwritten the securities transactions of the bank in some manner or that there was some other consideration for these payments. The fact that the losses were in most cases funded out of broker A.D. Narottam's account in the Bank of Karad Ltd. clearly establishes a link between the two brokers, Hiten P. Dalal and A.D. Narottam.

6(a) On 10 April 1992, Citibank purchased from ANZ Grindlays Bank on behalf of its fiduciary clients 15 lakh equity shares of Reliance Industries Ltd. @Rs.400 through broker Hiten P. Dalal. The above transaction is not recorded in the books of ANZ Grindlays Bank but the cheque for Rs.60 crores issued by Citibank has been credited to the account of broker Harshad S. Mehta in ANZ Grindlays Bank.

(b) On 13 April 1992, Citibank sold the shares at the identical price of Rs.400 per share to broker Hiten P. Dalal. On the same day, it also purchased 150 lakhs units of Cantriple @Rs.50 per unit from broker Hiten P. Dalal and made a net payment to broker Hiten P. Dalal of Rs.15 crores.

(c) The purchase and resale of the Reliance shares appears to be an accommodation of Rs.60 crores for three days to broker Harshad S. Mehta to settle part of his dues to the State Bank of India.

7.(a)(i) On 8 April 1992, Citibank sold on behalf of its fiduciary clients, GIC Rise II units of the face value of Rs.25 crores @Rs.10.60 per unit to broker Stewart & Co. for Rs.26.50 crores. On the next day, Stewart & Co. sold the said units to Canfina @Rs.16.20 per unit for Rs.40.50 crores, thereby making a profit of Rs.14 crores.

(ii) On 11 April 1992, Citibank sold on behalf of its fiduciary clients, GIC Rise I units of the face value of Rs.28.55 crores @Rs.12.00 per unit to broker Stewart & Co. for Rs.34.26 crores. On the same day, Stewart & Co. sold the said units of the face value of Rs.25 crores to Canfina @Rs.18.95 per unit for Rs.47.38 crores, thereby making a profit of Rs.17.38 crores.

(b)(i) On 8 April 1992, Citibank sold on behalf of its fiduciary clients, GIC Rise II units of the face value of Rs.25 crores @Rs.10.60 per unit to broker C.Mackertich for Rs.26.50 crores. On the next day C.Mackertich sold the units to Canfina @Rs.16.20 per unit for Rs.40.50 crores, thereby making a profit of Rs.14 crores.

(ii) On 11 April 1992, Citibank sold on behalf of its fiduciary clients, GIC Rise I units of the face value of Rs.28.55 crores @Rs.12.00 per unit to broker C.Mackertich for Rs.34.26 crores. On the same day, C.Mackertich sold the said units of the face value of Rs.25 crores to Canfina @Rs.18.95 per unit for Rs.47.38 crores, thus making a profit of Rs.17.38 crores.

(iii) On 20 April 1992, Citibank sold on behalf of its fiduciary clients, GIC Rise II units of the face value of Rs.25 crores @Rs.10.60 per unit to broker C.Mackertich for Rs.26.50 crores. On the same day C.Mackertich sold the units to Canfina @Rs.20.00 per unit for Rs.50 crores, thus making a profit of Rs.23.50 crores.

(c) Therefore without any investment of funds the brokers, Stewart & Co. and C.Mackertich made a profit of Rs.31.38 crores and Rs.54.88 crores respectively.

(d) The GIC Rise I units of face value Rs.28.55 crores each sold by Citibank to Stewart & Co. and C.Mackertich respectively on 11 April 1992 and in turn sold (face value Rs.25 crores each) by these brokers again to Canfina on the same day were in fact purchased by Citibank from Canfina on 10 April 1992 @Rs.12.02 per unit. Therefore, Canfina sold units of the face value Rs.57.10 crores on 10 April 1992 @Rs.12.02 to Citibank and repurchased Rs.50 crores of the same units @Rs.18.95 per unit on the next day and in the process gave a profit of Rs.34.65 crores to the brokers.

(e) For all the above transactions, there are no contract notes or delivery orders available on the bank's records.

(f) Canfina has in turn sold the units to ANZ Grindlays Bank at a small difference of Re.0.05 per unit.

(g) There is no satisfactory explanation as to why there should be this large difference between the rates at which the units were sold by Citibank and the rates at which the purchases were ultimately made by ANZ Grindlays Bank. In this connection it needs to be noted that in respect of GIC Rise II, Citibank sold units of the face value of Rs.25 crores on 20 April 1992 @Rs.10.60 per unit when GIC Rise II units were sold by C.Mackertich on the same day to Canfina @Rs.20 per unit. There is also no satisfactory explanation as to why Canfina sold GIC Rise I units on 10 April 1992 @Rs.12.02 per unit and repurchased them the next day @Rs.18.95 per unit.

(h) The series of transactions clearly suggest that artificial securities transactions have been effected to make a compensatory payment to the broker. In the process, if any loss is suffered by Citibank, it has been at the cost of the fiduciary clients, whose best interest the bank was required to protect. The matter therefore needs further investigation.

8.(a) On 31 March 1992, Citibank entered into sale contracts with broker Hiten P. Dalal for sale of shares and debentures on behalf of fiduciary clients for an aggregate value of Rs.130.40 crores and received a bankers' cheque from Bank of Karad Ltd. for Rs.132.61 crores.

(b) In the books of Bank of Karad Ltd., this amount was debited in the account of broker A.D. Narottam and was funded by an identical amount received from Standard Chartered Bank.

(c) On 2 April 1992, Citibank refunded the excess amount of Rs.2.21 crores received from Bank of Karad Ltd. which was credited to the account of A.D. Narottam in Bank of Karad Ltd. books.

(d) On 3 April 1992, Citibank reversed the above deal and entered into identical contracts, value dated 31 March 1992 with Bank of Karad Ltd.

(e) Citibank issued BRs for an aggregate value of Rs.51.91 crores and has stated that it effected physical delivery for the balance but copies of delivery letters addressed to broker Hiten P. Dalal are not available for securities having an aggregate value of Rs.39.34 crores.

(f) On 3 April 1992, Citibank repurchased the securities by issue of a cheque for Rs.131.41 crores which was credited to A.D. Narottam's account in Bank of Karad Ltd. and out of which proceeds, payment was made to Standard Chartered Bank, covering certain security deals.

(g) There are no contract notes issued for this transaction, nor are they reflected in A.D. Narottam's investment ledger maintained by Bank of Karad Ltd.

(h) It appears this is a pure financing transaction on 31 March 1992 whereby funds have been obtained by Citibank from its broker Hiten P. Dalal but which has been recorded as a securities transaction with Bank of Karad Ltd.

9. There are a number of transactions recorded by Citibank as securities transactions but where there is no evidence of movement of securities and broker's contract notes and delivery orders are not available. Even if these are accepted as securities transactions, these would be in the nature of ready forward deals in

PSU bonds in contravention of RBI guidelines. A few illustrations are given below :

(a) On 22 July 1991, Citibank entered into contracts with Bank of Karad Ltd. for sale of 9% HUDCO Bonds for Rs.68.28 crores and Rs.35.17 crores through brokers M/s.V.B. Desai and Hiten P. Dalal and issued BRs in respect thereof. In Bank of Karad Ltd. these amounts were funded by the broker A. D. Narottam by sale of 16 crore Units costing Rs.212.80 crores to Canfina. On 25 July 1991 these sales were reversed for Rs.103.53 crores and BRs received back. The debits and credits for the payment and receipt are recorded in the Bank of Karad Ltd. in the account of broker A.D. Narottam.

(b) On 31 July 1991, Citibank entered into sale contracts with Bank of Karad Ltd. for sale of 9% HUDCO bonds and 9% IRFC bonds for an aggregate value of Rs.52 crores through broker Hiten P. Dalal and issued BRs in respect thereof. In Bank of Karad Ltd. this amount was funded by the broker A. D. Narottam by sale of 19 crore Units costing Rs.255.44 crores to Canfina. On 14 August 1991, these sales were reversed for Rs.51.67 crores and BRs received back. The debits and credits for the payment and receipt are recorded in the Bank of Karad Ltd. in the account of broker A.D. Narottam.

(c) There are the following transactions for sales and repurchases of 9% HUDCO bonds with Bank of Karad Ltd.

Face (Rs.in crores)	Value sale	Rate of purchase	Rate of sale	Date of purchase	Broker
100	100	100	22.7.91	25.7.91	Hiten P. Dalal
25	100.95	100	31.7.91	14.8.91	-do-
20	101	100	31.7.91	14.8.91	-do-

10. There are also a number of transactions in PSU bonds and Units which appear to be ready forward transactions in contravention of the RBI guidelines. A few examples are given below :

Counterparty	Security	Face value (Rs.in crores)	Date of purchase	Date of sale	Broker
Standard Chartered Bank	9% IRFC	47.00	10.12.91	11.12.91	Hiten P. Dalal
Andhra Bank	-do-	25.00	12.12.91	13.12.91	-do-
Andhra Bank	-do-	25.00	13.12.91	24.12.91	-do-
Standard Chartered Bank	9% IRFC	200.00	17.3.92	18.4.92	-do-
Standard Chartered Bank/ Andhra Bank	9% HUDCO	25.00	10.12.91	24.12.91	-do-
ANZ Grindlays/ Standard Chartered Bank	9% IRFC	100.00	17.3.92	18,4.92	-do-
Central Bank of India	7.5% IDBI 1997	38.00	22.2.92	8.2.92	

11.(a) The bank has a large number of clients who have placed funds with the bank under the Portfolio Management Scheme (PMS). The aggregate amount of such funds stands at Rs.1275.73 crores. A category-wise summary of fiduciary funds as on 28 May 1992 is furnished below :

Category	No.of accounts	No.of companies	Total (Rs.In crores)
1. Public Sector Units	14	13	395.07
2. Financial Institutions	11	3	269.99
3. Private Sector companies	35	23	610.42
4. Others (individual)	4	4	0.25
	64	43	1275.73

During the month of May/June 1992, the accounts of some of PMS clients were allowed to be overdrawn. As at the 29 June 1992, the aggregate overdraft in such accounts amounted to Rs.237.74 crores. As explained by the bank, it had forward purchase/sale commitments in respect of its PMS clients. The forward sale commitments were not taken up by the counterparties, mainly Canfina, for Rs.235 crores but the bank honoured the forward purchase commitments resulting in the overdrafts. No interest has been charged on the overdrafts.

(b)(i) Citibank has also received large sums from PSUs under arrangements which are recorded in Citibank books as ready forward transactions. As an example, the transactions with one such PSU are explained in subsequent paragraphs.

(ii) During the period from 30 August 1990 to 19 August 1991, the PSU placed with Citibank deposits ranging from terms of 2 days to 182 days at rates of return ranging from 12 per cent to 28 per cent. The maximum amount outstanding at any point of time was Rs.50.68 crores.

(iii) In the books of the PSU, these amounts are shown as deposits with Citibank but in the books of Citibank, the funds are shown as received under ready forward deals executed by Citibank on behalf of its fiduciary clients. However, out of the aggregate value of such transactions of Rs.500.62 crores, transactions for Rs.450.20 crores (i.e. 89.93 per cent) are not supported by contract notes and delivery memos, nor are there lodgement and delivery memos in respect of the custodial services related to such transactions. In respect of five transactions on 30 August 1990 and 22 October 1990 covering sale and repurchase of PSU bonds for face value of Rs.45 crores, discharged BRs were not available.

(iv) A comparison of the statement submitted by the PSU with Citibank's records shows that 9 items shown by the PSU as deposits do not appear in Citibank's books. The matter is under investigation.

(v) Citibank is not permitted to enter into ready forward transactions except in Government securities but these transactions have been in PSU bonds and Units. It has been claimed by Citibank that as the transactions were not on its own account but on account of its fiduciary clients, there is no violation of the RBI guidelines. The validity of this claim may need to be examined.

12(a). On 30 December 1991 Citibank purchased 9% IRFC bonds of the face value of Rs.50 crores from Canfina for which Canfina issued its BR No.1401.

(b) According to Citibank it received a letter dated 28 February 1992 from Canfina asking it to take delivery of the securities from Standard Chartered Bank. Citibank claims it had issued its BR No.47 dated 19 February 1992 in respect of a sale of 9% IRFC bonds of face value of Rs.72.50 crores to Standard Chartered Bank and instead of making delivery thereagainst it issued a fresh BR No.47 dated 4 March 1992 for Rs.22.50 crores and discharged the BR No.1401 issued by Canfina for Rs.50 crores and exchanged it against the BR No.47 dated 19 February 1992 issued by it earlier.

(c) According to Canfina, it delivered allotment letters No.41-50 totalling Rs.50 crores at Delhi and the BRs were registered in the name of Punjab National Bank at the instance of Citibank but the latter did not return the BR No.1401 duly discharged to Canfina.

(d) According to Standard Chartered Bank, when it received from Citibank the discharged BR No.1401, it was represented by Citibank that Standard Chartered Bank could directly collect the securities represented by the BR from Canfina.

(e) Standard Chartered Bank has claimed the bonds from Citibank, which claim has been disputed. The broker involved is Hiten P. Dalal. The matter needs further investigation.

13.(a) On 27 May 1991, Canbank Mutual Fund bought 11.5% GOI loan 2009 of the face value of Rs.44.58 crores from Bank of Karad Ltd. On the same day it sold the security to Citibank. Against the purchase, Canbank Mutual Fund received an SGL transfer form from Bank of Karad Ltd. and against its sale it issued its SGL transfer form.

(b) Both forms bounced because of insufficient balance when lodged on 27 May 1991.

(c) On 18 September 1991, Citibank with full knowledge that the SGL issued by Canbank Mutual Fund on 27 May 1991 had bounced, sold 11.50% GOI loan 2009 for the face value of Rs.42 crores to Standard Chartered bank and on 19 September 1991 it made a further sale of Rs.8 crores to Standard Chartered Bank and it issued two BRs, without balance in the SGL A/c. with PDO, based on bounced SGLs earlier issued by Canbank Mutual Fund.

(d) In exchange for the duly discharged BRs, Standard Chartered Bank obtained from Citibank an SGL transfer form for Rs.5.42 crores and the bounced SGL form of Canbank Mutual Fund for Rs.44.58 crores. Standard Chartered Bank is still holding the bounced SGL form and has claimed the amount from Citibank.

(e) Along with its purchase of 11.5% GOI loan 2009 of Rs.44.58 crores from Bank of Karad Ltd. on 27 May 1991, Canbank Mutual Fund had also bought from the bank 11.5% GOI loan 2008 for Rs.58.39 crores and sold the same on the same day to Citibank. The SGL forms issued by Bank of Karad Ltd. and by Canbank Mutual Fund in respect of these transactions also bounced. However, on 27 July 1991, Citibank sold the above GOI loan back to Canbank Mutual Fund by way of BR which was liquidated by Citibank by returning the bounced SGL form to Canbank Mutual Fund.

(f) Between 23 August 1991 and 4 September 1991, these securities for Rs.58.39 crores were again sold by Canbank Mutual Fund to Standard Chartered Bank and issued its SGL transfer form which has bounced. Standard Chartered Bank has claimed the amount of the securities from Canbank Mutual Fund.

(g) The broker in all the above transactions was Hiten P. Dalal. The payment by Canbank Mutual Fund on 27 May 1991 for the original purchase of both GOI loans of the face value of Rs.102.97 crores has been credited in Bank of Karad Ltd. to the account of broker Abhay D. Narottam.

14. Citibank has entered into a large number of ready forward transactions in respect of which in certain cases it does not hold counterparty confirmations. There is therefore a possibility that the counterparties may not complete the second leg of the transactions. There are also cases where the second leg of the transactions has not been completed. For example, in respect of transactions with Canfina on behalf of fiduciary clients, in IRFC, CIL, NPTC, NTPC and HUDCO bonds of an aggregate value of Rs.235 crores when the second leg of the transaction fell due between June and August 1992, the same have not been accepted by Canfina. Similarly contracts with Canfina for PSU bonds of face value Rs.35 crores and with Standard Chartered Bank for 2 crore units have become overdue.

V. Bank of America

1.(a) Bank of America (BoA) was one of the largest players in the securities market during the period April 1991 to 23 May 1992 as could be seen from the following :

(Rs. in crores)

Security	No.of transactions				Total No.	Amount
	Purchase	Amount	Sale	Amount		
Government securities (including other SLR securities)	1396	48102.78	1572	46451.66	2968	94554.44
Taxfree bonds	1162	21658.49	1190	21458.25	2352	43116.74
Units	672	6703.15	671	6841.94	1343	13545.09
Others (CDs/CPs)	37	243.55	78	186.35	115	429.90
Total	3267	76707.97	3511	74938.20	6778	151646.17

It may be seen from the above that the bulk of BoA's securities transactions during the period both number-wise (43.8% of total) and amount-wise (62.4% of total) was in Government securities, followed by taxfree bonds (34.7% of total number of transactions constituting 28.4% of the aggregate amount involved) and Units (19.8% of the total number of transactions constituting 8.9% of the aggregate amount involved).

(b) Of the total 6778 transactions, 2367 (34.9%) transactions of the value of Rs.37,590 crores were put through directly with the counterparty banks and the remaining 4411 (65.1%) for an aggregate amount of Rs.1,14,056 crores were put through various brokers. Of these 4411 transactions, BoA concluded 845 transactions for Rs.26,200 crores through M/s.Bhupen Champaklal Devidas (BCD), 577 transactions for Rs.18,262 crores through Somayajulu & Co., 556 transactions for Rs.14,280 crores through N.K. Aggarwala & Co. (NKA), 281 transactions for Rs.7,743 crores through M/s.V.B. Desai (VBD), 260 transactions for Rs.7,952 crores through M/s.C.Mackertich (C.Mac), 218 transactions for Rs.4,174 crores through M/s.Asit C. Mehta and 160 transactions for Rs.3,561 crores through M/s.Harshad S. Mehta.

2. Some of the irregularities noticed during the scrutiny are mentioned below :

i) It was observed from the bank's records that on 8 and 9 April 1991, BoA borrowed on call basis amounts of Rs.26.50 crores and Rs.101.50 crores respectively from SBI Mutual Fund. These transactions are however, not appearing in the books of SBI Mutual Fund. In the first case, the funds came from the current account of Harshad S. Mehta maintained at Bombay (Hamam Street) branch of UCO Bank; in the second case though the funds came from SBI as per BoA's records, they were repaid to UCO Bank, Bombay (Hamam Street) branch which is not an authorised branch of UCO Bank to deal in call money operations. Both the borrowings were repaid with a day's interest on the next day and the amounts were credited to the current account of Harshad S. Mehta at UCO Bank, Bombay (Hamam Street) branch. The receipts issued by BoA in favour of SBI Mutual Fund in respect of these transactions were discharged by Shri R.Sitaraman, an Officer of SBI, Bombay Main Branch.

ii) On 31 July 1991 as per the instructions in a handwritten letter received from Bank of Karad Ltd. (BoK) and only initialed by an unidentified signatory along with a cheque of Rs.13,69,58,000, BoA issued a BR in favour of Andhra Bank showing a sale of Units of the face value of Rs.10 crores @Rs.13.6958 through the broker BCD to Andhra Bank. The above amount came from the current account of A.D. Narottam (ADN) at BoK. There is no such transaction in the books of BoK or in the investment account of ADN in BoK on that day. This transaction does not appear in the books of Andhra Bank also. The Units were shown as bought by BoA from Andhra Bank on 2 August 1991 @Rs.13.2500 and the BR under reference (No.20240) was returned to BoA by Andhra Bank duly discharged on 2 August 1991 on behalf of HPD. It is not clear why Andhra Bank discharged the BR when the transaction was not appearing in its books. The amount received from BoA was credited to the current account of HPD at Andhra Bank. BoA earned a profit of Rs.44,58,000 in this transaction.

iii) In a good number of purchase transactions entered into by BoA, it is observed that there is a sizeable difference in the amounts indicated in the cost memos of counterparty banks and the actual amounts paid by BoA. A few such transactions are listed in Annexure. (See Page No.92)

The counterparty banks did not claim the shortfall in the amount received by them from BoA. The difference in amount was received as indicated in the Annexure I. (See Page No.93)

iv) In respect of many transactions of the bank with Standard Chartered Bank, SGL transfer forms issued by the latter bounced. On many occasions these bounced SGL transfer forms were replaced by BRs or they were returned by BoA to Standard Chartered Bank by undertaking sale transactions in the same securities after an interval, which went up to 42 days in one case. At times BoA accepted new SGL transfer form for part amount and BR for the balance amount. For many of these transactions HPD was the broker for BoA. Despite frequent bouncing of SGL transfer forms issued by Standard Chartered Bank, there was no reduction in the volume of BOA's transactions with it. A few such cases are mentioned below :

(a) On 26 February 1992 BoA purchased from Standard Chartered Bank 11.5% GOI loan 2008 of face value Rs.60 crores @Rs.96.75. The SGL transfer form received for the purchase bounced and this transaction was finally squared by BoA by selling the same securities and returning the bounced SGL transfer form @Rs.96.6638 i.e. at a lower rate, on 5 March 1992. For BoA, HPD was the broker for this transaction.

(b) On 6 April 1992 BoA purchased 8.5% GOI loan 1994 of face value Rs.75.00 crores from Standard Chartered Bank. SGL transfer form issued by Standard Chartered Bank for this sale bounced and in lieu thereof it issued a BR No.2235 on 23 April 1992 in favour of BoA. The BR was replaced by the bank by a fresh SGL transfer form dated 2 May 1992. This was lodged by BoA on 5 May 1992 and this SGL transfer form also bounced. BoA relodged this SGL transfer form on 18 May 1992 and got credit for the above security. For BoA, HPD was the broker for this transaction.

(c) Again on the same day, i.e. 6 April 1992 BoA purchased 7.25% GOI loan 1992 of face value Rs.75.00 crores from Standard Chartered Bank. The SGL transfer form issued for the sale bounced and in lieu thereof Standard Chartered Bank issued BR No.2236 in favour of BoA on 23 April 1992. Subsequently on 2 May BoA sold these securities to Standard Chartered Bank and returned the above BR in settlement. For BoA, NKA acted as broker for this transaction.

In this type of transactions, it would appear that BoA put Standard Chartered Bank or certain brokers in funds for certain periods. The fact that bounced SGLs were replaced later with BRs would indicate that there were no underlying securities.

v) On 13 January 1992 BoA purchased from Citibank various PSU bonds of aggregate face value Rs.117.52 crores @Rs.92.25 when transactions in these bonds were taking place around Rs.85.00. BoA sold these bonds to Andhra Bank on the same day at the same rate and bought back from Andhra Bank on the same day the relative securities at @Rs.85.00. All these transactions were booked through the broker, BCD. The bank did not earn any profit in these transactions nor incurred any loss. The rationale for undertaking these transactions is not clear. BoA however received an amount of Rs.8,52,04,682.50 representing the difference of Rs.7.25 (Rs.92.25 - Rs.85.00) by means of a banker's cheque from Andhra Bank. On enquiry with Andhra Bank it is revealed that the amount of difference came from the current account of HPD in Andhra Bank.

vi) On 2 November 1991 BoA purchased from ANZ Grindlays Bank 9% IRFC bonds of face value Rs.150 crores through the broker NKA. In the books of BoA the transaction was booked @Rs.910.00 but in Grindlays Bank's books the transaction was shown @Rs.940.65 and it accordingly sent the cost memo. The difference between the contract rate and delivery rate (940.65 - 910.00) worked out to Rs.4,59,75,000 which was payable by the broker to BoA. This was recovered later by adjusting it against a payment of Rs.4,05,42,000 due to the broker in a transaction on 15 November 1991 booked with Canfina through the same broker for Rs.100 crores by allowing a difference of Rs.40.542 in the contract and delivery rates. The balance amount of Rs.54,33,000 was received from the broker.

On 2 November 1991, BoA booked a dummy forward sale of 9% IRFC bonds of face value of Rs.150 crores to Canara Bank through NKA with value date 16 November 1991. This forward sale was extended from time to time up to 9 January 1992 when these bonds were sold by BoA to Andhra Bank @Rs.936.745 and were purchased from Andhra Bank on the same day @Rs.900.00 thus booking a profit of Rs.5,51,17,500 through broker NKA. This amount came from the current account of HPD in Andhra Bank by a banker's cheque dated 8 January 1992 i.e. one day earlier.

Similarly, BoA had shown in its records two forward sale deals booked on 2 January 1992 and 9 January 1992 with Canara Bank and Canfina for sale of 9% IRFC bonds of face value Rs.100 crores and Rs.50 crores maturing on 3 January and 11 January 1992 respectively, through the same broker (NKA). The above forward deals were extended from time to time up to 22 February 1992. On that day instead of selling these bonds to Canara Bank and Canfina, BoA sold them to Andhra Bank @Rs.908.083 and @Rs.908.574 respectively, by setting off the forward sale deals mentioned above. This sale appears to have been undertaken by BoA to conclude the ready forward deal with Andhra Bank, the first leg of which was entered into by it on 9 January 1992 @Rs.900.00 referred to earlier.

On the same day i.e. 22 February 1992 BoA purchased from Andhra Bank these securities @Rs.850.00 which appears to be the beginning of another ready forward deal. The sale and purchase transactions undertaken by BoA on 22 February 1992 which were settled through exchange of BR issued by BoA, resulted in net payment of Rs.8.74 crores by Andhra Bank to BoA. Of this amount, BoA received Rs.7.50 crores from the current account of HPD at Andhra Bank by a banker's cheque issued on 21 February 1992 i.e.a day before the value date of the transaction, and the balance amount of Rs.1.24 crores came from ABN AMRO, New Delhi from the current account of NKA. This transaction does not appear in the books of Andhra Bank on 22 February 1992 but is shown as sale to BoA on 24 February. Apparently, these transactions were undertaken by Andhra Bank on behalf of broker NKA. It is difficult to believe BoA's claim that it was not aware that the payment was received from ABN Amro instead of Andhra Bank and that this became known to it only during the RBI scrutiny. Though ready forward deals in PSU bonds are prohibited by RBI, BoA was violating these instructions by putting through such deals, which also resulted in substantial profit to the bank.

vii) During March 1992 (5 and 9 March) BoA purchased through the broker C.Mackertich 13% MTNL and 13% NTPC bonds of face value Rs.61 crores from SBI Caps and of face value Rs.39 crores (11 March) from Canfina @Rs.100 when the transactions in these bonds in the market were being undertaken around Rs.80. The loss taken by the bank in these transactions (Rs.20 crores approx.) was reported to have been the result of a misunderstanding about the nature of the PSU bonds to be delivered, i.e., 17% bonds as against 13% bonds actually received. However, the bank has stated that consequent on sale of these bonds to Punjab National Bank (PNB) and Citibank on 28 March and 9 April 1992 at an average rate of Rs.84 and four other transactions arranged by the above broker, the details of which are given below, the bank has in totality not incurred any loss.

(Rs. in crores)

Contract date	Value date	Security	Purchase/ Sale	Face value	Rate	Counter-party banks	Profit
06.03.92	06.03.92	7.5% IDBI bonds	Purchase	30	87	Citibank	
06.03.92	06.03.92	7.5% IDBI bonds	Sale	30	99	Allahabad Bank	+ 3.60
13.03.92	13.03.92	13% DVC bonds	Purchase	65	78.1225	Grindlays Bank	
13.03.92	13.03.92	13% DVC bonds	Sale	65	83.2500	Canfina	+ 3.33
15.05.92	18.05.92	11.5% GOI 2010	Sale	120	97.75*	Allahabad Bank	+ 5.10
18.05.92	14.12.92	11.5% GOI 2010	Sale	70	99.60*	-do-	+ 4.27
						Total	+16.30

* Market rate Rs.93.50

The bank had thus entered into purchase and sale transactions at the behest of the broker to enable SBI Caps/Canfina to unload the bonds at a higher price and book profit or avoid loss.

viii) On 7 April 1992 Canfina sold 11.5% GOI loan 2010 of face value Rs.200 crores @Rs.91 to Andhra Bank. On the same day BoA bought these securities from Andhra Bank @Rs.93.50 and sold the same to Canfina @Rs.91 through the broker NKA by taking a loss of Rs.5 crores. All the three transactions were settled through exchange of SGL transfer forms issued in favour of one another. BoA could not give any satisfactory clarification for taking a loss of Rs.5 crores in the transactions These transactions, it appears, were undertaken by BoA to accommodate the broker NKA for Rs.5 crores.

ix) BoA has concluded a number of sale and purchase transactions in the same security, of the same value, and on the same day with the same counterparty banks. In all these one day transactions BoA sold the security and issued its BR to the counterparty and squared the transaction by getting the BR duly discharged by the counterparty bank. Deal numbers of many such transactions conclusively prove that these deals were booked simultaneously. In respect of many such transactions it is observed that the balance held in its books in the concerned security on the date of transaction was negligible compared to the value of security sold. In a majority of these one-day paper transactions BoA earned sizeable profits and took marginal losses in a few transactions. Andhra Bank appeared as counterparty bank in most of the transactions, followed by Standard Chartered Bank and BoK. Majority of the transactions was put through the broker BCD, followed by NKA, HPD and VBD. Particulars of some of the transactions in which BoA earned substantial amounts of profit/ incurred loss are furnished in Annexure II. (See Page No. 94)

On 31 October 1991 BoA earned a profit of Rs.24.07 crores in five transactions in different securities with Andhra Bank booked through BCD. In Andhra Bank these transactions were booked on behalf of HPD. Of the total amount of Rs.24.07 crores, Rs.4.86 crores was paid by Andhra Bank from the current account of HPD and balance amount of Rs.19.21 crores was paid on 1 November 1991 from the current account of HPD after getting a credit of Rs.19.21 crores from BoK from ADN's account. In fact BoK had prepared a banker's cheque for Rs.19.21 crores favouring BoA on 31 October 1991 itself, but the same was cancelled later.

In Andhra Bank most of such transactions were booked on behalf of HPD and the amount of difference between the sale and purchase price of the securities came from the current account of HPD maintained by it. At BoK these transactions were booked on behalf of BCD and the amount of difference came from OD/ CC account of BCD with it. In respect of the transaction on 21 April 1992 where BCD took a loss of Rs.6 crores it was observed that an amount of Rs.6 crores was transferred in BoK from the current account of ADN to BCD's OD/CC account on 20 April 1992 itself.

At Standard Chartered Bank it was learnt that the transaction listed in Annexure II was booked on behalf of HPD and the amount of difference of Rs.4.50 crores was received from HPD.

Looking at the off market variation on the same day in the sale and purchase prices of the securities traded, and the fact that the real counterparties to the transactions were only the brokers represented by the banks merely in name, these transactions appear to be tailormade transactions for transferring funds to each other, i.e. BoA and brokers, for the consideration received in the past or to be received in future transactions or any other purpose. This needs to be probed further.

3. Off the Books (OB) deals

Apart from the regular securities transactions, the bank has also undertaken a large number of transactions which are treated as Off the Books (OB) transactions. The basis of such transactions is explained below.

(a) The bank accepts short term funds from customers including PSUs and corporate bodies. The aggregate turnover of such placements by PSUs amounted to Rs.2,940 crores in 225 transactions and Rs.4,014 crores in 700 transactions of corporate bodies. The maximum outstandings in such placements at any given point of time has not been ascertained. These funds are accepted at predetermined rates for specific periods of 15 days/30 days/60 days, etc. In several cases letters on record from some of the limited companies placing such funds clearly indicate that they are keeping the funds with the bank as call deposit or deposit for specified periods at specified rates of interest. On the date of placement of funds, the bank shows in its books a spot sale of securities mainly PSU bonds and Units, through BR issued in favour of the placer of funds either from its own investment account or against BR issued in its favour by another bank/financial institution. Simultaneously, the bank shows in its books through a broker a forward purchase of the same securities of the same value with another counterparty bank/financial institution. The counterparty for the forward transaction in almost all the cases is shown as Canfina or UCO Bank. In many cases contract notes from brokers were not found on record in respect of such forward deals and in no case confirmation from the counterparties confirming the forward deals was available in the bank's records. These in effect are dummy deals. On the pre-determined value date i.e. the date of maturity of the deposit placement, the securities are purchased from the placer of the deposit and are shown as bought outright from the dummy counterparty with which the earlier forward sale transaction is shown in the books. Thus, the dummy deal is squared off in the books. The deal, of course, recognises the bank's forward commitments. The interest at the pre-determined rate is loaded into the rate at which the securities are purchased on the maturity date of the deposit. In the process, the bank has not only avoided the discipline of the PMS guidelines but also violated RBI directives relating to rates of interest on deposits. The deals in effect are ready forward in nature which are prohibited by the RBI guidelines.

(b) While scrutinising OB deals it was observed that, apart from the above, the bank was booking dummy forward sale/purchase of securities (i.e. PSU bonds/ Units) from Canfina, Canara Bank, UCO Bank, etc., and on value date these dummy counterparties were replaced by other counterparties. The bank reversed the dummy deals showing purchase/sale of the same securities from/to the earlier named counterparties at the same rate at which the forward sale/purchase is booked initially. There is wide variation between the rate at which the forward sale or purchase is booked and the rate at which the actual spot purchase/sale took place on value date with the substituted counterparty. It was also observed that invariably in all such cases there was a difference between the contract rate and delivery rate which was passed on to/recovered from the brokers, in full. The amount of such difference (payment/recovery) at times was found to be as high as Rs.4.05 crores. A few such transactions are given in the Annexure III. (See Page No. 95)

(c) In many of the cases contract notes in respect of dummy forward deals are not on record, and such forward deals when sent for confirmation to counterparties were returned by them stating that these deals were not appearing in their books. It looks as if, in the process, the brokers have been enabled to take forward positions.

4. Current account of Harshad S. Mehta

The bank maintains, among other brokers, current account of Harshad S. Mehta (HSM). It has been observed that during the period from January 1991 to December 1991 the bank allowed credits of substantial amounts in the current account of HSM ranging between Rs.31.50 lakhs and Rs.20 crores without any specific authorisation for the purpose. Though there is no claim on these amounts from anybody so far, the bank violated the normal banking norms. The bank has pleaded that this lapse occurred due to clerical error which is difficult to believe especially in view of the call money transactions undertaken by the bank on 8 and 9 April 1991 discussed in paragraph 2(i).

5. Free Exchange of BRs

Though BR is a non-transferable document it is observed that for its sales of securities BoA has been giving BRs received from banks (other than the counterparty) held by it on account of its earlier purchases. Similarly for purchases, it has been accepting from counterparty banks BRs issued to them by other banks. When a single BR for the full amount was not available two or more BRs adding up to the face value of sale transaction were given for settlement. Cases of netting of BRs were also frequent.

6. Use of Cash Credit facility for purchase of securities

It is observed that BoA has allowed its corporate borrowers to use credit facilities sanctioned for working capital requirements for investing in securities thereby defeating the purpose for which the facilities were sanctioned.

A few cases noticed during the scrutiny are as under :

(Rs. in crores)

Name of the borrower	C/C limit sanctioned	Date of investment	Amount of investment	Security in which invested
1. Polyolefins Industries Ltd.	18.0	15.10.91	10.00	Units
2. Sandvik Asia Ltd.	8.5	03.01.92	2.03	9% IRFC bonds
3. 20th Century Finance Corporation Ltd.	4.0	08.06.91	4.00	9% IRFC bonds

VI. Andhra Bank

Andhra Bank's investment operations and call money borrowings/lendings are mainly undertaken at its Bombay (Fort) branch. The branch has also undertaken a large volume of security transactions on account of various broker-clients.

A. Transactions in securities on Head Office Investment Account

A verification of securities has revealed that the branch was not holding 11.5% NHB bonds 2009 (2nd series) for Rs.200 lakhs. This was subscribed by the bank during December 1989. The bank has taken this up with National Housing Bank.

The total turnover in H.O. investment account (purchases and sales) for the period 1 April 1991 to 30 May 1992 was Rs.2396.20 crores. Scrutiny of the security deals revealed certain features/irregularities and some of the major instances are given below :

(a) Andhra Bank sold on 1 June 1991 the following securities on ready forward basis to two banks through the broker Batliwala & Karani. The relative contract note was not found at the branch.

Particulars of the securities	Face Value	Rate	Settlement Amount	Name of the bank
11.5% GOI 2009	Rs.10 crs.	99.9073	Rs.10.03 crs.	United Bank of India
11.5% GOI 2010	Rs.10 crs.	99.5547	Rs.10.36 crs.	Dena Bank
			Rs.20.39 crs.	

There was nothing on record to indicate that Andhra Bank has received banker's cheques for the sales. Cost memos were prepared by the bank but not sent to the concerned banks. Instead fresh cost memos were prepared at a rate higher than the rate already fixed by H.O. and were sent to the banks as noted below.

Particulars of the securities	Face Value	Rate	Settlement Amount	Name of the bank
11.5% GOI 2009	Rs.10 crs.	100.8914	Rs.10.13 crs.	United Bank of India
11.5% GOI 2010	Rs.10 crs.	101.1017	Rs.10.52 crs.	Dena Bank
			Rs.20.65 crs.	

Banker's cheques for the above amounts were received from the concerned banks but H.O. A/c. was credited with only Rs.20.39 crores as agreed upon earlier. The difference of Rs.25,31,100 was credited to the broker's current account. In the daily report to H.O., the branch had shown only the original contract rates instead of the actual rates at which the deals were concluded.

(b) In the case of two sale transactions with UCO Bank on 18 May 1991 on ready forward basis through the broker Batliwala & Karani in respect of 11.5% GOI loan 2015 face value Rs.10 crores and 11.5% GOI loan 2010 face value Rs.5 crores for Rs.10.52 crores and Rs.5.23 crores respectively (including interest), Andhra Bank has not received the banker's cheques from the counterparty bank. The total amount of Rs.15.75 crores receivable from UCO Bank was adjusted by debiting the current account of the broker on 18 May 1991 maintained at the branch. The BR for Rs.10 crores duly discharged and the SGL transfer form for Rs.5 crores received from UCO Bank for the purchases made earlier (on 4 May 1991 and 6 May 1991 respectively) were returned to UCO Bank by Andhra Bank. Payments for these purchases amounting to Rs.15.70 crores had been made to UCO Bank by means of banker's cheques which had been credited to the broker's account in that bank. If the veil of ready forward transaction is lifted, it will be seen that the transaction is really a clean loan of Rs.15.70 crores to the broker for 14 days. While Andhra Bank lent the money, UCO Bank lent its BR and SGL transfer form.

(c) On 27 May 1991, Andhra Bank sold to Bank of Madura on ready forward basis through the broker Batliwala & Karani 11.5% GOI loan 2008 face value Rs.10 crores @ 99.3898 and a cost memo for Rs.9.95 crores was sent to Bank of Madura. It returned the BR received earlier from Bank of Madura (duly discharged) for its purchase of the same security made on 18 May 1991 for Rs.10.48 crores (@Rs.100.55). The sale consideration of the security i.e. Rs.9.95 crores was received from Bank of Karad (BoK) and not from the counterparty bank i.e. Bank of Madura. BoK while forwarding its banker's cheque to Andhra Bank requested that it may be credited to the current account of Batliwala & Karani. However, Andhra Bank did not act on this letter and instead it debited the current account of Batliwala & Karani with Rs.57.50 lakhs on 27 May 1991 and the total amount of Rs.10.52 crores was passed on to H.O. The reason for this additional debit was that the selling rate did not cover the funding cost. However, the reasons for receiving a banker's cheque from BoK instead of from Bank of Madura could not be explained by bank officials.

In BoK, it was found that no security transaction was entered into by it with Andhra Bank on that day. The amount received from BoK was a transfer of funds from the current account of Batliwala & Karani maintained at BoK to his current account at Andhra Bank. On verification with Bank of Madura, it was observed that no purchase transaction was booked by it on 27 May 1991 although it has in its possession its own BR dated 18 May 1991 of the face value for Rs.10 crores duly discharged by Andhra Bank. No satisfactory explanation was forthcoming from Bank of Madura.

B. Call Money Transactions

The branch undertakes call money borrowing/lending only as per H.O. instructions and such transactions are required to be reported to H.O. on a daily basis.

Broker M/s.Hiten P. Dalal (HPD) has a current account No.4819 in Andhra Bank, Fort Branch. An analysis of this account shows his need for funds of about Rs.18.13 crores on 19 December 1991 for payment to Andhra Bank Financial Services Ltd. (ABFSL). This requirement has been accommodated by the following sequence of transactions :

a) Andhra Bank lent Rs.18.09 crores on 19 December 1991 as call money to Standard Chartered Bank for one day at the rate of 13% per annum.

b) On the same day, Standard Chartered Bank entered into a ready forward deal with ABFSL for purchase of 1.35 crore Units @Rs.13.40 for a consideration of Rs.18.09 crores. The amount paid by Standard Chartered Bank was credited to the account of HPD in Andhra Bank on the same day.

c) Standard Chartered Bank repaid the call money borrowing of Rs.18.09 crores on 20 December 1991 with interest of Rs.64,430 (@13%). However, as per the relative voucher in Andhra Bank, the rate at which the money was lent to Standard Chartered Bank was recorded as 17% p.a. and the difference of 4% amounting to Rs.19,824.79 was debited to the current account of HPD on that day.

d) The ready forward deal between Standard Chartered Bank and ABFSL was reversed on 23 December 1991. Consequent debit of Rs.18.09 crores was made to HPD's account in Andhra Bank.

It is significant to note that this ready forward deal was not reflected in the books of ABFSL. It has not been ascertained as to how Standard Chartered Bank recovered the funding cost for four days from the broker.

C. Security transactions on account of broker-clients

a) The branch has undertaken purchase and sale transactions in Government securities, PSU bonds, Units, etc. on a large scale on account of broker-clients. Under the arrangement, the brokers approach the branch with details of purchases/sales of various securities to be effected with different banks/financial institutions. Normally, the quantum of such purchases and sales are the same; thereby the transactions are generally squared on the same day. Andhra Bank receives SGL transfer forms or BRs/scrips for the purchases from the selling banks and issues SGL transfer forms to the counterparty banks for the sales. Andhra Bank issues its banker's cheques for the purchases to the selling banks and receives banker's cheques for the sales from the purchasing banks. The total payments and receipts are debited/credited to the broker's current account. On certain occasions, purchases and sales are netted and only the net position is reflected in the current account. The transactions are generally effected on the days following reporting Fridays. Andhra Bank charges an agency commission of Rs.500 per Rs.1 crore or fraction thereof for each purchase and sale.

b) The total turnover (both purchases and sales) on account of broker-clients' transactions for the period 1 April 1991 to 30 May 1992 as appearing in the branch books amounted to Rs.38759.60* crores involving about 1690 deals in securities. Of these, transactions on account of the undernoted five brokers amounted to Rs.37593.61 crores constituting 97% of the total transactions and the balance was on account of other brokers.

(Rs.in crores)

Name of the broker	Purchases	Sales	Total
(i) Hiten P. Dalal	9639.18	9623.43	19262.61
(ii) Batliwala & Karani	5094.50	5150.50	10245.00
(iii) M/s.V.B. Desai	2133.27	2138.46	4271.73
(iv) N.K.Aggarwala & Co.	1405.00	1378.27	2783.27
(v) Mukesh Babu	508.00	523.00	1031.00
	18779.95	18813.66	37593.61

It will be seen that the share of Hiten P. Dalal alone worked out to around 50% of the total turnover.

The operations (both credits and debits) in the current accounts of major five brokers maintained at the Bombay (Fort) branch, on account of security transactions and others during the period 1 April 1991 to 30 May 1992 were as under :

	(Rs. in crores)
(i) H.P. Dalal	21521.86
(ii) Batliwala & Karani	10247.51
(iii) M/s.V.B. Desai	4372.25
(iv) N.K.Aggarwala & Co.	1240.45
(v) Mukesh Babu	929.47

* **Note** : The difference between this figure and Rs.26,449 crores appearing in paragraph 7 of Chapter III is apparently due to an incorrect classification by the bank's Head Office. It is being reconciled.

Out of the total turnover of Rs.38,759.60 crores, transactions with the undernoted four foreign banks amounted to Rs.18,856.00 crores which constituted 49 per cent.

	(Rs. in crores)
(a) Bank of America	7252.00
(b) Citibank	5254.00
(c) Standard Chartered Bank	4213.00
(d) ANZ Grindlays Bank	2137.00
	18856.00

It was also observed that of the total transactions, transactions in 11.5% GOI loan 2010 alone accounted for Rs.21,024 crores and in PSU bonds and Units accounted for Rs.6,280 crores. The balance amount of Rs.11,456 crores was on account of other Government/approved securities. The security 11.5% GOI loan 2010 was traded to the extent of Rs.5,461 crores (both purchases and sales including turnover of Rs.840 crores against BRs) in the month of April 1992 alone. On a single day i.e. on 6 April 1992 the rates of purchases varied widely between Rs.89.50 and Rs.98.2864 and that of sales between Rs.90.01 and Rs.99.50.

c) The branch has a separate SGL account with PDO for recording broker-clients transactions in Government securities. There are a number of cases where SGL transfer forms issued by counterparty banks have bounced. These SGL transfer forms were either re-lodged and credits have been obtained subsequently, or they were returned to the issuing banks and in turn, the SGL transfer forms issued by the branch have been received back and the position has been squared up. During the month of April 1992, in respect of 11.5% GOI loan 2010, as against the total purchases of Rs.2,311 crores made by the branch against SGL transfer forms, credits have been afforded only for Rs.1366 crores. Similarly, as against the total sales of Rs.2310 crores for which Andhra Bank has issued its SGL transfer forms, debits reflected in the SGL account aggregated only Rs.1385 crores. It was also noticed that in respect of certain transactions involving large amounts SGL transfer forms have not been lodged with PDO.

d) The branch has not maintained the security-wise ledger of the broker-clients properly and there was no system of monthly reconciliation of the balances shown in the ledger with that of the statements obtained from PDO. Physical verification of securities such as PSU bonds, Units, etc. kept at the branch on behalf of brokers was also not carried out by the branch.

e) Some of the irregularities observed during the course of scrutiny are summarised below.

(1) (i) Andhra Bank purchased on 7 March 1992 on behalf of Mukesh Babu 6% GOI loan 1994 - face value Rs.50 crores @Rs.89.40 (settlement amount Rs.45.11 crores) from Punjab National Bank for which the SGL form was issued by it to Andhra Bank. Against the SGL transfer form issued by PNB, it held the SGL form of BoA which had sold to it the same security on 7 March 1992.

(ii) Andhra Bank in turn sold the security on the same day to Citibank @Rs.89.52 (settlement amount Rs.45.17 crores) and the SGL transfer form was issued by Andhra Bank to Citibank.

(iii) As the SGL transfer form lodged by Andhra Bank bounced, that issued by it to Citibank also bounced.

(iv) The same security was purchased back by Andhra Bank from Citibank on 24 March 1992 @Rs.90.25 and this was sold to BoA by Andhra Bank on the same day at the same rate.

(v) While Citibank returned the SGL form of Andhra Bank of 7 March 1992, the latter has issued a fresh SGL transfer form for this sale to BoA on 24 March 1992. Although there was no difference in the rates of purchase and sale, banker's cheques for identical amounts were exchanged by the two banks.

(vi) BoA advised Andhra Bank to return to it the bounced SGL form of PNB held by it from 7 March 1992 onwards, to enable it to return the same to PNB and to retrieve its own SGL transfer form originally issued to PNB on 7 March 1992.

(vii) Thus all the SGL transfer forms were received back by the respective banks. In the above deals there was no underlying security. The rationale for undertaking such transactions is not clear.

(2) Purchase and sale of securities were effected on the same day on behalf of broker-clients by accepting BRs from the selling banks and returning the same to the issuing banks duly discharged; thereby the net difference, as a gain or loss, was reflected in the respective current accounts of the brokers. A good number of such transactions were between Andhra Bank and BoA. A few illustrations are given below :

Date	Name of broker	Security	Face Value (Rs.in crs)	Purchased from	Sold to	Net difference (in Rupees)
8.2.92	NKA & Co.	11.5% GOI loan 2010	60	BoA	BoA	1,36,60,800 (+)
	(Purchased @Rs.94.2232 sold @Rs.96.50)					
22.2.92	NKA & Co.	11.5% GOI loan 2010	25	BoA	BoA	75,75,000 (+)
	(purchased @Rs.94.00 sold @Rs.97.03)					
27.3.92	H.P.Dalal	11.5% GOI loan 2010	100	Citi-bank	Citi-bank	1,00,000 (+)
	(purchased @Rs.96.94 sold @Rs.96.95)					
9.1.92	NKA & Co.	9% IRFC bonds	150	BoA	BoA	5,51,17,500 (-)
	(purchased @Rs.936.745 sold @Rs.900.00)					
24.2.92	NKA & Co.	9% IRFC bonds	150	BoA	BoA	8,73,70,000 (-)
	(purchased @Rs.908.083 for Rs.100 crores and purchased @Rs.908.574 for Rs.50 crores, sold @850.00 for Rs.150 crores)					
13.1.92	H.P.Dalal	Six different PSU bonds	117.52	BoA	BoA	8,52,04,682 (-)
	(purchased @Rs.92.25 sold @Rs.85.00)					

(3) Although Andhra Bank has not issued its own BRs for the broker-client transactions, it was observed that it received BRs either in its name or in the names of other banks for the purchases made by it on behalf of the brokers; these BRs were in turn transferred to other banks by showing them as a sale to these banks. In the process, Andhra Bank has helped the brokers to mobilise funds by acting as an intermediary. In a few cases the bank has also circumvented RBI instructions on buy-back deals in PSU bonds between banks and financial institutions.

(i) On 31 March 1992, Andhra Bank purchased from Canfina on behalf of H.P. Dalal, Cantriple for the face value of Rs.8 crores @Rs.11 and accordingly a BR was received from Canfina. A banker's cheque for Rs.8.80 crores was issued to Canfina. On 10 April 1992, Andhra Bank sold the same security to Standard Chartered Bank @Rs.20 and accordingly it transferred the BR held by it duly discharged, to the latter bank. A banker's cheque for Rs.16 crores was received by Andhra Bank from Standard Chartered Bank and the same was credited to the current account of the broker in Andhra Bank. In this transaction, the broker, H.P. Dalal has gained to the extent of Rs.7.20 crores. This matter is now under dispute. Standard Chartered Bank has written to Andhra Bank that it has not received the Cantriple certificates as per the BR since the same was reported to have been delivered to Andhra Bank by Canfina. Andhra Bank has denied the claim.

Further, Andhra Bank, at the request of the same broker, H.P. Dalal, purchased Cantriple of face value Rs. 50 crores @Rs.16.45 from Standard Chartered Bank on 31 March 1992 and sold the same to Citibank @Rs.20.00 on the same day. This resulted in a profit of Rs.17.75 crores to the broker which was reflected in his current account. It will be thus seen that the same security was traded at rates ranging between Rs.11 and Rs.20 on a single day i.e. 31 March 1992 and the broker in the process made substantial profits.

(ii)Andhra Bank purchased from Canara Bank on behalf of H.P. Dalal 9% IRFC bonds face value Rs.100 crores @Rs.97.08 on 16 November 1991 and received a BR issued by Citibank to Canara Bank for the latter's purchase of the same security from Citibank. Andhra Bank sold back the same security at the same rate on the same day to Citibank by returning the latter's BR received from Canara Bank at the time of purchase. In this case, the transaction was in effect a buy-back deal between Citibank and Canara Bank the first leg of which was concluded a day earlier, and Andhra Bank lent its name for transferring the same through its books of account. For Citibank, the transaction resulted in a loss of Rs.8 lakhs, as its sale to Canara Bank on 15 November 1991 was at Rs.97.

(iii) On 14 January 1992, Andhra Bank sold to Standard Chartered Bank 9% Coal India bonds face value Rs.40 crores @ Rs.93 (sale value Rs.38.83 crores) on behalf of broker H.P. Dalal. It is seen from the cost memo of Andhra Bank that physical bonds were delivered to Standard Chartered Bank. At the same time, H.P. Dalal has delivered to Andhra Bank a BR No.429 issued by Punjab National Bank in favour of SBI Mutual Fund with instructions to give it to Standard Chartered Bank and this was treated by Andhra Bank as a purchase from "Self". This BR was transferred to Standard Chartered Bank for the sale by Andhra Bank but no banker's cheque for the sale was received by Andhra Bank. Since it was a purchase from "Self", no payment was also made by Andhra Bank. It was found from the delivery advice of the broker to Andhra Bank for the sale to Standard Chartered Bank that "Proceeds will be with Chartered Bank only" and hence no banker's cheque was received. Andhra Bank is not in a position to offer a satisfactory explanation for this transaction.

(4) A reference is invited to a transaction in Units between BoA and Andhra Bank on 2 August 1991, mentioned in the Chapter on BoA. The proceeds of the banker's cheque for Rs.13.25 crores received from BoA for its purchase of 1 crore Units was credited to the account of H.P. Dalal in Andhra Bank. In H.P. Dalal's account in Andhra Bank, there is a debit of Rs.16.13 crores on 2 August 1991 representing payment to ANZ Grindlays Bank by an A/c. Payee Cheque. ANZ Grindlays Bank has confirmed that this payment was received towards sale of shares by it to H.P. Dalal. It is thus evident that funds of A.D. Narottam have been transferred from his account in BoK to that of Hiten Dalal in Andhra Bank for purchase of equity.

(5) It was observed in the current account of H.P. Dalal that there was a debit of Rs.11 crores on 3 September 1991. This represented a payment to Canbank Mutual Fund (CBMF). Andhra Bank made an application dated 28 August 1991 for investment in

CANCIGO on behalf of H.P. Dalal for Rs.11.00 crores. However, the bond was not found under client's holding. There was, as per Canfina's books, a purchase of Cancigo face value Rs.11 crores from Andhra Bank on 6 February 1992. The relative certificate for Rs.11 crores is in the possession of Canfina. However, there is no such sale by Andhra Bank on that day as per its books. It is seen from the bank's records that at the request of H.P. Dalal, it made the application during August 1991 to CBMF towards subscription in Cancigo for Rs.11 crores on account of the broker and the bond, on receipt, was intended to be given to ABFSL towards security for the transactions by the broker with ABFSL. Subsequently, when Andhra Bank came to know that transfer of Cancigo holding from one person to another person is not permitted, it brought this clause to the notice of the broker and advised him to cancel the application already made. This was not pursued thereafter. On 8 January 1992, the branch received an interest warrant in the bank's name from CBMF for Rs.45,20,548 for the period from 3 September 1991 to 31 December 1991 on the investment of Rs.11 crores, and this was credited to the current account of H.P. Dalal. A second interest warrant for Rs.68,56,164 for the period from 1 January 1992 to 30 June 1992 received from CBMF has not however been credited to H.P. Dalal's account so far. The matter is reported to be under investigation of the bank's Head Office.

(6) It was observed on a scrutiny of the current account of H.P. Dalal that the branch has accommodated the broker by affording credit of some of the banker's cheques received from other banks to his account one working day prior to the day on which these instruments were sent for clearing, with a view to avoiding overdrawings in the account on these days. The funds so credited have been utilised by the broker either for purchase of securities or making some other payments. Instances noticed are given in the annexure. It will be seen therefrom that in the case of item No.(i), the branch had afforded the credit even before the actual date of the instrument.

D. Claims on Andhra Bank by banks

(a) Andhra Bank has received three claims from Standard Chartered Bank for a total sum of Rs.71.80 crores details of which are shown below :

(i) Payment made by Standard Chartered Bank on 12 February 1992 to Andhra Bank for purchase of security of 11.5% GOI 2011 face value Rs.40 crores — Rs.38.47 crores

Standard Chartered Bank vide its letter dated 24 June 1992 has claimed from Andhra Bank either the delivery of the above security or refund of the amount paid by it with interest @20% from 12 February 1992 till date of payment. As per the books of accounts and other records at Andhra Bank there was no sale transaction of the said security on that day with Standard Chartered Bank. The banker's cheque for Rs.38.47 crores received from Standard Chartered Bank has been credited to the current account of H.P. Dalal on 12 February 1992 in terms of the covering letter to the instrument. Andhra Bank has denied the contention of Standard Chartered Bank that its payment was in consideration of purchase of the security from Andhra Bank.

(ii) Payment made by Standard Chartered Bank on 27 March 1992 to Andhra Bank for purchase of 9% IRFC bonds face value Rs.27.5 crores — Rs.25.33 crores

Standard Chartered Bank vide its letter dated 26 June 1992 has demanded from Andhra Bank either delivery of the above security or refund of the amount paid by it to Andhra Bank with interest thereon from 27 March 1992 till date of payment. It further claimed that Andhra Bank has delivered to it Letters of Allotment issued by IRFC for the purchase made by it. As per records at Andhra Bank, there was no sale transaction in the above security with Standard Chartered Bank on that day. However, the banker's cheque for Rs.25.33 crores received from Standard Chartered Bank has been credited to the current account of H.P. Dalal although there was no covering letter to this effect. Andhra Bank has clarified that this was done as per the existing practice. Andhra Bank has denied having delivered any letters of allotment issued by IRFC to Standard Chartered Bank . It has refuted its liability to pay any amount to Standard Chartered Bank.

(iii) Claim for delivery of Cantriple of face value 8 crores

The dispute between the two banks in respect of the delivery of Cantriple units of the face value of Rs.8 crores by Andhra Bank has already been mentioned earlier in this Chapter.

(b) ABN Amro Bank, Bombay has made payment by means of banker's cheque for Rs.9.76 crores on 9 March 1992 in favour of Andhra Bank and the same has been credited to the current account of H.P. Dalal by Andhra Bank. ABN Amro has stated in its letter dated 11 June 1992 that the said payment was for the purchase of 17% NPC bonds from Andhra Bank through the broker, N.K. Aggarwala & Co. for investment on behalf of one of its fiduciary clients. As the bonds were not delivered either by Andhra Bank or the broker, ABN Amro has made a claim for delivery of the said securities or in the alternative, refund of the said sum with interest @20%. From the records at Andhra Bank, it is observed that there is no security transaction with ABN Amro on 9 March 1992. Andhra Bank has denied the claim made by ABN Amro on the ground that no contract subsisted between Andhra Bank and ABN Amro Bank.

VII. Bank of Karad Ltd. (in liquidation)

The securities transactions of the Bank of Karad Ltd. (BoK) were mainly on account of its broker clients. The bank maintained accounts of 23 brokers including three brokers who enjoyed secured overdraft limits upto Rs.25 lakhs. The major brokers' accounts which have been operated were in respect of A.D. Narottam, M/s.Excel & Co., M/s.Bhupen Champaklal Devidas and M/s.Darashaw & Co.

2. BoK maintained two SGL accounts in the PDO, one in respect of its own transactions and the other in respect of brokers' transactions. It also maintained separate securities ledgers for its broker clients. While the bank had laid down procedures for keeping appropriate records for brokers' transactions, several irregularities have been observed in the manner in which brokers' transactions have been effected.

3. A large number of irregularities have been observed in the operation of the account of broker A.D. Narottam. These can be broadly grouped as follows:

(a) Firstly, in violation of RBI instructions, sales were effected on behalf of the broker by issue of bank's BRs and no entries were reflected in BoK books. For example, on 30 March 1992, BoK sold to Standard Chartered Bank on behalf of the broker 12.5% GOI loan 2007 of the face value of Rs.250 crores and Rs.85 crores and issued its BRs No.3571 and 3572. The sale proceeds of Rs.335.44 crores were not received by BoK. Against the amount due from Standard Chartered Bank, the broker set off a purchase of bonds/Units for Rs.317.44 crores and received a pay order in favour of Andhra Bank for Rs.18 crores which was credited in Andhra Bank to the current account of Hiten P. Dalal. The bonds purchased by the broker were not deposited with BoK but the securities of face value of Rs.250 crores purchased by Standard Chartered Bank on 30 March 1992 were resold to BoK by Standard Chartered Bank on 18 April 1992 and BR No.3571 was returned to BoK. In respect of BR No.3572 for Rs.85 crores, BoK issued its SGL transfer form which bounced as it was issued against non-existent securities. The bounced SGL form is held by Standard Chartered Bank and is still outstanding.

(b) Secondly, on several occasions, BoK issued its BRs on behalf of the broker when there was nil or insufficient balance in the broker's security account. To cover up this position, the sales entries in the broker's securities ledger were post dated after the broker arranged for suitable backing and the sales and purchases were recorded as having been effected on the same day. A few examples are listed below :

Date of actual sale	Security	Face Value (Rs.in crs)	Balance on date of actual sale	Date of sale as recorded
04.04.91	11.5% GOI loan 2015	75	Rs.400	09.04.91
06.04.91	11.5% GOI loan 2007	25	NIL	22.04.91
06.04.91	11.5% GOI loan 2008	25	Rs.1300	16.09.91
18.05.91	11.5% GOI loan 2010	82.54	NIL	23.05.91
18.05.91	11.5% IDBI 2010	10.00	NIL	01.06.91
20.11.91	11.5% GOI loan 2009	30.00	NIL	14.12.91
15.12.91	8.25% GOI loan 2005	6.75	Rs.6 crores	18.12.91
21.12.91	11.5% GOI loan 2009	4.00	Rs.1,95,000	27.12.91

Similar irregularities were noticed in the account of M/s.Bhupen Champaklal Devidas. A few examples are listed below :

Date of actual sale	Security	Face Value (Rs.in crs)	Balance on date of actual sale	Date of sale as recorded
11.04.91	6.75% Mah. 1992	0.009	Rs.14,400	22.04.91
11.01.92	11.5% GOI loan 2010	20	Rs.33 crores	15.01.92
11.01.92	11.5% GOI loan 2010	15		
20.04.91	11.5% GOI loan 2010	15	Rs.14 crores	23.04.91

(c) Thirdly, there were cases where the broker deposited with BoK, BRs issued by other banks/ institutions for which alleged purchases no payment was made by BoK. These BRs were recorded in the securities ledger as "bought self-free" or "Agst Rs.". On examination of some of these entries, it is ascertained that the broker has in fact not made payment for the alleged purchases or having made the payment, received back the amount on the same day. A few examples of such transactions with Metropolitan Co-operative Bank (MCB), a small-sized Bombay based urban co-operative bank, are given below :

(i) MCB issued BRs Nos.1 to 3 for 11.5% IDBI loan 2010 for an aggregate value of Rs.31.25 crores. BoK paid this amount on 21 March 1991 to MCB by debit to the account of Dhanraj Mills Pvt. Ltd. On the same day, Rs.31.15 crores was received by BoK from MCB with instructions to credit the amount to the account of M/s.Excel & Co. and the amount was thereafter credited back to the account of Dhanraj Mills Pvt. Ltd. The BRs received from MCB were used to cover earlier sales effected in February 1991 out of A.D. Narottam's account which sales were made when there was no balance in the broker's security account.

(ii) MCB issued BRs Nos.4 to 9 for 11.5% IDBI loans of various maturities for an aggregate value of Rs.53.40 crores. BoK paid this amount on 26 March 1991 to MCB by debit to the account of Dhanraj Mills Pvt.Ltd. On the same day, Rs.53.30 crores was received by BoK from MCB and credited to the account of Dhanraj Mills Pvt. Ltd. The BRs received from MCB were used to cover earlier sales effected between January 1991 and March 1991 out of A.D. Narottam's account which sales were made when there was no balance in the broker's security account.

(iii) MCB issued the following BRs for which BoK made payment by debit to the account of A.D. Narottam on 16 September 1991.

(Rs. in crores)

BR No.	Security	Amount of BR	Amount received back
12	11.5% GOI loan 2008	25.93	25.93
13	Units of UTI	212.80	212.80
14	Units of UTI	252.70	252.55

The amounts received back were credited to the account of A.D. Narottam. The BRs received from MCB were used to cover earlier sales effected in April 1991 and July 1991 out of A.D. Narottam's account which sales were made when the balance in the broker's security account was only Rs.1300.

(iv) MCB issued BR No.15 on 21 October 1991 for 9% IRFC Bonds for Rs.180.99 crores for which no payment appears to have been made by BoK and no amount appears to have been received by MCB. On the same day BoK issued its own BR for a sale to Canfina for the same amount and this was credited to A.D. Narottam's account.

4. Similar irregularities have been noticed in the account of M/s.Excel & Co. as indicated below : -

(a) MCB issued BRs Nos.17 and 23 on 28 December 1991 and 26 February 1992 for 12% IDBI loan 2011 for an aggregate value of Rs.22.10 crores for which no payment appears to have been made by BoK and no amount appears to have been received by MCB. On the same day BoK issued its own BRs for sales to UCO Bank and Bank of Madura Ltd. for an aggregate value of Rs.22.10 crores and this was credited to M/s.Excel & Co.'s current account.

(b) MCB issued BR No.24 on 25 March 1992 for 12% IDBI loan 2011 for face value Rs.14 crores for which no payment appears to have been made by BoK and no amount appears to have been received by MCB. The BR received from MCB was used to cover the sale effected on 24 March 1992 to Bank of Madura Ltd. for Rs.13.50 crores and the sale proceeds were credited to Excel & Co.'s account.

5.(a) The securities transactions of BoK indicate that huge deposits were "created" in the current account of A.D. Narottam through sale of securities which were backed by BRs issued by BoK. These BRs were issued without backing of securities or were backed by BRs issued by MCB without backing of securities. An analysis of the deposits and withdrawals in the account for the period 1 April 1991 to 5 May 1992 to the extent details are available is summarised below :

(Rs. in crores)

	Party	Withdrawals (Outflow ofl funds)	Deposits (Inflow of funds)	Net Inflow	Net Outflow
1.	Hiten P. Dalal/ Andhra Bank	941.83	343.75	-	598.08
2.	Citibank	1024.80	906.40	-	118.40
3.	Standard Chartered Bank	912.04	1746.78	834.74	-
4.	ANZ Grindlays Bank	312.35	213.63	-	98.72
5.	Canfina, Canara Bank, Canbank Mutual Fund	1189.55	1410.25	220.70	-
6.	Bank of Karad	124.67	115.51	-	9.16
7.	Other banks and withdrawals by banker's cheques which could not be classified	1724.10	1607.80	-	116.30
8.	B.C. Devidas	74.93	4.42	-	70.51
9.	Gupta & Co./M/s.V.B. Desai/ Dhanraj Mills Pvt.Ltd.	4.55	14.82	10.27	-
10.	Excel & Co.	197.86	158.93	-	38.93
11.	Other withdrawals by personal cheques	22.63	7.89	-	14.74
		6529.31	6530.18	1065.71	1064.84

(b) Out of the total outflow of Rs.941.83 crores in favour of broker Hiten P. Dalal/Andhra Bank, as much as Rs.578.50 crores can be directly traced to the current account of Hiten P. Dalal in Andhra Bank. In addition, there are payments made to other banks, e.g. Standard Chartered Bank and Bank of America where the amounts may ultimately have been used by Hiten P. Dalal for his securities transactions with these banks. It is also seen that there is a net inflow of Rs.834.74 crores from Standard Chartered Bank and a net inflow of Rs.220.70 crores from Canfina, Canara Bank and Canbank Mutual Fund. This assumes significance when considered in the context of the fact that out of the total exposure of Rs.1470.12 crores in respect of outstanding BRs/SGL forms of BoK and MCB (referred to in the Committee's second report - paragraph II.3) the exposure of Canfina/Canbank Mutual Fund is Rs.538.28 crores and of Standard Chartered Bank is Rs.931.84 crores.

6. The scrutiny of Hiten P. Dalal's account with Andhra Bank is in progress. An analysis of the withdrawals by personal cheques (as opposed to banker's cheques normally used for security transactions) for the period 1 April to 31 October 1991 is given below :

	Paid to	Amount (Rs.in crores)
1.	ANZ Grindlays Bank	50.53
2.	Citibank	3.54
3.	Standard Chartered Bank	27.67
4.	Canfina	5.96
5.	Canbank Mutual Fund	129.92
6.	Self/miscellaneous withdrawals	1.50
7.	Brokers and individual parties	93.67

The payments by personal cheques could be for purchase of shares. Some transactions which can be identified are listed below :

(i) On 25 June 1991, a payment of Rs.21.07 crores was made to Canbank Mutual Fund for purchase of shares for a value of Rs.9.30 crores and debentures of a value of Rs.11.77 crores.

(ii) The total sales of shares by Canbank Mutual Fund to Hiten P. Dalal between 5 April 1991 and 30 October 1991 aggregated to about Rs.38 crores.

(iii) There are also a large number of transactions for sale/ purchase of shares between Hiten P. Dalal and ANZ Grindlays Bank.

VIII. Metropolitan Co-operative Bank Ltd. (in liquidation)

The Metropolitan Co-operative Bank Ltd. (MCB) is a licensed non-scheduled small urban co-operative bank with only one office in Bombay. This bank is not a member of the Indian Banks' Association (IBA). The bank has no authority to issue Bank Receipts (BRs). The BRs issued were not in the form prescribed by IBA. The other guidelines of IBA for issuance of BRs were also not followed by this bank.

2. MCB had issued BRs to Bank of Karad Ltd. (BoK) and Standard Chartered Bank and the constituents involved were Excel & Co. and Dhanraj Mills Pvt. Ltd. The modus operandi of the transactions according to the bank was as under :

"The representatives of the MCB viz. Vice Chairman and Accountant or Vice Chairman and Manager (Chief Executive Officer) /Officer used to go to the Security Department of BoK at Share Bazar or at the office of the Share Broker namely M/s.Hiten P. Dalal and receive the pay orders issued by either BoK or Standard Chartered Bank in favour of the MCB and issue BRs equivalent to the amount of the Pay Orders, indicating the sale of securities as detailed therein, and undertaking to deliver the securities at a later date. Even when the printed receipts state that securities will be delivered when ready, we have never received or delivered the securities and this work probably was handled by the clients themselves. The description of securities was written on the BRs as informally indicated by the concerned constituents/brokers who were also present on the occasion. At the same time, the MCB was also issuing a Pay order/s for an equal or nearabout amount to BoK. For this purpose, a requisition from the constituents was obtained in some cases directing the bank to issue the pay orders. The necessary entries in the ledgers were being made after returning to the bank. Although the pay orders received from BoK/Standard Chartered Bank were favouring MCB, the pay orders were credited to the current account of the above constituents on the basis of informal understanding. The return pay order issued by MCB on the same occasion was also indicated as by debit to the above current accounts of the constituents. The dealings in respect of Standard Chartered Bank were also taking place at the above premises of the BoK/Broker.

Further, there were also occasions when the BRs were issued without any exchange of pay orders or any other transactions. These were also done in the similar sittings at BoK on the informal advice of the constituents/BoK/Share Broker. While in the case of issue of BRs where exchange of pay orders had taken place, the bank had taken commission @10 paise per Rs.1,000 by debit to the constituent's current account, there was no such income in the case of issue of BRs without such exchange of pay orders/transactions. Some of such BRs did not indicate any amount or were indicated as "Free"."

3. The officials of the bank who used to attend the meetings and sign the BRs/banker's cheques/pay orders have not been given the power by the Board of the bank to sign such documents. The banks in whose favour the BRs were issued had also not objected to this practice.

4. The pay orders/banker's cheques issued by BoK and Standard Chartered Bank were exchanged simultaneously in the meeting with the BRs of the MCB. The BRs were however issued without holding any security on its portfolio. The accounts of the two constituents were credited thereafter. The funds so received were credited back to BoK.

5. The bank issued in all 30 BRs between 25 March 1991 and 5 May 1992 of which in 4 BRs the value of BRs has not been indicated but only the value of securities covered by the BR has been mentioned. The aggregate value of the BRs issued was Rs.1944.51 crores.

6. Of the 26 BRs, 11 BRs aggregating Rs.1305.36 crores were issued without having received any consideration. The bank has certified that this was done at the instance of the brokers viz. Sarvashri J.P. Gandhi, Manubhai, Abhay Narottam and T.B. Ruia. Of the 26 BRs, 17 BRs aggregating Rs.923.21 crores were issued favouring BoK and 9 BRs aggregating Rs.1021.31 crores favouring Standard Chartered Bank.

7. Of the remaining 4 BRs issued without indicating value, one BR was favouring BoK (value of security Rs.14 crores) and 3 were favouring Standard Chartered Bank (value of security Rs.156 crores).

8. As on 21 May 1992, 14 BRs were outstanding including the 3 BRs where the value of BR is not specified. The outstanding amount of the 11 BRs aggregated Rs.1245.71 crores of which 4 BRs for Rs.592.30 crores and 7 BRs for Rs.653.41 related to BoK and Standard Chartered Bank respectively. As per Standard Chartered Bank records 6 BRs were outstanding for Rs.534.20 crores. Of the 3 BRs outstanding where no value was specified one was favouring BoK (value of security shown as Rs.14 crores) and 2 were favouring Standard Chartered Bank (value of securities Rs.56 crores).

9. Though 16 BRs were received back by the bank, there was nothing on record to show whether the securities covered by these BRs have been fully delivered before they were retired.

IX. Syndicate Bank

It was mentioned in the first Report that out of Rs.622 crores repaid by the broker Harshad Mehta to SBI in April 1992 to cover the shortfall in its Investment account, Rs.47.76 crores had come from Syndicate Bank. On verification it has been found that the above payment was made by Syndicate Bank to SBI towards the purchase consideration of certain PSU bonds for an aggregate contract value of Rs.47.76 crores (face value Rs.50 crores) purportedly bought from SBI through Harshad Mehta. While making the payment, the bank had taken physical delivery of the allotment letters/bonds. However, though the counterparty named was SBI, Syndicate Bank did not have the relative sale contract in its books. Further, the above transaction does not appear as a sale in SBI's books, but it was evidently aware of the transaction as the above amount was collected and kept in SBI's books in sundry deposit account to be adjusted towards the shortfall. The above securities were sold by Syndicate Bank to ANZ Grindlays Bank on the very next day for an aggregate contract value of Rs.47.81 crores.

2. In a number of transactions done through the

broker Harshad Mehta, the transactions did not appear in the books of the counterparty bank. However, insofar as the bank was concerned, it received/made payments directly to the counterparty and issued/ received BRs/SGL transfer forms from the counterparty banks.

3. The bank commenced accepting funds for management under PMS on 4 November 1991. During the period November 1991 to June 1992 Funds Investment and Merchant Banking Department (FIM), Bombay and Bombay (Nariman Point) Branch of the bank accepted funds aggregating Rs.337.07 crores (Rs.134.22 by FIM and Rs.202.85 crores by Nariman Point branch), under PMS mainly from the public sector undertakings. Out of the funds of Rs.134.22 crores accepted by FIM, an amount of Rs.90.58 crores (or 67 per cent) was invested in equity shares purchased from Fairgrowth Investments Ltd. (FGIL) through Fairgrowth Financial Services Ltd. (FGFSL) and other brokers. Out of the shares purchased from FGIL through FGFSL, shares worth Rs.46.16 crores were still in the name of FGFSL and those for Rs.0.38 crore were in the name of FGIL.

4. At the Nariman Point branch where the bank had collected an amount of Rs.202.85 crores, practically the entire transactions have been routed through only one broker, viz. Kishore Narottamdas Amarchand (KNA). The ultimate beneficiary of the transactions done through KNA was however FGIL. Out of about Rs.200 crores invested in shares/bonds purchased from FGIL/FGFSL mainly through KNA, shares for Rs.21.04 crores were still in the name of FGFSL and FGIL. Majority of the transactions though apparently made on outright basis, appear to be on ready forward basis to recover the cost of funds made available to the broker/FGIL and FGFSL. In most of the transactions the broker has paid the differences. Though the underlying securities were purported to be PSU bonds/ shares, for all practical purposes these appear to be clean accommodation extended by the branch to FGFSL through the broker KNA. From the contract notes of the broker it is seen that he was having all the particulars of the PMS clients and was making sales/purchases in the individual accounts as if he, along with FGFSL and FGIL, was operating the PMS on behalf of the bank.

5. The bank was asked to undertake physical verification of the shares held by it and submit a statement. From the statement furnished by the bank, it is seen that there is a shortfall in shares of 28 companies to the extent of about Rs.1 crore.

6. The position of the securities held by the bank on behalf of PMS clients is as under :

		(Rs. in crores)
i)	Shares/bonds purchased from FGIL/FGFSL directly or indirectly	290.58
ii)	Shares/bonds standing in the name of the above companies	62.44
iii)	Shares termed as "bad deliveries"	59.73

X. Bombay Mercantile Co-operative Bank Ltd.

Between 2 August 1991 and 8 April 1992, Bombay Mercantile Co-operative Bank Ltd. (BMCBL) entered into 13 ready forward transactions in securities for an aggregate contract value of Rs.97.34 crores through broker M/s.Bhupen C. Devidas. The payments were made by pay orders issued in favour of Bank of India. In respect of the purchases, BMCBL has not deposited any SGL transfer forms nor does it have an SGL account with the PDO.

2. The details of these transactions are as under :

(Rs. in crores)

Security	Face Value	Amount	Date of Purchase	Date of Resale
11.5% GOI Loan 2007	5.00	5.19	2.8.91	10.9.91
11.5% GOI Loan 2007	10.00	10.39	8.8.91	10.9.91
11.5% GOI Loan 2007	3.00	3.12	12.8.91	17.9.91
11.5% GOI Loan 2010	5.00	5.11	19.8.91	4.11.91
11.5% GOI Loan 2010	10.00	10.31	18.9.91	22.10.91
11.5% GOI Loan 2010	10.00	10.46	4.11.91	28.12.91
11.5% GOI Loan 2011	5.00	5.23	8.11.91	19.12.91
12% GOI Loan 2011	10.00	10.24	3.1.92	17.2.92
12% GOI Loan 2011	4.95	5.08	8.1.92	28.2.92
12% GOI Loan 2011	2.97	3.05	13.1.92	24.3.92
12% GOI Loan 2011	4.45	4.62	12.2.92	28.2.92
12% GOI Loan 2011	10.10	10.49	17.2.92	24.3.92
12.5% GOI Loan 2007	14.00	14.05	8.4.92	5.5.92
	94.47	97.34		

3. On resale, BMCBL received payment through pay orders issued by Bank of Karad (BoK). BMCBL claims it has returned to Bank of India through the broker M/s.Bhupen C. Devidas the SGL forms received from Bank of India. There is no record in BMCBL of the receipt or subsequent delivery of the SGL forms.

4. In the books of Bank of India there is no record of the sale or purchase, or of the issue of the SGL transfer forms. The pay orders issued by BMCBL were credited in the current account of broker Haresh K. Dalal maintained with the Bombay Stock Exchange branch of Bank of India, on the basis of instructions received from BMCBL. These instructions are recorded in a letter which is not on BMCBL's letter-head but on a cyclostyled sheet. There is also no request in that letter to send the SGL form along with the contract note though such a request is included in other letters forwarding cheques.

5. In respect of 11 out of the 13 transactions, the payments made by the BoK are debited to the current account of broker M/s.Excel & Co. In respect of the other two transactions, the accounts to which such payments were debited are still to be ascertained.

6. It appears that through these transactions BMCBL has made available the funds to brokers though ostensibly the transactions were shown as being with Bank of India.

XI. The Nedungadi Bank Ltd.

On 3 March 1992 the Nedungadi Bank Ltd. had purchased 9% NPTC bonds of the face value of Rs.5 crores from Fairgrowth Financial Services Ltd. (FGFSL) at par, though the bonds at that time were available at a discount. Payment for the above purchase was made by the bank by means of a pay order in favour of ANZ Grindlays Bank with instructions to credit the amount to the account of FGFSL, against a security receipt dated 3 March 1992 issued by FGFSL. The bank is yet to receive the bonds from FGFSL. It is, however, holding photostat copy of Allotment Letter standing in the name of Andhra Bank Financial Services Ltd. (ABFSL) with a transfer form with ABFSL as the transferor and the bank as transferee. The original, duly signed by an official of the bank is stated to have been handed over to FGFSL for lodgement with NPTC. ABFSL has written to the bank to the effect that it has not so far received payment from FGFSL for its sale of the bonds to FGFSL. In the light of this claim from ABFSL, the bank has written to FGFSL that it is exercising its lien on fixed deposits of FGFSL worth Rs.5 crores with it.

The Bangalore branch of the bank was acting as a conduit for putting through call money transactions of FGFSL. The branch was entering into call money transactions on behalf of FGFSL by debiting the bank's account with RBI towards the proceeds of call money lent and splitting up the same and issuing pay orders in the names of different banks so as to avoid the disclosure of the true nature of the transactions. The pay orders for the credit of FGFSL's accounts with the bank and other banks were received and issued in the names of respective banks without mentioning the name of FGFSL, and they were routed through the special Clearing meant for inter-bank clearing settlement purposes only. Pay orders on behalf of FGFSL were issued by the branch against the pay orders received in the name of the bank on behalf of FGFSL, without routing the transactions through its current account.

XII. Functioning of the Public Debt Office

The Committee has in its first Report given its observations (paragraph 8) on the functioning of the Public Debt Office (PDO) and made certain recommendations (paragraph 9[9]) in respect thereof.

2. As a result of these observations and recommendations the RBI has introduced a computerised system for the processing of SGL transactions in the PDO. The Committee was informed that the system had been made operational for Central Government loans at Bombay and would be extended shortly to State Government loans. Thereafter it would be extended to the other major PDOs.

3. A demonstration of the system was made to the Committee and the Committee had also visited the PDO and observed the functioning of the system. The system as formulated incorporates substantially the recommendations of the Committee and in particular provides for :-

(a) prompt and immediate processing of SGL transfer forms and (b) despatch of the following statements to the individual SGL account holders, viz.,

(i) objection memos,

(ii) credit/debit advices to buyer/seller,

(iii) daily statement of details and balances in respect of transacted loans, and

(iv) weekly statement of loan-wise balances to SGL account holders (only banks and financial institutions) in respect of all Central loans.

XIII. General

1. Since the submission of the second Report of the Committee, the Inspecting Officers of the RBI assisting the Committee have collected further material on the irregularities in securities transactions in banks and financial institutions; in some cases, their scrutiny is almost complete and in the others, further scrutiny is continuing. A Joint Parliamentary Committee (JPC) has been appointed on 7 August 1992 to look into the securities transactions of banks and financial institutions. The terms of reference of the JPC cover substantially the ground envisaged by the terms of reference of this Committee. The Committee therefore feels that its continuing with further investigations would not only involve duplication of efforts but is also likely to hamper the work of the JPC. Besides, the work of the other investigating agencies is also in progress and all of them would need to draw, among others, upon the resources of the Departments of the Reserve Bank dealing with this work and have access to the same records and individuals in banks and institutions. The Committee therefore proposes to confine its future work to an examination of the findings of the scrutiny already undertaken by the RBI Inspecting Officers under the direction of the Committee and to report thereon.

2. The Committee feels that it may not be necessary nor will it be appropriate for it to examine one part of its terms of reference, namely, to fix responsibility for the malpractices and to recommend the action to be taken in respect thereof, as the JPC, by its terms of reference, will be examining this aspect. This term of reference has not as yet been examined by the Committee in detail and in any case, accessing the relevant records which are in the custody of or which are being examined by the other agencies and giving a hearing to the concerned individuals will be beset with delays and difficulties.

3. Shri Y.H. Malegam is a partner of the firm of Chartered Accountants which has carried out the audit of the Bank of America's Indian branches for the year ended 31 March 1992. He has therefore not participated in the enquiry into the transactions of that

bank or in the discussions of the Committee in respect thereof nor is he a party to Chapter V of this Report which specifically refers to the Bank of America.

R.Janakiraman
Chairman

Y.H. Malegam **V.G. Hegde**

C.P. Ramaswami **E.N. Renison**

Vimala Visvanathan
Member-Secretary

BOMBAY
23 AUGUST 1992.

ANNEXURE

Date	Security	Face Value (Rs.in crores)	Rate (as per books of BoA	Counter-party of selling bank	Amount indicated in the cost memo of selling bank	Amount paid by BoA	Broker at BoA	Difference in amount received from
20.4.91	8.75% IDBI 2001	2.1125	87.45	Standard Chartered Bank	2,07,52,509.09 (@ 97.4500)	1,86,40,009.09	NKA	*
1.6.91	11.5% GOI 2010	107.00	98.15	Citibank	112,44,40,002.44 (@101.00)	109,39,45,002.44	BCD	ADN's a/c. in BoK
23.10.91	8.25% IFCI 1995	18.0975	90.00	Standard Chartered Bank	17,65,55,711.50 (@95.3500)	16,68,73,549.00	BCD	*
-DO-	9% IDBI 1999	5.00	87.00	-do-	4,89,60,306.00 (@95.7000)	4,46,10,306.00	BCD	*
-DO-	7.5% IDBI 1997	20.00	84.00	-do-	18,53,71.489.67 (@90.6000)	17,21,71,489.67	BCD	*
8.11.91	9% IRFC 1998	25.00	91.00	Canfina	25,21,50,684.93	23,46,50,684.93 (@98.0)	NKA	HPD's a/c. in Andhra Bank.
14.12.91	11.5% GOI 2010	20.00	94.5218	Citibank	18,97,84,276.66 (@94.8200)	18,91,87,876.67	NKA	B.S.Gandhi's a/c.in Citibank.
10.1.92	11.5% GOI 2007	15.00	94.50	Grindlays Bank	15,33,46,100.00 (@99.9223)	14,52,12,650.00	NKA	Brisk Financial (NKA)

*In the case of Standard Chartered Bank, from the vouchers of the relative transactions it could not be ascertained as to from whom the difference amount was received.

ANNEXURE - I

Name of the bank	Amount and date of banker's cheque	Date of credit afforded to current a/c.	Date on which the instrument was sent for clearing	Closing balance as on the date of credit	Amount of over-drawings enjoyed otherwise
i) Bank of Karad	2,00,00,000 dt.20.5.91	18.05.1991	20.05.1991	74,11,849.75	1,25,88,150.25
ii) Bank of Karad	1,00,00,000 dt.5.7.91	05.07.1991	06.07.1991	11,18,912.60	88,81,087.40
iii) Grindlays Bank	86,62,500				
)Bank of Karad	75,00,000				
	1,61,62,500 dt. 6.11.91	06.11.1991	08.11.1991	1,05,61,410.54	56,01,089.46
iv) Standard Chartered Bank	2,37,29,755 dt. 13.11.91 However, credit was afforded for 1,50,00,000	13.11.1991	14.11.1991	10,13,695.56	1,39,86,304.44
v) Bank of Karad	7,00,00,000 dt. 4.12.91	04.12.1991	05.12.1991	3,98,17,538.10	3,01,82,461.90
vi) Standard Chartered Bank	8,80,95,890.41 dt. 16.12.91	16.12.1991	17.12.1991	4,92,41,104.92	3,88,54,785.49
vii) Bank of Karad	4,00,00,000 dt. 7.4.92	07.04.1992	08.04.1992	1,22,04,719.05	2,77,95,280.95

ANNEXURE - II

(Rs.in crores)

Deal	Date	Sale/ Purchase	Type of security	Face value	Rate	Counterparty	Broker	Terms of settle-ment	Profit
357	31.10.91	Sale	9% IRFC 1998	100	102.48	Andhra Bank	BCD	BR)	12.48
358`	31.10.91	Purchase	9% IRFC 1998	100	90.00	Andhra Bank	BCD	BR)	
359	31.10.91	Sale	Units	60	14.23	Andhra Bank	BCD	BR)	5.63
362	31.10.91	Purchase	Units	60	13.30	Andhra Bank	BCD	BR)	
932	27.11.91	Purchase	11.5% GOI 2011	300	95.00	Andhra Bank	BCD	BR)	12.36
933	27.11.91	Sale	11.5% GOI 2011	300	99.12	Andhra Bank	BCD	BR)	
4445	21.4.92	Purchase	11.5% GOI 2010	200	90.2	Andhra Bank	NKA	BR)	3.53
4446	21.4.92	Sale	11.5% GOI 2010	200	91.967	Andhra Bank	NKA	BR)	
4447	21.4.92	Purchase	11.5% GOI 2010	200	90.2	BoK	BCD	BR)	6.00
4448	21.4.92	Sale	11.5% GOI 2010	200	93.2	BoK	BCD	BR)	
4497	23.4.92	Sale	11.5% GOI 2010	250	93.09	Andhra Bank	VBD	BR)	6.97
4493	23.4.92	Purchase	11.5% GOI 2010	250	90.3	Andhra Bank	VBD	BR)	
4499	23.4.92	Purchase	12% GOI 2011	200	95.2	Andhra Bank	HPD	BR)	4.00
4500	23.4.92	Sale	12% GOI 2011	200	97.2	Andhra Bank	HPD	BR)	
4501	23.4.92	Purchase	12% GOI 2011	200	95.25	Standard Chartered Bank	HPD	BR)	4.50
4502	23.4.92	Sale	12% GOI 2011	200	97.50	Standard Chartered Bank	HPD	BR)	
4504	23.4.92	Purchase	11.5% GOI 2010	200	92.1	BoK	BCD	BR)	2.00
4503	23.4.92	Sale	11.5% GOI 2010	200	93.1	BoK	BCD	BR)	
1796	8.1.92	Purchase	Units	80	13.65	Grindlays Bank	C.Mac	BR)	2.40
1795	8.1.92	Sale	Units	80	13.35	Grindlays Bank	C.Mac	BR)	LOSS
1842	10.1.92	Purchase	11.5% GOI 2010	200	94.25	Citibank	C.Mac	BR)	3.00
1839	10.1.92	Sale	11.5% GOI 2010	200	92.75	Citibank	C.Mac	BR)	LOSS

Deals booked through HPD subsequently shown as "direct" in the bank's records.

ANNEXURE - III

Date	Purchase/ Sale	Security	Broker	Original counter-party	Substi-tuted counter-party	Face value (Rs.in crores)	Contract rate	Delivery rate	Difference amount (Rs.in crores)
8.10.91	Sale	13% NTPC	BCD	Canara Bank	Citibank	29	100.6546	96.500	1.21 @
8.10.91	Sale	13% NLC	BCD	Canara Bank	Citibank	24	100.8211	96.500	1.04 @
8.10.91	Sale	13% MTNL	BCD	Canara	Citibank	25	100.5705	96.500	1.02 @
15.11.91	Sale	9% IRFC	NKA	Canara Bank	Canfina	100	91.3758	95.430	4.05 *
11.3.92	Sale	9% IRFC	NKA	Canfina	Citibank	100	92.9431	91.050	1.89 @

@ Amount received from the broker.
* Amount paid to the broker.

Fourth Interim Report

March 1993

I. Introductory

1.1 Based on its examination of the securities transactions of banks/institutions and findings which could be derived therefrom, the Committee has so far submitted three Reports dated 31 May 1992, 5 July 1992 and 23 August 1992 to the Governor, Reserve Bank of India. This Report which is based on the scrutiny made to date by the officials of the Reserve Bank of India, details further findings in respect of the undermentioned banks/ institutions :

1. Standard Chartered Bank
2. Canbank Financial Services Ltd.
3. ANZ Grindlays Bank
4. Andhra Bank Financial Services Ltd.
5. State Bank of Patiala
6. Vijaya Bank

Aggregate Problem Exposure

1.2 In its second Report, the Committee had on the basis of its findings upto that date estimated the total problem exposure in securities transactions at Rs.3192.79 crores. In the light of its further findings detailed in this Report, the estimate of total problem exposures needs to be revised as under :

(Rs.in crores)

(A) Total value of investments made by banksand institutions for which they do nothold any securities, SGL transfer forms or BRs :			
(i) National Housing Bank		1271.20	
(ii) State Bank of Saurashtra		174.93	
(iii) SBI Capital Markets Ltd.		121.36	
(iv) Standard Chartered Bank :			
As per second Report	400.35		
Additional exposures as per items (a),(b) & (c) of paragraph 7 of Chapter II of this Report	110.26		
	510.61		
Less: Recovery as per item (f) of paragraph 3.3 of Chapter II of this Report	(4.00)	506.61	
(v) Canbank Financial Services Ltd. (Canfina) : As per items 5 to 10 of paragraph 2.1 of Chapter III of this Report		188.47	
			2262.57
(B) Total exposure against BRs/SGL transfer forms issued by Bank of Karad Ltd. or Metropolitan Co-operative Bank Ltd.			
(i) Canfina - as revised in terms of items 1, 2 and 3 of paragraph 2.1 of Chapter III of this Report	438.66		
(ii) Canbank Mutual Fund	102.97		
(iii) Standard Chartered Bank	931.84		
		1473.47	
			3736.04
(C) Other items- as per this Report			
(i) Standard Chartered Bank : - as per items (d), (e) and (f) of paragraph 7 of Chapter II	43.69		
(ii) Canfina : - as per item 4 of paragraph 2.1 of Chapter III	39.60		
(iii) Andhra Bank Financial Services Ltd. : - Securities found to be forged/fabricated as shown in paragraph 13(b) of Chapter V	205.12		
		288.41	
Gross problem exposure			4024.45

Notes :

(i) Standard Chartered Bank had reportedly received from broker M/s.Hiten P. Dalal securities at which a value of Rs.350 crores was initiall· 1. As shown in paragraph 6.1 and 6.2 of Chapte is a depreciation in the value of the PSU recorded above of atleast Rs.150 crores.

(ii) Against the securities found to be forge fabricated, Andhra Bank Financial Services Ltd. has received from Fairgrowth Financial Services Ltd. (FGFSL), securities of Rs.101.59 crores before FGFSL was notified under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992 and securities of Rs.112.29 crores after the notification.

(iii) The above gross problem exposure also does not include the depreciation/loss suffered by several banks/institutions by reasons of the fact that "ready-forward" transactions in securities could not be reversed (including on account of PMS and similar schemes) and the banks/institutions were left holding securities which had depreciated in value as also losses which may occur in settlement of matters which are in dispute.

II. Standard Chartered Bank

1. Standard Chartered Bank (Stanchart) has been an active player in the securities market.

Net Exposure

2.1 In the second Report of the Committee, the net exposure of Stanchart was provisionally placed at Rs.982.19 crores made up as under .

		(Rs.in crores)
(a)	Value of investments for which Stanchart does not hold either securities, SGL transfer forms or BRs	400.35
(b)	Value of BRs/SGL transfer forms held by Stanchart and issued by Bank of Karad Ltd. (BoK) and the Metropolitan Co-operative Bank Ltd. (MCB) for which those banks do not appear to have sufficient backing, whereof:	
	(i) issued by BoK	355.94
	(ii) issued by MCB	575.90
		1332.19
c)	Against this, the value of securities reportedly recovered by Stanchart from the broker M/s.Hiten P.Dalal (HPD) was placed at	350.00
	Net exposure	982.19

2.2 The details of item (a) of paragraph 2.1 above are given in paragraphs 3.1 to 3.4 below. The details of item (b) (i) of paragraph 2.1 are given in paragraph 4. The details of item (b)(ii) of paragraph 2.1 are given in paragraphs 5.1 and 5.2 and the details of item (c) of paragraph 2.1 are given in paragraphs 6.1 and 6.2.

2.3 The above net exposure needs to be revised in the light of the following :

		(Rs. in crores)
(a)	The additional exposures detailed in paragraph 7 below	153.95
(b)	The recovery of Rs.4 crores made by Stanchart as explained in item (f) of paragraph 3.3 below	(4.00)
		149.95

2.4 In addition Stanchart has absorbed a loss of approximately Rs.23 crores in respect of the assets left in its hands because of non-reversal of purchases under CCDS as explained in paragraph 10.9(d) below.

2.5 Finally, as explained in paragraphs 6.1 and 6.2 the title to the securities recovered from HPD is the subject matter of dispute and the value of these securities is at least Rs.150 crores less than the value of Rs.350 crores estimated in the second Report of the Committee.

Value of investments not supported by securities, SGL transfer forms or BRs

3.1 The details of the above exposure in respect of securities not received are as under :-

(a) 9% Power Finance Corporation bonds of the face value Rs.28.69 crores were purchased on 26-3-1992 from Andhra Bank Financial Services Ltd.(ABFSL) @Rs.94.95 for Rs.27.24 crores for which Stanchart paid Rs.24.36 crores (net of other items) to Andhra Bank for credit of broker HPD. According to ABFSL's letter dated 20-7-1992,

	(Rs.in crores)
the deal was cancelled.	27.24
(b) 13% NPC bonds of face value Rs.10 crores were purchased on 16-12-1991 @ Rs.84.00 from ABFSL and payment was made of Rs.8.81 crores (including interest of Rs.0.41 crore) to Andhra Bank which was credited to the account of the broker HPD. There is no record in ABFSL for this transaction. On 12-2-1992, securities of the face value Rs.8.5 crores were sold to Andhra Bank and on 9-5-1992, further securities of the face value Rs.0.5 crore were sold to Andhra Bank. No deliveries were effected for securities purchased or sold. The cost of the balance securities of Rs.1 crore is Rs.0.84 crore.	0.84
(c) On 19-2-1992, Stanchart purchased 9% IRFC bonds of the face value Rs.72.50 crores from Citibank for which it paid Rs.69.13 crores (excluding interest). It received Citibank BR No.47.On 4-3-1992, this BR was returned to Citibank in exchange for a fresh BR from Citibank for Rs.22.5 crores and Canfina BR No.1401 dated 30-12-1991 for Rs.50 crores issued in favourof Citibank. The BR from Citibank was redeemed on 26-3-1992 but no securities have been received against Canfina's BR in favour of Citibank for Rs.50 crores. The cost applicable to this BR is Rs.47.67 crores.	47.67
(d) Stanchart purchased from Citibank 11.5% GOI Loan 2009 of the face value Rs.42 crores and Rs.8 crores on 18-9-1991 and 19-9-1991 respectively for which Citibank issued BR Nos.091261140 and 0912621480 respectively. Stanchart paid against these BRs Rs.42.20 crores and Rs.8.03 crores respectively. The BRs are reported to have been returned to Citibank on 19-9-1991 duly discharged in exchange for two SGL transfer forms for Rs.44.58 crores and Rs.5.42 crores respectively.	

	(Rs.in crores)
The SGL transfer form for Rs.5.42 crores was honoured. However, the SGL transfer form for Rs.44.58 crores is an SGL transfer form dated 27.5.1991 issued by Canbank Mutual Fund (CBMF) in favour of Citibank which had already been dishonoured. The cost applicable to this BR is Rs.44.79 crores.	44.79
(e)(i) Stanchart purchased from Bank of America (BoA) on 24-1-1992,13% HUDCO bonds of the face value of Rs.13 crores @ 81.8898. A net payment of Rs.10.64 crores was made against this purchase, for which BoA issued its BR No.137 dated 24-1-1992. According to Stanchart, it returned this BR duly discharged to BoA in exchange for a CBMF BR to be delivered by BoA. Stanchart claims that the CBMF BR was not received. According to BoA the BR was delivered over the counter. The ischarged BR No.137 held by BoA bears the remark "exchanged against the CBMF BR received by us No.2309 February 18, 1992". BR No.2309 is available with CBMF duly discharged and bears the remark "Bonds delivered on 3.4.1992".	
(ii) Against this purchase of bonds of the face value of Rs.13 crores, there is a sale on 9.5.1992 of bonds of the face value of Rs.6.40 crores to Andhra Bank for which no delivery is effected and which transaction does not appear in Andhra Bank's books. The net cost for which securities are not delivered is therefore Rs.5.40 crores (F.V.Rs.6.60 crores). Reference is invited to paragraph 3.2 below.	5.40
(f)(i) On 3-3-1992, Stanchart purchased from Hongkong and Shanghai Banking Corporation (Hongkong Bank) 9% PFC bonds of the face value of Rs.5 crores @Rs.92.30. The cost of these bonds excluding interest of Rs.0.02 crore is Rs.4.62 crores. According to Stanchart there was no delivery of bonds against this purchase.	

(ii) According to Hongkong Bank, though the cost memo issued by it related to 9% PFC bonds, NLC bonds bearing Nos.PC.10088 to 10092, endorsed in blank were delivered to HPD, broker for Stanchart by Naresh K. Aggarwala & Co. (NKA) broker for Hongkong Bank. NKA's letter dated 30.6.1992 addressed to Hongkong Bank confirms this claim and states that the bonds were purchased from Andhra Bank who delivered NLC bonds in lieu of PFC bonds. However, Andhra Bank's cost memo No.2459 dated 3.1.1992 issued on behalf of the broker HPD to Hongkong Bank states that PFC bonds Nos.570250-299 dated 30.9.1991 for Rs.5 crores were enclosed with the cost memo. There is also a delivery order of HPD to Andhra Bank to deliver 9% PFC bonds to Hongkong Bank but no face value is indicated in the delivery order.

(iii)The 9% NLC bonds in question are in possession of Stanchart but it claims that these were purchased from Andhra Bank on 16.3.1992 @Rs.92. There is no cost memo from Andhra Bank towards this deal nor is the transaction reflected in Andhra Bank's books. Stanchart has paid Rs.4.63 crores on 16.3.1992 which amount has been credited to HPD's account in Andhra Bank. 4.62

(g)(i)On 7.8.1991, Stanchart purchased from CBMF 13% CIL bonds of the face value Rs.10 crores @Rs.93 and paid Rs.9.91 crores (including interest). CBMF issued its BR No.2591 dated 7.8.1991 to cover this purchase.

(ii)According to Stanchart, on 25.1.1992 it returned his BR to be replaced by Citibank's BR for Rs.7 crores and a fresh BR for Rs.3 crores.

(iii)According to CBMF, it issued a fresh BR No.2760 on 25.1.1992 for Rs.3 crores to cover the difference between the sales of Rs.28 crores (Rs.18 crores to Hongkong Bank against BR No.2214 and Rs.10 crores to Stanchart against BR No.2591) and purchases of Rs.25 crores from HPD through Andhra Bank. Incidentally, further verification shows that CBMF liquidated BR No.2214 by payment of Rs.18.60 crores and not by exchange of BRs.

(iv)HPD did not deliver bonds of Rs.25 crores against his sales but returned CBMF's BR No.2214 undischarged and BR No.2591 discharged by Stanchart.

(v)CBMF BR No.2760 for Rs.3 crores was liquidated by physical delivery on 2.2.1992. Stanchart had thus to receive delivery of bonds of face value of Rs.7 crores. On 13.12.1991 it sold bonds of face value of Rs.6.5 crores to Andhra Bank for which it did not effect delivery. This transaction does not appear in the books of Andhra Bank. Stanchart therefore has a net shortfall of bonds of the face value of Rs.0.50 crore whose cost is 0.46

(h) On 9.5.1992, Stanchart as per deal slip purchased units of Cantriple of face value of Rs.45.5 crores @Rs.58.50 per unit from Andhra Bank for an aggregate cost of Rs.266.18 crores. There is no record of this transaction in the books of Andhra Bank nor are there any cost memos available and no securities were received from Andhra Bank. On the same day, Stanchart as per deal slips sold PSU bonds aggregating Rs.266.12 crores to Andhra Bank. (Refer paragraph 3.4 below). There is no record of these transactions in the books of Andhra Bank and no securities were delivered. A pay order No.257131 for the difference of Rs.0.06 crore was prepared but not delivered to Andhra Bank. These transactions appear to have been put through merely to coverup a gap in respect of various earlier purchase deals for which neither securities nor BRs were available. The details of these

	(Rs.in crores)
earlier transactions are explained in paragraphs 3.3 and 3.4 below.	266.18
(i) On 27.11.1991, Stanchart purchased from BoK 13% NPC bonds of the face value of Rs.3.5 crores @Rs.90 for Rs.3.15 crores. Payment was made to BoK and credited in BoK to the account of A.D. Narottam (ADN). Stanchart has not received delivery but holds CBMF discharged BR No.2742 dated 18.11.1991 favouring ABFSL for the same bonds of the same face value.	3.15
	400.35

3.2 Reference is invited to item (e)(i) of paragraph 3.1 above. The transaction as appearing in the books of CBMF is as under;

(a) CBMF made the following purchases of 13% HUDCO bonds:

Date	Counterparty	Face Value (Rs.in crores)	B.R.No.
2.5.1991	Citibank	19	205
1.10.1991	Citibank	23	394
		42	

(b) CBMF made the following sales of 13% HUDCO bonds:

Date	Counterparty	Face Value (Rs.in crores)	B.R.No.
4.6.1991	BoA	13	2309
13.9.1991	Citibank	7	2475
1.10.1991	ANZ Grindlays Bank	23	2728
		43	

(c)The broker in all the above transactions was HPD. CBMF has claimed that on 3 April 1992, HPD brought back CBMF's BRs Nos.2309, 2475 and 2728 duly discharged by the respective banks and in turn CBMF returned to HPD BRs Nos.205 and 394 duly discharged. (However, according to Citibank, BR No.394 was exchanged against CBMF BR No.2451 dated 13 September 1991). It also made physical delivery to HPD of bonds of the face value of Rs.1 crore.

3.3 Reference is invited to item (h) of paragraph 3.1 above. The details of the purchases aggregating to Rs.288.90 crores (face value) for which neither securities nor BRs were available and which shortfall was covered up by the sale transactions recorded on 9 May 1992 (vide paragraph 3.4) are as under:

(a) On 13 March 1992 Stanchart purchased from ABFSL, 9% HUDCO bonds of face value Rs.25 crores for which it paid Rs.22.56 crores to Andhra Bank and which amount was credited to HPD's account in that bank. There is no such transaction recorded in ABFSL's books.

(b) On 26 February 1992 Stanchart purchased from ABFSL 9% NPC bonds of the face value of Rs.50 crores for which it paid Rs.42.52 crores. ABFSL issued a BR No.23728 dated 26 February 1992. According to ABFSL it delivered an original allotment letter against which it received back the BR duly discharged. According to Stanchart it holds only a photocopy of the allotment letter. ABFSL has written to NPC conveying its "no objection" to the bonds being issued to Stanchart and the matter is under correspondence.

(c)(i)On 27 January 1992, Stanchart purchased from ABFSL, 9% HUDCO bonds of the face value of Rs.75 crores. The transaction amount of Rs.68.68 crores was offset against some other sales and a net amount of Rs.0.0044 crore was received from ABFSL as per the voucher on record. No bonds or BR had been received by Stanchart. This transaction does not appear in the books of ABFSL.

(ii) On 26 March 1992 Stanchart sold 9% HUDCO bonds of face value Rs.83 crores to Canbank Financial Services Ltd. (Canfina). It gave to Canfina BR No.2724 dated 26 September 1991 for Rs.8 crores issued by CBMF leaving a balance of Rs.75 crores of bonds to be delivered. On the same day Stanchart purchased from Canfina 9% REC bonds of face value Rs.83 crores for which it did not receive delivery. The net cost of this shortfall of PSU bonds of Rs.8 crores is Rs.7.38 crores. This transaction does not appear in the books of Canfina and no payment was made. Difference of Rs.125.06 was debited to "commission on securities".

(d)(i) On 16 December 1991 Stanchart purchased from Hongkong Bank, 13% NPC bonds of the face value of Rs.16.5 crores @Rs.109.5317 for which payment of Rs.18.07 crores (excluding interest) was made. According to Stanchart it did not receive delivery. According to Hongkong Bank, the bonds had been purchased by it on 15 November 1991 from CBMF, for which it held CBMF's BR No.2751. This BR duly discharged was given to Stanchart through Hongkong Bank's broker NKA and Stanchart's broker HPD.

(ii)On 16 December 1991 Stanchart purchased 13% NPC bonds of the face value of Rs.0.5 crore from ABFSL for which it paid Rs.0.42 crore but for which it did not receive delivery.

(e) On 24 January 1992, Stanchart purchased from Bank of America (BoA) 13% HUDCO bonds of the face value Rs.13 crores. (Please refer item (e)(ii) of paragraph 3.1 above.) Against this purchase for which delivery was not received, the short delivery to the extent of Rs.6.40 crores was regularised through a dummy sale transaction.

(f) On 4 October 1991, Stanchart purchased 13% CIL bonds of the face value Rs.14 crores from Punjab National Bank (PNB). It received delivery of bonds of the face value Rs.10 crores and for the balance it holds BR issued by CBMF in favour of ANZ Grindlays Bank (Grindlays) and discharged in blank by the latter. The cost of these bonds of face value Rs.4 crores is Rs.4.04 crores (excluding interest) which has since been recovered.

(g)On 16 March 1992, Stanchart purchased 13% CIL bonds of face value Rs.13.5 crores from Hongkong Bank for which it has not received delivery. The cost of these bonds was Rs.13.37 crores (excluding interest). According to Hongkong Bank the bonds had earlier been purchased from CBMF for which it held CBMF's BR. This BR duly discharged was given to Stanchart through Hongkong Bank's broker NKA and Stanchart's broker HPD.

(h)(i) On 26 February 1992, Stanchart purchased from ABFSL 17% NPC bonds of face value Rs.50 crores for Rs.48.02 crores. According to ABFSL it issued its BR No.23727 which was returned duly discharged against delivery of the allotment letter. According to Stanchart, it only received a photocopy of the allotment letter.

(ii) On 19 October 1991 Stanchart purchased from BoK 11.5% GOI Loan 2007 of face value Rs.155 crores and 11.5% GOI Loan 2010 of face value Rs.114 crores. It simultaneously sold to BoK 11.5% GOI Loan 2011 for face value Rs.254 crores. It paid a net amount of Rs.1.13 crores which was credited in BoK to the account of broker A.D. Narottam. Against the purchase of 11.5% GOI Loan 2007 it sold to BoK the same security of face value Rs.131.50 crores on 11 December 1991 and Rs.9.50 crores on 10 December 1991 without effecting delivery. There remained therefore a balance of Loan of Rs.14 crores (transaction value Rs.13.54 crores) for which it has still to receive delivery.

(iii) On 25 January 1992 Stanchart purchased from ABFSL 11.5% GOI Loan 2010 for face value Rs.157 crores for which it did not receive delivery. Out of this Rs.7 crores was covered up by a purchase of Cantriple (refer item (h) of paragraph 3.1) leaving a balance of Rs.150 crores (refer item (c) of paragraph 5.2).

(iv) Purchases of face value of Rs.19 crores have not been identified.

3.4 Against the above transactions, the sale transactions presumably made on 9 May 1992 without delivery is for the following securities:

Securities	Face value (Rs. in crores)	Rate (Rs.)	Amount (Rs. in crores)	Whereof Interest (Rs. in crores)
(a) 9% HUDCO bonds	25	91	23.16	0.41
(b) 9% NPC bonds	50	91	46.40	0.90
(c) 9% REC bonds	83	91	76.37	0.84
(d) 13% NPC bonds	17	85	14.91	0.46
(e) 13% HUDCO bonds	6.40	85	5.54	0.10
(f) 13% CIL bonds	4.00	85	3.54	0.14
(g) 13% CIL bonds	13.50	85	11.89	0.42
(h) 8.25% GOI Loan 1995	90.00	93	84.31	0.61
	288.90		266.12	

BRs/SGL transfer forms issued by Bank of Karad Ltd.

4. The details of the exposure in respect of BRs/ SGL transfer forms issued by BoK are as under:

(Rs.in crores)

(a) On 8.1.1992 Stanchart purchased Units of the face value Rs.150 crores @ 13.40 per Unit and paid to BoK Rs.191.79 crores after adjusting a sale on the same day of Rs.9.21 crores for which it issued its BR No.1765. The amount was credited in BoK to the account of ADN. Stanchart holds BoK BR No.003513/ ADN dated 8.1.1992. 201.00

(b) On 14.10.1991 Stanchart purchased from BoK 11.5% IDBI bonds 2011 of the face value of Rs.50 crores @ 99.75. A net amount of Rs.0.24 crore (after adjusting other sales and purchases) was paid to BoK which was credited in BoK to the account of ADN. Stanchart holds BoK BR No.3455/ADN dated 14.10.1991. 49.88

(c)On 20.4.1991 Stanchart purchased 9% IDBI bonds 1999 of face value Rs.15 crores @95.50 and 8.75% IDBI bonds 2000 of face value Rs.10 crores @95.50 from BoK. An amount of Rs.22.64 crores was paid to BoK and credited in BoK to the account of ADN. It holds BRs Nos.3275 to 3278 issued by BOK. It sold the bonds to CBMF. After a series of transactions, Stanchart repurchased the bonds from IOB for Rs.23.88 crores and received back the BRs issued by BoK. 23.88

(d) (i) On 30.3.1992 Stanchart purchased 12.5% GOI Loan 2007 of face value Rs.335 crores for Rs.319.93 crores (excluding interest) for which it received from BoK BRs Nos.3571 and 3752 for Rs.250 crores and Rs.85 crores respectively. It made a net payment of Rs.17.99 crores (afteradjusting various other purchases and sales) to Andhra Bank though deals were with BoK. The amount was credited in Andhra Bank to the account of HPD.

(Rs.in crores)

(ii)On 6.4.1992 Stanchart sold to Bok, 12.5% GOI Loan 2007 of the face value of Rs.250 crores for Rs.225 crores (excluding interest) and returned back BoK BR No.3571.

(iii)BR No.3572 was replaced by SGL transfer form dated 18.4.1992 which was dishonoured. The cost applicable to this purchase of bonds of facevalue of Rs.85 crores is Rs.81.18 crores. 81.18

355.94

BRs/SGL transfer forms issued by Metropolitan Co-operative Bank Ltd.

5.1 The details of the exposure in respect of BRs/SGL transfer forms issued by MCB are as under:-

(a) (i) on 2.5.1992, Stanchart purchased from MCB 9% IRFC bonds of face value Rs.400 crores for Rs.385.95 crores and on the same day sold various GOI Loans of the face value Rs.399.50 crores for Rs.385.85 crores. The difference of Rs.0.10 crore paid by Stanchart to MCB is held by the latter in its Suspense account. For its purchases it holds MCB BR No.31 dated 2.5.1992 for Rs.189.20 crores (excluding interest) and MCB BR No.30 dated 2.5.1992 for Rs.189.20 crores (excluding interest). For its sales, it has not issued any BRs or SGL transfer forms.

(ii) The sale transaction is obviously designed to square off various purchases made earlier for which Stanchart did not have any securities or SGL transfer forms. These are detailed in paragraph 5.2 below. 378.40

(b) On 4.1.1992 Stanchart purchased

	(Rs.in crores)
from BoK Units of face value Rs.60 crores @Rs.13.30 for Rs.79.80 crores. It paid Rs.37.64 crores to BoK after adjusting its sale on the same day of 10% GOI Loan 2014 of Rs.50 crores face value for Rs.42.16 crores against which it returned BoK's BR No.3456 dated 14.10.1991. The amount was credited in BoK to the account of A.D.Narottam. Stanchart holds a MCB BR No.18 for Units of face value Rs.6 crores only instead of Rs.60 crores.	79.80
(c)On 6.4.1992, Stanchart purchased from BOK 6% GOI loan 1994 of face value Rs.125 crores and 6.25% GOI loan 1993 of face value Rs.125 crores. On 2.5.1992 as per the deal slips the bank sold 6% GOI Loan 1994 of face value Rs.75 crores and 6.25% GOI Loan 1993 of face value Rs.125 crores to MCB. A net payment of Rs.50 crores was made to BoK which was credited in BOK to the account of ADN. The bank holds a bounced SGL transfer form of MCB dated 6.4.1992 though MCB has no SGL account with the PDO of the RBI.	50.00
(d) On 22.2.1992, Stanchart purchased from MCB, 11 % IDBI bonds 2002 of the face value of Rs.20 crores for Rs.19.20 crores (excluding interest). The counterparty indicated in the deal slips was Citibank but the cost memos wereissued by MCB. Stanchart holds MCB BRs.Nos.21 and 22 dated 22.2.1992 though these are not recorded in the BR register. Payment was made to MCB and credited to the account of broker Excel & Co. On the same day, MCB transferred the amount of Rs.19.85 crores (including the above Rs.19.20 crores) to BoK though the voucher in MCB states that the pay order was to be issued in favour of Stanchart. In BoK, the amount was credited to the account of Excel & Co.	19.20
(e)On 28.12.1991, Stanchart purchased from BOK 12% ICICI bonds of 2011 of face value Rs.50 crores for Rs.48.50 crores (excluding interest). No payment was made but the amount was adjusted against amounts due from the broker H.P. Dalal. The bank holds MCB BR No.19 dated 14.2.1992.	48.50
	575.90

5.2 Reference is invited to item (a)(ii) of paragraph 5.1 above. The details of the purchases for which neither securities nor SGL transfer forms were available and which shortfall was covered up by the transaction recorded on 2 May 1992 are as under:

	Face Value (Rs.in crores)
(a) On 6.4.1992 Stanchart purchased from BOK 6% GOI Loan 1994 of face value Rs.125 crores. BoK delivered a bounced SGL transfer form of MCB for Rs.50 crores referred to in item (c) of paragraph 5.1 above.	75.00
(b) On 6.4.1992 Stanchart purchased from BOK 6.25% GOI Loan 1993 of face value Rs.125 crores.	125.00
(c) On 25.1.1992 Stanchart purchased from ABFSL 11.5% GOI Loan 2010 of the face value of Rs.157 crores. (Please refer to item h(iii)of paragraph 3.3 above). Out of this the loan of face value Rs.7 crores is covered up by the transaction recorded on 9.5.1992.	150.00
(d)(i) On 28.10.1991 Stanchart purchased from BOK 11.5% GOI Loan 2011 of face value Rs.92 crores for Rs.88.60 crores. After adjustment of various other purchases and sales a net amount of Rs.0.65 crore was paid which in the books of BoK was credited to the account of ADN. No delivery was effected.	
(ii) Between 14.1.1992 and 27.1.1992 Stanchart sold to Andhra Bank 11.5% GOI Loan 2011 of face value Rs.82.50	

(Rs.in crores)

crores without effecting delivery.

(iii)There remained therefore a shortfall of Loan of the face value of Rs.9.50 crores for which delivery was not effected.	9.50

(e)(i) On 28.10.1991 Stanchart purchased 12% GOI Loan 2011 of face value Rs.100 crores from BOK for Rs.100 crores. The payment for this was included in the net amount of Rs.0.65 crore paid to BOK as mentioned in (d) above. No delivery was effected.

(ii)On 23.1.1992, the same Loan of the face value of Rs.20 crores was sold to Andhra Bank and on 27.1.1992 Loan of the face value of Rs.40 crores was sold to ABFSL without effecting delivery.

(iii)There remained therefore a shortfall of this Loan of the face value of Rs.40 crores for which delivery was not effected.	40.00
	399.50

Securities recovered from Hiten P. Dalal

6.1 The details of the securities reportedly recovered by Stanchart from broker H.P. Dalal are as under :

Cantriple units of face value Rs.35.50 crores @ 58.50	206.00
Shares based on market value as on 16.10.1992	107.00
NCDs and third party BRs	37.00
	350.00

6.2 There has been a considerable depreciation in values since the above values were determined. Thus the market value of Cantriple units as on 15 February 1993 was only Rs.16 per unit. Therefore, on these units alone, there is a depreciation of nearly Rs.150 crores. There must be depreciation in the other investments also and therefore the realisable value of the investments recovered will be considerably lower than the figure of Rs.350 crores mentioned in paragraph 2.1. The title of Stanchart to these investments is also the subject matter of dispute.

Additional exposures

7. After the net exposure of Stanchart was provisionally determined in the second Report of the Committee, the following additional exposures have been identified :-

(Rs. in crores)

(a) On 10 March 1992, Stanchart purchased Cantriple units of the face value of Rs.25 crores from ABFSLat Rs.14/- for Rs.35 crores. Payment was made to Andhra Bank and credited to HPD's account by Andhra Bank. There is no cost memo available with Stanchart, nor is the transaction recorded in the books of ABFSL. Andhra Bank has on its record two delivery orders (Nos.12313 and 12314 dated 10 March 1992) from HPD asking Andhra Bank to receive the units from Canfina and deliver the same to Stanchart. It also has a copy of its letter dated 10 March 1992 addressed to Stanchart indicating delivery of a BR. According to Stanchart it has not received the units and it has filed a suit against ABFSL/Andhra Bank	35.00

(b) On 10 April 1992, Stanchart purchased Cantriple units of the face value of Rs.8 crores from Andhra Bank at Rs.20/- for Rs.16 crores, which was credited to HPD's account by Andhra Bank. Stanchart has not received delivery but it holds Canfina BR No.1730 dated 31 March 1992 issued in favour of Andhra Bank and duly discharged by the latter. Canfina has denied liability and claimed that it has already delivered the

(Rs.in crores)

units to Andhra Bank. The latter has also denied liability claiming that it has not received the units and that this was a "broker's" transaction in which it merely acted on the instructions of HPD and there is as such no privity of contract between it and Stanchart 16.00

(c) Stanchart had purchased from CBMF 11.5% GOI loan 2008 face value Rs.10 crores on 23.8.1991 for Rs.10.15 crores, Rs.7 crores on 26.8.1991 for Rs.7.11 crores and Rs.43 crores on 4.9.1991 for Rs.43.65 crores against which SGL transfer forms were submitted by CBMF. The SGL transfer forms for Rs.10 crores dated 23.8.1991 and Rs.43 crores dated 4.9.1991 were presented to the PDO on 19.9.1991 and bounced even after several re-presentations. For the purchase of Rs.7 crores on 26.8.1991 there were two separate SGL transfer forms of Rs.5.39 crores and Rs.1.61 crores dated 19.12.1991. The latter was presented to the PDO and honoured but the SGL transfer form for Rs.5.39 crores was presented only on 15.5.1992 when it bounced. The total cost of the purchases of face value Rs.58.39 crores for which Stanchart holds only bounced SGL transfer forms is Rs.59.26 crores. The matter is under dispute with CBMF. 59.26

(d) (i) On 10.2.1992, Stanchart purchased from Hongkong Bank, 9% IRFC bonds of face value Rs.27.50 crores for Rs.25.18 crores (exclusive of interest) for which it received BR No.1050 dated 10.2.1992. Stanchart has not received bonds against the BR.

(ii) According to Hongkong Bank, letters of allotment Nos.41-45 and 150, 152 and 170 had been delivered against the BR but the same duly discharged had not been returned.

(Rs.in crores)

(iii) According to Stanchart, the letter of allotment had been delivered by Andhra Bank in respect of its purchase on 27.3.1992 of bonds of the same value from Andhra Bank, the payment whereof has been credited to HPD's account with Andhra Bank. 25.18

(e) (i) On 24.4.1992 Stanchart had purchased 9% IRFC bonds of face value Rs.10 crores for Rs.7.60 crores from Hongkong Bank. It received through broker NKA letter of allotment No.0056 from Hongkong Bank. There is no cost memo from Hongkong Bank.

(ii) On 8.1.1992 Stanchart had purchased the same bonds of an identical value from Karur Vysya Bank Ltd. (KVB) for Rs.9.19 crores. The broker for KVB was again NKA. KVB issued a BR to Stanchart. Stanchart has not received bonds against the BR. KVB claims that it had delivered letter of allotment No.0056 to Stanchart through NKA, though it has not received the discharged BR from Stanchart. The broker acting for Stanchart was HPD. 9.19

(f) (i) On 20.1.1992, Stanchart had purchased 9% IRFC bonds of face value Rs.10 crores for Rs.9.32 crores from KVB for which KVB issued its BR. Stanchart has not received bonds against the BR. KVB claims it delivered allotment letter No.0016 through its broker NKA to Stanchart. The broker acting for Stanchart was HPD.

(ii) According to IRFC the bonds covered by the allotment letter have been received by IRFC for registration in the name of ABN Amro Bank. 9.32

153.95

Dealings with broker H.P. Dalal

8.1 A large number of the securities transactions of Stanchart were either with or on behalf of broker HPD. The transactions with HPD appear in the names of "routing" institutions like Andhra Bank, BoK, ABFSL, etc. but the payments and receipts are effected through HPD's account or ADN's account with Andhra Bank or BoK respectively. The transactions on behalf of HPD appear to be under an informal arrangement with HPD whereby Stanchart is assured a return on its funds outlay of 15% in respect of transactions in SLR securities and at call money rates or better in respect of non-SLR securities.

8.2 Under the informal arrangement, Stanchart at the direction of HPD bought securities from bank counterparties. The subsequent sales of these securities were negotiated by HPD and Stanchart made the sales at such negotiated prices to counterparty banks designated by HPD. A desired sale price was derived to assure to Stanchart the required return for the period it held the security and the difference between the actual sale price and the derived sale price was payable to or recoverable from HPD. The desired sale prices were computed on computer spread sheets.

8.3 The differences payable and recoverable were accumulated and the net recoverable amounts were periodically adjusted by artificial transactions and by differences between contract rates and delivery rates in genuine transactions. The artificial transactions were simultaneous sale and purchase transactions for the same face value and with the same counterparties but with differences between sale and purchase rates. To determine the differences and to keep control of the amounts payable and receivable, an informal diary was maintained by the dealer for SLR securities. The diary maintained by one of the dealers for some period is available. In respect of non-SLR securities no diary was maintained but the differences payable and receivable were maintained on the computer sheets referred to in paragraph 8.2 above.

8.4 It is believed that a similar arrangement also existed earlier with broker M/s.V.B. Desai. In the minutes of the Fund Committee meeting held on 20 February 1990, there is a reference to the fact that Stanchart "had sold Rs.200 crores of our SLR portfolio on a 'committed forward sale' basis at 15% p.a. for the rest of the year" and that "this was effectively a lending of Rs.200 crores at 15% p.a. till 31 December 1990 against SLR stocks". This suggests that Senior Management of Stanchart was aware of the arrangements with HPD and earlier with M/s.V.B. Desai.

8.5 The following is a summary of the entries appearing for the period from 11 January 1992 to 23 April 1992 in the diary maintained by one of the dealers.

Date		No.of transactions	Deficit	Surplus (Rupees in lakhs)	Balance
11.1.92	Balance b/f				(534.19)
14.1.92		1		3.41	3.41
					(530.78)
			"Recovered"		534.00
					3.22
17.1.92 to 28.1.92		27	578.51	398.67	(179.84)
					(176.62)
29.1.92	"Recovered 4/- on 7 and 1/2 G'teed Stock"				260.00
					83.38
29.1.92 to 8.2.92		26	2028.61	256.24	(1772.37)
	"11.5% GOI 2010 140 Crs. Bought at 94.7894 inputted in ZZZZ"				

Date	No.of transact-ions	Deficit	Surplus (Rupees in lakhs)	Balance
				(1688.99)
13.2.92 to 22.2.92	23	247.82	514.73	266.91
				(1422.08)
22.2.92 "11.5% GOI 2010 BB 980 @ 97.0879 SS 999 @ 96.6490 ZZZZ 19 @ 95.0060"				(398.90)
				(1820.98)
26.2.92	5	84.50	510.10	425.60
				(1395.38)
26.2.92 "Sheet attached SBI deals(G'teed)"				1549.33
				153.95
27.2.92 to 30.3.92	100	5855.63	1785.19	(4070.44)
				(3916.49)
30.3.92 "Recovered"				3015.00
				(901.49)
30.3.92	1		9.45	9.45
				892.04
31.3.92 "Recovered"				1000.00
				107.96
2.4.92 to 3.4.92	5	120.64	100.54	(20.10)
				87.86
6.4.92				(5000.00)
6.4.92 to 23.4.92	78	4528.73	3169.06	(1359.67)
				(6271.81)
23.4.92 "Recovered"				6300.00
				28.19

8.6 The entries appearing in the diary represent both (a) same day transactions when purchases and sales of identical securities and identical face values have been made on a single day and the difference is payable to or recoverable from HPD and (b) ready-forward transactions where purchases are reversed by forward sales after a period of time and there is investment of funds by Stanchart on which a guaranteed rate of return is earned by Stanchart.

8.7 An illustrative example of same day transactions appearing in the diary on 24 March 1992 is given below :

"7	STA	1999	4775	(88	(-)	91.51)	(167.60)
12	MSEB	2011	4000	(95	(-)	99.10)	(164.00)
7.25	IDB	1997	2500	(82.50	(-)	88.61)	(152.75)
12	ICI	2011	5850	(95.00	(-)	98.90)	(228.15)
11.5	GOI	2011	3800	(91.50	(-)	94.83)	(126.54)
9.5	GOI	2004	1700	(81.50	(-)	87.92)	(109.14)
7.25	IDB	1996	2838.38	(82.50	(-)	88.50)	(170.30)
9.5	GOI	2008	500	(79	(-)	82.78)	(18.90)
10	GOI	2014	2900	(78	(-)	83.94)	(172.26)
10.8	GOI	2008	1000	(87.50	(-)	93.75)	(62.50)"

The first figure in the brackets shows the sale rate and the second figure the purchase rate and the difference is recoverable from or payable to HPD.

8.8 An illustrative example of "ready-forward" transactions appearing in the diary on 8 February 1992 is given below :

" 6%	1993	14100	(90.60	(-)	94.3332)	=	(526.38)
11.5%	2009	5000	(96.50	(-)	96.1822)	= +	15.89
12 MSEB	2011	4000	(99	(-)	98.9678)	= +	1.29
9 Sta.	1999	4775	(91	(-)	89.2452)	= +	83.79
9.5	2004	(87.65	(-)		88.8572)	=	(20.52)
10	2014	(83.65	(-)		84.6933)	=	(30.26)
7.5 IDB	97	2500	(88	(-)	93.1570)	=	(128.93)
7.5 IDB	97	3000	(87.	(-)	92.8679)	=	(176.04)"

All the above transactions are transactions which originate with a purchase on an earlier date and are reversed by a sale on 8 February 1992. The first figure in the bracket shows the rate at which the sale is actually made whereas the second figure is the derived rate at which sale should have taken place in order to yield to Stanchart a return of 15%. The derived rates are computed on computer spread sheets which are available and which show how the rates are computed. When the actual sale rate exceeds the derived rate the difference is payable to broker HPD and is shown as a positive item. When the actual sale rate is lower than the derived rate the difference is recoverable from HPD and is shown as a negative item.

8.9 Some of the entries shown in the diary and reproduced in paragraph 8.5 above are detailed below:-

(a) On 29 January 1992, Stanchart sold to Citibank 7.5% IFCI bonds 1997 face value Rs.14.88 crores, 7.5% IDBI bonds 1997 face value Rs.6.45 crores and 7.5% IDBI bonds 1997 face value Rs.43.68 crores, aggregating to Rs.65.01 crores @Rs.91 as per the contract rate. However, Citibank made payment only @Rs.87. The difference of Rs.2.60 crores was received from HPD and adjusted against the accumulated difference due from him. Thus the amount of Rs.2.60 crores recovered from HPD was accounted for by booking an artificial profit on the sale to Citibank.

(b) On 26 February 1992, Stanchart booked 22 sales transactions with Citibank in respect of securities purchased on 26 February 1992, mostly from State Bank of India. The net difference between the sale rate and the purchase rate aggregated to Rs.15.4933 crores which was shown in the diary as due to HPD.

(c) On 30 March 1992, Stanchart purchased from BoK 12.5% GOI Loan 2007 of face value Rs.335 crores @95.50 and sold the same security of face value Rs.250 crores to Hongkong Bank and of face value Rs.85 crores to Credit Lyonnais at a contract rate of Rs.104.50, thus booking a profit of Rs.30.15 crores, which was used to reduce the aggregate amount recoverable from HPD as per the diary. As explained in paragraph 8.10(e) below, the delivery rates for this sale were lower and the difference was recovered from HPD.

(d)(i) On 31 March 1992, Stanchart purchased from Cochin Refineries and from its CCDS department 3.5 crores and 1.5 crores respectively units of Cantriple @ Rs.14.45 per unit. On the same day it sold the units to Andhra Bank on account of HPD @ Rs.16.45 thereby booking a profit of Rs.10 crores which was used to reduce the aggregate amount recoverable from HPD as per the diary.

(ii) However, in order to adjust the amount in the diary, Stanchart booked the sale only at Rs.14.45 per unit but passed the following dummy transactions [listed in sub-paragraphs (iii)and (iv) below] to record the excess receipt of Rs.10 crores from Andhra Bank.

(iii) It purchased and sold to Andhra Bank on the same day the following securities:

Security	Face Value (Rs.in crores)	Purchase rate (Rs.)	Sale rate (Rs.)	Difference (Rs.)	Profit (Rs.in crores)
11.5% GOI 2008	75	94.15	97.5543	3.4043	2.55
11.5% GOI 2009	25	94.05	98.05	4.00	1.00
11.5% GOI 2010	20	93.75	99.75	6.00	1.20
11.5% GOI 2011	40	93.20	95.20	2.00	0.80
11.5% HP 2009	25	94.05	98.05	4.00	1.00
12% AP 2011	10	97.00	100.00	3.00	0.30
					6.85

(iv) It sold to Hongkong Bank on the same day 8.25% GOI Loan 1995 of face value Rs.45 crores where the contract rate was Rs.99.50 and the delivery rate was Rs.93.50 thus yielding a difference of Rs.2.70 crores.

(v) The above amounts of Rs.6.85 crores and Rs.2.70 crores were adjusted against the excess amount of Rs.10 crores received from Andhra Bank by debit to HPD's account. The transactions for the balance of Rs.0.45 crore have not been identified.

(e) On 6 April 1992, Stanchart made the following simultaneous purchase and sale transactions:-

(i) it purchased 12.5% GOI Loan 2007 of face value Rs.250 crores at par from Hongkong Bank and sold the same to BoK at Rs.90 thus making a loss of Rs.25 crores;

(ii) it purchased 6.25% GOI Loan 1993 of face value Rs.125 crores at Rs.99.60 from BoK and sold the same to Bank of America at Rs.92.60 thus making a loss of Rs.8.75 crores;

(iii) it purchased 6% GOI Loan 1994 of face value Rs.125 crores at par from BoK and sold the same to Bank of America at Rs.87.00, thus making a loss of Rs.16.25 crores.

The aggregate loss of Rs.50 crores was shown in the diary as recoverable from HPD. This transaction is part of the series of transactions referred to in paragraph 8.10 below.

(f) On 23 April 1992, as per the diary, a sum of Rs.62.72 crores was recoverable from HPD. This is shown as cleared by a recovery of Rs.63 crores. This recovery was not made in cash but was part of certain transactions which are explained in paragraph 8.11 below.

8.10 (a) On 30 March 1992, Stanchart purchased from BOK 12.5% GOI Loan 2007 of face value Rs.335 crores @ Rs.95.50 for Rs.319.925 crores (excluding interest). However, the delivery rate was Rs.100 resulting in an excess payment of Rs.15.07 crores.

(b) On the same day, Stanchart sold to BoK the undermentioned securities, where the contract rates and delivery rates were as stated below:

Security	Face Value (Rs.in crores)	Contract rate (Rs.)	Contract Value (Rs.in crores)	Delivery Rate (Rs.)	Delivery Value (Rs. in crores)
9% HUDCO bonds	50	98.20	51.29	90	47.19
13% NPC bonds	45	98	44.68	90	41.08
9% IRFC bonds	183	95	182.02	90	172.87
13% CIL bonds	23.50	90	21.55	90	21.55
Units	18	14.9535	26.92	14.9535	26.92
9% NHPC bonds	8.29	90	7.83	90	7.83
			334.29		317.44

There was therefore a short receipt of Rs.16.85 crores.

(c) On the same day, Stanchart also made a simultaneous purchase from and sale to Andhra Bank of 9% IRFC bonds of face value Rs.100 crores where Stanchart made a profit of Rs.3 crores.

(d) All the above transactions were in fact transactions with HPD though recorded as transactions with BOK and Andhra Bank. For these transactions an amount of Rs.34.92 crores was due from HPD.

(e) On the same day, Stanchart purchased from BoK 12.5% GOI Loan 2007 of face value Rs.335 crores [referred to in item (c) of paragraph 8.9 above] and sold the same to the extent of Rs.250 crores to Hongkong Bank and Rs.85 crores to Credit Lyonnais. The contract rate was Rs.104.50 and the delivery rate Rs.100.00. There was thus a difference of Rs.15.08 crores which was also recoverable from HPD.

(f) The total amount recoverable from HPD was therefore Rs.50 crores. This amount was however received through a cheque issued by Reliance Industries Ltd.(RIL) on its overdraft/current account with Fort branch of Syndicate Bank.

(g) On 6 April 1992, the overdraft/ current account of RIL with Fort branch of Syndicate Bank shows a credit of Rs.50.16 crores representing a cheque received from BoK and debited to the account of ADN.

(h) RIL has volunteered the information that it had instructed HPD to buy 9% IRFC bonds of face value Rs.51.50 crores. HPD when sending his bill requested RIL to make payment of the purchase price of Rs.50 crores directly to Stanchart on behalf of HPD. As HPD failed to deliver the bonds, he was asked to refund the money with market yield equivalent to prevalent call money market rate.

(i) (i) On 6 April 1992, Stanchart purchased from BoK, 6% GOI Loan 1994 of face value Rs.125 crores and 6.25% GOI Loan 1993 of face value Rs.125 crores where the contract rates and delivery rates were as under :

Security	Face value (Rs.in crores)	Contract rate (Rs.)	Contract value (Rs.in crores)	Delivery rate (Rs.)	Delivery value (Rs. in crores)
6% GOI Loan 1994	125	100	125.00	87	108.75
6.25% GOI Loan 1993	125	99.60	124.50	92.60	115.75
			249.50		224.50
Interest			3.04		3.04
			252.54		227.54

(ii)On the same day, it sold to BoK, 12.5% GOI Loan 2007 of the face value Rs.250 crores where the contract rate and delivery rate were as under :

Security	Face value (Rs.in crores)	Contract rate (Rs.)	Contract value (Rs.in crores)	Delivery rate (Rs.)	Delivery value (Rs.in crores)
12.5% GOI Loan 2007	250	90	225.00	100	250.00
Interest			0.72		0.72
			225.72		250.72

For its purchases Stanchart had to pay Rs.227.54 crores to BoK and an additional amount of Rs.25 crores to the broker (excess of contract value over delivery value). For its sales Stanchart had to receive Rs.250.72 crores from BoK which included an excess payment of Rs.25 crores (excess of delivery value over contract value) which was payable to the broker. Thus Stanchart had to receive Rs.23.18 crores (Rs.250.72 crores - Rs.227.54 crores) from BoK and pay Rs.50 crores to the broker in settlement of this set of transactions. Stanchart paid to BoK Rs.50 crores which was credited in BoK to the account of ADN. Stanchart passed an entry in its books showing Rs.23.18 crores as receivable from BoK and debited P.O. Receivable Account which presumably would be cleared when the payment order was received from BoK. In fact, BoK did not issue any such payment order on that day.

(j) If all the transactions recorded in items (a) to (i) above are considered together with the transaction recorded in item (e) of paragraph 8.9 above, the following picture emerges :

(i) Stanchart had as on 30 March 1992 an amount of Rs.39.16 crores recoverable from HPD as per the diary maintained for SLR securities. It had other amounts recoverable for non-SLR securities. Stanchart presumably wanted to book a profit of Rs.50 crores before finalising its accounts for the year ended 31 March 1992. The transactions recorded in items (a), (b), (c) and (e) above were therefore entered into to book this profit of Rs.50 crores.

(ii) HPD paid this amount to Stanchart by utilising funds received from RIL for the purchase of IRFC bonds which he did not deliver.

(iii) On 6 April 1992, Stanchart made available to HPD through ADN Rs.50 crores. This amount was utilised by HPD to return the amount to RIL. This payment was entered in the books through the transactions recorded in item (i) above.

(iv) As the transactions recorded in item (i) above resulted in a loss, the loss was recorded in the diary on 6 April 1992 as recoverable from HPD. For this purpose, the transactions recorded in item (e) of paragraph 8.9 above were entered into.

(v) The profit booked on 30 March 1992 by Stanchart was in fact reversed on 6 April 1992. This loss together with other differences recoverable from HPD were finally cleared as per the diary through a recovery of Rs.63 crores in end-April 1992, which is discussed in paragraph 8.11 below.

8.11 Reference is invited to item (f) of paragraph 8.9 above regarding a recovery of Rs.63 crores from HPD shown in the diary regarding SLR securities. A similar recovery of Rs.14.85 crores is recorded as made for non-SLR securities. The details of these recoveries are as under:-

(a) On 3 April 1992, Stanchart had sold to BOK the under-mentioned securities:-

Deal No.	Security	Face Value (Rs.in crores)	Rate (Rs.)	BR No.	Date of BR
9492	13% NPC bonds	45	85	2136	3.4.92
9494	Units	18	15	2135	3.4.92
9495	13% CIL bonds	23.5	85	2137	3.4.92
9491	9% HUDCO bonds	50	88.35	Physical Delivery	

Payment for this sale aggregating to Rs.132.72 crores was received from BoK by debit to the account of ADN.

(b) On 28 April 1992, Stanchart repurchased the above securities from BoK (except that the face value of 9% HUDCO bonds repurchased was Rs.25 crores) at an aggregate value of Rs.107.31 crores. Against this purchase, HPD returned to Stanchart its original BRs and also made physical delivery of 9% HUDCO bonds of face value of Rs.25 crores. However no payment was made to BoK against this purchase, but the amount payable was credited to "P.O. Received Account" and not to "P.O. Issued Account" as would normally be made for purchases.

(c) Having thus created a credit of Rs.107.31 crores in "P.O. Received Account", dummy entries were passed to show a recovery from HPD of Rs.63 crores in respect of SLR securities and Rs.14.85 crores in respect of non-SLR securities as under:-

(i) In respect of SLR securities, there was a simultaneous purchase and sale of the following securities with Andhra Bank.

Security	Face Value (Rs.in crores)	Purchase Rate Rs.	Sale Rate Rs.	Difference Rs.	Profit (Rs.in crores)
11.5% GOI 2006	100	90	98	8	8.0
9.25% GOI 1992	100	90	100	10	10.0
8.25% GOI 1995	125	90	100	10	12.5
7.25% GOI 1992	125	90	100	10	12.5
11.5% GOI 2006	100	90	100	10	10.0
11.5% GOI 2008	125	90	98	8	10.0
					63.0

(ii) In respect of Non-SLR securities there was a simultaneous purchase and sale of the following bonds with ABFSL.

Security	Face Value (Rs.in crores)	Purchase Rate Rs.	Sale Rate Rs.	Difference Rs.	Profit (Rs.in crores)
9% IRFC bonds	100	84	89	5	5.0
9% HUDCO bonds	125	84	90	6	7.5
9% IRFC bonds	100	85	87.3506	2.3506	2.35
					14.85

(iii) The profit on the above transactions was debited to P.O. Received Account and set-off partly the credit created on that account.

8.12 Computer spread sheets for non-SLR Securities are available and the manner of operation in respect of such securities was similar to the operations in SLR securities.

8.13 Tentative figures of the differences determined in respect of transactions in securities and the recoveries made from HPD as collected by Stanchart for the period from January 1991 to May 1992 are as follows:

Type of Security	Differences as Computed	Differences as per Diary	Recoveries made
			(Rs. in crores)
SLR	213.38	212.37	213.86
Public Sector Bonds	97.80	97.55	97.02
Units	8.92	8.92	6.76
	320.10	318.84	317.64

8.14 At first sight it might appear that by providing a guaranteed return HPD suffered during the period from January 1991 to May 1992 a loss of Rs.317.64 crores. However on a closer scrutiny it will be seen that:-

(a) to the extent the transactions were with HPD himself (though booked in the names of other institutions like Andhra Bank, BoK, ABFSL, etc.) funds were in fact being lent to HPD at the guaranteed rate during the period between the purchase and the subsequent sale;

(b) to the extent transactions were with other counter-party banks, Stanchart was in fact carrying the broker's 'open position' as its own open position.

8.15 A scrutiny of the transactions in securities shows that in a large number of cases there were very large differences between the contract rates and the delivery rates. The transactions were booked at the contract rates but actual payments and receipts were at delivery rates, the balance of the payment or receipt being made good by the broker HPD or paid to the broker.

8.16 Several examples of such transactions have already been referred to earlier. A few more instances are given below:-

(a)(i) On 7 March 1992, Stanchart sold to Citibank 11.5% GOI Loan 2010 of face value of Rs.100 crores at Rs.97.25 as per cost memo issued by Stanchart and on record with Citibank. However Citibank made payment only at a delivery rate of Rs.95.25 and the difference of Rs.2 crores was considered by Stanchart as recoverable from HPD and debited to "Interbank P.O. Received Account".

(ii) On 12 March 1992, Stanchart sold to State Bank of India (SBI) 11.5% GOI Loan 2008 of face value Rs.50 crores. The contract rate was Rs.95.0675, but SBI made payment at Rs.99.0675. An excess payment of Rs.2 crores was therefore received.

(iii) On 12 March 1992, Stanchart sold to SBI 11.5% GOI Loan 2010 of face value Rs.43 crores. The contract rate was Rs.99.5211 but SBI made payment at Rs.98.8024. There was thus a short payment of Rs.0.31 crore.

(iv) The net excess amount of Rs.1.69 crores received from SBI was credited to "Interbank P.O. received account" and used to partly offset the debit of Rs.2 crores to the same account.

(b) On 14.12.1991, Stanchart purchased from SBI the undermentioned securities:

Security	Face Value (Rs.in crores)	Contract Rate (Rs.)	Contract Value (Rs.in crores)	Delivery Rate (Rs.)	Delivery Value (Rs.in crores)
11.5% GOI 2007	50	93.60	46.80	99.85	49.93
11.5% GOI 2008	50	92.75	46.38	99.00	49.50
11.5% GOI 2009	40	92.10	36.84	98.35	39.34
11.5% GOI 2010	100	92.50	92.50	98.75	98.75
			222.52		237.52

Stanchart made payment to SBI of Rs.237.52 crores and received the difference of Rs.15 crores from HPD by payment order issued by Andhra Bank but the accounting vouchers showed the amount as received from SBI.

(c) On 13 December 1991 Stanchart purchased from SBI the undermentioned securities:

Security	Face Value (Rs.in crores)	Contract Rate (Rs.)	Contract Value (Rs.in crores)	Delivery Rate (Rs.)	Delivery Value (Rs.in crores)
11.5% GOI 2007	50	94.85	47.425	99.85	49.925
11.5% GOI 2008	50	94.00	47.000	99.00	49.500
11.5% GOI 2009	60	93.35	56.010	98.35	59.010
11.5% GOI 2010	100	93.75	93.750	98.75	98.750
			244.185		257.185

Stanchart paid SBI Rs.257.185 crores and adjusted Rs.13 crores against the purchase on the same day from BoK of the following securities for which it did not make payment.

Security	Face Value (Rs.in crores)	Rate	Value (Rs.in crores)
9% HUDCO bonds	8	90	7.20
9% NLC bonds	5	90	4.50
13% NLC bonds	1.13	85.2091	0.96
			12.66
Interest			0.34
			13.00

Accounting Rules

9.1 Stanchart's Head Office had prescribed BR exposure limits for various banks on a net basis. However these were neither adhered to nor monitored. Thus:-

(a) In respect of BoK, the stipulated limit was as high as Rs.70 crores. Despite this, BRs were accepted far in excess of this limit and as mentioned in paragraph 2.1, Stanchart has an aggregate exposure on account of BRs issued by BoK of Rs.355.94 crores whereas the outstanding BRs issued by Stanchart to BoK aggregate to Rs.1.40 crores only.

(b) There was no limit prescribed for MCB. However, as mentioned in paragraph 2.1, Stanchart has an aggregate exposure on account of BRs issued by MCB of Rs.525.90 crores.

(c) There were no limits prescribed for Karur Vysya Bank Ltd. and National Housing Bank. However Stanchart had accepted BRs issued by these institutions to the extent of Rs.20 crores and Rs.100 crores respectively.

9.2 There were also overall holding limits in respect of SLR stocks on asset basis and on open position basis and on non-SLR stocks on asset position basis. However these limits were grossly exceeded and long and short positions were held in non-SLR stocks.

9.3 In October 1991, the bank discontinued maintaining a manual investment ledger which had indicated security-wise the balance after each deal. Thereafter only computer print-out is available which gives only end-day balance of securities held but does not indicate the break-up of such holdings between physical securities, SGL transfer forms and BRs.

9.4 There was no SGL shadow register and SGL transfer forms were issued without ensuring that there was sufficient balance in the SGL account or that credit had been afforded for SGL transfer forms lodged. Therefore as many as 78 SGL transfer forms issued by Stanchart between 1 December 1991 and 2 May 1992 bounced. Similarly 51 SGL transfer forms received by Stanchart and deposited during 4 January to 11 May 1992 also bounced.

9.5 In several cases delivery was effected against sales without receiving payment thereagainst. Similarly for purchases made, payment was made without receiving securities, or BRs or SGL transfer forms. Even where BRs were received, discharged BRs were handed over to the brokers to be exchanged against bonds but there was inadequate follow up to ensure that the bonds were in fact delivered to Stanchart.

9.6 On sale of securities, the accounting entries passed were to debit "pay order received account" and credit the "investment account". When the sale proceeds were received they were credited to the former account to clear the debit.

9.7 A scrutiny of the transactions shows that:-

(a) in a number of cases "pay order received account" has been debited when no pay orders have in fact been received on that date;

(b) on a number of days, the "pay order received account" showed debit balances;

(c) there is no record maintained of pay orders received nor are the pay orders identified in the vouchers.

9.8 This suggests that often sales were booked without the full sale proceeds being received and differences due from the broker HPD were being carried forward in "pay order received account". It is also clear that these differences though receivable from HPD as also similar differences in respect of purchases were shown in the vouchers as recoverable from the counterparty. A few examples are given below :-

(a) On 16 January 1992, Stanchart purchased from Hongkong Bank 12% GOI Loan 2011 of face value Rs.80 crores. The contract rate was Rs.96.55 but the delivery rate was Rs.99.55. Stanchart paid Rs.79.64 crores (excluding interest) to Hongkong Bank and showed as per the voucher a recovery of Rs.2.4 crores from Hongkong Bank but no recovery was in fact received from that bank.

(b) On 16 January 1992, Stanchart sold to Hongkong Bank, 8.25% IFCI bonds 1995 of face value Rs.15 crores @96.65 and 11.5% GOI Loan 2015 of face value Rs.68 crores @96.00 to Hongkong Bank. The delivery rates were Rs.90.65 and Rs.93.00 respectively. Stanchart received from Hongkong Bank Rs.76.84 crores (excluding interest). It recorded the difference of Rs.2.94 crores as received from Hongkong Bank though no recovery was in fact received from that bank.

(c) On 30 March 1992, Stanchart sold to Hongkong Bank, 12.5% GOI Loan 2007 of face value Rs.250 crores @Rs.104.50. The rate given on the relevant cost memo was only Rs.100 and delivery was made at that rate. The voucher records the difference of Rs.11.25 crores as received from Andhra Bank but Andhra Bank has not issued any cheque to Stanchart on that date.

(d) On 25 September 1991, Stanchart made the undermentioned sales :

Counterparty	Security	Face value (Rs.in crores)	Contract rate (Rs.)	Delivery rate (Rs.)	Difference (Rs.in crores)
Canara Bank	9.25% GOI 1992	12.50	101.60	99.60	0.25
Canara Bank	11.5% GOI 2006	12.94	102.62	101.00	0.21
Canara Bank	11.5% GOI 2002	15.00	103.00	100.00	0.45
British Bank of the Middle East	9.75% States 1998	43.00	98.60	95.60	1.29
					2.20

The voucher records Rs.2.20 crores as received from BoK - HPD but no cheque has been issued by BoK to Stanchart on that date.

(e) (i) On 23 October 1991, Stanchart sold to BoA the following securities :

Security	Face value (Rs.in crores)	Rate as per cost memo (Rs.)	Rate as per BoA (Rs.)	Amount recorded as received (Rs.in crores)	Amount actually received (Rs.in crores)
8.25% IFCI 1995	18.10	95.35	90.00	17.65	16.69
7.5% IDBI 1997	20.00	90.60	84.00	18.54	17.22
9% IDBI 1999	5.00	95.70	87.00	4.90	4.46
				41.09	38.37

The voucher records Rs.41.09 crores as received from BoA whereas the actual receipt was only Rs.38.37 crores. The difference of Rs.2.72 crores has been deducted from a net payment of Rs.3.61 crores due to BoK against certain other transactions.

(ii) The transactions against which the difference was adjusted are as under :

(a) Purchase of 11.5% GOI Loan 2011 of face value Rs.59 crores @Rs.95.73 (including interest) Rs.57.61 crores

(b) Sale of Units of face value Rs.40 crores @Rs.13.50 Rs.54.00 crores

Balance due from Stanchart	Rs. 3.61 crores
Difference adjusted	Rs. 2.72 crores
Net payment	Rs. 0.89 crore

Rs.0.89 crore was paid to BoK and was credited to the current account of ADN on 30 October 1991. There was no exchange of securities between Stanchart and BoK and the transaction is not recorded in the books of BoK.

9.9 There are a number of cases where investment transactions do not appear to be recorded in the books of accounts. A few such transactions are shown in subsequent paragraphs.

9.10 (a) On 10 April 1992, Stanchart bought Cantriple units of an aggregate value of Rs.75 crores from various banks and resold the same to other banks on the same day. All the transactions were through broker HPD. The details of purchases and sales are as under :

Purchases

Sr. No.	Deal No.	Counterparty	Face Value (Rs.in crores)	Rate (Rs.)	Total value (Rs.in crores)	Time of deal
1.	9706	Andhra Bank	8.00	20.00	16.000	2.30 p.m.
2	9707/9697	Grindlays	17.00	12.25	20.825	2.00 p.m.
3.	9691	Citibank	50.00	20.00	100.000	12.30 p.m.
			75.00		136.825	
Sales						
4.	9702	Union Bank	5.00	40.00	20.00	2.30 p.m.
5.	9701	Grindlays	10.00	15.00	15.00	2.30 p.m.
6.	9715-16	Grindlays	10.00	20.00	20.00	2.30 p.m.
7.	9717	Grindlays	5.00	20.00	10.00	2.00 p.m.
8.	9700	Canara Bank	5.00	20.00	10.00	2.45 p.m.
9.	9708	Canara Bank	10.00	15.00	15.00	11.30 a.m.
10.	9698	Bank of Madura	10.00	15.00	15.00	2.00 p.m.
11.	9709	Hongkong Bank (New Delhi)	10.00	15.00	15.00	12.30 p.m.
12.	9699	American Express	10.00	16.825*	—	
				15.000@	15.00	2.00 p.m.
			75.00		135.00	

* Contract rate @ Delivery rate

(b) It will be noticed that (i) the rates have on the same day varied from Rs.12.25 to Rs.40 per unit, (ii) even for the same counterparty rates have been different, and (iii) units have been bought from and sold to the same counterparty on the same day at different rates.

(c) Though several banks are mentioned as counterparties, in a number of cases payments and receipts have in the counterparty banks' books been credited or debited to brokers' accounts.

Thus:-

i) in respect of the purchase under item 1, the payment has been credited to HPD's account with Andhra Bank;

ii) in respect of the sale at item 4, the amount has been debited to the account of Jayantilal Khandwala & Sons. in Union Bank;

iii) in respect of the sales under items 5, 6 and 7, Rs.20 crores was debited to the account of Shri Harshat Mehta and Rs.10 crores was debited to the account of Enam Securities (Pvt.) Ltd. in Grindlays. The balance of Rs.15 crores was received not from Grindlays but from ABN Amro Bank and debited to the account of broker NKA.

iv) in respect of the sale under item 12, the payments by American Express Bank have been debited to the accounts of brokers Stewart & Co. and C.Mackertich.

(d) The purchase and sale transactions are not recorded in Stanchart's books though entries have been passed for the payments and receipts by debit and credit to Inter Bank P.O. Issued Account and Inter Bank P.O. Received Account respectively.

9.11 (a) On 19 December 1991, Stanchart purchased from ABFSL Units of the face value of Rs.13.5 crores @Rs.13.40 for a total value of Rs.18.09 crores. The amount paid was credited to HPD's account in Andhra Bank. On 23 December 1991, Stanchart resold this security to ABFSL at the same price and received Rs.18.09 crores through HPD's personal cheque.

(b) There is no record of the transactions in the books of ABFSL nor is there any record that security or BRs were delivered by ABFSL to Stanchart or returned back by Stanchart to ABFSL. This appears to be therefore a clean loan to HPD by Stanchart of Rs.18.09 crores for 4 days.

9.12 There are a number of instances where Stanchart had purchased/sold investment on which interest payments became due on the "interest due" dates but Stanchart/purchasing bank was unable to collect the interest because it did not have custody of the investments. However, the interest due has been funded by HPD. A few examples are given below :

(a) On 23 January 1992, Stanchart received from Andhra Bank a pay order for Rs.1.14 crores. In Andhra Bank's books this was debited to HPD's account. Out of this amount Rs.0.51 crore was used to fund half-yearly interest to British Bank of the Middle East on 9.25% GOI Loan 1992 of face value Rs.11 crores for which Stanchart had issued BR No.1595 dated 27 November 1991 to British Bank of the Middle East.

(b) On 25 November 1991, Stanchart received Rs.3.45 crores from HPD. Out of this, Rs.1.38 crores was used to fund the half- yearly interest on its purchase of 11.5% GOI Loan 2008 of face value Rs.24 crores from CBMF and Rs.1.49 crores was used for funding half-yearly interest on 11.5% GOI Loan 2008 of face value Rs.26 crores for which Stanchart had issued a BR to BoA.

(c) On 25 November 1991, Rs.2.37 crores was received from HPD and used to fund the half-yearly interest on the purchase of 11% Bihar Loan 2002 of face value Rs.43.15 crores from BoA.

(d) On 25 November 1991, Rs.2.56 crores was received from HPD to fund half-yearly interest on 11.5% GOI Loan 2009 of face value Rs.61 crores for which Stanchart had issued a BR to BoA.

9.13 The fact that interest on the above securities is paid by HPD seems to suggest that these transactions were not in fact supported by the existence of securities and were in fact merely financing transactions.

9.14(a) There were several "dummy" transactions in securities recorded merely to transfer profits between different securities viz. SLR securities, PSU bonds and

Units. For example, in the first three months of the budget year 1992, the performance was well below the budget in the SLR portfolio whereas it was well above the budget in the Units portfolio.

(b) Thus the following dummy transactions with Andhra Bank showing purchases and sales on the same day for identical securities and identical face value were recorded :-

Security	Face Value (Rs.in crores)	Purchase Rate (Rs.)	Sale Rate (Rs.)	Profit (Rs.in crores)	Profit Booked (Rs.in crores)
11.5%GOI 2008	75.00	94.15	99.15	3.75	3.64
11.5%GOI 2011	50.00	93.20	94.20	0.50	0.50
11.5%GOI 2010	100.00	93.75	96.25	2.50	2.50
11.5%GOI 2010	100.00	93.75	95.75	2.00	2.00
				8.75	8.64

The small difference between the notional profit and the profit booked arises due to the fact that for calculation of book profit, investments are accounted on a "first in first out" basis.

(c) Against the above transactions in SLR securities which yielded a profit of Rs.8.75 crores, the following dummy transactions in Units with Andhra Bank were also recorded:

	Face Value (Rs.in crores)	Rate (Rs.)	Total Value (Rs.in crores)
Purchases			
	100.00	14.90	149.00
	30.00	14.90	44.70
	110.00	14.80	162.80
	10.00	14.75	14.75
			371.25
Sales			
	50	14.55	72.75
	50	14.68	73.40
	70	14.45	101.15
	80	14.40	115.20
			362.50
	Loss		8.75
	Loss booked		8.67

(d) Thus a profit of Rs.8.75 crores was made in the SLR portfolio and compensated by a loss of Rs.8.75 crores in the Units portfolio.

9.15 (a) There are also instances where dummy transactions have been recorded to conceal the true extent of depreciation in securities.

(b) For example, in late March 1992, due to a coupon hike, the SLR portfolio would have shown a depreciation of approximately Rs.2.64 crores. To conceal this depreciation, 45 dummy deals were recorded for transactions with Andhra Bank in respect of 44 SLR securities for an aggregate face value of Rs.90.51 crores. The transactions were for purchase and sale of identical scrips at identical rates. Though there was no profit or loss in the transactions, there was a book loss because of Stanchart's accounting policy of calculating profit or loss by considering cost of investments sold on the "first in first out" basis. Thus the holding cost of investments was reduced and a net loss of Rs.2.44 crores booked as a trading loss. Consequently the depreciation in the portfolio was reduced from Rs.2.64 crores to Rs.0.20 crore.

Corporate Cash Deployment Service Scheme

10.1 In order to get round the RBI guidelines on Portfolio Management Scheme (PMS) which required that there should be a minimum "lock-in" period of 1 year for the amounts accepted, Stanchart devised a Corporate Cash Deployment Service Scheme (CCDS).

10.2 Under the scheme Stanchart presumably sold securities to clients with an implied agreement to repurchase them at the end of the specified period at an agreed rate which provided to the depositor an agreed rate of return. This was clearly indicated on

Stanchart's copy of the deal slip. For example, if the deposit was accepted for 46 days at an agreed rate of return of 17%, the deal slip would indicate in the bottom corner the notation "04617". These transactions were occasionally also in the form of bills sold to customers.

10.3 The funds received under the CCDS scheme were credited to "CCDS account" and the disbursements made out of such funds were debited to the same account. From copies of the deal slips, Stanchart has prepared a statement as at 31 March 1992 of the funds collected and outstanding under the scheme at Bombay of Rs.695.86 crores and the disbursement outstanding of Rs.771.85 crores, which shows an excess disbursement of Rs.75.99 crores. According to the financial accounts, the excess disbursement was Rs.76.57 crores. The difference of Rs.0.58 crores represented amount invested for compliance with SLR requirements.

10.4 The sources of funds are represented by deal slips recording sale of securities, bills, Units, commercial paper, etc. to the clients from whom funds have been collected whereas the disbursements represent purchase of such items. An analysis of the outstanding position as at 31 March 1992 shows the following over-bought or over-sold position for various types of securities.

Security	Purchased (nos.)	Sold (nos.)	Over-bought (nos.)	Over-sold (nos.)
13 % IPCL bonds	50,000	-	50,000	-
Units	150,900,000	123,812,020	27,087,980	-
9% IRFC bonds	8,870,000	8,380,000	490,000	-
13% CIL bonds	1,900,000	1,595,000	305,000	-
13% HZL bonds	2,600,000	2,370,000	230,000	-
Canpremium Units	21,000,000	20,650,000	350,000	-
17% Kotak NCD	3,000,000	-	3,000,000	-

10.5 If under the CCDS scheme there were genuine purchases and sales of securities, then in respect of the over-bought position, the securities should have formed part of Stanchart's investment portfolio on 31 March 1992 and in respect of over-sold position, Stanchart should have reduced the securities from its investment portfolio on that date. This does not appear to have been done as Stanchart has confirmed that the net debit balance of Rs.76.57 crores on CCDS account at Bombay office representing the excess of "disbursements" over "sources" has been grouped under "Other Inter-office adjustments (net)" forming part of "other assets".

10.6 There is no evidence to show either that the securities or bills were actually delivered to customers at the time of sale and received back at the time of purchase or that Stanchart was actually holding the securities or bills on behalf of customers; and no securities register appears to have been maintained.

10.7 It would therefore appear that the CCDS was only a facade for the receipt of deposits from customers on which interest was allowed at rates in excess of the maximum rates stipulated by the Reserve Bank. For funds obtained in this manner, Stanchart paid brokerage to parties (e.g. Anandini Financial Services, Professional Management Services Pvt.Ltd. etc.) which was in violation of RBI directives. Finally, the deployment of these funds under ready-forward purchase deals with non-bank clients including brokers, corporate entities, etc. was also in violation of RBI directives.

10.8 There were a large number of transactions with Shri Harshad Mehta and his associate concerns, e.g. Growmore Research and Assets Management Services Ltd. (GRAMS) and in many cases the resale by Stanchart was not made on the due date but the funds were rolled over by simultaneous sale and purchase transactions.

10.9 As in several cases, Stanchart was not in a position to reverse its purchase transaction with these parties but in fact had to reverse its sale transactions with its customers, it had to deploy its own funds. As at 2 December 1992, the CCDS account therefore showed a debit balance of Rs.283.15 crores representing its own funds so lying invested. The details of this balance and the underlying security held are as under:-

(a)

Date of Purchase	Counterparty	Security	Face Value (Rs.in crores)	Cost (Rs.in crores)	Security held
14.2.1992	GRAMS	13% NPC bonds	5.50	4.48	Canfina BR No. 1687 dated 20.2.1992 for Rs.5 crores and bonds Rs.0.5 crore.
17.1.1992	GRAMS	9% IRFC bonds	8.00	6.61	Bonds
13.2.1992	GRAMS	Canpremium	11.00	12.60	Canfina BR No. 190 dated 5.12.91/23.4.91
22.5.1992	PNB-GRAMS	17% PFC bonds	50.00	50.58	PNB BR No.164 dated 11.4.92.
10.4.1992	BoK	State Bank "MRIS"	1.25	1.58	Bonds
20.5.1992	SBI Caps	17% NTPC bonds	5.00	5.20	Bonds
20.5.1992	SBI Caps	13% NPC bonds	17.00	15.94	Bonds
27.3.1992	Kotak Mahindra	17% KOTAK NCD	15.00	15.00	Bonds - Direct Subscription
31.3.1992	-do-	17% KOTAK NCD	15.00	15.00	-do-
	Money & Investment Dept.of Bank	Cantriple	15.00	22.50	With M & I Dept
-	-do-	Cantriple	10.00	15.21	-do-
3.4.1992	Canfina	17% NTPC bonds	58.04)		
3.4.1992	Canfina	17% NTPC bonds	1.56)	62.25	
5.4.1992	Canfina	9% CIL bonds	4.00	3.85	Bonds
				230.80	

(b) In addition, Stanchart holds the following securities for which the cost is recorded but no further details are available.

Security	Face Value (Rs.in crores)	Cost (Rs.in crores)	
i) Canpremium units	10.00	11.10	
ii) Essar Gujarat NCD	5.00	4.85	
iii) UTI Master plus	0.15	0.43	
iv) GIC Rise II units	10.00	11.10	
v) 9% PFC bonds	2.00	1.90	
vi) Sahu Bros Saurashtra Ltd. NCD	5.00	5.55	
vii) 9% PFC bonds	4.00	4.27	
viii) 9% IRFC bonds	24.50	22.78	
ix) 9% PFC bonds	4.00	3.76	
x) 9% NPCL bonds	32.50	32.50	@
xi) Investment in CRR/SLR		1.78	
		100.02	

@ face value, as cost not available.

(c) Against the aggregate assets of Rs.330.82 crores, there are the following liabilities :

(i) Securities to be delivered against BRs issued:

Counterparty	Security	Face value (Rs.in crores)	Cost (Rs.in crores)
Canfina	Cantriple units	10.00	15.21
SBI Caps	9% NPC bonds	28.00	25.95
FGFSL	9% NPC bonds	1.50	1.37
			42.53
(ii) Amount held in Sundry Creditors Account			3.05
			45.58

(d) The net assets available therefore aggregate Rs.285.24 crores as against the debit balance in CCDS account of Rs.283.15 crores. These net assets were taken over as bank's "own" investments at book value. The loss so absorbed by Stanchart on this account is estimated at around Rs.23 crores.

10.10 On 30 March 1992, Stanchart sold on CCDS account 9% IRFC bonds of face value Rs.61.25 crores for Rs.55.18 crores to NHB, which represented a reversal of an earlier purchase from GRAMS. According to Stanchart, it had under instructions from Shri Harshad Mehta delivered bonds of face value Rs.80 crores to Canfina of which bonds of Rs.61.25 crores which were to be delivered to NHB were adjusted against a sale of bonds by NHB to Canfina. NHB has claimed that it has not received the bonds and the matter is in dispute.

Nexus between dealers and broker H.P. Dalal

11.1 Stanchart's dealers are believed to have been bailed out by broker HPD on occasions when they had incurred huge losses when dealing on Stanchart's account and did not want to report these losses to senior management. Some examples are given below:

(a) Towards the end of 1990,the dealers had made a potential loss of about Rs.2 crores on transactions in PSU bonds of face value of about Rs.50 crores. HPD acquired the total holding of Stanchart at cost, thus absorbing the loss of about Rs.2 crores.

(b) In July 1991, Stanchart had a forward position in Unitsof face value of around Rs.200 crores on which there was a potential loss of approximately Rs.10 crores to Rs.15 crores. HPD took over these Units at holding cost to Stanchart and thus took over this potential loss.

(c) Stanchart held in late March 1992, a forward "long" position in 11.5% GOI Loan 2010. There was a hike in the coupon rate announced by the Government on its new loans as a result of which there was a sharp drop in the market price of 11.5% GOI Loan 2010. Consequently Stanchart was left with a potential loss of around Rs.10 crores. HPD was reported to have had forward "short" positions in this Loan and he is stated to have picked up potential losses of around Rs.5 crores.

11.2 The transactions referred to in item (c) of paragraph 11.1 are explained below:

(i) On 21 March 1992, Stanchart completed the following transactions in 11.5% GOI Loan 2010 for which presumably it had forward contracts :

Face Value (Rs.In crores)	Rate (Rs.)	Total Value (Rs.In crores)	Counterparty
Purchases:			
25	96.77	24.1925	Hongkong Bank
25	97.30	24.3250	Bank of America
50	97.365	48.6825	Citibank
100		97.2000	
Sales:			
25	97.09	24.2725	Bank of Madura
25	96.84	24.2100	Bank of Madura
50		48.4825	
50	Net purchase	48.7175	

(ii) On 6 April 1992 and 18 April 1992 it completed the following further purchase transactions presumably against forward contracts.

Date	Face Value (Rs.in crores)	Rate (Rs.)	Total Value (Rs.in crores)	Counterparty
6.4.1992	100	97.18	97.1800	Canfina
18.4.1992	95	97.0263	92.1750	Deutsche Bank
	195		189.3550	

(iii) Thus, the aggregate purchases amounted to face value Rs.245 crores with a total cost of Rs.238.0725 crores giving a holding cost of Rs.97.17. With the coupon hike, the market price dropped to around Rs.91 and thereafter recovered to Rs.93. There was thus a depreciation of around Rs.4 per Rs.100 of face value, aggregating to approximately Rs.10 crores and HPD appears to have thus picked up the whole of the loss made by Stanchart as shown in (iv) below:

(iv) The above securities taken over by HPD are recorded in the dealer's diary and on sale the differences have been accumulated for HPD's account. The details of the transactions are as under:

Date	Face value (Rs.in crores)	Rate (Rs.)	Total value (Rs.in crores)
21.3.1992	45	97.35	43.8075
6.4.1992	100	97.18	97.1800
18.4.1992	95	97.0263	92.1750
	240		233.1625
			Average 97.15

11.3 The dealers were also under pressure from senior management to realise budgeted profits in securities transactions. These budgeted profits were far in excess of the returns which could normally be expected from investments in securities and therefore the dealers were dependent upon HPD to generate the extra profits through transactions which were in fact not the normal transactions in SLR securities.

11.4 As a consequence of the above, a close nexus appears to have developed between the dealers and HPD and the former were willing to accommodate HPD in a number of ways. In particular, the customary safeguards when dealing with securities appear to have been abandoned and the clear demarcation of responsibilities between the 'front'office and the 'back' office got diffused and consequently controls got weakened. Thus deal slips were sometimes endorsed "please release cheque first", and consequently payments were made without receipt of securities and HPD was allowed to deliver securities other than the security contracted for or to give BRs issued by banks other than the named counterparty. Similarly, discharged BRs were handed over to HPD without receipt of bonds and there was inadequate follow-up. Thus a 'hole' developed in Stanchart's investment portfolio with investments not being supported by securities, SGL transfer forms or BRs.

Conclusions

12.1 The findings detailed in earlier paragraphs clearly establish that Stanchart has been carrying on its securities transactions in total contravention of RBI guidelines and in violation of the norms of prudent banking. These contraventions include "ready-forward" transactions with "non-bank" counter parties and transactions other than in SLR securities.

12.2 A large volume of its transactions have been with or through broker HPD. These transactions have been under an arrangement whereby, in order to obtain a guaranteed rate of return on its investments, Stanchart has in fact totally surrendered its discretion regarding dealings in securities and has acted entirely under the directions of the broker. In this process, it has used its own funds to actually carry the "broker's" position in forward contracts. There is sufficient evidence to show that senior management were in fact aware of this situation.

12.3 There was a close nexus between Stanchart's dealers and HPD, and the dealers, in order to meet stiff budgetary targets, totally surrendered their independence and looked upon HPD to bail them out for huge losses which they incurred in the dealings in the bank's "own" account.

12.4 As a consequence of this loss of independence, the safeguards customarily used in securities transactions were abandoned. Thus payments were made in advance of receipt of securities and SGL transfer forms or BRs, discharged receipts were returned without receipt of securities and delivery was accepted of securities other than those contracted for and of BRs issued in favour of other banks. Inevitably this led to an ever-expanding "hole" in Stanchart's investment portfolio. To cover this "hole", the dealers entered into wholly fictitious transactions mainly involving the BoK and the MCB which transactions were not backed by securities or were backed by BRs of doubtful value.

12.5 Stanchart's investment and accounting records have been manipulated to camouflage the real arrangement with HPD and later to record the fictitious transactions to cover up the "hole" in Stanchart's investment portfolio. Thus, a number of dummy transactions have been recorded, transactions have been recorded at rates different from the rates at which transactions have actually taken place, and transactions have been recorded to hold back or book profits which profits have been later reversed.

12.6 Stanchart has collected huge amounts under the CCDS in total violation of RBI guidelines. This scheme appears to have been devised to get round RBI regulations both on interest rates on deposits and on PMS but the manner in which the scheme has been operated shows that funds collected under the scheme were in fact in the nature of deposits on which interest was paid at rates which exceeded the maximum rates specified in RBI guidelines.

12.7 As a consequence of its securities transactions, Stanchart has a net exposure estimated at Rs.1132.14 crores. This does not include the further exposure due to the fact that as explained in paragraphs 6.1 and 6.2 above, the title to the securities recovered from HPD is the subject matter of dispute and the value of the securities would be considerably lower than the value of Rs.350 crores assumed for calculating the exposure. In addition, Stanchart has had to absorb a loss of about Rs.23 crores in respect of purchases under the CCDS scheme where reversals were not honoured by the counterparties.

III. Canbank Financial Services Ltd.

1.1 The Committee in its second Report had made certain observations on the securities deals of Canbank Financial Services Ltd. (Canfina) a fully owned subsidiary of Canara Bank. The observations based on the further scrutiny carried out are furnished in the following paragraphs.

1.2 Canfina started its operations with effect from June 1987. Its activities consisted of Merchant Banking, Leasing, Hire-Purchase and Portfolio Management. Portfolio services were conducted through the Funds Department of the company, while the other services were conducted through its Merchant Banking Division.

1.3 Canfina started accepting funds from clients for portfolio management from August 1987. The Board of the company had approved the Portfolio Management Scheme (PMS) on 27 August 1987. Simultaneously, it also approved another scheme styled "Buying and Selling of Securities" on behalf of customers. While communicating this scheme to the branch offices, it was specifically stated that buying and selling of securities was "outside the purview of Portfolio Management and thereby RBI norms". The latter scheme was discontinued after March 1991 and in its place, another scheme known as "Corporate Investment Advisory Services" (CIAS) was adopted. The introduction of CIAS did not, however, have any specific approval of the Board of the company.

1.4 Funds placed with the company by customers with a minimum lock-in period of one year were classified under PMS, while funds placed with the company with a shorter lock-in period were classified under CIAS. In all other respects, the schemes were alike.

1.5 The aggregate funds accepted from clients during the period from 1 April 1991 to 20 July 1992 and amounts outstanding as on 20 July 1992 under the schemes were as under :

Scheme	No.of clients	Amount (Rs. in crores)	
		Accepted	Outstanding as on 20.7.1992
PMS	8	1089.31	940.85
CIAS	95	5262.09	1011.31
Total		6351.40	1952.16

Apart from PSUs, the customers placing funds with the company under the schemes included foreign and public sector banks and their subsidiaries, private companies, export houses, financial institutions and finance companies, Delhi Stock Exchange, a Co-operative bank, a grameen bank and also brokers.

1.6 Canfina had subscribed to bonds issued by certain PSUs on private placement basis and the PSUs in turn simultaneously placed funds with it under PMS/CIAS. From 1 April 1991 to 31 March 1992, it had so subscribed to PSU bonds on 10 occasions for an aggregate amount of Rs.2182.18 crores. An amount of Rs.2122.80 crores was placed with the company under PMS/CIAS.

1.7 In several cases, as per the company's records funds have been received by it by utilising the services of brokers. Significant amount of security transactions has been put through these brokers or with them as counterparty. It is also observed that brokers placing funds with the company and clients brought by brokers received better return than other clients. The return passed on to the clients was significantly high in certain cases.

1.8 The funds received under the schemes were deployed by way of bridge loans, ready forward transactions in Government securities, PSU bonds, Units of UTI, units of other mutual funds, mainly Canbank Mutual Fund (CBMF), shares and also placement of funds with the parent bank. The funds collected under the schemes were also lent at a rate of interest of 15% p.a.to other divisions of the company for their other operations. As on 30 June 1992, the amount so lent out of the funds collected under the schemes was Rs.219 crores.

1.9 Canfina had also kept large amounts in fixed deposit with Canara Bank. The instances noticed are given below :

Date of placement	Amount	Period	Rate of interest
12.1.1991	Rs.100 crores	90 days	8%
27.2.1991	Rs.200 crores	180 days	8%
30.11.1991	Rs.300 crores	180 days	11%

1.10 Canfina invested Rs.310 crores out of PMS/CIAS funds in various schemes floated by CBMF during 1 April 1991 to 31 March 1992. In return for the support given by Canfina, CBMF entered into Ready Forward (RF) purchase transactions in PSU bonds with Canfina. From 1 April 1991 to 20 July 1992, Canfina's sale of PSU bonds, NCDs and Government securities to CBMF amounted to Rs.2145 crores (FV) and purchases amounted to Rs.1930.05 crores (FV).

1.11 The various instruments (i.e. assets) in which PMS/CIAS funds were deployed as on 20 July 1992 are shown below :

Investment Avenue	Amount (Rs. crores)	Percentage to total
CBMF instruments	538.24	31.3
Units of UTI	498.82	29.0
Units of other Mutual Funds	31.20	1.8
Bonds/NCDs	480.34	27.9
Bridge loans/Inter-company deposits	33.90	2.0
Commercial Paper	1.65	0.1
Shares	133.75	7.8
GOI security	0.72	0.1
Total	1718.62	100.0

1.12 The company had not prescribed any specific documentation to be executed by the customers placing funds with it under the two schemes. Proposals for specific documentation were formulated in September 1989 but they were not implemented. Subsequently, the company started exchanging correspondence with the customers specifying terms of placement of funds such as amount to be placed, period, yield, etc. While in some cases the company had issued letters of offer containing its terms to customers, in other cases, it had responded to enquiries from customers. The customers' letters of acceptance were not on record in many cases. Several of the letters of acceptance which were on record did not specify the manner in which the funds were to be deployed. Under both the schemes, funds were accepted on the assurance of guaranteed returns and there was no documentation to indicate that the funds were accepted to be deployed at the risk of the customer. In fact, there were no instances where less than the assured return was paid to the customers. The manner in which the schemes were operated by the company amounted to acceptance of deposits for specified periods, the company being in a position to deploy the funds in any manner. There was no definite commitment to deploy the funds in the best interests of the customers. In the process, significant funds had been placed with the parent bank and also utilised by the company itself for its other operations at concessional rates.

1.13 The company did not comply with the following RBI guidelines in regard to the operations of the two schemes.

(i) Funds were accepted for a period of less than one year.

(ii) Funds were accepted with the promise of an assured return.

(iii) The acceptance and deployment of funds were without any risk to the customer.

(iv) No management fee was charged.

(v) Periodical reports were not made to clients regularly about funds received, securities tied up, untied balance, etc.

(vi) Securities were not evaluated periodically with reference to market rates. The depreciation on securities held under PMS/CIAS schemes was not passed on to clients.

(vii) Funds were deployed in other than permitted investments. For example, funds were deployed by way of bridge loans, placement with parent bank and utilisation of funds for other operations of the company.

(viii) A large number of forward/ready forward deals were undertaken in total violation of RBI guidelines. Securities were sold to CIAS clients on RF basis and repurchased on maturity at a higher rate, so as to create the agreed rate of return. Under CIAS scheme, funds accepted were ostensibly against sale of specific securities but securities were not physically delivered nor were BRs issued to the customers. There was no earmarking of specific securities with distinctive numbers for any individual customer or transaction. After 1 April 1992, the total PMS/CIAS funds were treated as tied up with a basket of securities, giving it the characteristics of a mutual fund.

1.14 There were serious deficiencies in the operation/control systems relating to the management of portfolio funds. Certain essential safeguards like fixing exposure limits, norms and procedures for investment of the funds, etc. were not stipulated. There was also no appropriate system of reporting. The entire operations relating to the portfolio management were left in the hands of the Chief Dealer and there was no regular monitoring system in position. Although certain powers were delegated to the Chief Dealer for undertaking deals, there was no system to ensure that the transactions were within the powers and were undertaken judiciously. The Chief Dealer routinely transgressed the delegated powers. The dealing and back-up operations were not separated. Back-up was reduced to merely generating computer records of the transactions and passing the accounting entries as indicated by the Chief Dealer and his staff without independent verification of the transactions with reference to basic documents like contract note, cost memo, movement of securities, etc. Decisions taken by the Chief Dealer on purchase/sale transactions were conveyed over phone to other offices for implementation; such oral messages were not followed up by written communication. Transactions were noted in the dealer's pad/memo only after they were completed. Entries in the dealer's pad and corrections/ alterations therein were not authenticated. No reasons were recorded for changing the name of the counterparty/broker/deal rates, etc. Deal rates did not correspond with contracted/market rates in many cases. Differential in deal rates was settled with/ routed through brokers.

1.15 The transactions detailed in subsequent paragraphs suggest that no proper internal control was functioning in Canfina. In particular, there was inadequate follow-up of outstanding BRs, short/excess payments and receipts to brokers, recovery of sale proceeds and improper functioning by the 'back-up' office. This is also confirmed in the report of the management audit (carried out during the period December 1991 to February 1992 by the ED's Secretariat of Canara Bank) and issued in July 1992. The internal audit function was entrusted to an outside firm of auditors but it appears a detailed audit of the company's Funds Department (which managed the PMS and CIAS) was not carried out. Surprisingly, the statutory auditors have in their report on the accounts for the year ended 31 March 1992 confirmed that the company had an internal audit system commensurate with the size and nature of its business, there existed a reasonable internal control system and that satisfactory records had been maintained for the company's transactions relating to its dealings in shares, securities, debentures and other investments.

2. Net Exposure

2.1 In its second Report, the Committee had estimated the problem exposure of Canfina at Rs.435.31 crores [vide paragraph II(3)]. This represented the cost to the company of acquisition of 26 crore Units of UTI which the Bank of Karad (BoK) could not deliver to it. In addition the SGL transfer forms issued by BoK for 11.5% GOI Loan 2008 of the face value Rs.25 crores had also bounced. The problem exposure of the company has now been computed at Rs.666.73 crores as shown on the next page. Thus there is a net increase of Rs.231.42 crores in the exposure.

2.2 Apart from the above problem exposures, there are a few items where the company would suffer losses.

(a) Canfina has incurred a loss of Rs.130.78 crores (provisional) on its PMS and CIAS schemes duringthe period from 1 April 1992 to 20 July 1992 made up as under:

		(Rs. in crores)
(i) Intercrest earned on securities	89.59	
Brokerage earned	1.75	
	91.34	
Guaranteed yield paid to clients	(128.11)	(36.77)
(ii) Loss incurred on sale of securities		(94.01)
		(130.78)

It may be noted that durintg the year ended 31 March 1992 Canfina had booked an income of Rs.43.48 crores on these schemes.

(b) On a physical verification of securities as of 20 July 1992 there was reportedly a shortfall between the book balance and the securities available of 70 lakhs Units showing a book value of Rs.10.99 crores and other securities having a book value of Rs.0.02 crores making an aggregate shortfall of Rs.11.01 crores.

(c) There is an outstanding claim from Stanchart for delivery of 9% IRFC bonds or reimbursement of Rs.87.06 crores in respect of two transactions undertaken on 27 September 1991 through broker HDP. Stanchart has served legal notice on Canfina (vide paragraph 12).

(d) Canara Bank went to the rescue of Canfina to improve its liquidity and purchased PSU bonds/ CBMF units from Canfina during the period 20 May - 8 July 1992, as shown on page 130 :

Net exposure of Canfina (para 2.1 page 128)

Sr. No.	Dues from	Particulars	Amount of exposure (Rs.in crores)	Remarks	Vide para-graph
1.	Bank of Karad	7 crore Units-64	110.25	Non-receipt of securities. The amount shown against each item represents the cost of acquisition of the relative securities to the company for settling the transaction which it had in turn entered into on the basis of BR/SGL issued by BoK.	12
2.	-do-	19 crore -do-	299.25		
3.	-do-	11.5% GOI 2008 (F.V.Rs.25 crores)	29.16		
4.	Hiten P.Dalal (HPD)	Cancigo (F.V.Rs.33 crores)	39.60	Although the company holds the Cancigo Certificates, these stand in the name of ABFSL and Andhra Bank and the securities are not transferable.	10
5.	Andhra Bank Financial Services Ltd. (ABFSL)	Canpremium (F.V.Rs.12 crores)	15.60	Holding BR of Citibank discharged by ABFSL.	12
6.	Stanchart/ HPD	i) 13% DVC Bonds (F.V.Rs.28.5 crores) ii)13% HPF bonds (F.V.Rs.5 crores)	32.24	The company does not have any BR or security	12
7.	Hongkong Bank/ CBMF/N.K. Aggarwala(NKA)	13% CIL bonds (F.V.Rs.18 crores)	18.60	The company does not have any BR or security.	12
8.	Ashwin Mehta	Share deals	27.90	Non-receipt of shares/sale proceeds.	9
9.	Hiten P.Dalal	-do-	21.06	-do-	9
10.	Pallav Sheth	-do-	73.07	-do-	9
	Total		666.73		

(Rs. in crores)

Bonds sold by Canfina	Face Value	Rates at which sold	Consideration received (excluding interest)
9%	931.28	91.3666	850.87
10%	8.50	104.3500	8.87
13%	503.79	89.7386	452.10
17%	263.00	97.5468	256.55
CBMF Units			
Candouble	54.00	226.62	122.37
Canpremium	156.00	139.44	217.53
Canstar	75.00	195.88	146.91
	1991.57		2055.20

The securities were purchased by Canara Bank on the express understanding that any loss/depreciation in the value of the securities suffered by the bank was to the account of Canfina. Since the value of these bonds/units has shown significant depreciation, Canfina will have to bear the burden of depreciation/loss estimated at Rs.181.03 crores for the bonds alone.

(c) As on 20 July 1992, Canfina held PSU bonds of the face value Rs.354.63 crores (Book value Rs.337.71 crores) as shown below. Depreciation estimated at Rs.63.67 crores in these bonds too will have to be borne by Canfina.

Bonds held by Canfina

(Rs. in crores)

	Face value	Book Value
9% bonds	118.03	107.42
10% bonds	14.81	15.53
13% bonds	178.24	169.37
14% bonds	38.55	40.30
17% bonds	5.00	5.09
	354.63	337.71

3. **Short sales of securities**

3.1 Canfina had on a number of occasions, made short sale of securities. Such sales had also, often been undertaken when it was already holding an oversold position in the relative security. During 1991-92, oversold position was observed in respect of 29 securities on various days. The table on page 131 shows the extent and the number of days the security had remained oversold.

3.2 The transactions were invariable on buy-back basis and put through on the basis of issue of Bankers' Receipts which were in effect not backed by any security, thus violating RBI guidelines. This facilitated the company raising resources on clean basis to meet its commitments to CIAS clients and to buy back the securities sold.

3.3 As on 20 July 1992, oversold position persisted in nine securities to the tune of Rs.127.63 crores (Face Value) as shown on page 131.

3.4 In respect of securities mntioned at Sr Nos. 1 to 4, 6 and 8, the oversold position arose when the company sold securities to its parent bank. In respect of securities at 5 and 7 the oversold position was due to the sales effected to CBMF. These transactions

The oversold position of Canfina during 1991-92 (para 3.1 page 130).

Sr. No.	Name of security	Oversold Position (Face Value) Minimum (Rs.)	maximum (Rs.)	Total no of days the security remained oversold
1.	Units - 1964	1,48,200	5,79,48,200	28
2.	9% HUDCO 4/3	7,30,47,000	59,30,47,000	8
3.	9% IRFC 1/4	3,47,13,000	66,91,87,000	9
4.	9% IRFC 15/1	6,58,60,000	1,28,10,00,000	12
5.	9% IRFC 1/7	1,50,70,000	61,50,70,000	15
6.	13% cil 15/2	9,25,00,000	20,00,00,000	48
7.	13% MTNL 18/2	4,50,30,000	50,51,30,000	13
8.	17 MTNL 10/2	30,00,00,000	1,10,00,00,000	12
9.	13% NPC 4/4	82,00,000	26,82,00,000	12
10.	13% NPC 23/2	1,74,65,000	57,04,65,000	11
11.	9% NTPC 1/1	4,75,000,000	54,25,00,000	8
12.	9% PFC 27/6	20,000	51,00,00,000	9
13.	9% PFC 9/4	2,00,00,000	28,00,00,000	17

The oversold position of Canfina as on 20 July 1992 (para 3.2 page 130)

Sr. No.	Name of security	Oversold to the extent of (Face Value) (Rs.)	Oversold position reversed Date of repurchase	Amount
1.	9% HUDCO 4/3 BONDS	9,30,47,000.00	13.8.1992	8,52,76,940.00
2.	9% HUDCO 19/2 BONDS	9,000.00	1.10.1992	9,142.100
3.	9% NPTC 10/3 BONDS	18,000.00	@	18,207.15
4.	13% MTNL 18/2 BONDS	51,30,000.00	13.8.1992	47,01,041.80
5.	13% NHPC 1/1 BONDS	36,00,00,000.00	@	30,60,15,398.15
6.	17% MTNL 10/2 BONDS	2,40,000.00	@	2,49,424.80
7.	17% NPTC 10/3 BONDS	11,00,30,000.00	@	10,74,45,773.20
8.	17% NTPC 22/1 BONDS	11,18,72,000.00	13.8.1992	10,92,70,617.15
9.	17% NTPC 31/3 BONDS	59,60,00,000.00		59,60,00,000.00
	TOTAL	127,63,46,000.00		120,89,86,544.35

@ Delivery outstanding

were apparently undertaken with the intention to raise money to meet its commitments to its CIAS clients.

3.5 The manner in which Canfina continuously oversold the securities can be illustrated by the following summary of transactions in 13% NHPC bonds (item 5 above).

Date	Counterparty	Purchase (Rs.)	Sale (Rs.)	Balance (oversold)
6.5.92	Opening balance			28,99,25,000
11.5.92	CBMF		70,00,00,000	(41,00,75,000)
13.5.92	Bank of America(BoA)	18,00,00,000		(23,00,75,000)
15.5.92	BoA	23,00,00,000		(75,000)
21.5.92	Canara Bank		40,00,00,000	(40,00,75,000)
2.6.92	CBMF	6,00,00,000		(34,00,75,000)
4.6.92	CBMF	2,00,00,000		(32,00,75,000)
6.6.92	Canara Bank	19,99,25,000		(52,00,00,000)
8.6.92	CBMF	1,00,00,000		(51,00,00,000)
10.6.92	CBMF	10,00,00,000		(41,00,00,000)
8.7.92	Canra Bank	40,00,00,000		(1,00,00,000)
9.7.92	Peerless General Finance & Investment Co.Ltd.		40,00,00,000	(41,00,00,000)
20.7.92	Canfina's Investment Account	5,00,00,000		(36,00,00,000)

Even though these bonds had been oversold to Peerless General Finance and Investment Company Ltd. (PGFIC), it appears delivery was made to PGFIC out of Canara Bank stocks and the oversold position is being reflected in Canfina as bonds remaining to be delivered to Canara Bank.

3.6 The outstanding commitment to Stanchart (item No.9 above) arose out of a sale on 3 April 1992 for which Canfina's New Delhi Office issued two separate unnumbered BRs for Rs.58.04 crores and Rs.1.56 crores respectively against cheques for these amounts received from Stanchart. These amounts were treated by Canfina as monies received under CIAS to be returned in the first week of July 1992. The sale of securities was not recorded in the books and entries for the sale were passed only as of 20 July 1992 as of which date a special account of PMS and CIAS schemes was prepared.

4. Funding transactions

4.1 Between 1 April 1991 and 20 July 1991, Canfina made 13 payments aggregating to Rs.134.75 crores presumably for the purchase of 14% Non-Convertible Debentures (NCDs). In respect of these presumed purchases :-

(a) there is no indication of the name of the company which issued the debentures;

(b) there are no deal slips, contract notes or cost memos;

(c) the transaction list gives no details of securities or BRs received;

(d) there are only notings in the dealer's pad and physicals register in some cases suggesting that these were treated as "ready-forward" transactions and specifying the date on which the transaction had to be reversed.

There is therefore no evidence to show that these transactions were infact supported by under-lying securities.

4.2 In respect of six of these transactions, the payments were directly made to brokers through Canara Bank. The details of these payments are as under :

Sr. No.	Date of remittance by Canfina	Amount (Rs.in crores)	Name of the broker to whom paid	Canara Bank branch on which Inter Branch Advice (IBA) was drawn
1.	16.8.1991	1.00	Rehlan & Co.	Janpath, New Delhi.
2.	4.12.1991	0.35	-do-	-do-
3.	28.1.1992	4.90	V.B.Desai/ Andhra Bank	F & I Division Bombay
4.	28.1.1992	24.33	DBF/Asit C. Mehta	-do-
5.	11.2.1992	25.00	Ashwin Mehta	-do-
6.	9.4.1992	25.00	S.G. Mantri	B.S.Marg,Bombay
		80.58		

4.3 In respect of the balance seven of these transactions, the payments were made to Canara Bank presumably for the account of CBMF and in turn payments were made in five cases to brokers and in one case to a finance company. One payment is in dispute. The details of these payments are as under:

Sr. No.	Date of remittance by Canfina	Amount (Rs.in crores)	Name of broker to whom paid	Canara Bank branch on which IBA was drawn
1	2.5.1991	17.17	Shrikant Mantri	Tamarind Lane Br.
2.	19.9.199	1	7.00	CBMF -do-
3.	23.8.199	1	1.00	Shrewd Finance & -do- Investment Pvt.Ltd.*
4.	22.10.1991	12.00	Shrenik Jhaveri	-do-
5.	16.1.1992	5.00	HPD	-do-
6.	7.2.1992	5.00	Manubhai Maneklal	-do-
7.	11.2.1992	7.00	-do-	-do-
		54.17		

* In Canfina's books, the security is shown as purchased from Powmex Steels Ltd.

4.4 That CBMF was used as a "routing" agency is clear from the fact that (a) in CBMF books the amounts received from Canfina were credited to Sundry Creditors account and the payment to the brokers debited to the same account, (b) there are no sales contracts available with CBMF and (c) from letter dated 9 September 1992 written by CBMF to Canara Bank which reads as under : -

"We note from our records, there were few remittances received by Mutual Fund from Canfina for making payment to various brokers. However, it is seen that there is no other transactions for Canbank Mutual Fund to receive such remittances other than to make payment to brokers. We have furnished in the enclosure the particulars of such transactions. We would like you to impress upon Canfina not to make such remittances in future which are not backed by any valid transaction between Canbank Mutual Fund and Canfina."

4.5 Thus, under these 13 transactions, Canfina has made available PMS funds aggregating to Rs.134.75 crores mainly to brokers under what appear to be clean loans given under the facade of "ready-forward" transactions.

5. Funding of M/s.V.B. Desai under Ready Forward Deals

5.1 Canfina entered into three Ready Forward Purchase deals with/through broker M/s.V.B. Desai as per details given below :

Date of Transaction	Security	Quantity (crore)	Rate (Rs.)	Amount paid(Rs. in crs.)	Ready Forward reversal period
25.9.1990	Canstar	1.00	@ 10	10.00	15 days
11.9.1990	Canshare	0.0685	@ 25	1.7125	-
9.4.1992	Cantriple	1.00	@ 18.467	18.467	-

The first two transactions were directly taken up with M/s. V.B. Desai as counterparty. The third transaction was with Standard Chartered Bank (Stanchart) with M/s.V.B. Desai as broker.

5.2 In respect of the first two transactions, Canfina paid M/s.V.B. Desai Rs.11.7125 crores against lodgement of Canstar and Canshare units. Against the third transaction, it paid Rs.18.467 crores to Stanchart which issued its BR.

5.3 Though the third transaction with Stanchart was recorded by Canfina @Rs.18.467, it appears that in the books of Stanchart, the transaction is shown as a sale to Canfina @Rs.15.21 per unit. Canfina has made payment to Stanchart of Rs.15.21 crores @Rs.15.21 per unit and the balance of Rs.3.257 crores has been adjusted against amounts due from Grindlays (broker M/s.V.B. Desai) against a sale of 13% NTPC Bonds of Face Value Rs.3.50 crores @Rs.93.05714. In effect, therefore, M/s.V.B. Desai have been credited with a profit of Rs.3.257 crores. The broker's note from M/s.V.B. Desai and the sales memo from Stanchart are not available with Canfina.

5.4 Though Canfina held, under the first two transactions, the units along with blank transfer forms, it did not lodge the same for transfer and presumably the dividend/bonus shares on these units were availed of by the broker M/s.V.B. Desai. For the third transaction, no delivery has been effected and the BR is still outstanding.

5.5 According to Canfina, all the transactions were "ready forward" transactions with M/s.V.B. Desai at an expected yield of 25% p.a. for which reversal was not made by M/s.V.B. Desai. It therefore issued legal notice to M/s.V.B. Desai on 2 September 1992 demanding Rs.38.89 crores which represent the aggregate payment of Rs.30.1795 crores together with interest upto 24 August 1992 at a rate of 25% p.a. compounded at quarterly rests. Following this, M/s.V.B. Desai bought back 2.20 lakh Canshares at a total value of Rs.91.35 lakhs. The balance is still to be recovered.

6. Ready Forward Transactions with C.Mackertich

6.1 On 20 April 1992, Canfina is shown to have bought 2.5 crore GIC Rise I units @Rs.20 per unit from American Express Bank (AMEX) through brokers Stewart & Co. on RF basis. A contract note relating to the transaction from C.Mackertich (and not Stewart & Co.) is on record. The note, however, indicates the securities purchased as GIC Rise II and not GIC Rise I. The cost memo No.Bill No.Sec/92/3 dated 20 April 1992 from C.Mackertich had advised the company to credit the proceeds of Rs.50 crores to their account maintained with AMEX after adjusting the sale proceeds of certain shares purchased by the firm from the company on 12 and 13 February 1992. The company issued a banker's cheque for an amount of Rs.28.86 crores on 20 April 1992 in favour of AMEX for credit to the account of the broker. Thus the dealing officials were aware that the name of the counterparty indicated in the dealer's pad as AMEX and the security indicated as purchased on 20 April 1992 as GIC Rise I were incorrect.

6.2 The nature of transaction (ready forward) reversible on 18 May 1992 at Rs.20.40 is also not substantiated as there is no contract note from C.Mackertich for fulfilling the reversal buyback commitment on a later date. As per the dealer's pad the transaction was reversed on 18 May 1992 though on 20 April 1992, the column RF/RFR in the dealer's pad was completely struck off in ink without any authentication. However, the dealer's pad shows the security as GIC Rise. As per this, 2.5 crore 'GIC Rise' units were sold to Dhyan Investments and Trading Co. Ltd., on an outright basis @ Rs.16 per unit as against the expected reversal rate of Rs.20.40 per unit (i.e. with 26.1% return). Canfina received a banker's cheque dated 18 May 1992 for Rs.40 crores from Syndicate Bank. In the process Canfina suffered a loss of Rs.10 crores in respect of its holding rate and a shortfall of Rs.11 crores as compared to the expected reversal rate. This shortfall was not recognised in the accounts on 18 May 1992. Canfina debited this amount in its accounts under the head "Amount Receivable from Other Banks" (AROB) belatedly on 18 July 1992.

6.3 C.Mackertich remitted to the company a part amount of Rs.4.40 crores by means of two pay orders of Rs.1.20 crores dated 6 August 1992 and Rs.3.20 crores dated 8 August 1992 issued by AMEX. The balance of Rs.6.60 crores is pending settlement due to a short delivery by Canfina of 3,34,350 shares of Reliance Industries Ltd. to the broker in respect of the shares purchased by him from Canfina on 12 and 13 February 1992, the payment in respect of which was adjusted as mentioned in paragraph 6.1 above.

7. Transactions with D.K.Audikesavulu Group

7.1 Canfina made the following payments to the companies belonging to the group of D.K. Audikesavulu, Bangalore and recorded the same as purchases of the securities mentioned in the table below.

7.2 According to the note dated 12 October 1992 placed before the Board of Canfina on 15 October 1992 :-

(a) Though the payments are recorded as purchases in Canfina's books, Shri D.K. Audikesavulu has insisted that there was no purchase of shares but it was only a loan given by Canfina.

(b) The Canshares were with CBMF and had been delivered by CBMF to Canfina only recently. The shares were mostly third party shares without transfer deeds.

(c) The Canstocks were with CBMF and had not been received by Canfina. The Canstars were with Canfina.

(d) The Cancigo stands in the name of Saptagiri Distilleries Ltd. and is not a transferable instrument.

(e) The payments made to the Group were reportedly in the nature of a bridge loan given to the Group against NCD issue to be made by Karnataka Breweries and Distilleries Ltd. which was to be placed with

(Rs.in crores)

Date of purchase	Name of the counterparty	Nature of security	Face Value	Total purchase price
16.4.1992	Karnataka Breweries and Distilleries Ltd.	Canshare 28,55,300	2.00	5.00
2.2.1990	Mysore Food Products Ltd.	Canstock 22,580 Canstar 6,60,000	0.2258	1.00
2.2.1990	Saptagiri Distilleries Ltd	Cancigo 8,800	0.88	0.22
				6.22

There are no documents for these transactions.

CBMF.

7.3 The amount still remains outstanding and Canfina does not have transfer forms in respect of most of the securities.

8. Transactions in Cantriple Units

8.1 Subscription under Cantriple scheme launched by CBMF was officially closed for public on 7 December 1991. The total collection amounted to Rs.346.29 crores.

8.2 Even after the scheme officially closed, Canfina itself made three remittances, namely, Rs.42 crores on 9 December 1991, Rs.58 crores on 10 December 1991 and Rs.50 crores on 24 December 1991. These remittances aggregating Rs.150 crores are part of the total collections of Rs.346.29 crores. Out of the Rs.150 crores; an amount of Rs.50 crores was on its own account, Rs.75 crores were on account of Indian Railway Finance Corporation Ltd. (IRFC) and Rs.25 crores were on account of PGFIC. Thus the original issue of Cantriple was boosted to the extent of almost 44% by funds from Canfina provided after the issue closed.

8.3 (a) Citibank had subscribed to the scheme to the extent of Rs.100 crores and out of this, Canfina purchased Cantriple of face value Rs.36.50 crores from Citibank through broker HPD on 20 December 1991 (i.e. within 13 days of the close of the issue). According to Canfina this was a loan given to HPD on a "ready-forward" basis, which was reversed to the extent of Rs.25 crores on 10 March 1992, Rs.3 crores on 30 March 1992, Rs.8 crores on 31 March 1992 and Rs.0.50 crore on 7 April 1992. Curiously all these reversals have been made at a uniform rate of Rs.11 per unit.

(b) On 10 April 1992, HPD sold Cantriple units of face value Rs.8 crores to Stanchart @Rs.20 per unit through Andhra Bank thus making a profit of Rs.7.20 crores on this lot alone (Reference is invited to paragraph 7(b) of Chapter on Stanchart).

8.4 (a) Between 31 March 1992 and 15 May 1992, Canfina made further bulk purchases of Cantriple units as shown in the table below.

(b) It will be noticed that the rates at which these purchases were made ranged from a low of Rs.15.705 per unit at which purchase was made from Hongkong Bank to a high of Rs.50 per unit at which purchase was made from broker C.Mackertich. No explanation has been provided for this wide difference in rates.

8.5 As a result of the above purchases, Canfina held as on 20 July 1992, Cantriple units of the face value Rs.88.84 crores (i.e.25.7% of the total subscription to Cantriple).

9. Transaction in shares

9.1 Canfina commenced purchase and sale of equity shares in the market from July 1991 on its own account. In February 1992 it commenced investing in shares on behalf of one of its PMS clients viz.,IRFC.

Sr. No.	Date of purchase	Counterparty	Face Value (Rs.in crores)	Rate (Rs.)	Remarks
1.	09.04.1992	Stanchart/V.B. Desai	10.00	18.467	Refer paragraph 5 above.
2.	27.04.1992	C.Mackertich	10.00	50.00	Refer paragraph (b) below.
3.	07.05.1992	Grindlays	5.00	33.00	Outright purchase
4.	11.05.1992	Hongkong Bank/RR	10.00	15.705	Outright purchase
5.	15.05.1992	Rahul & Co.	5.00	22.40	

The business turnover up to 20 July 1992 was as under:

(Rs. in crores)

	Company's own Investment		PMS (IRFC)		Total	
	No	Amount	No.	Amount	No.	Amount
Purchases	212	246.99	63	268.82	275	515.81
Sales	156	267.72	35	122.94	191	390.66
Total	368	514.71	98	391.76	466	906.47

9.2 The guidelines approved by the company's Board delegated powers to the extent of Rs.75 lakhs per transaction to the Chief Dealer. The Executive Director was authorised to operate within a limit of Rs.1 crore on his own and of Rs.2 crores jointly with one Executive Vice President/Senior Vice President. All transactions were to be entered with the intention of taking/ giving delivery of contracted shares. The upper limit for investment in a company's shares was limited to 1% of the paid up capital of the company at its nominal value. The exposure limit for shares as a whole was fixed at Rs.6 crores. Strict monitoring of the dealings was to be done at the Registered Office. In general, the above guidelines were not observed. The Chief Dealer exceeded his per transaction powers in 57.2% of the purchases made on Canfina's own investment account and in 87.9% of the purchases made an account of PMS client. The Executive Director had no occasion to exercise his powers. In fact, there is no evidence to show that he was involved in the process. Board's ratification for exceeding the delegated powers in respect of purchases made for the PMS client was not obtained.

9.3 The Company did not maintain under PMS share investment account uptodate record of broker-wise purchases and sales, scrips position, contract notes register, scrips movement register, etc. and did not keep a close watch on share delivery to/receivable from, brokers periodically. Several transactions put through on Canfina's account were not entered in the Chief Dealer's Sauda book. PMS funds were released to the brokers before receipt of contract notes. In respect of several sales transactions, the proceeds were received after much delay. The company did not ensure balancing of the physical holdings with its books from time to time.

9.4 In 25 out of 63 purchase transactions on the PMS account, the relative purchase price aggregating Rs.101.23 crores (37.7% of the total amount) was released to the brokers without obtaining/ensuring receipt of contract notes. In 38 out of 212 purchase transactions on Company's account, an amount of Rs.57.41 crores (23.2%) was released to brokers without contract notes. There is no indication that the contract notes in respect of the above transactions were received subsequently.

9.5 The company did not maintain proper records of the sales and purchase transactions in shares undertaken by it on account of the PMS client. There was also no regular system of monitoring the receipt of scrips in respect of purchases and receipt of sale proceeds in the respect of the sales. In the case of several purchases, the delivery of the shares was made by the brokers much after the purchase consideration was released by the company. Similarly, in respect of sales, the sales proceeds were received after much delay. As a result of lack of appropriate follow-up the company is saddled with significant amount of problem exposure.

9.6 As per the provisional statement compiled, the dues of the brokers to Canfina under its share deals as at the end of October 1992 were as under :

(Rs.in crores)

Name of the broker	Company's Investment A/c.	PMS Account	Total
Pallav Sheth	-	73.07	73.07
Hiten P. Dalal	19.70	7.38	27.08
N.K. Aggarwala	4.10	-	4.10
Ashwin Mehta	-	2.90	2.90
Prasad & Co.	0.38	-	0.38
Jayantilal Khandwala	0.71	-	0.71
S.S. Dalmia	0.63	-	0.63
	25.52	83.35	108.87

9.7 Canfina was holding shares of the value of Rs.11.93 crores standing in the names of notified persons.

9.8 The broker-wise position is detailed in the following paragraphs.

(i) Pallav Sheth

(a) Pallav Sheth was the most favoured broker in Canfina's share transactions undertaken on behalf of the PMS client. The following table gives the position of deals undertaken with the broker, part delivery/non-delivery of shares and the net amount recoverable by the company from the broker.

Share transactions with Pallav Sheth

(Rs.in crores)

Sr. No.	Date of release of funds	Amount released	Particulars of shares to be purchased	Delivered in full		Delivered in part		Not delivered	
				No.	Value	No.	Value	No.	Value
1.	10.3.92	22.50	500000 Tisco	-	-	180900	8.14	319100	14.36
2.	2.4.92	12.75	85000 Nahar Spinning	85000	12.75	-	-	-	-
3.	2.4.92	2.10	15000 Castrol	15000	2.10	-	-	-	-
4.	6.4.92	7.50	100000 ITC	-	7.50	-	-	-	-
5.	8.4.92	25.00	40000 ACC	-	-	-	-	40000	25.00
6.	16.4.92	5.00	125000 RIL	-	-	-	-	125000	5.00
7.	3.6.92	20.00	N.A.	-	-	-	-	-	20.00
8.	3.6.92	42.90	1500000 RIL	-	-	1000000	28.60	500000	14.32
9.	7.7.92	0.02	Tax deducted at source borne by Canfina.	-	-	-	-	-	-
		137.77			22.35		36.74		78.68

(b) As regards transaction listed at item (2) above, delivery of the relative shares was taken by CBMF which not only sent these shares for transfer in its name but also remitted an amount of Rs.1.85 crores towards application money for the rights shares issued by the company. Canfina is expecting to collect from CBMF, relative shares as also right entitlements.

(c) In respect of the transaction listed above at item (4), an amount of Rs.7.50 crores was paid to the broker on the 6 April 1992 for the purchase of one lakh ITC shares at Rs.750 per share for which there was no contract note from the broker. There was also no entry in the Souda book maintained by the dealer. The records show that these shares were sold through C.Mackertich five days later at the same rate of Rs.750 and payment was received from C. Mackeritch. Thus, an amount of Rs.7.50 crores given to Pallav Sheth on 6 April 1992 was received back on 11 April 1992. There was no losses or gain to the company. The Rs.7.50 crores for the period 6 April to 10 April 1992.

(d) As regards item (7) i.e. the release of Rs.20.00 crores on 3 June 1992, no records are available to indicate the particulars of the shares for the purchase of which this amount has been released.

(e) Although the broker had not delivered or only part delivered shares in respect of the purchases made by the company in March / April 1992, it agreed to adjust on 3 June 1992 an amount of Rs.62.90 crores from the receivables / sales transaction proceed of Rs.69.60 crores due fromthe broker. It is not clear why the company entered into these transactions.

(f) The total dues of the broker to the company was Rs.78.68 crores. While the broker was yet to deliver the contracted shares as indicated int he table above, he had subsequently delivered other shares worth Rs.5.61 crores for which there were no entries in the Sauda book. The company accepted the shares and adjusted the relative value of Rs.5.61 crores against his dues of Rs.78.68 crores, reducing the net exposure to Rs.73.07 crores as at the end of October 1992.

(g) The shares shown as delivered in the table above include shares of the approximate value of Rs.7.22 crores which stand in the names of notified persons. The broker had in June 1992 tendered listed/ unlisted shares of the aggregate value/estimated value of Rs.13.98 crores which included shares unacceptable to the company. He also gave the company five post-dated cheques for an aggregate amount of Rs.62 crores, in addition to submitting title deeds of certain immovable properties. In August 1992, Canfina issued a legal notice to the broker calling upon him to pay the dues with interest at 24% p.a. The broker then withdrew the settlement proposal and also issued stop notices to the bank on which the cheques for Rs.62 crores were drawn.

(ii) Hiten P. Dalal

(a) Canfina entered into 26 transactions with broker HPD for purchase/sale of shares valued at Rs.109.85 crores during the period September 1991 to April 1992. Business of Rs.94.74 crore was on account of Canfina's own investment and of Rs.15.11 crore was on account of PMS client. HPD did not deliver in full or part certain shares for which purchase consideration had been released to him. He did not pay in full in respect of shares which he had taken delivery of. He also gave partial delivery of partly paid BSES debentures to other brokers on Canfina's account where Canfina was forced to adjust/ reconcile the accounts of these brokers. HPD's dues to Canfina at the end of October 1992 were Rs.13.68 crores on account of Canfina's own investment and Rs.7.38 crores on account of PMS client. Details of the share/ debenture deals are detailed in subsequent paragraphs.

(b) HPD was paid Rs.9 crores on 2 April 1992 on PMS account to purchase 2 lakh TISCO shares @ Rs.450 per share. Neither the contract note nor the shares were delivered by him. Against the payment of Rs.9.00 crores an amount of Rs.1.62 crores shown as payable to him under the head "Amount Payable to other Banks" (APOB) has been adjusted. Details as to how this amount became payable to him were not available. The net amount due from HPD after adjusting Rs.1.62 crores has been shown as Rs.7.38 crores in the company's books.

(c) On 12, 13 and 14 February 1992 the company on its own investment account entered into three transactions with the broker for purchase of 30 lakh RIL shares for Rs.42 crores. On 12 and 14 February 1992 a sum of Rs.14 crores and Rs.28 crores respectively was paid to CBMF on broker's oral request. The company also simultaneously sold the shares on the same three days to various other brokers. HPD was to deliver the shares purchased by the company to these brokers for fulfilment of the company's sale contracts. On the 31 March 1992, the company reversed the entries relating to the payment of Rs.42 crores in the account of CBMF and debited the amount in HPD's account. The company could not explain why the payment entries were initially made in the name of CBMF. The company did not monitor the delivery of shares to the brokers by HPD. In October 1992 it came to the notice of the company that out of 30 lakh shares sold by it, HPD was yet to make delivery of 8,80,100 shares. On this account, the company is to receive an amount of Rs.12.32 crores from the broker.

(d) Against deliveries of shares given to HPD by other brokers on Canfina's account, dues of HPD to Canfina were as under (as reported to the Board of Canfina on 15 October 1992).

(Rs.in crores)

	Contract Date	Scrip		Quantity	Rate	Amount
i)	26.8.1991	Tata Power		10,000	2275	2.28
ii)	13.9.1991	Baroda Rayon		10,000	900	0.90
iii)	8.11.1991	Bombay Dyeing		60,000	395	2.37
iv)	8.11.1991	Bombay Dyeing		16,000	395	0.63
v)	10.1.1992	BSES	75000			
	Less : Delivery		61490	13,510	550	0.74
Calls in arrears/interest paid by the buyers of partly paid BSES debentures delivered by HPD						0.46
				Total		7.38

(e) The total dues of HPD to Canfina as at the end of October 1992 were :

	(Rs. in crores)
I. PMS Account	7.38
II. Company's Account [Paragraph (c) above]	12.32
Company's Account [Paragraph (d) above]	7.38
	27.08

(f) Canfina had in its possession undemoted shares without transfer deeds received from HPD on 20 February 1992.

(Rs. in crores)

	Scrips	Quantity	Rate as on 20.2.1992 (Rs.)	Amount	Holders
i)	SCICI	5,00,000	62.50	3.12	Canara Bank
ii)	Glaxo	20,000	213.75	0.43	Canara Bank
iii)	Protchem Ind.	1,16,400	40.00	0.47	H.P. Dalal
iv)	Chubb Diamonds	4,50,000	31.00	1.39	Naresh Mehra
				5.41	

(g) In December 1991, Canfina purchased 2 lakh Telco shares through HPD. However, the amount of Rs.5.55 crores was not paid to HPD. Subsequently, these shares were sold through Harshad S. Mehta (HSM) and the proceeds were received by Canfina. Canfina does not have any documentary proof to show that HPD delivered the shares to HSM. Since it has received the sale proceeds, Canfina considers that the shares were delivered by HPD to HSM. There was no claim to the contrary from HSM.

(h) The total amount thus payable to HPD is estimated as under :

	(Rs.in crores)
Paragraph (f) (iii) above	0.47
Paragraph (g) above	5.55
Total	6.02

(i) The position of net dues of HPD to Canfina on account of its share transactions under Canfina's own account and PMS account is, therefore, as under:

	(Rs. in crores)
As per paragraph (c) above	27.08
As per paragraph (h) above	6.02
Net dues from HPD	21.06

iii) Naresh K. Aggarwala

During the period January to April 1992, Canfina entered into 4 purchase and 6 sale transactions in shares of the aggregate value of Rs.4.16 crores and Rs.8.77 crores respectively with NKA. In respect of these deals, a net amount of Rs.4.10 crores is due from NKA. NKA has not disputed the deals listed above. He has, however, linked settlement of his dues to Canfina with (a) the latter's non-fulfilling its sale commitment of 5 lakh shares of SAIL (PSU) to him, (b) non delivery of one lakh RIL shares by HPD, and (c) non-adjustment by company of the price difference on his forward sale of 2 crore Units to the company due for delivery on 31 July 1992. As regards item (a) above, the company's bid valued at Rs.13.04 crores for purchase of shares of PSUs which included 9,00,000 shares of SAIL (face value Rs.10 each) was accepted by Ministry of Industry on 26 February 1992. Out of this, Canfina contracted to sell 5,00,000 shares to broker NKA @Rs.51 on 27 February 1992. The broker note was unstamped. The basis of striking the deal at Rs.51 on 27 February 1992 i.e., on the date of payment itself was not clear as shares were neither listed nor quotations from others were on record. The company subsequently rescinded the contract. On the two other issues, Canfina maintains that delivery of RIL shares to him by HPD was complete and that the forward Units deal was an independent "strip" transaction taken up by Canfina with Punjab National Bank earlier on 5 May 1992. Since the broker failed to deliver the Units covered under the Forward Deal, Canfina advised him that it was not interested in sorting out his transactions in Units with Punjab National Bank. Canfina was contemplating legal steps to recover the dues. The company holds 100 shares of Ruchi Soya Industries standing in the names of notified persons for which it has not made payment to NKA.

iv) S.G. Mantri

(a) Broker S.G. Mantri did business of Rs.12.61 crores with Canfina in 15 share deals. Of these, in 11 transactions (Rs.8.88 crores) under Canfina's investment account (all purchases), he did not submit contract notes. Canfina delivered for sale 10,000 shares of Castrol @ Rs.900/- to the above broker on 3 March 1992. Canfina did not receive the sale proceeds from him.

(b) The broker was also paid an amount of Rs.25 crore on 9 April 1992 for which full details were not available in the dealer's memo. In the physical register, the amount of Rs.25 crores was recorded as for purchase of 14% NCD against the additional security of 6,73,250 shares of the promoters of Jindal Iron Ltd. Thus as on 9 April 1992, amount due from him was Rs.25.90 crores. (The transaction of Rs.25 crores has been mentioned in paragraph 4).

(c) In order to facilitate return of the above shares to the promoters, the broker arranged for payment of Rs.14 crore in June 1992 on three different dates and Rs.2 crores on 29 July 1992. He also tendered 35.85 lakhs Cantriple units @Rs.30 each with transfer deeds and a cheque of Rs.1 crore on Canara bank on 6 August 1992. Following these payments, Canfina returned the shares and settled the account with 30% return to it. For both the deals there does not appear any entry in the Sauda book nor are contract notes on record. The absence of record and supporting documents and the manner of repayment/settlement proposal clearly indicate Canfina's role as provider of funds to the broker and its slackness in collecting the proceeds from him. Canfina merely held in its custody the shares of the promoters of Jindal Iron Ltd. and did not ascertain who was the ultimate beneficiary of the funds. The manner of settlement indicates the possibility that the promoters of Jindal Iron Ltd. may have been the ultimate beneficiaries on clean basis through the services of S.G. Mantri.

(d) The broker has delivered to Canfina shares of Bombay Dyeing (18350 - Rs.70.83 lakh) and Sterlite Industries (10,000 - Rs.43 lakhs) standing in the names of notified persons.

(v) Ashwin Mehta

(a) Ashwin Mehta did total business of Rs.9.11 crores with Canfina under its share transactions. On 3 March 1992, Canfina arranged for sale of 10 lakh Reliance Petro Ltd. shares @Rs.29 through him. Till date, he has not remitted the proceeds of Rs.2.90 crores.

(b) Canfina also released to him on 11 February 1992 an amount of Rs.25 crores for purchase of unspecified 14% NCD. In this deal, Canfina did not receive any contract note from the broker but had on record a letter dated 11 February 1992 (wherein date of receipt is not recorded) seeking the release of an amount of Rs.25 crores towards funding of debentures of L & T, and J & H series of debentures of RIL stating that the securities were ready for delivery. The amount released to the broker was in the nature of clean funding since the transaction recorded in the book did not materialise. This transaction is mentioned at paragraph 4.

(c) Under these two deals, PMS funds to the extent of Rs.27.90 crores are outstanding. Ashwin Mehta being a notified person, Canfina has a serious problem exposure to the extent of Rs.27.90 crores.

(vi) Manubhai Maneklal

(a) Canfina did business worth Rs.39.39 crores with Manubhai Maneklal (MM) under 17 share deals.

(b) In February 1992, under various deals Rs.10.62 crores were due from MM. Against this, Rs.11.59 crores were received from MM by five separate payments. There was thus an excess payment by MM of Rs.0.97 crore but on 31 March 1992, Canfina refunded Rs.1.50 crores to MM.

(c) On 8 April 1992, Canfina paid Rs.20 crores to MM on PMS client account as a result of which, taking into account the excess payment of Rs.0.53 crore on 31 March 1992, the total PMS funds with the broker aggregated to Rs.20.53 crores. There were no contracts/securities supporting this outstanding. Against this, MM repaid Rs.6.50 crores on 28 May 1992, Rs.1.70 crores in June 1992, Rs.1.66 crores in August 1992 and Rs.1 crore on 3 September 1992. Towards the balance together with interest @24% p.a., MM tendered in July and August 1992 shares of the value of Rs.11.21 crores. The account is under reconciliation.

10. Transactions in Cancigo Units

10.1 Cancigo is a redeemable non-debt security issued by CBMF. It is a condition of its issue that transfer of Cancigo holding from one person to another is not permitted. Yet from 1 April 1991 to 31 May 1992 Canfina put through 6 purchase deals valued at Rs.55.60 crores and 5 sale deals valued at Rs.22.60 crores with different parties including brokers on different dates on ready forward basis. The company purchased and sold this security internally from/to the PMS/CIAS clients accounts to the tune of Rs.186.70 crores and Rs.153.40 crores respectively between 1 April 1991 and 31 May 1992. One set of transactions is discussed below.

10.2 On 6 February 1992, Canfina purchased two Cancigo certificates of face value of Rs.33 crores from HPD at par. From the purchase price of Rs.33 crores payable in respect of the transaction an amount Rs.25.02 crores receivable from HPD in respect of two sale transactions with Citibank concluded on 6 February 1992 and 20 Janaury 1992 where Canfina was to receive differential amount of Rs.22.95 crores and Rs.2.07 crores was adjusted. The balance amount of Rs.7.98 crores was paid by a bankers' cheque dated 11th February 1992 and the relative amount was credited to his account with Andhra Bank. These two transactions find place in the Committee's second Report [Paragraphs VIII.4.d (i) and (iii)]. Although in the first transaction concluded on 6 February 1992 the counterparty and broker were Citibank and HPD as per the Company's records, the sale proceeds were received partly from C.Mackertich through AMEX (Rs.59.93 crores) and balance of Rs.22.95 crores from HPD by way of adjustment. On the observation of the Committee regarding different broker/counterparty to the transaction of 6 February 1992, Canfina has explained that the prices of debentures/bonds mentioned in the deal bought by it on ready forward basis from HPD depreciated heavily in the market, following the removal of coupon rate cap on PSU bonds/ debentures by the Government. Since HPD was not in a position to lift the deliveries at the contracted RF reversal rate, Canfina sold these securities to C.Mackertich at the prevailing market rates with the concurrence of HPD and recovered the difference between RF rates and market rates from HPD. Although entries in the books were made as though securities were sold to Citibank as originally intended, sale memoranda addressed to Citibank indicated the sale rates of different scrips at the lower rates (not at the contracted RF reversal rates). As against this, in the company's physical register, rates of scrips sold are recorded at higher RF rates. The brokers' contract note was not on record.

10.3. The two Cancigo certificates issued by CBMF dated 13 September 1991 and 3 September 1991 purchased by the Company on 6 February 1992 from HPD stand in the names of ABFSL (Rs.22 crore) and Andhra Bank (Rs.11 crore) respectively. Since holders cannot create any interest in Cancigo or transfer them to a third person, the securities acquired by Canfina did not give it legal title as holder of the security.

10.4 A note placed before the Board of the company at its meeting held on 26 August 1992 mentions as under :

"We understand that initially Andhra Bank and Andhra Bank Financial Services Ltd., have denied having invested any amount under Cancigo. However, they have now written to Canbank Mutual Fund for the original certificate."

10.5 As mentioned in the Committee's third Report (Paragraph VI.C.e 5) Andhra Bank applied for Cancigo certificate of Rs.11 crores on behalf of HPD by debiting the broker's current account. These units were intended as security to ABFSL towards HPD's some other deals with ABFSL. Interest on Rs.11 crores for the period 3 September 1991 to 30 June 1992 was credited to the broker's account with Andhra Bank. For subscribing to the other certificate of Rs.22 crores, the account of HPD was debited on 13 September 1991.

10.6 Against this backdrop, Canfina's purchase of Cancigo from HPD on 6 February 1992 had helped the broker more than Canfina as he not only chose his time to settle his account with company but also made Canfina buy from him non-transferable security. The transactions dated 20 January and 6 February 1992 also highlight that the broker did not confine his role to bringing two parties together for both legs of transactions but took position in the securities dealt. For culmination of reversal leg of transactions he remained free to choose different counterparty to derive/meet the gain/loss from the deals struck.

10.7 Canfina clarifies that the transactions dated 20 January 1992 were reversal of some of its RF deals entered into with CBMF on 3 July 1991 for purchase of PSU bonds. By not insisting on the reversal transaction on (20-1-1992) from the original counterparty (CBMF) and agreeing to claim the reveral deal amount from HPD, Canfina has left no doubt about its role as provider of funds to the broker through the agency of CBMF.

10.8 As regards Cancigo certificates, claims/counter claims of dues of/from HPD (a notified person) to ABFSL/Andhra Bank (if any), will have to be first settled. The certificate not being transferable can only be encashed by the holders after stipulated period of one year from the issue dates i.e. on or after 3 September 1992 and 13 September 1992. There has been no further development/progress in the matter.

10.9 The problem exposure in this deal is reckoned as on 20 July 1992 at Rs.39.60 crores as evaluated by Canfina. (on the basis of NAV of Cancigo as on 1 April 1992).

11. Transactions with Canbank Mutual Fund

11.1 Canfina entered into 75 purchase (Rs.1822.63 crores) and 62 sale (Rs.1918.84 crores) transactions in securities with CBMF between 1 April 1991 and 23 May 1992. A few of them were undertaken through brokers. In the case of 14 purchase and 5 sale transactions, rates recorded in the books of Canfina and CBMF varied, eventhough 10 of these transactions were concluded on direct basis. The difference in the rates was received from/paid to brokers/different banks by Canfina. In some instances, certain transactions shown in the books of Canfina as having been concluded on direct basis were recorded in the books of CBMF as broker-mediated and vice-versa. Seventeen purchase and eight sale transactions, most of them recorded in the books of Canfina as direct, did not find place in the records of CBMF. Seven such purchase transactions have been described in paragraph 4.3.

11.2 Scrutiny of these transactions between Canfina and CBMF reveals the chaotic situation prevalent in the record management of both the institutions. It is observed that there are outstanding disputes between the two subsidiaries of Canara Bank.

12. Stuck-up Deals

Non-delivery of Units with Bank of Karad

12.1 Canfina entered into two deals for purchase of Units from BoK on 22 and 31 July 1991 as per details given below :

(Rs. in crores)

Sr. No.	Date of Purchase	Face Value of Units	Rate Rs.	Broker	Amount Paid	Mode of Delivery
1.	22.7.1991	160.00	13.30	Hiten P. Dalal	212.75	BR No.3499/ADN/ dated 22.7.91 issued by BoK.
2.	31.7.1991	190.00	13.4442	-do-	255.44	BR No.3425/ADN/ dated 31.7.91 issued by BoK.

12.2 The units were sold on the same day to Stanchart (6 crore Units) and Citibank (10 crore Units) @ Rs.13.305 per Unit. Profit of Rs.0.08 crore was booked from the deal.

12.3 The amount paid to BoK was short by Rs.0.05 crore i.e. 16 crore Units @ Rs.13.30 work out to Rs.212.80 crores, against which Canfina had paid Rs.212.75 crores. The amount receivable from Citibank was Rs.133.05 crores but the actual payment received was Rs.133 crores. The amount received from Stanchart was Rs.79.83 crores. The deal was exclusively on Canfina's own account.

12.4 Subsequently there were two sales for a total of 9 crore Units to BoK (1.5 crores on 15 October 1991 and 7.5 crores on 18 October 1991) and the Units to be delivered to the company in respect of the BR No.3499 got reduced to 7 crores. (Incidentally, the sale of 7.5 crore Units on 18 October 1991 is not shown in the records of the Registered Office of Canfina). Canfina's exposure on account of this transaction for the 7 crore Units outstanding @Rs.15.75 repurchase rate is Rs.110.25 crores.

12.5 The transaction at Sr.No.2 above is arrived at by merging several forward purchase contracts into one and netting therefrom all the forward sale contract deals struck for delivery on 31 July 1991. The rate in four decimals is the netted average rate. Contract notes from the broker were not on record. Canfina did not insist till April 1992 on physical delivery of Units covered under this transaction (and also balance of 7 crore Units in respect of the earlier transaction on 22 July 1991).

12.6 Records suggest that these two Unit deals were in the nature of funding broker HPD to the extent of Rs.468.19 crores from 22 July/31 July 1991 to 15 October/ 16 October 1991 and Rs.348.54 crores thereafter. As mentioned in the Committee's third Report the payments and receipts by BoK on this account appear as debits and credits in the account of broker ADN with BoK.

12.7 The transactions of 22 July and 31 July 1991 involving outlay of Rs.212.75 crores and Rs.255.44

crores respectively were far beyond the delegated powers of the dealers. Even after the revision in November 1991, the limit per transaction was only Rs.50 crores. The list of monthly transactions placed to the Managing Director for information/ratification was returned with the remark 'Noted'.

12.8 Canfina has filed two separate suits aginst the provisional liquidator of BoK and others in the High Court of Bombay on 21 August 1992.

12.9 Canfina's exposure under this transaction for 19 crore Units @Rs.15.75 is Rs.299.25 crores.

Non-delivery of 11.5% GOI Loan 2008 - Rs.25 crores

12.10 On 6 April 1991, Canfina bought from BoK 11.5% GOI Loan 2008 of face value Rs.25 crores @ Rs.100.05 and paid an aggregate amount of Rs.25.81 crores against BR No.3259 dated 6 April 1991 issued by BoK. The broker to the transaction was HPD. On 25 July 1991 Canfina sold to Stanchart 11.5% GOI Loan 2008 of face value Rs.50 crores @Rs.99.30 and issued SGL transfer form for face value Rs.25 crores and BR No.868 for the balance. The SGL transfer form finally received from BoK on 18 April 1992 in lieu of the BR and lodged with RBI with delay on 6 May 1992 was returned by RBI, Bombay for insufficient balance in the account of BoK. Following the liquidation of BoK, Canfina is faced with the problem of non-delivery of security by BoK.

12.11 The company has filed suit against the Provisional Liquidator of BoK and others on 21 August 1992 for an aggregate amount of Rs.35.54 crores including interest. Canfina's bad exposure under this transaction is Rs.29.16 crores.

Non-delivery of 5 crore Units by State Bank of Saurashtra

12.12 On 2 September 1991, Canfina bought 5 crore Units from State Bank of Saurashtra (SBS) and in exchange of BR No.42 dated 2 September 1991 issued by SBS released purchase consideration of Rs.67.75 crores to it. The company is yet to receive delivery of Units from SBS. On 19 August 1992, Canfina filed a suit against SBS for delivery of Units and claimed damages. The total amount claimed is as under:-

Scrip	5 crore Units
Purchase price (Rs.)	67,75,00,000.00
Interest @ 24% p.a. (Rs.)	17,08,84,544.00
Interest upto	17.8.1992
Amount claimed (Rs.)	84,83,84,544.00

The broker to this transaction as reported in the Committee's second Report [paragraph VIII 4(b)] is C. Mackertich. Although computer print-out of purchase on 2 September 1991 shows the name of the broker to this transaction as 'C'Mack', the name of HSM is written in the Dealer's Memo-cum-transaction book after cancelling the name of C. Mackertich. The contract note received from Harshad S. Mehta tallies with the cost memo addressed by SBS to Canfina. Following the publication of the Committee's second Report, the company has, at the instance of C.Mackertich issued a letter to him stating that there was no such transaction with him.

12.13 Canfina's payment to SBS of Rs.67.75 crores on 2 September 1991 against BR.No.42 issued by SBS is not disputed by SBS.

Claim by Stanchart to deliver 9% IRFC bonds of Rs.70 crores

12.14 Stanchart has served a legal notice dated 12 August 1992 on Canfina demanding immediate physical delivery of 9% IRFC bonds of an aggregate face value Rs.70 crores along with interest thereon for the two half-years due on 1 October 1991 and 1 April 1992 or in the alternative to refund the amount of Rs.71.41 crores paid on 27 September 1991 to Canfina towards purchase consideration of this deal along with interest at 20% p.a. from 27 September 1991 till payment and/ or realisation. Canfina had earlier advised Stanchart that bonds in question were delivered to it against payment received. The transactions recorded in the books of Canfina were as under:-

Date of sale	Scrip	Face value (Rs.in crores)	Rate (Rs.)	Amount (Rs.)	Name of the broker	Name of the counter-party
27.9.91	9% IRFC bonds	50	95.06	497368493.15	Hiten P. Dalal	Stanchart
27.9.91	9% IRFC bonds	20	103.93	216687397.26	-do-	Stanchart
		70		714055890.41		

Records at Bombay office of Canfina indicate that securities sold to Stanchart were directly handed over to broker HPD and the delivery effected through the broker was as under:

(i) Exchange of BoS's BR dated 27 September 1991 for bonds of face value Rs.20 crores.

(ii) Exchange of Citibank's BR dated 25 September 1991 for bonds of face value Rs.15 crores.

(iii) Exchange of Citibank's BR dated 25 September 1991 for bonds of face vcalue Rs.35 crores.

12.15. The amount involved under this deal together with interest till 31 October 1992 works out to Rs.87.06 crores.

Claim by Stanchart to delivery 9% IRFC bonds of Rs.50 crores

12.16 Canfina undertook sale of 9% IRFC bonds of face value Rs.50 crores to Citibank on 30 December 1991 on direct basis and collected the sale consideration together with interest for 168 days on the same date from Citibank. The mode of delivery in respect of this transaction was not specified At the instance of Citibank, Canfina arranged for delivery of bonds to Punjab Natinal Bank (PNB) at Delhi but at the same time issued BR No.1401 dated 30 December 1991 in favour of Citibank through its Bombay Office. Canfina, however, could not ensure custody of its above BR duly discharged by Citibank. This discharged BR found its way from Citibank to Stanchart. Based on this BR, Statement has staked a claim for delivery of the bonds of Rs.50 crores from Citibank/ Canfina as explained below.

12.17 On 19 February 1992, Stanchart purched 9% IRRFC bonds of the face value Rs.72.50 crores from Citibank and obtained Citibank's BR No. 46 dated 19 February 1992 for Rs.72.50 crores. On receipt of reported telephone call to collect the securities in exchange for discharged BR No.46 the representative of Stanchart attended the Citibank to collect the IRFC bonds. He was handed over by Citibank its fresh BR No.47 dated 4 March 1992 for the face value Rs.22.50 crores and a discharged BR No. 1401 dated 30 December 1991 issued by Canfina for Rs.50 crores in favour of Citibank. Stanchart has claimed that it was represented to it that it could collect the securities directly from Canfina on the strength of Canfina's BR No.1401 discharged by Citibank. Subsequently, when Stanchart's domand for secrity was not entertained by Canfina, Stanchart served a legal notice on Citibank on 4 June 1992 demanding delivery of securities forthwith or in the alternative to repay Rs.50 crores received by Citibank. Canfina was asked to confirm that it was in a position to physically deliver the bonds or alternatively not to part with the bonds without the written consent of Stanchart.

12.18 Transactions with NHB

(i) NTPC / IRFC Bonds

(a) The following transactions appear int eh books of the Registered Office of Canfina at Bangalore.

Sr. No.	Date of transaction	Scrip	Rate @ (Rs.)	Name of broker	Nature of transaction	Amount Face value (Rs. in crores)	Name of counter-party	Amount (Rs. in (crores)	Mode of delivery
1.	3,2.1992	17% NTPC bonds	99	Direct	Ready Forward sale to be purchased back on 30.4.1992	81.00	GRAM	80.64	BR No.
2.	3.2.1992	9% IRFC bonds	93	HSM	Buyback of security sold on 2.1.1992	22.00	Corporation Bank	20.64	BR No. 1411 dated 2.1.92 exchanged
3.	3.2.1992	9% IRFC bonds	93	-do-	-do-	63.50	GRAM	59.57	BR No. 1414 dated 2.1.92 exchanged.

(b) In of item (1), the Bombay Office of Canfina under telephone instructions from its Registered Office issued its BR No.1544 in the name of NHB although the counterparty was GRAM. In Bombay Office the transaction is recorded as a sale to NHB with HSM as broker.

(c) Canfina did not receive sale proceeds either from GRAM or NHB but the amount of Rs.80.64 crores was netted out against the sum of Rs.80.21 crores due under items (2) and (3) above and Canfina received Rs.0.43 crore from HSM. BR Nos. 1411 and 1414 earlier issue dby Canfina were also received back.

(d) Corporation Bank had received from SBI the amount due to it under item (32) on 13 January 1992.

(e) Canfina still has to delivery securitis againt its BR No.1544. This BR is with NHB but NHB has not made any payment for this purchase.

(ii) **13% DVC Bonds**

12.19 On 23 March 1992 Canfina sold 13% DVC bonds of the face value Rs.10 crores @ Rs.99 to NHB and received a cheque for Rs.9.90 crores from NHB. The broker for the transaction was HSM. There is no contract note with Canfina with referenc to this transaction. Canfina did not issue a BR covering the security nor did it delivery physicals. As per NHB's record the payment of Rs.9.90 crores was made to Cnfina for purchase of 66 lakh Units and not DVC bonds. Canfina has stated that it is prepared to deliver the bonds while NHB has demanded delivery of Units. The matter is yet to be settled.

12.20 **Transaction in 13% DVC bonds and 13% HPF bonds**

(a) On 3 Septemebr 1991 Canfina purchased 13% DVC bonds of the face value Rs.28.50 crores @ Rs.95 (contract value Rs.27.44 crores). and 13% HPF bonds of the face value Rs.5 crores @Rs. 95

(contract value Rs. 4.81 crores) and sold 9% HUDCO bonds of the face value Rs. 30.85 crores @Rs.100/- (contract value Rs. 32.24 crores). The broker for the transaction was HPD. As per records of Canfina, the counterparty for th etransaction are not available with the company. The company had to pay a net amount of Rs. 1,07,000 in respect of the to transactions. Whether this amount was paid ad if so to whom is not ascertainable from the company's record.

(b) It is stated in a note dated 12 October 1992 placed before Canfina's Board on 15 October 1992, that physical delivery of 9% HUDCO bonds of the face value Rs. 30.85 crores which it had sold was given on 3 September 1991 whereas delivery of DVC and HPF bonds purchased was not obtained.

(c) The relative transactions did not appear in the book of Stancharrt and that bank in its letter dated 29 October 1992 addressed to Canfina has denied the transaction, although it expressed its willingness to investigate the matter further if it was furnished with photocopies of the cost memos, particulars of consideration stated to have been paid, etc. Stanchart has also called for full particulars of 9% HUDCO bonds alleged to have been delivered by Canfina on 3 September 1991 including distinctive numbers of the letter of allotment/bonds, certified copy of delivery momo, details and the manner of delivery, etc.

12.21 Transactions in 13% CIL bonds

(a) On 24 June 1991, Canfina's New Delhi Office purchased from Hougkong Bank through NKA 13% NIL bonds of face value Rs. 18 crores and remitted the purchase consideration of Rs. 18.60 croes to Hongkong Bank. There is no cost memo or contract note available with the company and Canfina has not received the bonds or BR.

(b) According to Hongknog Bank, it had purchased on 8 May 1991, 13% CIL bonds of face value Rs. 18 crores from CBMF for which it received BR No,2214 issued by CBMF. There was no delivery of bonds by CBMF but on 24 June 1991, Rs.1860 crores was received from Canfina and CBMF's BR No.2214 (undischarged) was returned to CBMF.

(c) The matter is under dispute,

12.22 Purchase of Canpremium from ABFSL

On 27 April 1992, Canfina purchased from ABFSL canpremium units of face value Rs.12 crores @ Rs. 13 per unit. Canfina issued cheque No.82740 dated 27 April 1992 for Rs. 15.60 crores favouring ABFSL. Canfina received against this transaction Citibank's BR No.75 dated 24 April 1992 (issued in favour of ABFSL and dicharged by it). There was no direct deal between Canfina and Citibank on 24 April 1992. Citiband denied in May 1992 any commitment to deliver securities under its discharged BR.

13. Return of SGL transfer forms

13.1 The company did not maintain proper records of the investments in Government securities, SGL transfer forms and adjustment thereof etc. As a result, it was not possible for the Registered Office of the company to confirm that it had sufficient securities when the company issued SGL transfer forms.

13.2 During the period 1 April 1991 to 23 May 1992, PDO, RBI, Bombay had returned 43 SGL transfer forms, aggregating Rs. 1471.78 crores lodged by Canfina in respect of its purchases, for want of sufficient balance in the sellers account. During the same period 62 SGL transfer forms aggregating Rs.2585.50 crores issued by Canfina in respect of its sales were returned by PDO, Bombay for want of balance in its own account. Of the 43 purchase SGL transfer forms, 31 forms aggregating Rs.1219 crores pertained to 11.5% GOI Loan 2010 security whereas out of the 62 sale SGL transfer forms issued by Canfina, 53 aggregating Rs.2213.59 crores pertained to the same security. Canfina maintained on an average SGL balance of Rs.0.26 crore in this security with the PDO, Bombay. It could not match its purchases and sales of this security on some days. For instance, the total value of SGL transfer forms issued by Canfina on 13 and 27 July, 26 August, 5 october and 28 December 1991, 8 February and 6 April 1992 was not adequately covered by sufficient balance of the security in its SGL account with RBI. The extent of the shortfall is. indicated in the following table.

(Rs. in crores)

Date of SGL transfer form	Balance in as per Canfina's record	Value of SGL transfer forms lodged but not credited	Total	Value of SGL transfer forms issued but not credited	Excess/ (Short-fall)
13.7.1991	0.2561	100.000	100.2561	210.000	(109.7439)
27.7.1991	19.2561	30.000	49.2561	100.000	(50.7439)
26.8.1991	0.2561	225.000	225.2561	245.000	(19.7439)
5.10.1991	0.2561	94.000	94.2561	190.000	(95.7439)
28.12.1991	0.2561	—	0.2561	232.000	(231.7439)
8.2.1992	0.2561	35.000	35.2561	175.000	(139.7439)
6.4.1992	0.2561	250.000	250.2561	325.000	(74.7439)

13.3 The returned SGL transfer forms in respect of sales/purchases were regularised by relodging the same subsequently, by undertaking reversal sale deal with the same bank or by exchanging them by obtaining from the sellers SGL transfer forms of a third bank. Some instances are given in subsequent paragraphs.

13.4 (a) On 26 August 1991 Canfina sold to BOA 11.5% GOI 2010 security of an aggregate face value Rs.290 crores in three transactions through three brokers somayajulu & Co. (Rs. 95 crores), C.Mackertich (Rs.175 crores) and Excel & Co. (Rs.20 crores). canfina had issued SGL transfer forms to cover these transactions. On the same day, Canfina purchased from Stancart the same security of the face value Rs.225 crores through two brokers · HPD (Rs. 200 crores) and NKA (Rs.25 crores) and obtained SGL transfer forms issued by Stanchart. Stanhart's SGL transfer forms Rs.225 crores and Canfina's SGL transer forms for Rs.245 crores were returned by PDO on 29 August 1991 due to insufficient balance.

(b) Canfina met its obligation to Stanchart by issuing a fresh SGL transfer form for Rs.20 crores and arranged to square off the balance of Rs.225 crores due to Stanchart with the latter's dues to BOA of a like amount, which BOA in turn had to pay to Canfina.

13.5 On 2 December 1991, Canfina sold 12% GOI 2011 securities of the face value Rrs.25 crores to ;grindlays and issued its BR No.1290 on 2 December 1991. On 14 December 1991. Canfina purchased from Grindlays 12% GOI 2011 securities of the face value of Rs.25 crores and against its payment obtained SGL transfer form from Grindlays. This SGL transfer forms lodged with PDO on 16 December 1991 was returned by PDO on 18 December 1991 due to insufficient balance in the seller's account. Canfina returned the SGL transfer form to Grindlays and in turn received back from Grindlays ;its own BR No.1290 dated 2 Decebcr 1991 covering its sale of the same security of the same face value on that date.

13.6 On 9 May 1991, Canfina purchased 9.75% Tamil Nadu 1998 securities of the face value Rs.8 crores and 9.75% Punjab 1998 securities of the face value Rs.1 crore from Stanchart. The two SGL transfer forms issued by Stanchart were returned by PDO on 11 May 1991 for want of sufficient balance in the seller's account. SGL transfer forms covering two different securities viz. (i) 9.75% Bihar 1988 for Rs.4.1735 crores and (ii) 9.75% Rajasthan, 1998 for Rs.4.8264 crores were accepted by Canfina on 15 July 1992 in the place of the returned SGL transfer forms. The period taken for regularising the returned SGL transfer forms extended to over 2 months.

14. Conclusion

14.1 Like other subsidiaries of banks, Canfina was required by the terms of Reserve Bank's approval for its incorporation to confine itself to the business of merchant banking, leasing, hire-purchase and portfolio management and not to do normal banking business.

14.2 However, the findings detailed in the earlier paragraphs clearly establish that Canfina obtained substantial sums of money from clients under Portfolio Management Scheme (PMS) and Corporate Investment Advisory Services (CIAS) and transferred these funds to brokers under RF deals. In many cases there is no evidence to show that there were underlying securities for these transactions.

14.3 On a number of occasions, Canfina made short sales of securities and thus raised money on a 'clean' basis. By issuing BRs without the backing of securities it iolated Reserve Bank guidelines.

14.4 Canfina also did not deal with Canara bank or with CBMF at "arms length". Thus, large amounts of funds collected under PMs and CIAS schemes were placed on deposit with Canara Bank and similarly funds so collected were used to boost collections for schemes floated by CBMF, in some cases even after the official closure of the schemes, Canifa also routed loans to brokers through CBMF.

14.5 Canfina had large transactions in shares, both on its own account and also on behalf of PMS client and large amounts remained outstanding from brokers against these transactions.

14.6 The manner in which securities transactions of Canfina have been undertaken has been not only in violation of RBI guidelines but has also exposed it to an aggregate net exposure which is far in excess of its capital an reserves and left it in a positionn where its assets will probably be inadequate to meet its liabilities.

IV. ANZ Grindlays Bank

1.1 ANZ Grindlays Bank (Grindlays) is also one of the major participants in the securities market.

1.2 The main brokers through whom the security transactions were effected were Hiten P. Dalal (HPD), Somayajulu & Co., Harshad S. Mehta (HSM), Asit C. Mehta, M/s. V.B. Desai, Batliwala & Karanani and Hemdev & Sons. HPD accounted for as much as 31% of the aggregate value of the bank's transactions put through brokers during the period from April 1991 to May 1992. During the same period, the value of transactions put through HSM accounted for 8.5% of the total amount transacted through brokers. The brokerage paid by the bank to various brokers during the period from 1 Aptil 1991 to 30 June 1992 aggregated Rs.4.65 crores. Of this, the brokerage paid to HPD, C. Mackertich, Asit Mehta and HSM alone accounted for 77.05% of the total brokerage paid, with the share of HPD being as high as 46.41%. The bank had not followed its internal guidelines to deal with brokers and it appeared that certain brokers enjoyed procedural privileges. The bank had entered into security transactions through brokers who were not on the panel of the bank.

1.3 Grindlays entered into ready forward deals both in SLR and non-SLR securities with financial institutions, companies, brokers and individuals as counterparties.

2. **Grindlays as a routing bank for Harshad Mehta**

2.1 In a number of transactions in securities, Grindlays has acted as a routing bank for HSM. An example is given below:

Sr. No.	Date	Sale/ Purchase	Security	Counterparty	Face Value (Rs. in crores)	Rate (Rs.)	Cost Price (Rs.)
1.	21.3.92	Purchase	11.5%GOI Loan 2010	Canara Bank	55.00	96.5587	54,42,98.249.44
2.	6.4.92	Sale	-do-	-do-	55.00	96.8483	54,78,74,859.11
3.	6.4.92	Purchase	-do-	Bank of America	55.00	90.50	51,29,59,209.11
				Difference between transactions at Sr. No.2 and 3			3,49,15,650.00
4.	7.4.92	Purchase	-do-	Growmore Research and Assets Management Ltd. (GRAM)	55.00	96.8483	54,80,07,113.56
5.	7.4.92	Sale	-do-	-do-	55.00	90.50	51,30,91,463.56
				Difference between transactions at Sr. No.4 and 5 credited to HSM's account			3,49,15,650.00

2.2 Originally, Grindlays purchased from Canara Bank on outright basis the securities in transaction at Sr. No.1 on 21 March 1992 and received a BR instead of an SGL transfer form. his tansaction was through broker HSM. Till 6 April 1992, the SGL transfer form was not provided by Canara Bank. At the instance of HSM, the BR of Canara Bank was returned and an SGL transfer form from Bank of America was substituted. To effect these changes, transactions at Sr. Nos. 2 and 3 were executed through broker M/s. V.B. Desai, acting on behalf of HSM. The bank made a profit of Rs.3.49 crores in these transactions. This profit was passed on to GRAM a group concern of HSM on 7 April 1992 by concluding the transactions at Sr. Nos.4 and 5. Grindlays calls this type of transactions as "put through transactions".

2.3. In the names of HSM and his family members, the bank's Adayar branch, Madras granted 19 individual overdrafts against shares. Significantly, all the current accounts, which were opened between April and June 1991 were introduced by the same person viz. Branch Manager Shri Bakshi Varunkumar, Adayar branch, Madras and a cheque book was iswsued only in the name of one account holder, Smt. Jyoti H. Metha. All the overdraft limits were sanctioned between 20 April 1991 and 24 July 1991 and on the very day of sanction the overdraft amounts were transferred to Smt. Jyoti H. Mehta's current account for operational convenience. This facility also appears to have been extended, as HSM was a 'significant customer'.

2.4 It is significant that HSM often enjoyed unauthorised debit balances in his current account at M.G. Road Bombay branch of the bank on various dates between 26 April 1991 and 22 April 1992. The debit balance ranged from Rs.0.01 crore to Rs.6.98 crores. Interest has been sought to be charged in June 1992 only after the accounts were frozen by the CBI authorities in May 1992.

2.5 From the facilities enjoyed by certain brokers, it is observed that some of the brokers were more equal than others. They enjoyed privileges, both substantive and procedural.

HSM was considered "a significant customer and was provided servicing" by Grindlays. Hence the claim of Grindlays regarding the privilege granted for credting bankers cheques/RBI cheques drawn in favour of Grindlays to HSM's account, without any covering notes from the issuing banks. For instance, 12 RBI cheques issued by Power Finance Corporation (PFC) from New Delhi during NOvember 1990 to Aprll 1991 for a total sum of Rs.216.26 crores. in vavour of Grindlays were credited to HSM's current account in New Delhi, without any credit instructions from PFC. These amounts were telegraphically transferred to HSM's account in the Bombay branch of Grindlays and then to his account in UCO Bank, Hamam Street branch, Bombay on the respective dates.

2.6 It was indicated in the first Report of the Committee (Chapter 7.I) that against the gap of Rs.669 crores representing the value of the securities transactions put through HSM by State Bank of India (SBI) for which no SGL transfer forms had been lodged with the PDO, SBI had received nine payment orders of Grindlays aggregating Rs.574.76 crores. Of these, eight were issued by debit to HSM's account in Grindlays. The ninth payment amounting to Rs.97.99 crores is discussed in paragraph 10.2 (vii) of this chapter. On verification of records at National Housing Bank (NHB), as indicated in the second Report (Chapter VI, paragraph 4) it was observed that NHB had 15 outstanding contracts with Grindlays for an aggregate sum of Rs.511.66 crores. After adjusting the value of a contract for Rs.5.11 crores, where Grindlays claimed that delivery of the securities was effected, the amount claimed by NHB from Grindlays was of the order of Rs.506.54 crores. This has arisen out of seven RBI cheques issued by NHB between 24 March 1992 and 20 April 1992 for a total sum of Rs.489.75 crores in favour of Grindlays being credited by the latter to HSM's current account without any written instructions from NHB. (The difference of Rs.16.79 crores between the total deal amount and the amount paid to Grindlays is due to the reversals of two earlier deals, as reported by NHB).

2.7 Grindlays has claimed that this was done as per the market practice. Grindlays's claim is not borne out by either its own practice in a large number of instances or its internal guidelines. For instance, whenever Grindlays issued a banker's cheque, there was a credit instruction invariably accompanying the same. Similarly, in a large number of cases of bankers cheques received by Grindlays and credited to HSM's account, there were express accompanying credit instructions. On their internal guidelines, the bank's Country Operations Manager wrote in his letter dated 3 July 1992 as under:

"Our Group Operations Manual Section 1001:10 - General Introduction contains the following instructions:

No cheque, draft or similar instrument issued or endorsed in favour of the bank will be processed in branch operations unless the instrument bears a clear indication as to the purpose for which funds are intended. Where an instrument is received which does not bear sufficient notation (i.e. name or number of account to be credited, collection number, etc.) the item should be referred to Management for approval before being passed to the operating department for processing.

Our Operating Procedures Manual Section 046 - Inter Bank Settlement contains the following instructions:

CHEQUES FAVOURING BANK	Cheques drawn in favour of the Bank, received for credit to a customer's account will be referred to the Account/Branch Manager, prior to crediting the account".

2.8 However, on 17 July 1992 the bank has written to the Inspecting Officer, RBI that the Group Operations Manual was replaced by the New Operating Procedures Manual in February 1991, which reiterates only section 046 of Operating Procedures Manual.

2.9 NHB has claimed in various letters written in May 1992 that certain securities transactions done with Grindlays in March and April 1992 had matured for payment from 5 May 1992 onwards and that Grindlays should reverse the deals and pay back all the amounts. Grindlays has denied any knowledge of the transactions referred to by NHB.

2.10 As the matter between NHB and Grindlays is under arbitration, the Committee does not propose to go into these transactions. Grindlays has complied with the RBI directive to pay the amount of Rs.506.54 crores to NHB on 4 November 1992, without prejudice to its claim before arbitration.

2.11 In a number of transactions, the bank has debited or credited HSM's current account with it, although the counterparty was another bank. The bank has explained that in these cases, it has been assumed that the broker has in effect been acting as a principal to the transaction. "For some internal reasons the counterparty either "backed out" of the trade at the last moment or, was never a party to the deal. In the absence of a firm counterparty the broker is thus effectively left "holding" the other side of the trade and is forced to settle directly with the firm counterparty, viz. Grindlays". Admitting to having recorded such transactions erroneously, the bank's response is that "the original deals as given to us by the broker should have been cancelled (as soon as the broker requested that we debit/credit his account) and new deals, stating the broker as the counterparty should have been input into the system". It is not clear why the bank did not consider it necessary to seek the confirmation of the counterparty named in the contract notes either initially, or later when the so-called substitution of the counterparty by the broker was effected

3. Transactions having a bearing on the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992.

3.1 The bank has carried out large volumes of transactions in shares on behalf of the broker HPD. On 8 June 1992 HPD was notified by the Custodian under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992. As on that date the bank was holding shares worth Rs.7.59 crores on behalf of HPD. The bank had received the consideration for these shares from HPD. There were also other transactions in which HPD was liable to pay approximately Rs.2.50 crores to the bank.

3.2 Grindlays sold on 2 June 1992 a portion of the above shares held on behalf of HPD to M/s.Enam Securities Pvt. Ltd. and received payments on 1 July 1992 and 18 August 1992 in the name of the bank to set off its claim [in respect of an earlier transaction with Canbank Mutual Fund (CBMF)] against HPD. Delivery of shares for these sales was effected on 9 June 1992, i.e., a day after the date of notification. Grindlays, however, sought legal advice on this matter only on 6 August 1992. These transactions were reported by the bank to the Custodian by its letter dated 12 December 1992 only in response to a letter dated 18 November 1992 from the Custodian.

3.3 It is expected that the Custodian will take appropriate action in the matter.

4. Lending and Borrowing of Shares by Grindlays

4.1. Grindlays had indulged in borrowing and lending of equities from and to different brokers, on a modest scale, during the period 9 August 1991 to 10 August 1992. It is observed that the bank indulged in this activity not only for facilitating settlements but also for onward lending to the broker HPD. For instance, the bank borrowed 25,000 shares of Chowgule Steamship, 1200 shares of Aban Lloyd, and 21,000 shares of Grasim on 25 November 1991 from M/s.Enam Securities Pvt.Ltd. for lending them to HPD. The bank returned them on 13 December 1991, 9 January 1992 and 4 January 1992 respectively to M/s.Enam Securities Pvt.Ltd. on receipt from HPD. On each such borrowing of shares, funds were released to Enam Securities and while on-lending them to HPD, funds were received from him. No documents like deal slips, etc. were said to have been prepared for these deals and the arrangements were done only verbally except for some vague notations made in the 'delivery register'.

4.2. Significantly, the bank has not charged any interest on such transactions, which is quite contrary to the practice usually followed by the brokers in this matter. Indeed, the rate of interest charged in the market on such transactions is normally 0.5% to 1% more than the badla rate because the borrower is saved from the desperate situation of facing an auction in the stock exchange for his failure to give delivery of share scrips as per contracts.

4.3. Initially in June 1992, the bank denied having undertaken any such transaction. Later, however, in October 1992 on the matter being pursued further, it tried to justify the transactions as facilities extended to complete settlements.

4.4. As badla financing itself is prohibited by RBI guidelines, these borrowal and loan transactions in equities represent an irregularity of a greater magnitude.

5. Badla financing to broker M/s. N K. Aggarwala

5.1. Grindlays has indulged in badla financing which is specifically prohibited by RBI guidelines.

5.2 On 14 November 1991, M/s.Esanda Finanz & Leasing Ltd. (Esanda), an associate of the bank is reported to have placed Rs.2 crores with the bank, for being deployed "on their behalf prudently, i.e. some form of secured investment without price risks". This amount was passed on by the bank to the broker M/s.N.K. Aggarwala (NKA) through a ready forward transaction in shares involving eight scrips. The initial ready forward transaction covering two scrips, for a period of 12 days, was rolled over for subsequent settlement dates and also by exchanging one set of scrips for another. The rates quoted in the ready forward transactions for the equities had no relevance to the prevailing market rates of the respective scrips. The rates appear to have been fixed keeping in view an agreed rate of return of about 32% to 34%. The bank has received back Rs.2,27,26,700 on 7 April 1992, which included a net return of Rs.27,19,329. In fact, the bank had to return the funds deployed by Esanda on 27 March 1992, i.e. prior to the due date, at the latter's request, "thereby taking the remaining 11 days of ready-forward through PMS books". It is claimed by Grindlays that ready forward transactions in equities are not specifically prohibited by RBI guidelines.

5.3 In another instance also, the bank advanced a sum of Rs.24 lakhs to the broker NKA on 22 February 1991 through an apparent purchase of 40,000 shares of Reinz Talbros. The same were sold back after 40 days, on 3 April 1991. The purchase rate was Rs.60 while the selling rate was Rs.62.37, an odd rate not in conformity with the prevailing market rate. It appears that the selling rate was fixed keeping in view an assured return of 36%.

6. Portfolio Management Scheme of Grindlays

6.1 Most of the RBI guidelines on PMS have been violated or sought to be circumvented by Grindlays. The bank introduced PMS in August 1986. By December 1990 there were 523 PMS clients and the amount outstanding therein was Rs.211.12 crores. But, by the end of December 1991 the number of PMS clients fell to 337 with the amount outstanding getting reduced to Rs.69.04 crores. Since 30 September 1992, the bank has unilaterally closed its PMS accounts by transferring all the assets and liabilities to its own books.

6.2 The following violations of RBI guidelines have been observed :-

(a) The bank did not charge a definite fee for the management services rendered to its clients.

(b) A few PMS accounts were closed before completion of the prescribed one-year lock-in period.

(c) The bank deployed PMS funds in discounting of usance promissory notes of private sector companies for varying periods between 30 days and 270 days, with a facility to roll-over for a further period of 270 days. These were reduced to nil only by September 1992.

(d) The guideline that deals between the bank's own investments and PMS clients should be at market rates was violated.

(e) The bank resorted to short sales in respect of a number of equities sold on behalf of its PMS clients. The bank claims to have indulged in "short sales" only against existing purchases. But it is not able to corroborate the claim with corresponding brokers' notes for existing purchases. Nor is there other evidence like deal slips. In the absence of such evidence, the claim that it was not resorting to short sales is untenable.

(f) The bank has paid almost a fixed rate of return ranging from 12% to 19% to its PMS clients.

(g) The bank's earning from PMS funds deployed in equities for the period April 1991 to May 1992, as worked out by the bank itself, is more than Rs.26 crores. The profit generated would be of the order of 200% for a period of 14 months. The surplus income after applying a fixed return (ranging from 12% to 19%) was credited to the commission account of the bank.

(h) The bank has received dividends on account of PMS investments but has not credited the same to the accounts of PMS customers, some of which have been closed. Nor are the details (of the customers to whom these dividends are payable) available. It is claimed by the bank that such default is due to "operating errors".

(i) The bank has received a sum of Rs.20 lakh (approx.) as interest on TELCO bonds and about Rs.56,000 as interest on HMG Industry debentures in April 1992. These amounts were not distributed to PMS customers but directly credited to the bank's commission account. The bank has merely regretted the error instead of following a policy of "better-late-than-never" and rectifying the mistake.

7. Transactions in equities

7.1 The bank acted as an unofficial broker for HPD by buying (from other brokers) equities in comparatively smaller lots and selling them off as a huge lot to HPD, at rates higher than the prevailing market rate. Such deals were carried out between November 1991 and March 1992 (about 75 deals involving an aggregate amount of Rs.42.46 crores).

7.2 The scrips traded were Bajaj Auto, Kirloskar Cummins, Parke-Davis, DCL Polyesters, India Cable, Hi-tech Gears, Hoechst Pharmaceuticals, Castrol, J.K. Industries and Mancklal Hari Mills. These transactions were not entered into the Investment Bank Operating System (IBOS). The bank termed these deals as "big deals". The bank made large profits in such deals with HPD. An illustrative list of such transactions including some of the big deals is given in the annexure on page 159.

7.3 The bank has tried to justify such deals by saying that "the broker was mostly interested in large lots, he possibly realised that this could cause a substantial spurt in the price if he were to try and buy such large quantities on the trading floor of the exchange, specially in a rising market, and hence preferred to approach sellers directly". The bank has added "the broker/his clients seem to have been very confident of greater appreciation in future even when buying these shares, as we find that the shares we sold generally appreciated much further subsequent to our sale". Such deals between the bank and HPD were presumably not through the stock exchange.

7.4 Such deals were the causes later, for Grindlays to be left with unexecuted contracts of sale with HPD which were frustrated due to non-payment of the consideration by HPD, when the market suddenly collapsed. The bank has been compelled to dispose of these shares at the prevailing market prices, thereby incurring losses. In some of these cases, as the deliveries under the bank's own (underlying) purchases from other brokers (for sale to HPD) were still outstanding, the bank has tried to square off the transactions through the same brokers at the prevailing market rates.

7.5 In a number of instances, the bank has "squared off" or "set off" its outstanding sale transactions in equities with brokers against its earlier purchases from them of the same equities, in respect of which also the deliveries are outstanding. The bank has claimed that the "square off" or "set off" is resorted to, to reduce the exposures to the brokers who are unable to deliver the scrips for some reason or other for a "considerable time" (which may "vary from a few days to weeks"). In such "square off" deals, which have been undertaken both on the bank's own investment account and on PMS clients' account, no delivery of shares was taken or given, for the purchase or sale respectively.

8. SGL transfer forms

8.1 During the period from April 1991 to May 1992, in 37 instances SGL transfer forms issued by the bank in respect of its sale transactions in securities were returned by the PDO of the RBI on account of insufficient balance in its SGL account. In five of these cases, the SGL transfer forms were issued by the bank against the BRs of other banks held by it. Though in a few cases dishonour of SGL transfer forms issued by the bank was on account of dishonour of SGL transfer forms received from other banks (against which the bank had issued its SGL transfer forms), the bank had not reported the same to the RBI as required. In a number of cases, the bank has not relodged the dishonoured SGL transfer forms with the PDO. Instead, it has settled the matter with counterparty banks by exchanging the SGL transfer forms/repurchasing the security.

8.2 (i) On 15 November 1991 Grindlays sold to Standard Chartered Bank (Stanchart) 9.25% GOI Loan 1992 security of face value Rs.28 crores through HPD without obtaining contract note. Against the above sale Grindlays delivered to Stanchart an SGL transfer form issued by Bank of Karad (BoK) on 23 May 1991 and outstanding with it. This SGL transfer form had bounced twice on 1 June 1991 and 8 June 1991 on account of insufficient balance in the SGL account of BoK with PDO, RBI. There is no reason why Grindlays should have issued in respect of its sale, an SGL transfer form issued in its favour by some other bank instead of issuing its own SGL transfer form or a BR. In effect, the transaction amounted to a short sale of security by Grindlays. It is also not clear how Stanchart accepted the SGL transfer form of another bank for its purchase of security from Grindlays.

(ii) As per the deal slip and the cheques issued by the bank for its purchase from BoK on 23 May 1991, the counterparty was originally Andhra Bank which was scored off by the bank and substituted by BoK. Neither the broker's contract notes, nor cost memos for the said transactions were available. This change of counterparty was not reported by the dealer to the General Manager, Investment Banking as required in terms of internal guidelines dated 18 June 1990.

(iii) Stanchart has since filed a suit against Grindlays in London on 27 November 1992.

8.3 (i) On 27 March 1991 the bank purchased 11.5% GOI Loan 2006 of face value Rs.20 crores from CBMF through the broker HPD against receipt of SGL transfer form. The SGL transfer form lodged by the bank with the PDO of RBI on 3 April 1991 was returned by the PDO on 4 April (received by Grindlays on 11 April 1991) due to insufficient balance.

(ii) On 8 April 1991 the bank sold the said security to Andhra Bank, the broker being HPD. The bank issued its SGL transfer form to Andhra Bank which was lodged by the latter on 9 April 1991. The SGL transfer form issued by Grindlays bounced as the SGL transfer form received by it from CBMF also bounced. The SGL transfer form of CBMF was relodged by Grindlays on 13 May 1991, but it again bounced due to insufficient balance. The SGL transfer form of Grindlays was relodged by Andhra Bank on number of times and it bounced every time.

(iii) According to Grindlays no further records are available with it in this regard. However, the fact remains that according to its books, Grindlays has not effected delivery to Andhra Bank against its sale nor has it received delivery from CBMF against its purchase.

(iv) It has subsequently transpired that the SGL transfer form duly marked "cancelled" was "received back by CBMF in or around May 1991", but that Grindlays had not received payment therefor.

(v) Grindlays has added that it was advised by Andhra Bank that the latter purchased the security on behalf of HPD. The bounced SGL transfer form was reported to have been given back to HPD by Andhra Bank. Grindlays has not received back this SGL form duly cancelled.

(vi) The SGL transfer form issued by CBMF on 27 March 1991 to Grindlays was against a purchase of 11.5% GOI Loan 2006 for Rs.22 crores (face value) on 20 March 1991 from Stanchart for which CBMF did not receive either an SGL transfer form or a BR from the latter. Thus the sale to Grindlays by CBMF on 27 March 1991 was without any backing of security.

(vii) In the books of Andhra Bank, the following further transactions done on behalf of HPD in respect of this security are recorded :-

Date	Purchased from	Rate (Rs.)	Date	Sold to	Rate (Rs.)	Remarks
---	---	---	8.4.91	Citibank	102.80	Andhra Bank issued SGL transfer form.
31.5.91	Citibank Bank	102.71	31.5.91	Hongkong	102.25	Andhra Bank received back its SGL transfer form from Citibank and issued a fresh SGL transfer form to Hongkong Bank.
1.7.91	Hongkong Bank	102.55	1.7.91	Stanchart	102.55	Andhra Bank received back its SGL transfer form from Hongkong Bank and issued three fresh SGL transfer forms (splitting the amount) to Stanchart.
25.7.91	Stanchart Face Value Rs.10.50 crs.	101.35	-	-	-	All the 3 SGL transfer forms issued to Stanchart have been received back.
1.8.91	Stanchart Face Value Rs.9.50 crs.	102.20	-	-	-	-

(viii) In the holding register on account of the broker HDP in ANDRA Bak, the same security of Rs.20 crores was sold by Andhra Bank to HPD on 2 August 1991 "free", and it presumably thereby returned Grindlay's SGL transfer form to HDP.

(ix) In effect, the trading in the security throughout the period from 20 March 1991 to 1 August 1991 was without the backing of security. The. The broker was apparently accommodated, during the period from 20 March 1991 to 8 April 1991.

(x) In the records of Standhart, a photocopy of an SGB transfer form for Rs.22 crores (face value) of 11.5% GOI Loan 2006 duly signed by two officials of CBMF as buyer, and showing Standchart as seller but unsigned by the letter, has been found,. There is no explanation from either CBMF or Stanchart about the relative SGL transfer form.

9. Deals in PSU Bonds

9.1 The bank made the following transactions in PSU bonds involving brokers R.K. Chari, Chandrakala & Co., Fairgrowth Financial Services Ltd. (FGFSL) and NHB as players.

9.2 On 6 April 1992 the bank sold to NHB PSU bands (9% PFC, NTPC and REC bonds) for an aggregate face value of Rs.20.764 crores and aggregate contract value of Rs.19.08 crores. It issued 5 BRs serially numbered 262 to 266 and is reported to have delivered the BRs to NHB 9% MTNL bonds of the face value of Rs.20 crores and contract value of Rs.19.24 crores. In both the transactions R.K. Chari was the broker. Physical delivery of the MTNL bonds is said to have been made at delhi by Chandrakala & Co. on behalf of NHB.

9.3 These two transactions were netted off and in settlement a sum of Rs.15.52 lakhs was paid to NHB. In the books of NHB there were no such transactions with Grindlays or any record of Chandrakala & Co. having been authorised to make delivery. NHB is holdingthe sum of Rs.15.52 lakhs in its sundry deposit account.

9.4 Again on 11 April 1992, Grindlays purchased 9% MTNL bonds of the face value of Rs.25 crores at the rate of Rs.755.7100 from NHB. The cost memo from NHB for the said transaction is not available at Grindlays. The cost price for the said purchase is Rs.19.11 crores. Delivery of MTNL bonds is said to have been made by FGFSL to the Delhi branch of Grindlays along with an unsigned covering letter.

9.5 On 13 April 1992 both the sale transactions entered into on 6 April 1992 and the purchase transaction entered into on 11 April 1992 were reversed, at Rs.19,11,48,714.66 and Rs.19,11,46,215.75 respectively. While the reverse purchase of PSU bonds was done through the broker Chandrakala & Co., the reverse sale of MTNL bonds was a direct deal. After netting these transactions, Grindlays issued an RBI cheque for a sum of Rs.2498.91 on 13 April 1992 to NHB. This cheque has been found lying unaccounted, in the drawer of the dealer in NHB.

9.6 It transpires that the purchase of MTNL bonds on 6 April 1992 by Grindlays represents reversal of an earlier sale transaction in the same security concluded by Grindlays on 26 February 1992 with NHB through the broker R.K. Chari.

10. Transactions undertaken at HSM's behest

10.1 There is evidence to show that dummy transactions were put through by Grindlays at the request of HSM. One such series of transactions is detailed in the following paragraphs :

10.2 (i) On 22 February 1992 NHB purchased from SBI, 11.5% GOI Loan 2008 of face value Rs.100 crores for Rs.100.62 crores. The payment made to SBI was credited in SBI to the account of HSM. SBI did not deliver the securities or issue a BR.

(ii) NHB in turn sold the securities to SBI Caps on the same day and issued its BR. SBI Caps then sold the securities to Grindlays and issued its BR No.316. In both these transactions HSM was the broker.

(iii) On 6 April 1992, Grindlays sold the securities to UTI for Rs.96.94 crores and issued its BR No.268. This sale was also made through HSM.

(iv) Between 10 April 1992 and 13 April 1992 Grindlays issued four RBI cheques for a total sum of Rs.97.41 crores in favour of UTI and debited this amount to HSM's account with Grindlays. UTI returned the BR No.268 duly discharged through HSM.

(v) HSM wanted Grindlays to issue against this BR No.268, a BR in favour of SBI. However, Grindlays had in its records already cancelled its BR No.268 against SBI Caps BR No.316.

(vi) To accommodate HSM, Grindlays booked the following dummy sale and purchase transactions. On 16 April 1992, it purchased 11.5% GOI Loan 2008 of face value Rs.100 crores from SBI Caps and sold the same to SBI for an identical price. No payment was made or received. The purchase from SBI Caps was shown as supported by the return of its BR No.268 and the sale to SBI was supported by a fresh BR No.360 issued in favour of SBI. This BR was not delivered to SBI.

(vii) On 18 April 1992 Grindlays purchased 11.5% GOI Loan 2008 of face value Rs.100 crores for Rs.97.99 crores from SBI and supported this by a cancellation of its BR No.360 shown earlier as issued to SBI. The payment made to SBI was utilised to adjust the dues from HSM to SBI in SBI books and was in reimbursement of the payment earlier made by HSM to UTI. The payment of Rs.97.99 crores by Grindlays forms part of the payments aggregating Rs.574.76 crores made to SBI, referred to in Chapter 7.I of the first Report of the Committee.

11. Deals on behalf of Esanda Finanz & Leasing Ltd.

11.1 The bank was entering into sale and purchase transactions of Units of UTI 1964 on behalf of Esanda. In the bank's records, sale of Units was shown as effected to Esanda, for which the bank issued BRs against receipt of funds from Esanda. On the dates when the funds were due to be returned to Esanda's clients, Grindlays made purchases of the Units from Esanda by liquidating the concerned BRs and credited Esanda's current account in its books. There are however no written instructions from Esanda to Grindlays about the manner of deployment of its funds. These sales and purchases were basically of buy-back nature.

11.2 During the period 1 April 1991 to 29 May 1992, the bank's total sales to Esanda were of the order of 15 crore Units of the sale value of Rs.208.1 crores for which BRs were issued to Esanda. It purchased back an equal number of Units valued at Rs.212.4 crores against which its BRs were liquidated. These were only book entries inasmuch as no physicals were exchanged except for one occasion on 29 May 1992 on which the bank delivered 5 lakh Units to Esanda. The buy-back arrangements are in contravention of RBI guidelines.

12. Conclusion

The findings detailed in earlier paragraphs show that :-

12.1 Grindlay's securities transactions were often conditioned by the special relationship which broker HSM enjoyed with Grindlays. This relationship enabled HSM to "route" his securities transactions through Grindlays, to ask Grindlays to undertake "put through transactions" for his benefit and to enjoy unauthorised overdraft facilities.

12.2 In consequence of the above facilities extended to HSM, Grindlays have credited bankers/RBI cheques drawn in its favour to HSM's account without any covering notes from the issuing banks and has operated HSM's current account for transactions which are recorded in its books as being with other counterparties. In doing so, Grindlays in a sense, lent its name and counterparties believed they were dealing with Grindlays, when in fact they were dealing with HSM. It has also put through a number of dummy securities transactions on HSM's behest.

12.3 Grindlays has borrowed and lent equities from and to different brokers, though on a modest scale, to facilitate settlements and also for onward lending to broker HPD. It has also acted as an unofficial broker for HPD in buying (from other brokers) equities in comparatively smaller lots and selling the same to HPD in larger lots. In doing so, it has exposed itself to a loss when it was left with unexecuted contracts of sale to HPD which were frustrated due to non-payment of consideration by HPD when the market suddenly collapsed. Grindlays has also done badla financing in violation of RBI guidelines.

12.4 Grindlays has entered into a number of transactions in PSU bonds ostensibly with NHB through several brokers but there are no corresponding entries for these transactions in NHB's books.

12.5 Grindlays has entered into several purchase and sale transactions with Esanda on a buy-back basis in contravention of RBI guidelines. These transactions appear to be only in the form of book entries with no physicals being exchanged.

12.6 Grindlays has also violated or circumvented most of the RBI guidelines on the operations of PMS.

ANNEXURE

(See paragraph 7.2 page 154)

List of equities sold by ANZ Grindlays Bank to Hiten Dalal (HPD) at a rate very much above the market rate

Sr. No.	Date of Sale	Name of the scrip	Quantity sold	Rate at which sold (Rs.)	Market rate (Range) (Rs.)	Approximate profit earned by bank i.e.loss of HPD (Rs.in lakhs)
1.	29.4.91	Laxmi Machine Works	500	5000	3900 - 4100	4.50
2.	29.4.91	Laxmi Machine Works	500	5000	3900 - 4100	4.50
3.	9.5.91	Bhadrachalam Papers	1,02,000	180	160 - 170	10.20
4.	21.5.91	M.R.F. Tyres	15,000	625	550 - 560	9.75
5.	21.5.91	Madras Cement	5,025	6000	4500 - 4625	69.09
6.	11.6.91	Escorts Ltd.	75,000	170	150 - 151	14.25
7.	11.6.91	M.R.F. Tyres	20,000	700	550 - 565	27.00
8.	18.6.91	Ipitata Sponge	1,50,000	62.50	53.50 - 55.50	10.50
9.	28.6.91	Escorts Tractors	75,000	175	122.50 - 140	26.25
10.	20.11.91	Apollo Tyres	6,00,000	165	137 - 143	132.00
11.	20.11.91	Gujarat Ambuja Cement	3,00,000	325	265 - 275	150.00
12.	29.11.91	Telco Ltd.	1,00,000	325	282.50 - 287.50	37.50
13.	29.11.91	Telco Ltd.	1,00,000	325	282.50 - 287.50	37.50
14.	20.12.91	Hoechst India	1,22,000	696	530 - 580	141.52
15.	20.12.91	J.K. Industries	2,50,000	174	135 - 145	72.50
16.	20.12.91	Castrol	72,000	711	577.50 - 593.75	84.42
17.	7.2.92	HMG Industries	1,00,000	90	80 - 87.50	2.50
18.	19.2.92	Essel Packaging	1,80,000	120	80 - 100	36.00
						869.98

V. Andhra Bank Financial Services Ltd.

1. Reference has been made in the second Report of the Committee (Chapter VIII) to the Andhra Bank Financial Services Ltd. (ABFSL), a wholly-owned subsidiary of Andhra Bank.

2.1 ABFSL is a company incorporated in February 1991 under the Companies Act, 1956 with an authorised capital of Rs.10 crores and a paid-up capital of Rs.5 crores.

2.2 Its operations are governed by the terms and conditions on which approval was granted to Andhra Bank for formation of the subsidiary. These terms and conditions inter-alia provide that "the subsidiary shall confine itself strictly to equipment leasing, hire purchase and merchant banking business and activities purely incidental thereto. It shall not carry on any other business set out under Section 6(1)(a) to (n) of the Banking Regulation Act, 1949 without the specific prior approval of the Reserve Bank".

2.3 Section 6(1)(a) to (n) of the Banking Regulation Act, 1949 lists inter-alia the following business:

i) borrowing, raising or taking up of money;

ii) lending or advancing of money;

iii) buying or discounting of bills; and

iv) dealing in securities.

In view of the terms of RBI approval, it was not permissible for ABFSL to undertake these activities unless they were incidental to the business of equipment leasing, hire-purchase or merhant banking. It will be evident from the subsequent paragraphs that ABFSL in effect carried on these activities not as incidental to approved business but as independent activities.

3.1 ABFSL commenced its business activities from 1 July 1991. It mobilised its deposits mainly through its branches at New Delhi, Madras and Bombay and deployed its funds mainly through its branches at Bangalore and Bombay.

3.2 As per the audited Balance Sheet of the Company as at 31 March 1992, ABFSL had unsecured loans of Rs.210.81 crores (consisting of fixed deposits Rs.6.67 crores and inter-corporate deposits Rs.204.14 crores) and owned funds of Rs.7.41 crores' thus, the aggregate available funds were Rs.218.22 crores. These funds were deployed as under :-

	(Rs. in crores)
Investments	129.57
Balance with Andhra Bank	81.19
Bridge loans against capital issues	5.11
Leased assets	3.53
Stock on hire under Hire Purchase Agreements	1.38
Other assets (Net)	(2.56)
	218.22

3.3 Thus, apart from marginal investments in leased assets and hire purchase assets, the bulk of the funds were either invested in securities or were placed with Andhra Bank. The funds placed with Andhra Bank as at 31 March 1992 were substantially withdrawn in the first fortnight of April 1992 and were possibly intended to boost the deposits of that bank as at 31 March 1992.

4.1 Of the unsecured loans of Rs.210.81 crores, Rs.204.14 crores represented inter-corporate deposits collected by ABFSL. The period for which the deposits were accepted ranged from one day to one year, and the interest paid on these deposits has ranged from 10.5% to as high as 37.5%. However, in addition to these inter-corporate deposits ABFSL also offered an "Investment Service" to its clients, under which it accepted short-term funds for deployment in securities. The total funds so collected and outstanding on 31 March 1992 were Rs.310.91 crores. These funds were presumably placed with ABFSL for investment purposes and therefore have not been reflected in ABFSL books as borrowings. However, the correspondence with the depositors, the form of receipt issued and the internal documentation make it quite clear that these were in fact deposits where the rate of interest and the period of the deposit were agreed with the client. There does not appear to have been any transfer of securities to the client on the sale of the securities by ABFSL, but only Security Receipts have been issued. ABFSL has been receiving/holding BRs/ Security Receipts issued to it by various entities with whom its funds are deployed, against the Security Receipts issued by it.

4.2 The Security Receipts issued by ABFSL were presumably for the sale of securities like Units or public sector bonds but there are instances where even the securities are not specified. Thus:-

(i) On 3 January 1992, ABFSL, New Delhi, wrote to Director Finance, HUDCO Ltd. referring to a telephonic confirmation dated 2 January 1992 "for investing through us an amount of Rs.50 crores in various money market assets so as to generate a composite yield of around 18.00% p.a. for a holding period of 45 days starting 3 January 1992". There is an endorsement on the letter addressed to the Managing Director, ABFSL, Hyderabad which reads "A sum of Rs.48 crores transferred to Bangalore and Rs.2 crores to Bombay. Please arrange to courier Bank Receipt to HUDCO /WITHOUT/ giving details of securities etc. under advice to us".

(ii) On 2 January 1992, ABFSL, New Delhi accepted a similar deposit of Rs.60 crores from HUDCO Ltd. with similar endorsement to the Managing Director.
(iii) In both cases, the letters from HUDCO forwarding the cheques for Rs.50 crores and Rs.60 crores state "Please arrange to invest the above amount today for the period of 45 days @18% (18.5%) p.a. and acknowledge receipt".

(iv) In both cases, the Security Receipts issued by ABFSL state that amount is received "for investment in various money market securities".

4.3 The 'Security Receipt' issued by ABFSL is similar to a "Banker's Receipt". It states that "the securities will be delivered when ready in exchange of this receipt duly discharged and in the meantime the same shall be held on account of" the client. Often these receipts were issued only after the transactions were completed and the monies refunded. Thus, ABFSL Hyderabad sent only on 19 December 1991, to its New Delhi Office, receipts for delivery to Power Finance Corporation in respect of the following deposits :

Date of receipt of funds	Amount (Rs.in crores)	Period of deposit (no.of days)	Due date
10.9.1991	5.47	91	10.12.1991
13.9.1991	3.13	52	4.11.1991
17.9.1991	9.28	70	26.11.1991
21.9.1991	6.86	83	13.12.1991
24.9.1991	6.00	80	13.12.1991
4.10.1991	6.25	74	17.12.1991
19.11.1991	54.20	30	19.12.1991

5. The bulk of the funds collected by ABFSL has been from public sector enterprises as is seen from an analysis of the "inter-corporate deposits" and "securities transactions" outstanding on 31 March 1992.

	Inter-corporate deposits		Securities transactions	
	Amount (Rs.in crores)	Percentage	Amount (Rs.in crores)	Percentage
Public Sector Enterprises	186.89	91.55	163.04	52.44
Others	17.25	8.45	147.87	47.56
Total	204.14	100.00	310.91	100.00

6.1 A substantial portion of the funds raised has been passed on to three parties namely, Fairgrowth Financial Services Ltd. (FGFSL), Hiten P. Dalal and Standard Chartered Bank presumably under ready-forward transactions. However, there is in most cases no evidence to show that there was a genuine purchase and sale of securities or delivery of the same but on the contrary, the internal documentation suggests that these were merely deposits of funds for specified periods at an agreed rate of interest. In fact, there is in most cases an exact identity between the funds received by ABFSL from its clients and the funds made available to these parties and also a fairly consistent margin between the rate of interest allowed to the client and the rate of interest received by ABFSL from these parties.

6.2 The fact that the ready-forward transactions with counterparties were in reality deposits at pre-determined rates is evident also from the rates at which transactions were effected. Thus, on 12 November 1991, ABFSL purchased from FGFSL 185 lakh Units @Rs.13.5135 for a total value of Rs.25 crores. On the same day it sold to FGFSL 185 lakh Units @Rs.14.4717 for delivery on 10 March 1992 for a total value of Rs.26,77,27,739.72. The transaction was therefore merely a deposit of Rs.25 crores with FGFSL for 119 days @21.75%.

7.1 During the period from 24 July 1991 to 29 May 1992, the Bangalore branch deployed an aggregate amount of Rs.913.01 crores under 127 contracts. All these contracts were with FGFSL. Though presumably ready-forward transactions, there was no exchange of securities and the payments were only supported by Security Receipts issued by FGFSL. The contracts were for various periods and the maximum amount of outstanding contracts during the period aggregated Rs.407.50 crores (on 24 January 1992).

7.2 During the period from 31 August 1991 to 26 May 1992, ABFSL as a whole (including its Bangalore branch) deployed through 229 contracts an aggregate sum of Rs.1731.80 crores. The parties with whom these funds were deployed are summarised below:

Name of counterparty	No.of contracts	Percentage	Aggregate value(Rs. in crores)	Percentage
FGFSL	124	54.15	894.81	51.67
Hiten P. Dalal	54	23.58	361.55	20.88
Standard Chartered Bank	11	4.81	314.02	18.13
National Housing Bank	2	0.87	31.02	1.79
Earmarked against ABFSL's own securities	11	4.80	8.15	0.47
Other parties	27	11.79	122.25	7.06
	229	100.00	1731.80	100.00

It will be seen that 78% in number and 73% in value of the contracts were only with FGFSL and broker Hiten P. Dalal.

8.1 The modus operandi intended to be used by ABFSL and FGFSL for the transactions between them is best illustrated by a letter ref:FGFSL:RO:1014:91 dated 4 February 1991 addressed by FGFSL to the Chairman, Andhra Bank, Hyderabad and marked for the attention of Shri Y.Sundara Babu, Deputy General Manager, who after the formation of ABFSL became its Managing Director. The letter from FGFSL was issued by Shri R.Lakshminarayanan, Director (Finance & Administration).

8.2 This letter, after referring to a discussion with Shri Y. Sundara Babu lists the services which FGFSL can render to ABFSL and states that -

> "Fairgrowth Financial Services Limited proposes to deal actively in major money market securities like Government securities, Guaranteed bonds, Units of UTI, Tax Free/Taxable Public sector bonds, Treasury Bills, Commercial Paper, Certificate of deposits, etc. Your Bank will act as our Bankers for carrying out the money market operations on our behalf. The broad requirements of this activity are given in Annexure 2".

8.3 Annexure 2 made inter-alia the following proposals :

> "As part of the Money Market operations we intend to carry out the following functions :
>
> * match-making in securities for a spread
> * Portfolio Management for Public/Private corporate sector clients backed by the aforesaid financial assets
> * Conducting Buy-Sell operations in financial assets on behalf of Public/Private corporate clients.

Our experience in the Money Market shows that this market is by and large a 'Bank/Money Receipt Market' rather than a 'Physical Securities Market'. Security purchase and sales are conducted in the Market place on the basis of 'Bank/Money Receipt' according a right on the within mentioned securities and these Receipts are exchanged for physical assets/SGL only after a considerable lapse of time.

Further, as we propose to mobilise surplus funds from Public/Private Corporate Sector, we reckon that we may encounter situations wherein the client may be willing to provide in funds for management but may be prevented by the restrictive covenants of their investment guidelines.

To overcome such procedural difficulties, we hereby propose that your bank act as our Bankers for carrying out the Money Market operations on our behalf. The broad requirements of such a role are listed here under:

a. To receive Bank/Money Receipts in your name, in respect of Securities purchased by us. Payment will be made by you to the debit of our account with you.

b. To issue YOUR Bank Receipt in respect of securities sold by us. Sale proceeds received will be credited by you to our account with you.

c. To make offers of Purchase/Sale to our clients in your own name, on our behalf.

d. To make offers to manage surplus funds of our clients in your own name, on our behalf.

e. To extend quotations and to respond to tenders in respect of Private Placement Issues of Public Sector Bonds and/or investment proposals, in your own name on our behalf."

The Annexure then listed out the back up commitments by FGFSL and the remuneration proposed.

The back up commitments proposed by FGFSL were as follows :

> "* in respect of match-making proposals, we undertake to square off the transactions on the same day
>
> * where offers of Purchase/Sales have been made by you on our behalf, reverse tie-up will be extended by us. For (ex) where an offer of purchase has been made by you on our behalf to X Ltd., we shall make an offer of purchase from you at a rate which is equal to the rate quoted by you to X Ltd.

- where offers to manage the surplus funds of our clients have been made by you, on our behalf, we shall provide you reverse tie-up for such transactions

- where quotations have been extended or tenders responded to by you on our behalf, back up quotation will be provided by us to you."

8.5 The remuneration proposed was 25% of the realised spread in respect of purchase/sale offers and quotations/tenders, and a minimum spread of 0.10% per annum for offers to manage surplus funds.

9.1 The fact that actual dealings between ABFSL and FGFSL were on the lines contemplated in the letter of 4 February 1991 is illustrated by the following transactions.

9.2 On 13 March 1992, Shri Tharian Chacko, Senior Vice President, Bangalore office wrote to the Managing Director, ABFSL regarding a subscription of Rs.25 crores by ABFSL to 9% tax free bonds issued by National Power Transmission Corporation (NPTC). This letter stated that :-

(i) On 10 March 1992, ABFSL had received from NPTC the allotment letters for Rs.25 crores.

(ii) The bonds were subscribed at the rate of 86/100 and the equivalent of Rs.21.50 crores was placed by NPTC with ABFSL @13.75% for a period of one year as inter-corporate deposit with interest payable half-yearly. The deposit was to mature on 10 March 1993.

(iii) The funds received from NPTC were placed together with a difference in sale price of 0.50/100 with FGFSL for a period of 12 months for an aggregate value of Rs.21.625 crores.

(iv) "Two contracts in continuation R/F against units" were made, the first contract to fall due on 30 September 1992 and the second contract to fall due on 10 March 1993. The rate of return was 14.75%.

(v) Xerox copies of the memoranda of sale and purchase and security receipts were enclosed. As bonds of Rs.5 crores were to be offered to the public, the sale contracts were for "Rs.20 crores (outright) @86.50/100" and for "Rs.5 crores R/F for 90 days due on 08/06/92 @86.50/100".

(vi) The documents enclosed included :-
- a security receipt No.S.R. 625/91-92 dated 10 March 1992 issued by FGFSL and signed by Shri R.Ganesh for 149,00,000 Units @Rs.14.51342.
- FGFSL's memorandum of purchase dated 30 September 1992 (i.e. post-dated) signed by Shri R.Ganesh for 160,00,000 Units @Rs.15.02 for delivery on 10 March 1993.
- FGFSL's memorandum of sale dated 30 September 1992 (i.e. post-dated) signed by Shri R.Ganesh for 160,00,000 Units @Rs.13.5156 and stating "delivery through Security Receipt SR No.626/91-92" (i.e. the next consecutive number to the security receipt No.625/91-92 issued on 10 March 1992.)

Thus the funds amounting to Rs.21.50 crores received from NPTC were passed on to FGFSL and fictitious paper work created to show a ready-forward transaction in Units.

10. The letter dated 4 February 1991 (referred to in paragraph 8 above) and the subsequent conduct of ABFSL and FGFSL clearly suggest that :-

(i) ABFSL was acting merely as a conduit for the diversion of funds mainly from public sector enterprises to FGFSL;

(ii) the public sector enterprises were really the clients of FGFSL who must have arranged for the funds;

(iii) this device was used to circumvent the restrictive covenants of the investment guidelines of those institutions and the procedural difficulties;

(iv) the money market was viewed as a "Bank/Money Receipt Market" rather than a "Physical Securities Market" and therefore transactions were made merely by exchange of Bank Receipts (with no assurance of the existence of underlying securities) and not by physical transfer of securities;

(v) the so-called "ready-forward" transactions were no more than a facade for the receipt of deposits from public sector enterprises for fixed periods and at fixed rates of interest and for the diversion of those funds to FGFSL again for fixed periods and at fixed rates of interest.

11. The modus operandi of the transactions with other parties particularly broker Hiten P. Dalal is not as candidly documented as in the case of FGFSL but the internal documentation of ABFSL can only lead to the conclusion that the nature of the transactions between ABFSL and these parties was no different from the nature of the transactions between ABFSL and FGFSL. This can be clearly seen from the following extracts from the "Daily Transaction Reports" submitted by the Bombay Branch to the Managing Director, ABFSL, Hyderabad.

"To,
The Managing Director
Andhra Bank Financial Services Ltd
Hyderabad

From :
Andhra Bank Financial
Services Ltd
Bombay

Transaction Report - 6.4.1992 (Rs.in crores)

	Funds received from			Amount (Rs.in crores)	Funds deployed				Amount (Rs.in crores)
Our Ref. No.	Centre/ Orgn. Repayment from	No. of days	Rate of Return		Through/ Remitted to	No. of days	Rate of yield	Due Date	
6/92	NDL/KRIBCO	236	22	25.00	FGFS	15	24	21/4	25.01
7/92	HYD/NMDC	30	19	2.15	BSG	30	21	6/5	2.15
8/92	BOM/NPC	90	21	25.00	HPD	90	22	5/7	25.00
9/92	HYD BDL	30	19.5	4.00	HPD	30	21	6/5	4.00
10/92	B'lore FGFS	1		15.00	SCB	1	22	7/4	15.00
11/92	(BSES FGFS Funds) of date 18/2			22.50	FGFS	80	22.5	25/6	22.48*

* 'BSES reinvested their total yield of their reversal of Rs.22.05 crores for 80 days @ 21.5%. Please take this as new investment 11/92'."

12. A letter dated 8 February 1992 addressed by the Bangalore Office of ABFSL to the Managing Director gives some details of ledger extacts of FGFSL where ready/forward deals have been entered into by FGFSL with varous money market operators as also the "name of the operator from whom purchase or sale is effected". A large number of these names are of sharebrokers and it is obvious that the funds made available by ABFSL to FGFSL have in turn become available to these brokers.

13.1 The absence of adequate securities to back ABFSL's alleged ready-forward transactions has exposed it to the risk of loss arising from the counterparties' inability to reverse the transactions.

13.2 As on 30 June 1992, ABFSL had 18 contracts outstanding at Bangalore branch and 18 contracts outstanding at Bombay branch with FGFSL for an aggregate value of Rs.170.34 crores and Rs.78.26 crores respectively making a total of Rs.248.60 crores for which reversals have not been effected by FGFSL. ABFSL holds against these contracts securities to the value of Rs.266.03 crores. However, the following securities have been found to be forged/fabricated.

		(Rs. in crores)
i)	Units of UTI	151.12
ii)	9% HUDCO bonds	45.00
iii)	9% NPTC bonds	15.00
		211.12
Less :	Earmarked to AB Homes	6.00
		205.12

Against these forged/fabricated securities, FGFSL delivered securities of Rs.101.59 crores before FGFSL was notified on 2 July 1992 under the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992 and securities of Rs.112.29 crores after the notification.

13.3 In this connection, it is interesting that before the forgery was detected in the circumstances explained in the Committee's second Report, according to a note submitted by Shri Y. Sundara Babu, Managing Director, ABSL, Shri R. Ganesh Asst. Vice President, FGFSL had called on him on 24 June 1992 pleading for the return of the Units lodged, stating that they were borrowed securities and on 25 June 1992, Shri R. Lakshminarayanan, Executive Director of FGFSL also met him and requested him not to liquidate any of these securities as the markets were very depressed.

13.4 As at 30 June 1992, the Bombay branch of ABFSL had the following outstanding contracts with parties other than FGFSL:-

Name of counterparty	Aggregate value of contracts (Rs.in crores)	Nature of security	Aggregate face value of securities (Rs.in crores)
Hiten P. Dalal	140.27	PSU bonds	156.87
V.B. Desai and equity	39.21@	PSU bonds	40.00@
B.S. Gandhi	2.50	PSU bonds	3.00
National Housing Bank	24.47*	BRs covering PSU bonds	26.50*
	206.45		226.37

@ Rs.9.56 crores outstanding as on 25 February 1993.
* Since repaid.

14.1 The audited Balance Sheet of ABFSL as at 31 March 1992, shows that it held the following investments :

	Face Value (Rs.)	Book Value (Rs.)
Kisan Vikas Patras	-	75,00,000
Units of U.T.I	-	65,65,36,151
9% IRFC bonds	5,09,59,000	5,09,01,123
9% PFC bonds	27,05,00,000	27,05,00,000
9% SCICI bonds	16,50,00,000	16,50,00,000
9% HUDCO bonds	2,70,28,000	2,69,67,488
9% NHPC bonds	6,00,00,000	6,00,00,000
9% REC bonds	57,84,000	53,33,151
13% NPC bonds	5,30,00,000	,30,00,000
		1,29,57,37,913

14.2 According to a certificate dated 15 June 1992 issued to the auditors of ABFSL by Shri Y.Sundara Babu, Managing Director, investments of Rs.62,82,37,913.36 were held by Bombay Office and investments of Rs.66,00,00,000 were held by Bangalore Office. Presumably the Kisan Vikas Patras of Rs.75,00,000 were held at its Madras Office. The certificate goes on to state that "We have as of date disposed of a majority of the above investments. Our Bombay Branch is holding investments of Rs.8,59,01,123/68 ps. and Bangalore Office is holding investments of Rs.21,50,00,000 out of the investments as on 31.3.1992. We certify that the investments are physically available."

14.3 It appears that the auditors have not visited the Bangalore and Bombay Offices and therefore have not verified the investments. There are on the records of the Head Office of ABFSL, copies of confirmations obtained by the Bombay branch of investments held in safe custody account by Andhra Bank as on 28 September 1991 and 12 December 1991. No such confirmation is available as at 31 March 1992. There is therefore no evidence to establish that the investments shown on the Balance Sheet as at 31 March 1992 were in fact available with ABFSL. There is also no evidence and in fact, there are no details available to show what investments were available with ABFSL for purchases made under ready-forward deals and outstanding as on 31 March 1992.

14.4 It will also be seen that the investments for which face values are shown in the Balance Sheet as at 31 March 1992 have book values which are almost the same as the face value. All the investments are unquoted but there must have been a considerable depreciation in realisable values of the investments (particularly for 13% NPC bonds - face value Rs.5.30 crores) for which no provision has been made in the accounts.

15. The financial position of liabilities and assets of ABFSL as at 30 June 1992 is as under :-

		(Rs.in crores)
Public Deposits		7.85
Inter-corpoarate Deposits		387.46
Security Transaction Deposits		119.32
		514.63
Bridge Loans	5.70	
Leased Assets	3.52	
Stock on Hire	1.38	
Cash and Bank Balances	18.62	
Kisan Vikas Patra	1.00	30.22
Excess liability over assets other than securities		484.41

Against the above, ABFSL holds securities of the face value of Rs.308.33 crores, whose market value is estimated at Rs.246.66 crores. In addition, ABFSL holds :-

	(Rs.in crores) Amount
(i) Shares lodged by FGFSL pending transfer	22.97
(ii) Bank receipts issued in favour of ABFSL	10.00
(iii) Additional securities lodged by FGFSL	68.60

16.1 ABFSL has confirmed that it is holding 13,50,000 shares of M/s.Gold Star Cements Ltd. and 324,720 shares of M/s.Solidaire India Ltd. for which it has no security transactions. The circumstances in which these investments are held have been explained by ABFSL as follows :

(i) "ABFSL arranged a loan of Rs.2.00 crores to one Shri N.Krishna Mohan, Managing Director of M/s.Gold Star Steel Alloys Ltd., given by Sri Hiten P. Dalal. As a security Shri Krishna Mohan had delivered 13,50,000 shares of M/s.Gold Star Cements Ltd. Shri Krishna Mohan repaid the principal amount including interest thereon amounting to Rs.22,15,140/- on 26 October 1992 and requested for the return of shares lodged by him. The total amount of Rs.2,22,15,140/- was placed in fixed deposit with Andhra Bank in the name of the Custodian".

(ii) "Loans aggregating Rs.40.50 lakhs were arranged to Sri A.N. Srinivasa Rao and Sri A.S. Ramana Prasad given by M/s.Fair Growth Financial Services Ltd., as a security they have delivered 3,24,720 equity shares of M/s.Solidaire India Ltd. They have not yet repaid the amount. We are holding the shares lodged by them. The matter was reported to the Custodian".

16.2 It is seen that on 21 April 1992 and on 28 April 1992, HPD paid to ABFSL two amounts of Rs.1 crore each out of his account with Andhra Bank. The receipt of the first amount is recorded in the carbon copy of the daily "transaction report" of 21 April 1992 submitted by the Bombay branch to the Managing Director. This entry appears to have been inserted later in ink and records the receipt from HPD, the deployment by transfer by Telegraphic Transfer to Hyderabad, the assets as 'Gold Star'. There is no similar entry for the second amount received on 28 April 1992 in the "transaction report" of that date.

16.3 In the statements submitted to the Board of Directors at its meeting on 23 March 1992 is a statement showing "details of the underwriting/standby support given by the company since December 1991 till March 15, 1992". This statement includes underwriting/standby support of Rs.50 lakhs for a right issue by M/s.Goldstar Steel and Alloys Ltd. with a remark "sanctioned Bridge loan for Rs.50 lakhs and acting as co. managers".

16.4 ABFSL were managers to the rights issue, had provided underwriting/standby support, and had sanctioned a bridge loan to M/s.Goldstar Steel and Alloys Ltd. Further, (i) the funds had been routed through ABFSL, (ii) the shares were lodged with ABFSL and (iii) the repayment by Shri N.Krishna Mohan was to ABFSL and not to HPD. The above facts suggest that ABFSL had not "arranged" the loan but in fact had entered into "back to back" transactions whereby it had borrowed the funds from HPD and lent the same to Shri Krishna Mohan but had not recorded the transaction as a borrowing and a loan.

17. On 30 March 1992 and on 6 April 1992, ABFSL received from Bombay Suburban Electric Supply Co. Ltd. (BSES) Rs.26.43 crores and Rs.22.485 crores respectively presumably for investment in Units, due for reversal on 29 June 1992 and 25 June 1992. These funds were passed on to FGFSL. These transactions were not reversed on the due dates. On a claim made by BSES, ABFSL has claimed that FGFSL was to make delivery of the Units. FGFSL initially claimed that Units had been delivered to BSES which claim was denied by BSES. Later, FGFSL stated that the securities offered to BSES were not accepted by them and it intended to earmark securities of Rs.40 crores for the benefit of BSES. Neither delivery has been made to date nor have the amounts been repaid to BSES.

18. On the basis of the facts enumerated in earlier paragraphs, it is obvious that ABFSL acted as a conduit for the transfer of large sums mainly from public sector enterprises to the stock market by diverting these funds mainly to FGFSL (who in turn presumably deployed the funds with brokers) and to Hiten P. Dalal. This diversion was done on a pre-determined basis enunciated in FGFSL's letter to Andhra Bank dated 4 February 1991 and contrary to the purpose for which Andhra Bank was given permission by the Reserve Bank of India to float a subsidiary. This debasement of the true role of ABFSL appears to have been done with the full knowledge of and under the direction of the bank's top management.

In fact the manner in which ABFSL has functioned since its inception would almost seem to suggest that ever since the subsidiary was formed, it has acted only for the benefit of FGFSL and Hiten P. Dalal.

VI. State Bank of Patiala

1. Though State Bank of Patiala (SBP) is not faced with any problem exposure, the functioning of

the bank's treasury operations, particularly during March-April 1992, exposed the bank to a high risk. As on 31 May 1992 the bank held BRs of face value Rs.275 crores of National Housing Bank (NHB) (purchase price Rs.337.85 crores) relating to deals routed through broker Harshad S. Mehta (HSM) concluded between 21 February 1992 and 20 April 1992. Details of these BRs are given below :

(Amount in Rs. crores)

Sr. No.	Particulars of Investment	Face Value	BR dated	Issued by	Transaction Amount	Broker
1.	182 days Treasury Bills	50.00	21.2.92	NHB	48.00	HSM
2.	3 crore Units of UTI	30.00	14.3.92	NHB	44.98	HSM
3.	1 crore -do-	10.00	16.3.92	NHB	14.98	HSM
4.	2 crore -do-	20.00	16.3.92	NHB	29.97	HSM
5.	6.5 crore -do-	65.00	13.4.92	NHB	99.77	HSM
6.	17% NTPC Bonds	100.00	20.4.92	NHB	100.15	HSM
		275.00			337.85	

However, NHB has since repaid the transaction amount of Rs.337.85 crores to the bank on 2 June 1992, 24 June 1992 and 6 July 1992 and the BRs have been discharged and returned to NHB.

2. An examination of the deals during the period indicates that an unwritten exposure limit of Rs.25 crores per deal was being maintained during the year 1991 though the Head Office had not framed any exposure limits. However, this unwritten limit was not observed in 1992, particularly in deals through HSM and with NHB, a completely new counterparty for SBP. The decision taken by the bank's Investment Committee regarding deals with NHB on 13 and 20 April 1992 deserves special mention. The investments in Units/PSU bonds (non-SLR investments) were usually made out of the bank's surplus funds which were around Rs.120 crores. In a departure from the practice of investing only from the bank's surplus funds, the Investment Committee gave post facto approval on 16 April 1992 for purchase of 6.5 crore Units at a cost of Rs.99.77 crores from NHB (deal date 13 April 1992) on an expected net gain of 2% per annum. Again, on 18 April 1992, the Committee approved purchase of 17% NTPC bonds of face value Rs.100 crores from NHB @Rs.96.00 (deal dated 20 April 1992). Both the purchases were financed out of funds borrowed from the call market at 42.5 per cent and 21 per cent per annum. Significantly, to pay for the purchase of 17% NTPC bonds of face value Rs.100 crores from NHB, the bank borrowed Rs.60 crores from NHB itself. There was nothing on record to indicate how the bank anticipated a rise in the market price of the bonds within one month, - the period for which it intended to hold the bonds before selling them.

3. Although SBP has claimed that the deals were outright purchases, as per the records of NHB these were ready forward transactions due for reversal in the first/last week of May 1992.

4. As mentioned in Chapter VI, paragraph 5 (d) of the second Report of the Committee, SBP on the instructions of NHB had made the payment of Rs.44.98 crores, being the purchase price of Units of the face value Rs.30 crores, directly to SBI on 14 March 1992 and the amount had been credited by SBI

to HSM's account. The money paid by SBP to NHB for its purchases found its way to HSM's current account at SBI and ANZ Grindlays Bank. It would appear that the purchases by SBP of the securities from NHB were a part of a total arrangement whereby funds were made available to HSM. Incidentally, of an aggregate turnover of Rs.1450 crores in the bank's investment transactions between 1 April 1991 and 23 May 1992 effected through brokers, the business routed through HSM was Rs.850 crores (59%).

VII. Vijaya Bank

1.1 The bank's investment transactions in Government securities are handled by the Merchant Banking and Marketing Division (MBMD), Nariman Point, Bombay on the basis of instructions received from its Head Office located at Bangalore. The bank did not trade in Government securities except in Treasury Bills.

1.2 The bank purchased Treasury Bills on several occasions on ready-forward basis from Discount & Finance House of India Ltd. (DFHI), e.g. on 18 and 28 June 1991, 1, 12, 26 and 29 July 1991, 21 March 1992, 3 and 16 April 1992, without receiving the SGL transfer forms from DFHI. Similarly, reversals were done without issue of SGL transfer forms. As such, these purchases and sales have not been reflected in the SGL accounts at RBI of both the bank and DFHI. It was observed that the "deal settlement sheet" received from DFHI merely recorded a remark "Bills with DFHI".

Portfolio Management Scheme (PMS)

2.1 The bank started rendering PMS services (earlier called Cash Management Scheme) since January 1987 mainly to cater to the needs of public sector corporations, e.g., National Airports Authority of India and Pawan Hans Ltd. As the bank's Investment Department was not geared to handle this activity, the funds were placed with Citibank, for a brokerage ranging from 1/4% to 3/4% per annum. Apart from the above arrangement, the bank also accepted and managed PMS funds by itself. The bank stopped fresh investment of PMS funds through Citibank on receipt of RBI circular dated 18 January 1991 which specifically stated that only those banks with necessary expertise and organisational capability to handle the services departmentally should offer PMS to their clients.

2.2 The Board of Directors at their meeting held on 22 June 1990 approved the setting up of a Portfolio Management Committee (PMC) and empowered the Chairman & Managing Director (CMD) to constitute the said Committee comprising General Managers and Dy. General Manager and Divisional Manager of the Investment Management and Marketing Department (IM&MD). The proposals were put up to the Committee by IM&MD and the decisions of the PMC were placed before the CMD for his approval.

2.3 The PMS funds were mobilised by the bank's New Delhi (Barakambha Road) branch, and deployed through Bombay (Nariman Point) branch. The securities were held at Bombay (Nariman Point) branch and at Head Office in Bangalore. A scrutiny of the bank's PMS operations revealed that the bank had not complied with several instructions/guidelines issued by RBI.

i) The bank did not conduct PMS in the nature of consultancy/ management for a fee at customer's risk. The same was conducted with an assured, predetermined return to the client.

ii) Though funds were accepted for periods exceeding a year, the bank agreed to disinvest the funds in durations of less than one year, e.g., in the case of Bharat Aluminium Co. Ltd. and International Airports Authority of India.

iii) Although the bank was maintaining a client-wise record of PMS funds accepted and investments made thereagainst, particulars of credits on account of realised interest, dividend, etc. and debits relating to the portfolio account were not reflected in the individual clients' accounts. Periodical statements of accounts were not furnished to PMS clients.

iv) Transactions between the bank's Investment Account and PMS clients' accounts were not put through at market rates.

v) The bank did not have an approved list of brokers. Most of the PMS transactions were put through the Kotak group; the bank's exposure to this group was to the tune of Rs.53.64 crores (66.6%) out of the total PMS funds of Rs.80.50 crores as on 31 March 1992.

3.1 The bank placed PMS funds aggregating Rs.20 crores with M/s.Kotak Mahindra Finance Ltd. (KMFL) at 15.75% p.a. on 8 August 1990. The amount was credited to the overdraft account of KMFL at the bank's Bombay (New Excelsior) branch. In terms of the bank (MBMD)'s letter dated 8 August 1990 addressed to KMFL, the amount of Rs.20 crores was for investment in negotiable bills of exchange. The company was required to send the bills to the branch. It was observed from the books of the branch that the bills/promissory notes lodged by the company for collection never aggregated Rs.20 crores on any day. Moreover, the first lot of bills aggregating Rs.4.11 crores was (as per the bank's PMS register) received only on 4 September 1990 though the entire Rs.20 crores had been disbursed on 8 August 1990. The deal which placed Rs.20 crores continuously for one year with KMFL, was therefore a clean advance to the extent of bills not lodged with the bank. The bank did not have title to the bills said to be held by the company and, as such, did not hold them as "assets" of its PMS clients.

3.2 In January 1991, as per RBI's instructions issued to all banks, deployment of PMS funds in bills was prohibited. However, the bank did not take any steps to withdraw the deployment with KMFL who repaid the amount only in August 1991. The bank's contention was that one of the reasons for not seeking refund from KMFL was the RBI guidelines which required that PMS funds should be placed for a minimum period of one year. This was not correct as the lock-in condition was applicable only between the bank and its PMS client. It is also observed that the arrangement with KMFL enabled the bank to circumvent RBI regulations in respect of bill discounting whereby only bills arising out of genuine trade transactions can be discounted. In the above case, the bills received for collection would have been scrutinised only in terms of the Letters of Credit under which they were drawn. It has been ascertained that KMFL had indeed discounted a few non-trade bills representing payment of utility charges (electricity bills) and had also lodged with the bank during the relevant period several promissory notes.

4.1 A scrutiny of the books of Vijaya Bank and KMFL has revealed that KMFL along with its associate company, Komaf Financial Services Ltd. (Komaf), has been acting as a conduit for diverting funds accepted by Vijaya Bank under its PMS service, into 'badla' financing. As on 19 June 1992, PMS funds of Vijaya Bank so routed by KMFL in badla financing stood at about Rs.36 crores. The modus operandi followed was similar to that in Ready Forward (RF) transactions and, in short, is as follows:

KMFL finances brokers against the security of their shares at rates of interest broadly comparable to the badla rates. Such financing of brokers against security of shares is duly supported by loan documentation and the brokers' authorisation to KMFL to sell the shares held as security. These shares which are received as security from the brokers are simulataneously sold to Komaf, which in turn sells the shares to Vijaya Bank in adequate quantities at prices comparable to those obtaining on that day in the secondary market. Vijaya Bank purchases these shares from Komaf on account of the PMS clients. The sale proceeds received by Komaf, are in turn passed on to KMFL which uses the money to finance the brokers who had lodged the shares. On the very day of sale by Komaf to Vijaya Bank, KMFL would separately agree and undertake to buy-back from Vijaya Bank the shares sold by Komaf to it at an agreed future date falling between six months to one year at a predetermined price which was agreed for and documented in the letters from KMFL to Vijaya Bank. This pre-determined price is so computed that it fetched Vijaya Bank (PMS) a fixed agreed yield. In some cases, KMFL has sold the shares directly to Vijaya Bank while Komaf has agreed to buy them back later. In this process,

(a) KMFL obtained funds from Vijaya Bank at the cost of its PMS clients at rates considerably lower than what it (i.e. KMFL) earned in the financing of the badla/vyaj badla transactions;

(b) PMS funds in fact were used to finance stock market operations.

4.2 Loans granted by KMFL to 29 borrowers as on 19 June 1992 aggregated Rs.78.50 crores; of this, the loans to Shri Uday S. Kotak (Rs.4.44 crores), Shri H.S. Jhaveri (Rs.28.48 crores) and J.S.B.Financial

Services Ltd. (Rs.10.23 crores) aggregating Rs.43.15 crores represented 'Vyaj' badla transactions. Amongst the rest, the largest borrower was Shri Subodh Shah at Rs.18.86 crores, also a broker who, like the other borrowers, had pledged his shares with KMFL as a security for the loan. It is ascertained that most of the sales to Vijaya Bank through Komaf were made out of the shares pledged by Shri Subodh Shah.

5.1 Some examples of typical PMS transactions put through by the bank are explained below.

The bank received Rs.3.30 crores on 27 June 1991 from Delhi State Lotteries and assured them a return of 14.75%. The amount was proposed to be invested in 13750 equity shares of ACC Ltd. @ Rs.2400 per share offered by KMFL. The deal was reversible on 27 June 1992 by sale to Komaf and the sale price of the shares was fixed at Rs.2787.50 to get a yield of 16.1%. KMFL is reported to have lodged the shares with blank transfer forms with the bank. But there is no record giving distinctive number of scrips at the bank to confirm this. The bank did not get the shares transferred to its name and it did not receive the dividend though it held the shares for one year. In effect this was a loan against the security of shares and violated RBI guidelines in the matter.

5.2 On 25 March 1992, out of surplus investible PMS funds, the bank purchased 6500 ACC shares at Rs.7700/- per share for an aggregate value of Rs.5 crores through Komaf and purchased other securities (shares) for aggregate value of Rs.2.98 crores through M/s.Fairgrowth Financial Services Ltd. Simultaneously, the bank entered into an agreement with KMFL to sell the same 6500 ACC shares on 23 June 1992 at Rs.8085.85 per share providing for a predetermined yield of 20.3%. Similarly, the bank entered into an agreement with M/s.Fairgrowth Investments Ltd. to sell the shares on 22 June 1992 providing for a pre-determined yield of about 21%.

5.3 On behalf of PMS clients, the bank purchased on 2 June 1992 various equity shares from Fairgrowth group companies for a consideration of Rs.5 crores. The bank also simultaneously entered into an agreement with these companies to sell back the same shares on 1 and 2 August 1992 for Rs.5.17 crores. The details of the two deals are given below :

Date of purchase/ sale	Equity share of	No.of shares	Rate (Rs.)	Total value (Rs.incrores)	Counterparty
PURCHASE					
2.6.92	South India Shipping Corporation	5700	3500.00	2.00	Fairgrowth Financial Services Ltd. (FGFSL)
SALE (Reversal leg)					
2.8.92	South India Shipping Corporation	5700		2.06	Fairgrowth Investments Ltd. (FIL)
PURCHASE					
2.6.92	Cochin Refineries Ltd.	1500	2250.00	0.34	FIL
	Eskayef Ltd.	8000	290.00	0.23	FIL
	GNFC Ltd.	25000	122.50	0.31	FIL
	GSFC Ltd.	10000	322.50	0.32	FIL
	Indian Rayon	50000	320.00	1.60	FIL
	NOCIL	1000	2060.00	0.20	FIL
				3.00	
SALE (Reversal leg)					
1.8.92	-do-	-do-		3.11	FGFSL

The two contracts were not reversed on the due dates and the bank was saddled with the shares it had purchased from the Fairgrowth group companies. The bank sold some of the shares at market price and realised Rs.1.50 crores. Against the balance dues of Rs.3.67 crores as on 2 August 1992, the bank is holding the undernoted shares purchased from these companies, the status of which is given below.

Particulars of security	Remarks
i) 5700 shares of South India Shipping Corporation	Shares are in the name of FGFSL and hence tainted.
ii) 1500 shares of Cochin Refineries Ltd.	Sent for transfer to bank's name.
iii)25000 shares of GNFC Ltd.	-do-
iv) 25500 shares of Indian Rayon	9000 shares are in the name of FGFSL and hence tainted; 800 shares received back with objection; 15700 shares have been transferred in bank's name.

The bank also held 2700 shares of South India Shipping Corporation, 2850 shares of Colgate, 11000 shares of Ponds (India) Ltd., 10000 shares of Siemen's India Ltd. and 9500 shares of Vam Organics pledged to the bank by the Fairgrowth group as collateral security. The above shares, except the shares of South India Shipping Corporation and Ponds (India) Ltd., have been transferred in the bank's name. It is surprising that the bank entered into the above deals on 2 June 1992 when the irregularities in the security transactions of the banks had already become known. The extent of likely loss to the bank has not been quantified.

6. In another instance of deployment of PMS funds, Vijaya Bank tried to window dress its profits as at end-March 1992 by putting through transactions in convertible debentures/shares of Reliance Petrochemicals Ltd. (RPL) between its own Investment Account and client's portfolio account at off-market rates.

i) In September 1988, the bank had subscribed to 60,000 12.5% fully convertible secured RPL debentures of Rs.200 each totaling Rs.120.00 lakhs. In April 1989, it had also purchased 2,50,000 additional debentures (Part B and C) at a market rate of Rs.174.50 as against their aggregate face value of Rs.190.00 each.

ii) In June 1990, when the market value of the debentures was less than their acquisition cost, the above debentures to the extent of book value of Rs.401.97 lakhs were transferred from the bank's own Investment Account to PMS clients account at book value with a view to avoiding provision for depreciation in its own investment account.

iii) These debentures of aggregate book value of Rs.401.97 lakhs stood converted into 48,90,000 equity shares of Rs.10/- each with effect from 26 October 1991.

iv) On 21 March 1992, the 48,90,000 equity shares were transferred to bank's own Investment Account from the clients' portfolio account again at book value when their market rates were much higher than the book value.

v) On 24 March 1992, the entire lot of 48,90,000 equity shares were sold by the bank at Rs.33.65 per share (net) for a total value of Rs.1645.49 lakhs which resulted in a net surplus of Rs.1243.52 lakhs to the bank.

By selling the RPL debentures to PMS clients at above market rates and subsequently purchasing them at rates below market prices, the bank deprived the PMS clients of their rightful dues. The Reserve Bank had taken a serious view of the bank's operating its PMS service to its own advantage and asked the bank not to take the profit of over Rs.12 crores derived from these transactions to its profit and loss account for the year ended 31 March 1992. The bank has complied with the instructions.

VIII. General

As mentioned in the third Report of the Committee, it is confining its work to an examination of the findings of the scrutiny already undertaken by the RBI Inspecting Officers under the direction of the

Committee and to report thereon. This work is still in progress and the Committee hopes to issue a further Report detailing its findings in respect of certain other banks and institutions. Simultaneously with the release of that Report the Committee will issue its final Report.

R.Janakiraman
Chairman

Y.H. Malegam

V.G. Hegde

C.P. Ramaswami

E.N. Renison

Vimala Visvanathan
Member-Secretary

BOMBAY
4 MARCH 1993.

Fifth Interim Report

April 1993

I. Introductory

On the basis of scrutinies carried out by the officials of the Reserve Bank of India, based on its examination of the securities transactions of banks and institutions and findings which could be derived, the Committee has so far submitted four Reports dated 31 May 1992, 5 July 1992, 23 August 1992 and 4 March 1993. It was mentioned in the fourth Report of the Committee that it will issue a further Report detailing its findings in respect of certain other banks and institutions. Accordingly, this Report is based on the scrutiny undertaken by the officials of the Reserve Bank of India, and contains findings in respect of some banks and institutions which have not been covered in the earlier Reports and further findings in respect of certain banks and institutions already covered in the earlier Reports.

II. Banque Indosuez

1.1 Banque Indosuez (BIS), a French bank, is having its only branch in Bombay. Till 24 July 1992 a specific investment policy was not framed by the bank. The Chief Executive Officer monitored the day-to-day operations in securities which were conducted by the Manager, Capital and Money Markets (CMM) Department in accordance with discussions held with the management at the "Treasury Meeting" every Monday. There was nothing on the record to show that any upper limit had been fixed for the Manager, CMM Department for undertaking operations in the investment portfolio, or that written confirmations were being obtained in respect of deals put through by him.

1.2 Some of the guidelines issued by the RBI in the circular of 26 July 1991 have not been complied with by the bank. There were a number of transactions in Government securities by issue of BRs when SGL facility was available. The BRs issued were not in the IBA format. There were several instances of bouncing of SGL transfer forms executed by the bank in respect of its sales transactions for want of sufficient balance in its SGL account. The bank had issued BRs covering sale transactions on account of its broker clients. In certain cases the rate of purchase or sale of securities was not in alignment with prevailing market rates. The bank was not maintaining any approved panel of brokers and was also not maintaining broker-wise record regarding brokerage paid.

1.3 The bank had entered into buyback deals in Government and other approved securities with non-bank clients and also undertaken buyback transactions in PSU bonds and Units, in contravention of RBI guidelines.

1.4 Reconciliation of SGL balance was being done only on half-yearly basis or as and when there were large transactions. As on 23 May 1992 it was found that there were differences in the case of 11.5% GOI Loan 2008 and 6.75% GOI Loan 1994 in which the balances as per the books of PDO were Rs.35.00 crores and Rs.20.00 crores respectively whereas the balances as per the bank's books were nil. These differences were subsequently reconciled.

2. Transactions through Harshad S. Mehta (HSM)

2.1 BIS had undertaken between 5 March 1991 and 23 April 1992, six deals in PSU bonds and Units aggregating Rs.94.00 crores on ready forward basis with UCO Bank (Hamam Street branch), Bombay and SBI Capital Markets Ltd. as counterparties. All these deals were entered into through the broker Harshad S. Mehta (HSM) or his associate concern M/s.Growmore Research & Assets Management Services Ltd. (GRAMS).

2.2 (a) The details of these transactions are given below :

Date	Nature of transaction	Particulars of security	Rate	Amount Face Value (Rs.in crores)	Settlement Value (Rs.)	Counter-party
5.3.1991	Purchase	9% REC bonds	102.40	4.00	4,26,16,986.30	UCO Bank
27.3.1991	Sale	-do-	100.00	4.00	4,00,88,767.12	-do-
3.4.1991	Purchase	-do-	100.00	10.00	10,03,94,520.54	-do-
6.4.1991	Sale	-do-	100.00029	10.00	10,04,68,783.15	-do-
26.6.1991	Purchase	9% IRFC bonds	97.87945	2.75	2,74,99,999.43	-do-
11.7.1991	Sale	-do-	98.12603	2.75	2,76,69,521.25	-do-
27.5.1991	Purchase	-do-	101.08	3.00	3,07,38,246.57	SBI Caps
26.6.1991	Sale	-do-	102.10878	3.00	3,12,68,798.38	UCO Bank
8.4.1992	Purchase	Units-1964	15.25	86 lakh Units	13,11,50,000.00	SBI Caps
23.4.1992	Sale	-do-	15.3503	-do-	13,20,12,580.00	Grindlays Bank
8.4.1992	Purchase	13% RINL bonds	85.00	14.00	11,95,98,356.16	SBI Caps
23.4.1992	Sale	-do-	85.02750	14.00	12,03,84,801.37	Grindlays Bank

(b) In respect of the three ready forward deals with UCO Bank's records that the amounts paid by BIAS (towards its purchases) were credited to HSM's current account with UCO bank and the payments received by BIS for its sales again came from HSM's current account with UCO Bank;. In the first ready forward deal, however, BIS incurred a loss of Rs.25.28 lakhs.

(c) Of the three ready forward deals with SBI Caps, the second (sale) leg of two deals was with Grindlays Bank and that of the third deal was with UCO Bank.

(d) The payments BIS for its purchases from SBI Caps under these three deals were made to SBI, where it has not been possible to verify the credits. On reversal, the payments to BIS came from HSM's current accounts in Grindlays Bank and UCO Bank.

(e) In the books of SBI Caps and Grindlays Bank, there is no record of these security transactions. Grindlays Bank has stated that these transactions had not taken place in its investment account with BIS and that it issued a pay order favouring BIS for Rs.25,23,97,381.37 on 23 April 1992 at the specific request of HSM.

(f) In the books of UCO Bank, the transactions were shown as being on account of the broker client HSM.

(g) All the six deals resulted in putting the broker HSM in funds for specific periods.

2.3 The deal slips and accounting vouchers prepared by the back office in BIS menion that the above transactions had been concluded through the receipt/ delivery of physical bonds/Units, However, there was no evidence to show that physical bonds/Units had actually been received or delivered from/to the counterparties in respect of these transactions. According to BIS, cheques for purchases were delivered against receipt of securities and sales were effected against receipt of cheques.

3. Transactions on account of broker M/s. Batliwala & Karani

3.1 The bank is maintaining a current account for the broker M/s. Batliwala and Karani. The security transactions were initiated and finalised by the broker for his own account and were routed through the Bank. The receipts and payments for sales and purchases were passed through the account. SGL transfer forms were issued by BIS in favour of the purchasing banks against SGL transfer forms from the selling banks brought by the broker for his purchases. The bank did not, however, maintain any separate SGL account for the broker's transactions and these were routed through the bank's own SGL account at the PDO.

3.2 There were a few instances of return of SGL transfer forms issued by the bank for want of sufficient balance in its account as SGL transfer forms received from other banks lodged by BIS with PDO for its purchases on account of the broker bounced. These were not reported to RBI as required.

4. Transactions with Fairgrowth group of companies

4.1 BIS had entered into 95 transactions (both purchases and sales) with Fairgrowth Investments Ltd. (FGIL) and eight transactions with Fairgrowth Financial Services Ltd. (FGFSL) between 1 April 1991 and 30 June 1992 in which FGIL and FGFSL were either counterparties or intermediaries, the details of which are as under :

		(Rs. in crores)
Purchases (58 transactions)		
	GOI securities (face value)	250.00
ii)	PSU bonds (face value)	147.80
iii)	Units of UTI (@ contract value at various purchase rates)	51.93
		449.73
Sales (45 transactions)		
i)	GOI securities (face value)	250.00
ii)	PSU bonds (face value)	147.80
iii)	Units of UTI (@ contract value at various sale rates)	51.72
		449.52

4.2 Some of the deals were found to be ready forward transactions in PSU bonds and Units. The back office records indicated Syndicate Bank and Corporation Bank as counterparties. The investment register also mentioned these banks as counterparties. Similarly, deal tickets, accounting vouchers and BRs were found prepared in the name of either Syndicate Bank or Corporation Bank. There were three purchase and sale deals in Units made out in the name of "Fairgrowth" as counterparty.

4.3 Between 1 April 1991 and 30 June 1992, BIS had issued, for its purchases (comprising 50 transactions) of PSU bonds and Units, cheques for a total amount of Rs.185.37 crores favouring these banks with instructions for crediting the same to the accounts of FGIL and FGFSL, as under :

(Rs.in crores)

Cheque favouring	FGIL	FGFSL	Total
Corporation Bank	63.71	-	63.71
Syndicate Bank	85.06	36.60	121.66
			185.37

In respect of some purchases, there were letters from Syndicate Bank and Corporation Bank which were in the nature of cost memos. In the case of some deals, although cost memos were received from FGIL and FGFSL, BIS recorded these deals naming one of the banks as counterparty. BIS has explained that the cheques in payment of all the purchases were issued in favour of either of the banks and that these were invariably delivered to the two banks with covering letters for crediting the amounts to the account of FGIL or FGFSL. The bank's computer print-outs had classified only three deals (in purchases) and four deals (in sales) as 'ready forward'. However, it would appear that all the deals had been concluded with the tacit understanding of the companies to buy back the securities and were thus in the nature of ready forward transactions with a view to putting the two companies in funds.

4.4 In the case of transactions in Units, purchases and sales had taken place only by exchange of cheques; delivery of Units did not take place. Of the 50 purchase deals pertaining to PSU bonds and Units concluded with Syndicate Bank and Corporation Bank, as many as 22 deals were through mutual exchange of cheques. The bank has stated that the Units were lying with it and the mode of delivery was mentioned as BR. However, scrutiny revealed that BRs were not issued in many cases. Till April 1992, the bank was not posting transactions in Units in 'Investment Register' and it has begun doing so only after the same was brought to its notice. There is no register to record physical Units held, receipts and issues thereof.

4.5 Between 6 November 1991 and 21 April 1992 BIS had entered into 23 ready forward deals in 13% MTNL bonds with FGIL/FGFSL mentioning Syndicate Bank or Corporation Bank as counterparty. These bonds of face value Rs.10.00 crores were originally purchased by BIS on 22 July 1991 from Standard Chartered Bank for which it received a letter of allotment issued by MTNL in favour of Canbank Financial Services Ltd. and endorsed in blank by the latter. Except in three transactions where BRs were received and issued by BIS the transactions were concluded by only exchange of cheques between BIS and the other two banks while the letter of allotment remained with BIS.

4.6 On 30 March 1992 BIS sold the above MTNL bonds to Corporation Bank by issuing its BR No.219. This BR came back to BIS on 21 April 1992 in reversal of the transaction of 30 March 1992, duly discharged on the reverse with a remark 'received payment'. On the same day (i.e. 21 April 1992) BIS sold these bonds to Syndicate Bank and issued its BR No.226. This BR was received back by BIS on 13 May 1992 duly discharged on the reverse with a remark 'discharged against Corporation Bank PO No.012406 dated 13 May 1992'. There was, however, no purchase by BIS from Syndicate Bank on that day. Enquiries made with Corporation Bank (Fort branch), Bombay revealed that it had issued the above pay order for Rs.10,33,79,722.26 in favour of Syndicate Bank on account of FGIL. Scrutiny of the photocopy of the letter of allotment in BIS revealed that there was an endorsement dated 13 May 1992 (name and designation of the signatory or the name of the bank/ institution was not mentioned) to the effect that "Received for obtaining BR No.226 from SB". It was stated by BIS that it had released the letter of allotment to an official of FGIL for obtaining back its BR No.226.

4.7 While scrutinising the transactions pertaining to 11.5% GOI Loan 2010 entered into through the intermediary of FGIL, it was found that BIS had received from FGIL besides its "handling charges" amounting to Rs.0.25 lakh, a sum of Rs.166.94 lakhs also. BIS has explained that this amount was paid to it on account of three deals entered into through the intermediary of FGIL in this security where the sale price as per the delivery order was lower than the purchase price and as the bank would not agree to suffer losses, FGIL had agreed to pay the difference. The bank could not show any evidence in support of this understanding, and apparently these deals were done over the telephone and thereafter cost memos etc. were prepared.

4.8 It is clear that the transactions with FGIL and FGFSL were purely money lending transactions, without security being transferred in most cases.

III. Corporation Bank

The bank's Funds, Investment and Merchant Banking (FIM) Department functioning at its Head Office in Mangalore was shifted to Bombay in August 1991.

2. The aggregate value of security transactions put through by the bank during the period April 1991 to May 1992 was Rs.5968.00 crores (face value) of which transactions for an amount of Rs.2122.00 crores (face value) were direct deals. Of the remaining transactions put through brokers, transactions through one broker, M/s.Kotak Mahindra Finance Ltd., accounted for 28.4 per cent. The bank had also put deals through brokers Harshad S. Mehta (HSM), Asit C. Mehta, Mukesh Babu, Excel & Co., Chandrakala & Co. and M/s.V.B. Desai who were not on its approved list.

3. The bank was not complying with the guidelines of the RBI and IBA relating to issue of BRs. Till 16 December 1991, it was issuing BRs in a format other than the one prescribed by the IBA. In some cases, BRs were signed by one official only. It was accepting BRs issued by other banks and institutions which were not in the IBA format. In two cases the bank returned the SGL transfer forms to the counterparty banks on reversal of the deals, without lodging them with the PDO at the time of purchase. The bank did not have on its record the specimen signatures of other banks' officials authorised to sign BRs.

4. The following transactions done by the bank through HSM may be noted.

(a) (i) On 1 January 1992, the bank purchased from SBI Caps through HSM 9% HUDCO bonds of the face value Rs.10 crores for which payment of Rs.9.44 crores was made to SBI.

(ii) On 31 January 1992, the above bonds were sold back to SBI Caps through the same broker and payment of Rs.9.56 crores was received from SBI.

(iii) The above transactions do not appear in the books of SBI Caps. There is nothing on the records of Corporation Bank to indicate that physical securities were received and delivered back.

(b)(i) On 9 January 1992, Corporation Bank purchased Units of face value Rs.10.00 crores from HSM and issued a pay order for Rs.13.55 crores in favour of Grindlays Bank with instructions to credit the amount to the account of HSM.

(ii) On 8 February 1992, the above Units were sold to SBI Caps through HSM, and the bank received a payment of Rs.13.71 crores from SBI.

(iii) There is nothing on the bank's records to show that the securities (physicals) or BRs were received from Grindlays Bank or HSM and delivered to SBI Caps.

(iv) The above transaction does not appear in the books of SBI Caps.

(c)(i) On 9 March 1992 Corporation Bank purchased from Punjab National Bank through broker HSM 17% NTPC bonds of the face value Rs.30 crores @96.2000. The bank made payment of Rs.29.52 crores to Punjab National Bank and received two BRs bearing No.389 for Rs.25.00 crores of PNB Mutual Fund and No.144 for Rs.5.00 crores of Punjab National Bank.

(ii) On 25 March 1992, the above bonds were sold to Grindlays Bank @95.9713 and the BRs of Punjab National Bank and PNB Mutual Fund were discharged against payment of Rs.29.67 crores received from Grindlays Bank.

(iii) The above transaction does not appear in the books of Grindlays Bank. The payment of Rs.29.67 crores was made by it by debiting HSM's account with it.

(iv) The records at Punjab National Bank show that the bonds covered by the two BRs were apparently delivered to Corporation Bank on receipt of the discharged BRs from it. As per remarks appearing on the discharged receipts, bonds for Rs.5.00 crores were delivered on 30 March 1992 and bonds for Rs.25.00 crores were delivered on 16 April 1992, although as stated at (ii) above Corporation Bank had already sold these bonds to Grindlays Bank on 25 March 1992. The original BRs are now stated to be with the CBI. Corporation Bank is unable to throw any light as to whom the bonds were delivered to. There is no claim from Grindlays Bank for the bonds.

(a) M/s. Fairgrowth Investment Ltd. (FGIL) an associate company of M/s. Fairgrowth Financial Services Ltd. (FGFSL) was maintaining a current account with the Bombay (Fort) branch of the bank since May 1991 and was obtaining pay orders in favour of other banks towards purchase consideration for its security transactions. The selling banks showed Corporation Bank as the counterparty to such transactions. On reversal of such transactions, while receiving payment from other banks on behalf of GFIL, the branch issued letters to those banks stating that the securities in physical from were being delivered. However, the letters did not contain any particulars of the scrips so delivered.

(b) There were 25 transactions during the period December 1991 to May 1992 in which the Bombay (Fort) branch had received payments from other banks in this manner. Of these, in 13 cases involving an amount of Rs.30.82 crores, payment was received from Banque Indosuez and in 10 cases involving an amount of Rs.81.69 crores payment was received from Syndicate Bank.

(c) In Syndicate Bank there is a clear indication (at least in four cases) that the statements made in Corporation Bank's letters that it was delivering securities were not true. Corporation Bank in its letters dated 27 March 1992, 30 March 1992 (two letters) and 6 April 1992 mentioned having made 'deliveries' of certain bonds purchased by Syndicate Bank and received payment. Immediately either on the same day or on the next day FGIL advised Syndicate Bank regretting its inability to deliver the said bonds and stating that instead, it was sending certain shares to be held till arrangement was made for delivery of bonds. There is also no record of any shares so delivered at Syndicate Bank.

(d) At Banque Indosuez, no evidence was available to show that it had received physical scrips in respect of these transactions.

(e) It appears that in these transactions, no physical scrips had changed hands and Corporation Bank had merely issued letters evidencing movement of securities at the behest of its client (FGIL). Corporation Bank has confirmed that in the purchase transactions of FGIL where it had issued pay orders at the request of FGIL, it did not receive any physicals or BRs on behalf of FGIL. Thus, these transactions were essentially money lending transactions by FGIL routed through its account with Corporation Bank, and the bank had willingly obliged it.

6. (a) During the first tranche of disinvestment of PSE shares by Government of India, Corporation Bank had bid for two bundles of shares (bundle Nos.65 and 120) at a bid price of Rs.16.51 crores and Rs.17.34 crores. Both the bids were successful and the bank was allotted the shares in February 1992.

(b) As per condition No.15 of the notice inviting bids for purchase of shares issued by Government, quoted in the Committee's second Report, the institutional purchaser could offload these PSE shares through the normal Stock Exchange transactions.

(c) The bank violated this condition by directly selling 6.10 lakh shares of MTNL to three brokers on 30 and 31 March 1992, before listing, as detailed below :

Name of the purchaser		No.of shares and rate	Amount received (Rs.in crores)	Date of sale
i)	Manubhai Maneklal	3.00 lakhs at Rs.285.00	8.55	30.3.1992
ii)	Desai & Dewanji	0.60 lakh at Rs.290.00	1.74	31.3.1992
iii)	Prime Securities Ltd.	2.50 lakhs at Rs.285.00	7.13	31.3.1992
			17.42	

The bank booked a net profit of Rs.7.61 crores in these transactions.

(d) The purchase of 2.50 lakh shares by Prime Securities Ltd. has been funded by the broker M/s.Jayantilal Khandwala & Sons through whom the firm had tendered its bid to Corporation Bank and which maintains an account with the Bombay (Fort) branch of Corporation Bank. Prime Securities Ltd. on the same day paid an amount of Rs.7.25 crores to M/s.Jayantilal Khandwala & Sons. through its current account at Standard Chartered Bank, Bombay. This account was in turn funded on the same day by receipt of an amount of Rs.7.58 crores from the current account of J.H. Mehta at Grindlays Bank, Bombay. Again, this account was funded on the same day by transfer of a sizeable amount (Rs.17.82 crores) from the current account of HSM at Grindlays Bank, Bombay. Thus, it would appear that payment for the purchase of shares has been made by HSM.

IV. Federal Bank Ltd.

The Federal Bank Ltd. (FBL) is one of the largest private sector banks in India. It has its headquarters at Aluva (formerly known as Alwaye) in Kerala State. The bank undertook a number of ready forward transactions in PSU bonds with other banks and some of the deals were also with non-bank clients.

2.1 FBL purchased and sold 9% NPTC bonds of face value Rs.15 crores at its Bangalore branch during March and April 1992, as set out in the table below. These deals as per books of FBL were shown as outright purchases and sales with ANZ Grindlays Bank (Grindlays), Andhra Bank and Andhra Bank Financial Services Ltd. (ABFSL). However, these transactions were actually found to be ready forward deals with Fairgrowth Financial Services Ltd. (FGFSL).

2.2 For the purchase on 17 March 1992, FBL's branch at Bangalore as per its records, received from FGFSL a contract note dated 17 March 1992 and an allotment letter of NPTC covering 9% NPTC bonds of face value Rs.15 crores. There was no record of receipt of transfer form duly signed by the holder in favour of FBL. The name of the holder was also not available in the records. Payment for the purchase was made by FBL's branch at Madras as advised by its Head Office to Grindlays in Madras by means of a pay order dated 17 March 1992 for Rs.13,52,58,904.11. The pay order was drawn in favour of Grindlays indicating therein "on account of purchase of 9% tax free bonds Rs.15 crores @ 90" and was reportedly handed over to a representat-

Date	Purchase/ sale	Rate	Counterparty as shown by FBL	Settlement amount (Rs.in crores)
17.03.1992	Purchase	90.00	Grindlays Bank	13.53
28.03.1992	Sale	90.2043	Andhra Bank	13.60
03.04.1992	Purchase	90.00	ABFSL	13.51
22.04.1992	Sale	90.3764	Grindlays Bank	13.63

(FGFSL was shown as broker in all the above deals.)

ive of FGFSL. In the books of Grindlays there was no sale of this security to FBL. The proceeds of the pay order were found credited by Grindlays to the account of FGFSL with it on the strength of a letter from FGFSL enclosing the pay order.

2.3 The sale consideration on 28 March 1992 was received by FBL's branch at Bangalore from Grindlays branch at Bangalore and the payment was by debit to FGFSL's account with the latter. In the books of FBL the counterparty for this deal was shown as Andhra Bank. There was no purchase transaction in the books of Andhra Bank, Bangalore branch. On receipt of the payment for the sale, the FBL's branch returned to FGFSL the NPTC's allotment letter. The contract note for this sale issued by FGFSL was dated 17 March 1992 i.e. the date on which the purchase was also effected, thus implying that it was a ready forward transaction and not an outright deal.

2.4 On 3 April 1992, the same security was again purchased from FGFSL and FBL again received NPTC's allotment letter. The purchase consideration was found credited by FBL's branch at Bangalore to FGFSL's current account maintained by the branch by debit to its Head Office account. For this purchase, the counterparty was shown as ABFSL.

2.5 While selling the security on 22 April 1992, FBL's branch received payment by means of a pay order from Grindlays with a covering letter that the pay order was issued on behalf of FGFSL. Evidently, the counterparty was FGFSL and not Grindlays as shown by FBL in its books. The NPTC's allotment letter was then returned to FGFSL by FBL's branch on that day.

2.6 The manner in which the payments were made to and received from FGFSL's account clearly established that the transactions were in effect deals under ready forward arrangement with FGFSL by FBL with a view to putting the company in funds to the extent of Rs.14 crores for about a month. These transactions could not have been put through without the knowledge of the top executives of FBL, as the payment instructions were issued by the Head Office. In the Head Office, the Board was informed through the note dated 26 September 1992 that the above mentioned four ready forward deals were outright purchases and sales with Grindlays/ Andhra Bank and that FGFSL was only the broker, which statement was incorrect.

3. In another case, FBL sold 9% IRFC bonds of face value Rs.6 crores on 27 April 1992 to a manufacturing company viz. Indian Rayon Industries @ 85.00 and bought back the same @ 86.4208 on 27 May 1992. The BR issued by FBL at the time of sale was received back by FBL on the reversal of the transaction. This amounted to placement of funds by the company with FBL for one month at an interest rate of around 30 per cent per annum. By treating it as a security transaction and not as a deposit, FBL has avoided maintenance of CRR and SLR and also violated the RBI's interest rate directive.

4. On 28 May 1992, FBL lent Rs.5 crores to Nedungadi Bank Ltd. (NBL) for one day and another sum of Rs.5 crores for four days. These transactions were not recorded in the books of NBL which after receipt of funds from FBL issued on the same day i.e. 28 May 1992 two pay orders for Rs.5 crores each in favour of Andhra Bank which credited the proceeds to the account of FGFSL. On the dates of the repayments, Andhra Bank debited the account of FGFSL and issued pay orders in favour of NBL which in turn issued its pay orders in favour of FBL. It will be seen that the money lent by FBL was intended for FGFSL apparently under an arrangement made by FGFSL with NBL as already mentioned in Chapter XI of the third Report of the Committee.

5. FBL's accounting for trading loss/gain on its investment portfolio is on average holding rate basis. It built up a huge position in 11.5% GOI Loan 2010 from the later half of 1991 and in January 1992, it was holding this loan to the extent of Rs.132.00 crores. The market value of this security depreciated after the hike in the coupon rates. The average holding rate of the security was around Rs.100.00. However, since this security suffered heavy depreciation, the bank accounted the purchases at the depreciated rates separately in order to take advantage of trading in this particular security instead of the normal accounting practice of booking the trading profit/loss on average holding rate basis. Adopting a different accounting procedure in a particular security alone is not in order. The bank has disposed of the major part of its investment in this security after April 1992 and absorbed the corresponding loss.

V. Karur Vysya Bank Ltd.

The total turnover of transactions in securities (both purchases and sales) by Karur Vysya Bank Ltd.

(KVB) on its own investment account for the period April 1991 to May 1992 amounted to Rs.9850.84 crores spread over 766 transactions which was disproportionate in relation to the size of its capital base and SLR requirements. The bank began trading in securities in a significant way since March 1991. Although it maintains SGL accounts in the PDO at both Madras and Bombay, the bulk of the transactions is put through in Bombay by its branch there, on the basis of specific instructions from its Head Office.

2. KVB had entered into certain purchase and sale transactions on the same day with the same bank in the same security through exchange of cost memos only without receiving or delivering any security by way of SGL transfer forms/BRs/physicals. The reasons for carrying out such transactions are not known. A few instances are shown as under :

Date	Counterparty	Name of broker	Security Value (Rs.in crores)	Face	Rate (Rs.in crores)	Cost
i) 4.5.1991	Purchase from UCO Bank	Harshad S. Mehta	11.5% GOI Loan 2010	10	100.78	10.42
4.5.1991	Sale to UCO Bank	-do-	-do-	10	101.2527	10.47
ii) 17.6.1991	Purchase from Bank of Karad	Excel & Co.	-do-	10	97.4703	9.76
17.6.1991	Sale to Bank of Karad	-do-	-do-	10	98.21	9.84
iii) 17.6.1991	Purchase from Bank of Madura	Ravi & Co.	-do-	10	97.6310	9.78
17.6.1991	Sale to Bank of Madura	-do-	-do-	10	98.75	9.89
iv) 26.8.1991	Purchase from Bank of America	Puran M.	-do-	20	99.955	20.35
26.8.1991	Sale to Bank of America	-do-	-do-	20	99.45	20.25

In the case of the transactions at item (i) above, the same were netted and KVB received the difference of Rs.4,72,700 from UCO Bank (Hamam Street branch). At UCO Bank the amount was debited to the current account of the broker Harshad S. Mehta (HSM) maintained with it. In the case of the transactions at item (ii), the amount of Rs.9.84 crores formed part of a Pay Order for Rs.14.79 crores (inclusive of the cost of another transaction for Rs.5 crores face value) received from Bank of Karad (BoK). The pay order had been issued by debit to the current account of Bhupen Champklal Devidas in BoK.

3. There was a simultaneous purchase and sale transaction with Citizen Co-operative Bank Ltd. (CCBL), details of which are shown below:

Date and nature of transaction	Name of broker	Nature of security	Face Value (Rs. in crores)	Contract Rate	Cost (Rs. in crores)
i) 22.2.1992 Purchase	P.R. Subramaniam	6% GOI Loan 1994	5	90.00	4.53
ii) 22.2.1992 Sale	Pushpanathan	-do-	5	94.6523	4.76

(a) Although the counterparty was indicated as CCBL, the transactions were netted out and the difference of Rs.23,30,700 was recived from ·UCO Bank. At UCO Bank, the amount was debited to the current account of the broker P.R. Subramaniam & Sons maintained with it.

(b) These transactions do not appear in the books of CCBL on 22 February 1992. The sale transaction at (ii) above through the broker Pushpanathan was a reversal of a ready forward transaction entered into with CCBL on 8 February 1992 @ Rs.94.60 for Rs.4.75 crores. KVB had entered into another ready forward transction in the same security with CCBL through the broker P>R> Subramaniam & Sons on 22 February 1992 @ Rs.90.00 for the purcchase (first leg) to be reversed on 6 April 1992.

(c) According to KVB, CCBL suggested that KVB keep the above security with it instead of delivering the same @ 94.6523 (reversal of the transaction of 8 February 1992), which was not acceptable to KVB. Instead, KVB asked the broker to cancel the transactions, which was not agreed to by CCBL. Consequently, the broker P.R. Subramaniam & Sons paid the difference of Rs.23,30,700 (between the prices at 94.6614 and at 90), referred to in item (a).

(d) The original ready forward transaction of 8 February 1992 was actually reversed on 6 April 1992 @ 94.8848 (settlement amount Rs.4.80 crores). KVB received the amount from CCBL and paid back Rs.23,30,700 to the broker P.R. Subramaniam & Sons.

(e) Apparently, the transactions (purchase and sale) put through on 22 February 1992 were intended to roll over the ready forward transaction originally entered into on 8 February 1992 which was to be reversed on 22 February 1992. The funding cost of this transaction to CCBL (earning to KVB) works out to 6.86 per cent per annum.

4. The bank had entered into 22 ready forward transactions for an aggregate amount of Rs.448 crores (face value) in PSU bonds/Units during the period April 1991 to May 1992 with banks/non-bank clients in contravention of Reserve Bank guidelines. These transactions were put through by exchanging BRs/physicals. Although these ready forward transactions were reversed on the due dates, KVB recorded them in its books as outright deals.

5.(i) KVB sold through HSM to State Bank of India (SBI) on 7 March 1992 11.5% GOI Loan 2010 of face value Rs.25 crores on ready forward basis. However, the reversal was made with Andhra Bank on 21 March 1992. According to KVB, the broker informed it on the date of reversal that these transactions were two different outright deals. In the books of SBI, the transaction does not appear as a purchase on its investment account, and the payment was debited to HSM's current account. In the PDO books, SBI's SGL account No.004 was credited with the purchase of Rs.25 crores. In the second leg, in Andhra Bank's books, its sale is reflected in the current account of the broker Batliwala & Karani, and in the PDO in the SGL account of the bank's clients.

(ii) On 20 April 1991 KVB purchased on ready forward basis through HSM 11.5% GOI Loan 2010 of face value Rs.10 crores from UCO Bank, for which UCO Bank issued its BR. The bank issued a pay order for Rs.10.42 crores in favour of UCO Bank which was credited to the current account of HSM maintained with it. On reversal of the transaction on 1 June 1991, although KVB returned the BR to UCO Bank, the payment of Rs.10.55 crores was received from SBI. The account to which the payment was debited in SBI books was not ascertainable, as the relevant records were seized by the CBI.

6.(i) A reference has been made by the Committee in its fourth Report in paragraph 7(e) and (f) of Chapter II regarding certain additional exposure of Standard Chartered Bank (Stanchart) covering two BRs issued by KVB for Rs.10 crores each (face value) relating to 9% IRFC bonds.

(ii) As regards the exposure of Rs.9.19 crores referred to in paragraph 7(e), the matter is still under dispute. According to Stanchart, although it had obtained the letter of allotment No.0056 from KVB, the matter was being investigated by it as its records indicated that there was an identical deal put through with another party at New Delhi for which the payment was released at Bombay. As reported earlier, KVB is yet to get back its BR duly discharged by Stanchart. Incidentally, the said security was in fact purchased by KVB from Stanchart earlier on 9 December 1991 for Rs.9.66 crores against the latter's BR, which was reportedly subsequently replaced by it with IRFC's letter of allotment No.0056. KVB accordingly discharged Stanchart's BR on 23 December 1991 and returned it to that bank.

(iii)(a) Regarding the exposure of Rs.9.32 crores referred to in paragraph 7(f), according to KVB, the letter of allotment No.0016 was delivered by it on 10 March 1992 to the broker N.K. Aggarwala & Co., New Delhi for onward transmission to Stanchart. The broker, in turn, delivered the letter of allotment to Hiten P. Dalal, the broker for Stanchart.

(b) On 11 May 1992, however, Stanchart sought the bank's confirmation that the BR issued by it for the sale was still outstanding. KVB drew Stanchart's attention on 11 June 1992 to the delivery of the letter of allotment No.0016 through its broker and sought the discharge and return of its BR.

(c) Stanchart informed KVB on 18 June 1992 of non-receipt of the letter of allotment and requested KVB to make alternate arrangements to deliver the allotment letter/physicals.

(d) In the meantime, ABN Amro Bank forwarded the above letter of allotment to IRFC together with blank transfer deed duly executed, under cover of its letter dated 26 June 1992 requesting them to transfer the letter of allotment in question in its favour. ABN Amro Bank came into possession of the above letter of allotment as an alternative security for its purchase of 17% NPC bonds for Rs.10 crores (face value) in a deal with Andhra Bank through its broker N.K. Aggarwala & Co. who had failed to deliver the same to it.

(e) Consequent on Stanchart reporting non-receipt of the letter of allotment, KVB approached IRFC on 26 May 1992 to withhold transfer of the bonds in anybody's name.

(f) KVB's request for issue of duplicate bonds was declined by IRFC, on the ground that there was no report from Stanchart about their loss or misplacement. Subsequently, on 2 July 1992, IRFC informed KVB that the original letter of allotment had been traced, as ABN Amro Bank had lodged it along with the transfer deed duly executed by KVB, and consequently the issue of duplicates of the bonds did not arise.

(g) The matter is still under dispute and Stanchart has since filed a suit in the Bombay High Court against KVB naming ABN Amro Bank and IRFC as co-defendents.

7. The other deficiencies observed are noted below :

(a) KVB had put through several transactions in Government securities, both outright and ready forward, by issuing/accepting BRs, when SGL facility was available for Government securities. Further, in the case of ready forward transactions in Government securities, it accepted BRs for its purchases or issued BRs for its sales and on the reversals, these BRs were either returned or received back. In some cases, it had also netted the SGL transfer forms for the purchases/sales made to certain banks on the same day.

(b) No register was maintained for recording the receipt of BRs. BRs issued by the bank did not bear any printed serial number and some BRs were issued without indicating any number.

(c) BRs issued by the bank were not in the format prescribed by IBA.

(d) The bank did not have a record of signatures of authorised officials of other banks for verification of signatures on BRs when received.

VI. Bank of Madura Ltd.

The Bank of Madura Ltd. (BoM), having its headquarters at Madras, conducts most of its treasury operations through its Bombay (Main) branch.

2.1 The total securities transactions undertaken by the bank between 1 April 1991 and 23 May 1992 totalled 2856 deals for Rs.18,621.73 crores (face value) on bank's investment account and 726 deals for Rs.7,255.50 crores (face value) on behalf of broker clients. The bank's own transactions were essentially arbitrage transactions in Government securities to book profit on account of interest/price differentials. The volume of trading had no relation to the bank's owned funds or SLR requirements. The turnover (both purchases and sales) in securities rose sharply from Rs.3,823.18 crores during 1989-90 to Rs.15,396.32 crores during 1991-92 in bank's investment account and from Rs.3410.56 crores to

Rs.6209.76 crores on behalf of clients.

2.2 In spite of a sharp rise in turnover, the returns on the trading undertaken in the bank's own investment account were not comparable with the returns obtained by its broker clients. For instance, between August 1991 and May 1992, on a trading volume of Rs.13,540.88 crores, the bank earned a meagre Rs.5.11 crores, while on a volume of Rs.5,079.78 crores, the brokers' earnings, as represented by net increase in credit balance in brokers' accounts, amounted to Rs.7.13 crores.

2.3 The reason for the wide variation appears to be the bank's practice of parting with its own securities for the benefit of broker clients. The method adopted was to sell its securities directly to broker clients or route the securities to them through the intermediation of another bank at such rates that the broker clients could trade in them on terms more favourable than those on which the bank was trading. In several cases the securities routed to the broker clients had been acquired by the bank under ready forward transactions and the brokers were then allowed to close these ready forward transactions with the counterparty/other banks at wide differentials resulting in large accrual of funds to them.

2.4 The bank's handling of broker clients' transactions which were back to back transactions, though not involving any outgo of bank's funds, exposed the bank to risk, totally disproportionate to the income derived particularly as the bank was maintaining only one SGL account with RBI for both its own and the brokers' security transactions.

3. Transactions for the benefit of, or on behalf of broker clients.

Some instances where broker clients were given undue benefits are discussed below :

(a) Chandrakala & Co., Broker/Client
11.5% GOI Loan 2007

Transaction date	Face Value (Rs.in crores)		Rate (Rs.)	Amount (Rs.in lakhs)	Counter-party	Mode	Dr/Cr to broker's current account (in Rs.)
IP 1.6.91	25	C	96.50	2446.16	Canfina	SGL	(Dr) 1 crore
		D	100.50	2546.16			
IS 5.6.91	25	C	96.5218	2449.11	Bank of Karad(BoK)	CM	(Dr) 7,70,500
		D	96.2136	2441.41			
CP 5.6.91	25		96.22	2441.57	-do-	CM	(Dr) 50,000 Services charges
CS 5.6.91	25		100.52	2549.07	Canfina	SGL	
11.5% GOI Loan 2010							
IS 1.6.91	25	C	100.29	2609.45	Canara Bank	SGL	(Cr) 1,00,16,750
		D	104.2967	2709.61			
IP 5.6.91	25	C	100.3082	2612.30	BoK	@	(Cr) 7,70,500
		D	100.00	2604.60			

C : Contract rate D : Delivery rate
IP - Investment Purchase, IS - Investment Sale
CP - Client Purchase , CS - Client Sale, CM - Cost Memo
@ - not available

(i) On 1 June 1991 BoM (Bombay) purchased the above security on ready forward basis for - 3 days - Rs.25.00 crores (face value) @ Rs.96.50 from Canfina. However, the transaction appears as outright in Canfina's books. Since, the delivery rate was higher at Rs.100.50, the broker paid the difference in price of Rs.1.00 crore.

(ii) On 5 June 1991 (instead of 4 June 1991) BoM sold the security to Bank of Karad (BoM) @ Rs.96.5218 instead of to Canfina (the original counterparty for the ready forward deal). However, since the delivery rate was Rs.96.2136, the broker paid the difference of Rs.7,70,500.

(iii)Simultaneously (5 June 1991), the broker Client Chandrakala & Co. purchased the same security @ Rs.96.22 from BoK and sold the same @ Rs.100.52 to Canfina thus completing the original ready forward transaction. Both the transactions involving BoK were on the basis of cost memos only.

(iv)On 1 June 1991 (as part of a double ready forward deal) BoM sold onready forward basis - 3 days - to Canara bank 11.5% GOI Loan 2010 - 25.00 crores (face value) @ 100.29. However, the transaction appears as outright in Canara Bank's books. Since the delivery rate was Rs.104.2967, the broker received the difference of Rs.1,00,16,750. On 5 June 1991 (instead of 4 June 1991) BoM purchased the same security @ Rs.100.3082 from BoK (instead of Canara Bank). The delivery rate being Rs.100.00 the broker received the difference amount of Rs.7.70,500. Thus the broker received a sum of Rs.1,079 crores, compensating him for Rs.1,077 crores paid to the bank on account of the difference in contract and delivery rates in the earlier set of transactions discussed at (i) (ii) and (iii) above.

(v) In the first transaction the bank earned Rs.2.95 lakhs only (besides service charges of Rs.0.50 lakh) while the broker earned Rs.107.50 lakhs.

(vi) The transactions in 11.5% GOI Loan 2010 recorded as a ready forward transaction (borrowing) in BoM's books at a cost of Rs.2.85 lakhs for 4 days, i.e. 9.8% p.a, is in reality a set of outright sale and purchase transactions structured so as to benefit the broker client.

(vii) Thus, in the entire set of transactions, BoM has earned Rs.0.10 lakh only, besides the service charges of Rs.0.50 lakh, against which the broker client earned Rs.107.50 lakhs.

(b) Chandrakala & Co. - Broker/Client
11.5% GOI Loan 2007

Transaction date	Face Value (Rs.in crores)		Rate (Rs.)	Amount (Rs.in lakhs)	Counter-party	Mode	Dr/Cr to broker's current account (Rs.)
IP 11.4.91	25	C	98.95	2477.36	Canara Bank	BR	(Dr) 51,25,000
		D	101.00	2528.61			
IS 12.4.91	25		98.9992	2479.19	UCO Bank	CM)	No cheque
IP 12.4.91	25		98.9992	2479.19	-do-	CM)	
IS 20.4.91	25		99.0173	2484.45	-do-	CM	
CP 20.4.91	25		99.025	2484.64	-do-	CM	
CS 20.4.91	25		100.60	2524.01	Canara Bank	BR(returned)	
CP 18.5.91	25		100.9335	2549.00	-do-	BR	
CS 18.5.91	25		101.8350	2572.00	Canfina	BR	

i) On 11 April 1991, BoM purchased on one day ready forward basis from Canara Bank 11.5 GOI Loan 2007. Rs. 25.00 crores @ Rs. 98.95, expecting an yield of 27 per cent. As the delivery rate was Rs. 101.00 the difference of

Rs.51,25,000 was paid by the broker. The difference was received from Andhra Bank by debit to the account of H.P. Dalal with that bank. The transaction appears as an outright transaction in the books of Canara Bank.

ii) On 12 April 1991, the broker, presumably on not being able to find a counterparty to reverse the transaction at the required rate suggested that he bank buy the security @ Rs. 98.99 for eight days at 9% yield. To give effect to this, the bank showed a dummy sale and purchase to/from UCO Bank on 12 April 1991 at the identical rate of Rs. 98.9992 which involved no cash outgo or inflow. The effect of the dummy sale was that the bank earned Rs. 1.83 lakhs in one day resulting in an yield of 26.6%. The dummy purchase resulted in the acquisition of the security at Rs. 98.9992. These dummy transactions thus enabled the bank to show closure of the ready forward transaction for 1 day on 11 April 91 at nearly the expected yield of 27 per cent.

iii) On 20 April 1991, the bank sold the same security to UCO Bank @99.0173 and earned Rs. 5.26 lakhs giving an yield of 9.5% for 8 days as per the offer of the broker client. In the two successive purported ready forward deals, the bank earned Rs. 7.09 lakhs at an average yield of 11.62%.

iv)Simultaneously on 20 April 1991 the broker client purchased the security from UCO Bank @ 99.025 and sold the same to Canara Bank @ 100.60. The UCO Bank thus "routed" the security from its portfolio to the broker on 20 April 1991 for a small profit of Rs. 0.19 lakh. The broker earned Rs. 39.37 lakhs.

v) The records of Canara Bank, however, indicate that the sale by BoM on 20 April 1991 was a ready forward transaction for one month up to 18 May 1991. Therefore on 18 May 1991 BOM purchased the security on client account @ 100.9335 and sold the same to Canfina @ 101.8350 giving a profit of Rs. 23 lakhs to the broker.

vi) The broker thus earned a profit of Rs. 62.37 lakhs in two same day purchase/sale transactions on 20 April 1991 and 18 May 1991. The net funds accrued to the broker was Rs. 11.12 lakhs due to his funding of BoM's purchase on 11 April 1991 to the extent of Rs. 51.25 lakhs.

vii) Compared to the broker client's net earning of Rs. 11.12 lakhs in this set of transactions, the bank earned Rs. 7.09 lakhs.

viii) The transactions with UCO Bank were on the basis of cost memos only while the others were undertaken with BRs, and no SGL transfer forms were issued or received.

(c) Chandrakala & Co., Broker/Client

Transaction date	Security	Face Value (Rs. in lakhs)	Rate (Rs.)	Amount paid (-) received (+) (Rs. in lakhs)	Counterparty
IS 9.3.92	8.75% ICICI 2000	25.00			
	8.75% IDBI 2000	280.00			
		305.00	87.10	(+) 273.44	Bank of Karad
		Profit on outright sale		1.83*	
CP 9.3.92	- do -	305.00	87.11	(-) 273.47	Bank of Karad
CS 9.3.92	- do -	305.00	92.50	(+) 289.91	Indian Bank
		Funds accruing to broker		16.44	

* as shown in the books of BoM with reference to the holding rate.

There is no acceptable explanation for the outright sale of 8.75% ICICI and IDBI bonds of face value Rs. 305 lakhs at a small profit of Rs. 1.83 lakhs. BoM's intention in selling the securities appears to be to enable the broker to pick up the securities at a low rate (87.11) vis-a-vis- the rate (92.50) at which they were sold to the Indian Bank. BoK was used to transfer the securities from BoM's portfolio at a small profit of Rs. 0.93 lakh. The broker earned Rs. 16.44 lakhs in this set of transactions.

(d) Chandrakala & Co., Broker/Client

Transaction	Security	No. of Units	Rate (Rs.)	Amount paid (-) / received (+) (Rs. in lakhs)	Counterparty banks
IP 20.5.92	Cantriple	1 crore	10.00	(-) 1000.00	Bank of Baroda (broker - K.R. Prakash & Co.)
IS 27.5.92	Cantriple	- do -	10.06	(+) 1006.00	Chandrakala & Co.
			Bank's earning	6.00	
CS 27.5.92	Cantriple	- do -	18.00	1800.00 C.	Mackertich & Co. and Stewart and Co.
		Earning to broker		784.00	

In the above set of transactions the security was directly sold to the broker client who sold it to another broker. While the bank made a profit of Rs. 6 lakhs only, the broker earned a sum of Rs. 789 lakhs.

(e) Ravi & Co., Broker /Client
8.25% GOI Loan 1995

Transaction date	Face Value (Rs. in crores)	Rate (Rs.)	Amount (Rs. in crores)	Counterparty	Nature of transaction
CP 06.04.1992	22.00	93.00	20.48	Citibank	Ready forward
CS 06. 04.1992	22.00	95.00	20.92	Indian Bank	- do -
IP 30.05.1992	22.00	93.60	20.82	Indian Bank	Outright
IS 30.05.1992	22.00	93.6181	20.82	Citibank	Outright

Unlike in the other cases, in the above set of transactions, the ready forward transactions entered into by the broker client on 6 April 1992 were reversed by the bank on 30 May 1992. While the bank earned Rs. 39,820, the broker earned Rs. 44 lakhs.

4 (a) It was observed that all client transactions were same day transactions, i.e. purchase from one bank and simultaneous sale to another. The transactions were put through by BoM on behalf of its clients for a small fee (2 paise per Rs. 1000). The proceeds of the sales provided funds required for the purchases of the broker clients. This is evident from the fact that the balance in the clients' accounts was generally not enough to cover the cost of purchases, which were to the tune of Rs. 5 crores and above. The balance in the broker clients' accounts was very low on certain days e.g. chandrakala & Co. - Rs. 2629.76 (24.3.1992); G.N. Hegde - Rs. 513.94 (10.7.1991), A.R. Financial Services - Rs. 1594 (12.4.1991).

(b) The gains accruing to the broker clients through the securities transactions were not retained in their accounts at a level required to support their purchase transactions. Instead, they were transferred to their own accounts with other banks or to the accounts of other broker clients. For example. In the case of Chandrakala & Co., it was observed that during the period May 1991 to May 1992 the broker had transferred amounts ranging between Rs. 11 lakhs and Rs. 5 crores to the account of Fairgrowth Investments Ltd. with Corporation Bank and Syndicate Bank. In the case of Batliwala and Karani, there were frequent transfers of funds from their account to the accounts of M.M. Muraraka and Company, Calcutta and Das & Company, New Delhi, besides transfer of funds to Batliwala & Karani's account at BoM's Madras Main branch.

(c) The bouncing of SGL transfer forms on account of clients' purchases presented a potential risk to BoM particularly when it was maintaining only one SGL account with the RBI as the client sales would get honoured against the bank's own holdings. The broker clients had neither adequate deposits nor adequate balances in their current accounts to cover such transactions in case of need. The commission earned in broker transactions was not commensurate with the risk involved when considered in the context of the returns obtained by the broker clients.

5 (a) In several cases, the reversal of the ready forward transactions was completed with banks/ financial institutions other than the original counterparties. A few examples are given below :

Sr. No.	Sale/ Purchase	Particulars of Security	Face Value (Rs. in crores)	Date of Contract	Date of Transaction	Name of broker	Counter-party
1.	Purchase	11.5% GOI Loan 2010	25	1.4.92	6.4.92	A.R. Financial Services	Deutsche Bank
	Sale	- do -	25	18.4.92	18.4.92	- do -	Banque Indo-suez
2.	Purchase	- do -	25	1.4.92	6.4.92	- do -	Deutsche Bank
	Sale	- do -	25	18.4.92	18.4.92	- do -	Banque Indo-suez
3.	Purchase	10.20% GOI Loan 1993	15	2.5.92	2.5.92	Batliwala &Karani	- do -
	Sale	- do -	15	15.5.92	18.5.92	- do -	ANZ Grindlays Bank
4.	Purchase	- do -	10	2.5,92	2.5.92	- do -	Banque Indo-suez
	Sale	- do -	10	15.4.92	18.5.92	- do -	ANZ Grindlays Bank

5. (b) In the above examples, Deutsche Bank, Banque Indo-suez and Grindlays Bank have shown these transactions in their records as on outright basis. Further, Deutsche Bank records indicate that that sales were made on behalf of its broker client, A.R. Financial Services and the amounts received were credited to its account. Similarly, Banque Niduses records indicate that the sale transactions were on behalf of its broker client Batliwala & Karani. It, therefore, seems that brokers have used these ready forward transactions of BoM to provide themselves with funds.

6. A few typical broker transactions undertaken by BoM intended to enable M/s. Chandrakala & Co. to raise funds from banks are given below :

(a) 9% IRFC bonds

Date	Face Value (Rs. in crores)	Rate (Rs.)	Amount (Rs. in crores)	Client	Counter Party	Remarks as per BoM's records
P 14.2.92	6.00	90.00	5.60	Chandrakala	Canfina	Bonds
S 14.2.92	6.00	100.00	6.20	- do -	Indian Bank Mutual Fund	Bonds
P 28.2.92	6.00	100.27	6.24	- do -	- do -	Bonds
S 28.2.92	6.00	90.05	5.62	- do -	Canfina	Bonds

In this case, it is seen that the broker raised funds to the tune of Rs. 0.60 crore from 14 February 1992 to 28 February 1992. On 28 February 1992 when he sold the bonds to Canfina, at an apparent loss of Rs. 0.62 crore, the actual loss was only Rs. 0.02 crore which was the interest paid for use of funds for 14 days @ 85.7%. Canfina paid Rs. 2 lakhs (9.2%) while the Indian Bank Mutual Fund receive Rs. 4 lakhs (16.6%).

(b) 13% NTPC bonds

Date	Face Value (Rs. in crores)	Rate (Rs.)	Amount (Rs. in crores)	Client	Counterparty	Remarks as per BoM's records
P 2.4.92	15.00	85.00	13.24	Chandrakala	Canfina	BR
S 2. 4.92	15.00	98.00	15.19	- do -	Syndicate Bank	BR
P 20. 4. 92	15.00	98.80730	15.41	- do -	- do -	BR
S 20. 4. 92	15.00	85.50	13.41	- do -	Canfina	BR

In the above example, the broker was provided with funds to the tune of Rs. 1.95 crores from 2 April 1992 to 20 April 1992, On 20 April 1992 when he returned the BR to Canfina, at a loss of Rs. 2 crores, the actual outgo was only Rs. 0.05 crore which was the interest paid for the use of the funds for 18 days @ 51.3%. Syndicate Bank earned Rs. 22 lakhs (29%) while Canfina had to pay Rs. 17 lakhs (25.7%).

(c) 13% MTNL bonds

Date	Face Value (Rs. in crores)	Rate (Rs.)	Amount (Rs. in crores)	Client	Counterparty	Remarks as per BoM's records
P 2.4.92	10.00	85.00	8.66	Chandrakala	Canfina	BR
S 2.4.92	10.00	98.00	9.96	- do -	Syndicate Bank	BR
P 20.4.92	10.00	98.68460	10.09	- do -	- do -	BR
S 20.4.92	10.00	98.00	10.02	-do -	Corporation Bank	BR
P 13.5.92	5.00	99.07520	5.11	- do -	- do -	BR
P 13.5.92	5.00	99.07520	5.11	- do -	- do -	BR
S 13.5.92	5.00	85.00	4.40	- do -	Canfina	BR

(i) From the above set of transactions, the following position emerges :

Date	Net amount received (+) / Paid (-) (Rs. in crores)
2. 4. 92	+ 1.30
20.4.92	- 0.07
13. 5. 92	- 0.86
	+ 0.37

(ii) From these transactions, it is evident that M/s. Chandrakala & Co. made a net profit of Rs. 37.00 lakhs and used Rs. 1.30 crores for the period 2 April 1992 to 20 April 1992 and Rs. 1.23 crores for the period 21 April 1992 to 13 May 1992. All the above transactions have been put through on the strength of Bank Receipts, issued on behalf of the client with no actual delivery of securities on any leg of the transaction. It is understood that Corporation Bank and Syndicate Bank were acting on behalf of Fairgrowth Investments Ltd.

7. Irregularities in the operation of the SGL account of BoM.

(a) The bank was having only one SGL account through which it was putting through transactions in respect of both its own investment account and transactions undertaken on behalf of its broker clients. As a result, the bank's investment transactions were mixed up with clients' transactions.

(b) On an average, the bank's investments in Government securities toward compliance with SLR requirement varied from Rs. 150 crores to Rs.175 crores, depending on the amount of deposits. As against this, the volume of transactions during January 1992 to May 1992 was as shown at the bottom of this page.

(c) BoM issued SGL transfer forms in respect of transactions in 11.5% GOI Loan 2010 for large amounts disproportionate to the bank's holding of the security as per the SGL account. On 7 March 1992, the sales were as high as Rs. 730 crores against a balance of Rs. 8.04 crores in the security; hence these sales relied very heavily on corresponding purchases on the same date to the extent of Rs. 725 crores. Of the sales, SGL transfer forms for an amount of Rs. 125.00 crores bounced, as against which forms for an amount of Rs. 115.00 crores of the purchases had bounced. The bank had not reconciled its balances with the PDO, Bombay and carried on trading activities in securities out of proportion to the balances as per its records. For each settlement Saturday about 50 to 75 deals involving on an average about Rs. 500 crores to Rs. 700 crores, sales and purchases together, were transacted.

(d) It is seen from the bank's records that the last such heavy trading activity was undertaken on 2 May 1992 with sales of Rs. 400 crores and purchases of Rs. 405 crores. Subsequently, there was an unwinding of the trading operations, the total sales being Rs. 665.00 crores and total purchases Rs. 638.00 crores for the entire month of May 1992. From 1 June to 20 June 1992, there had been only sales of Rs. 15 crores and no purchases.

(e) During the period June 1991 to May 1992, 62 SGL transfer forms issued by BoM amounting to Rs. 1069 crores had bounced. Bouncing of its SGL transfer forms was as high as Rs. 185 crores, Rs.245 crores and Rs. 207 crores during March, April

(Rs. in crores)

Month	Investment Account		Clients Account	
	Sale	Purchase	Sale	Purchase
January 1992	542.09	545.92	459.70	459.70
February 1992	829.07	843.26	233.39	233.39
March 1992	948.85	951.10	332.75	332.75
April 1992	777.00	787.00	202.05	202.05
May 1992	495.00	468.00	170.00	170.00

and May 1992 respectively.

(f) In some cases where the SGL transfer forms issued by BoM had bounced, these were subsequently repurchased by the bank.

8. **Other irregularities**

(a) The bank did not have an up-to-date record of the securities transactions undertaken by it.

(b) In some cases, the cost memos for the transactions were not available for verification.

(c) The register in which the transactions undertaken by the Bombay (Main) branch were recorded did not contain particulars of the cheques issued, date of debit/credit of the SGL Account, mode of liquidation of the BR, type of transaction (outright or ready forward) and whether the transaction was on own investment account or client account. In some cases, the name of the counterparty bank and the mode of delivery of the security (by bonds/BRs/SGL) has been incorrectly recorded.

VII. Karnataka Bank Ltd.

Karnataka Bank Ltd. (KBL) has undertaken very few security transactions on its own investment account. It has however undertaken some transactions on account of its constituent viz., Fairgrowth Financial Services Ltd. (FGFSL).

2. FGFSL is maintaining a current account (No.2000) with the Bombay branch of KBL. On a number of occasions funds in this account have been transferred to or received from mainly Syndicate Bank, (New Marine Lines branch) Bombay, National Housing Bank (NHB), Bombay and KBL's Bangalore (Kasturba Road) branch.

(a) The undernoted payments were made by KBL to NHB, Bombay at the request of FGFSL by debit to its current account.

Date	Amount (Rs.)
26.09.1991	2,59,75,821.92
23.10.1991	4,50,00,000.00
24.10.1991	7,00,00,000.00
11.11.1991	9,80,00,000.00
12.11.1991	13,00,00,000.00

(b) These payments as per the books of NHB, Bombay were received for security transactions with KBL and Syndicate Bank. However, no such security transactions are recorded in the books of KBL and Syndicate Bank. It would appear that FGFSL has used the names of Syndicate Bank and KBL as counterparty banks in respect of its transactions entered into with NHB.

3. The Bombay branch of KBL received a payment of Rs.2.56 crores from NHB on 22 August 1991. The payment was related to purchase of securities from KBL as per the books of NHB. However, there was no such security transaction at KBL ard the amount was credited to the current account of FGFSL on the basis of a covering letter from NHB.

4.1 The Bangalore (Kasturba Road) branch of the bank had issued four BRs in July 1991 for an aggregate amount of Rs.6.00 crores on account of sales by FGFSL on a buyback basis, as detailed below :

Sr. No.	Date of BR	Name of counter-party	Nature of security	Face value (Rs.in crores)	Rate	Amount (Rs.in crores)	Date of repurchase on behalf of FGFSL and name of counterparty
i)	9.7.1991	ABFSL, Madras	9% IRFC bonds	0.50	100.00	0.50	8.8.1991 ABFSL, Madras.
ii)	10.7.1991	SBI,Kochi	-do-	0.50	100.00	0.50	9.8.1991 SBI, Kochi
iii)	11.7.1991	NHB,Bombay	13% NPC bonds	2.50	100.00	2.50	26.9.1991 NHB, Bombay.
iv)	18.7.1991	BOI Finance, Bombay.	-do-	2.50	-	2.45	21.1.1992 BOI Finance, Bombay.

These transactions were not reflected in the books of Head Office under investment account. They were put through by the branch Manager without formal Head Office approval. The BRs were issued by the branch against the Security Receipts issued by FGFSL to KBL and not against any security held by the bank. Cost memos/sale memos were not available for all the transactions except one cost memo from BOI Finance Ltd. The Chairman approved all the four transactions in August 1991 on a letter dated 10 July 1991 written by the branch Manager to report the first two transactions, but the relative confirmation to the branch was conveyed in September 1992 only. There was not proper accounting of these transactions at the branch. There was laos no evidence to show that the payment in respect of the repurchase at item (iii) was received from FGFSL. In respect of item (iv), FGFSL had wide the payment directly to the counterparty in January 1992.

4.2 There is evidence to show that the branch had entered into these security transactions on behalf of FGFSL on oral (telephonic) instructions from Head Office. On issuing the BRs to different counterparty bank/non-bank clients, the proceeds received from them were credited to the account maintained by FGFSL at the branches of KBL in Madras, Kochi and Bombay. It would, thus, be clear that KBL had accommodated FGFSL by mobilising funds by lending its name to security transactions of FGFSL merely on the basis of security receipts received from FGFSL. The income earned by KBL on these transactions amounted to Rs.60,700.

5. Apart from the above, six BRs for an aggregate amount of Rs.15.00 crores purported to have been issued by KBL, Bangalore (Kasturba Road) branch have been recovered by CBI. These BRs were shown by CBI in October 1992 to the branch officials who disclaimed issuing these BRs. The matter is under investigation by CBI. So far, the bank has not received any claim on the basis of these BRs.

VIII. BOI Finance Ltd.

1.1 BOI Finance Ltd. (BOIFIN), a wholly-owned subsidiary of Bank of India commenced business in June 1989. The company's activities comprise merchant banking, leasing, portfolio management services and securities operations. It stopped accepting fresh deposits under PMS from mid-March 1991 after the receipt of RBI's detailed guidelines on PMS operations in January 1991. The securities operations essentially arose by way of deployment of inter-corporate deposits placed with the company and back to back deals in securities. During the period April 1991 to June 1992 the company's total turnover (both sales and purchases) in securities transactions aggregated Rs.15,081.05 crores. These were mostly in PSU bonds and Units. Out of these, the value of transactions entered into with Fairgrowth Financial Services Ltd. (FGFSL) and Kotak Mahindra Finance Ltd. (KMFL) amounted to Rs.4,405.66 crores.

1.2 The company's Executive Committee comprising its Chief Executive Officer and three other officers could exercise in respect of security transactions the same powers as its Board of Directors. Even though transactions for substantial amounts were undertaken, these were not reported to the Chairman or the Board at periodical intervals. The four notes submitted to the Board for its meetings in the year 1991 about the company's activities did not cover security transactions. The weekly reporting system that was introduced in July 1992 was also discontinued after submission of the first two reports to the Chairman. Thus, the management was not kept informed about the transactions for huge amounts.

1.3 BOIFIN became a member of the Indian Banks' Association in August 1991 and started issuing BRs in the format approved by IBA from 1 April 1992. Till then it issued what were called "security receipts".

1.4 The internal controls within the company were lax, and there were no clear-cut written procedures for the officials engaged in security transactions. The dealing room was not delinked from the back-up section. The dealer was not only responsible for striking the deals but also for putting through the deals, checking of accounts, issue/receipt of BRs, cheques and scrips. He was also one of the custodians of the securities. No records of the BRs and SRs issued and received were maintained and there was no system of follow-up of outstanding BRs and SRs. It also issued BRs against the BRs of other banks. On certain occasions it had parted with the cheques without getting back its BRs duly discharged at the time of reversal of earlier sales. There was no system of verifying the signatures of officials who had signed the BRs received from other banks. In fact, it was not maintaining a list of officers of other banks authorised to sign the BRs and also their specimen signatures.

1.5 Although BOIFIN dealt extensively with FGFSL and KMFL in securities transactions, no exposure limits were fixed for them and it readily accepted "security receipts" issued by them without limit.

2. Transactions with Fairgrowth Financial Services Ltd. (FGFSL)

2.1 The company had 277 transactions for an aggregate amount of Rs.2743.87 crores with FGFSL during the period July 1991 to June 1992. The dealings with it commenced in July 1991. FGFSL being a private sector non-bank finance company could not directly obtain from the PSUs private placements of bonds when they raised funds in the form of taxable or tax free bonds. It, therefore, made a proposal on 27 March 1992 to BOIFIN suggesting that BOIFIN bid for 17% NPC bonds, on its behalf. It offered to buy these bonds of face value Rs.100 crores @Rs.97.25. It also mentioned that funds for the purchase of these bonds would be provided by NPC itself, by placement of an inter-corporate deposit. FGFSL further stated that the funds made available to it by BOIFIN would be at 18 per cent per annum against PSU bonds and Units of UTI on ready forward basis. The bonds and Units would be sold to BOIFIN at "prevailing market rates", such that a return of 18 per cent was possible.

2.2 Accordingly, BOIFIN subscribed Rs.97 crores to 17% NPC bonds of face value Rs.100 crores on 31 March 1992. The amount thus received by NPC was deposited with BOIFIN on the same day as five inter-corpoate deposits at 17.5 per cent per annum repayable on five different dates between 30 June 1992 and 31 March 1993. On 31 March 1992, BOIFIN sold these bonds of the face value of Rs.80 crores for Rs.77.84 crores to FGFSL at the agreed rate of Rs.97.25. The balance of bonds of the face value Rs.20 crores (or such lesser amount of bonds as remained with BOIFIN) was to be sold after the period of three months laid down by NPC for sale to the public over the counters was over. On the same day viz. 31 March 1992, the NPC bonds of the face value of Rs.80 crores were purchased by BOIFIN from FGFSL on ready forward basis to provide funds to the latter. The understanding was that through a series of ready forward transactions in PSU bonds and Units FGFSL would place BOIFIN in funds to enable BOIFIN to repay the inter-corporate deposits of NPC on the due dates. At the instance of FGFSL, the securities in the hands of BOIFIN were changed from time to time and the position as on 30 June 1992 was that BOIFIN had in its hands PSU bonds of the value of Rs.99.63 crores (purchase cost) which included unsold NPC bonds for Rs.19.98 crores. The aggregate face value of these bonds was Rs.109.98 crores. BOIFIN has got all these bonds transferred in its name.

2.3 FGFSL, due to liquidity problems, failed to meet its commitment to buy back the PSU bonds so as to provide funds to BOIFIN on 30 June 1992 to make payment to NPC on that date towards a maturing deposit. It could not honour subsequent commitments also as it became a "notified person". BOIFIN had to repay the deposits aggregating Rs.97 crores to NPC on the respective due dates or later, either by mobilising deposits from other corporate clients or by borrowing from Bank of India.

2.4 On 30 June 1992, as the securities held by BOIFIN in the above arrangement had fallen in value, BOIFIN called for and FGFSL gave as additional collateral security, 151950 fully convertible debentures of an aggregate paid-up value of Rs.3.42 crores of Larsen & Toubro Ltd. BOIFIN could not get these debentures transferred in its name as Larsen & Toubro Ltd. refused to register the transfer on the ground that FGFSL was a "notified person".

2.5 BOIFIN has filed a miscellaneous petition on 26 February 1993 in the Special Court for ordering performance of the ready forward contract made by FGFSL with it and also for transfer of the Larsen & Toubro debentures to its name. The court has posted the case for hearing on 14 June 1993.

2.6 BOIFIN enjoyed an overdraft limit of Rs.6 crores from Bank of India since October 1989. With the acute strain on its liquidity caused by the drying up of inter-corporate deposits from the PSUs and discontinuance of ready forward transactions as a means of funding its operations, the overdraft limit was raised to Rs.35 crores in September 1992 and further to Rs.41 crores, Rs.47 crores and to Rs.100 crores on 23 February 1993, 16 March 1993 and 31 March 1993 respectively. The limit of Rs.100 crores which is far above the RBI norm for such borrowing was necessary to meet the maturing inter-corporate deposits and other obligations of BOIFIN.

2.7 The PSU bonds for Rs.109.98 crores (face value) held by BOIFIN against FGFSL's dues to it of Rs.99.63 crores would have depreciated considerably in market value. Besides BOIFIN also holds as at end March 1993 shares, debentures and other securities for Rs.36.54 crores (cost price) which would face a similar depreciation.

3. Transactions with National Housing Bank (NHB)

3.1 BOIFIN entered into a contract with NHB on 31 January 1992 for purchase of 7 crore Units of UTI for a sum of Rs.95.83 crores on ready forward basis at the rate of Rs.13.69. The transaction was due for reversal on 30 April 1992. Due to strike by bank employees on 30 April 1992, the deal was rolled over for a period of five days upto 5 May 1992.

3.2 On 29 April 1992, BOIFIN entered into two transactions with NHB for sale of 9% NPC bonds and Units totalling Rs.58.68 crores (transaction value) on a ready forward basis for reversal on 5 May 1992. On 5 May 1992, BOIFIN sent an RBI cheque (drawn by Bank of India) for Rs.59.05 crores against receipt of BOIFIN's two BRs duly discharged by NHB. However, on learning that NHB was not making payment in fulfillment of its obligations, BOIFIN stopped payment of the cheque it had already issued.

3.3 On 7 July 1992, NHB wrote a letter to BOIFIN listing the outstanding transactions, as under :

			(Rs. in crores)
(a)	31.1.1992	Sale of 7 crore Units to BOIFIN	95.83
(b)	31.7.1991	Purchase of 50 lakh Units	6.70
(c)	29.4.1992	Purchase of 2.60 crore Units	39.00
(d)	29.4.1992	Purchase of 9% NPC bonds	19.68
		[a - (b + c + d)] =	30.45

In settlement of these transactions, NHB issued two cheques for Rs.7.85 crores on 18 June 1992 and Rs.22.60 crores on 9 July 1992, leaving the issue regarding interest to be decided separately. Incidentally, the payment of interest has not been settled till date.

IX. Indbank Merchant Banking Services Limited

The company, a wholly owned subsidiary of Indian Bank, was set up in August 1989. As per the authorisations issued by RBI, Indbank Merchant Banking Services Limited (IMBSL) was permitted to undertake merchant banking, besides equipment leasing and hire-purchase business and activities purely incidental thereto. However, an analysis of the income earned by the company during 1991-92 showed that nearly 76 per cent of the income was earned from placement of inter-corporate deposits, 20 per cent from short term investment operations on ready forward basis and only the balance 4 per cent through issue management, project counselling, equipment leasing and hire purchase business. Most of the business is transacted by the company's corporate office located in Bombay.

2. The company was actively involved in ready forward transactions in Units of UTI, PSU bonds and shares during the period 1 April 1991 to 30 June 1992 with such deals accounting for 93.04 per cent of the total deals aggregating Rs.4125.89 crores. The ready forward deals were routed mainly through Kotak Mahindra Finance Ltd. (31.25 per cent), D.S. Purbhoodas (15.63 per cent) and Batliwala & Karani (10.37 per cent). There was no approved panel of brokers nor was any broker-wise or bank-wise exposure limit fixed by the Board of IMBSL. In most of the cases company officials exceeded their delegated powers in deployment of funds through ready forward deals. These transactions were treated as a matter of routine and ratification was never sought. The investments often exceeded the powers of even the company's Chairman (who was Indian Bank's Chairman) but there is nothing on record to show that such excesses were placed before the Board for approval. Top management, however, did not object, thus giving tacit approval to such transactions.

3. Deals with Kotak Mahindra Finance Ltd.

(a) Scrutiny of some of the large inter-corporate deposits accepted from PSUs reveals that a good proportion thereof was placed with Kotak Mahindra Finance Ltd. (KMFL) in ready forward transactions.

(b) The company took the risk of accepting security receipts issued by KMFL instead of actual physical securities. It also accepted in one case a third party BR issued by Citibank favouring KMFL, in a deal made on 16 April 1991.

(c) In some deals with KMFL (as counterparty), funds were parted without obtaining any security. For example, on 20 April 1991 an amount of Rs.5.06 crores was paid to KMFL for purchase of 34 lakh Units of UTI without receiving physical Units or a BR. The transaction was reversed on 22 April 1991.

(d) The company arranged funds for KMFL under cover of ready forward deals. For example, on 20 September 1991 KMFL lodged a certificate for 100 lakh Units of UTI with the company who sold 75 lakh Units to IDBI for a consideration of Rs.10.04 crores. The amount received from IDBI was passed on to KMFL by issuing a pay order favouring Grindlays Bank for credit of KMFL's current account. On the date of reversal, i.e. 11 October 1991, the amount was received by IDBI from Mitsui Taiyo Kobe Bank (now Sakura Bank) when they sold the Units for Rs.10.12 crores. The Pay Order was issued by Sakura Bank by debit to the current account of KMFL. The company's Security Receipt (SR) dated 20 September 1991 was received back from IDBI duly discharged. The company received Rs.7500/- by cheque from KMFL for issuance of its SR favouring IDBI. For the balance 25 lakh Units, the company had issued two SRs favouring SBI Capital Markets Ltd. and KMFL. No funds were received from either of the two parties, nor were the two SRs received back duly discharged. However, there was no claim on the company.

4. In certain ready forward deals repayment has been received from parties other than the contracted parties. For example, reversal of a deal in 13% NTPC bonds for Rs.10.06 crores with Bank of America on 11 March 1992 was done by receipt of payment from Syndicate Bank a/c. KMFL. The broker in this case was KMFL and apparently the transaction was routed through its account with Syndicate Bank. Again, on 18 May 1991, in two separate deals covering 13% NPC bonds and 13% ITI bonds through broker Batliwala & Karani (B & K), payments were received from Bank of Karad a/c. B & K even though the counterparty was SBI Mutual Fund.

5. In almost all cases, the BRs/SRs received by IMBSL for its purchases were not discharged by delivery of scrip but were returned on the date of reversal to the counterparty on receipt of sale proceeds. A few such instances are enumerated below :

Date	Security	Contract Value (Rs.in crores)	Counterparty
10.4.1991	Units	2.24	BOI Finance
10.4.1991	Units	3.43	UCO Bank
4.5.1991	Units	5.93	Standard Chartered Bank
14.5.1991	13% HPFC bonds	6.97	Canbank Mutual Fund
5.7.1991	13% RINL bonds	10 12	Canfina
12.8.1991	9% IRFC bonds	5.11	SBI Caps
14.10.1991	9% IRFC bonds	8.88	BOI Finance

6. Though 96 per cent of the company's income came from investments done through Bombay corporate office and only 4 per cent through leasing and hire-purchase and merchant banking activities (prime functions of the company), the Bombay office was not subjected to any internal inspection/audit by its Head Office at Madras, indicating lax control. Management Information System statements on daily basis were introduced only recently in April 1992 while a monthly statement had been introduced in April 1991.

7. The other irregularities observed are enumerated below :

(a) No deal ticket was prepared for any of the transactions.

(b) Contract notes were not available in many cases, especially for deals through the brokers KMFL and D.S. Purbhoodas.

(c) SRs were issued against the BRs of other banks or financial institutions.

(d) The company had no record of the authorised signatories of other banks nor did it have any system of verifying these signatures on receipt of BRs.

(e) There was no system of confirming broker contracts with counterparty banks.

(f) The vouching of transactions was misleading. For instance, in a deal of 13% HUDCO bonds with Standard Chartered Bank, the voucher is dated 5 July 1991 while payment and transaction date was 4 July 1991. In several cases of purchase of Units on 4 April 1991, 4 May 1991, 20 June 1991, 21 June 1991, 1 July 1991 and 5 July 1991, while the voucher showed counterparty as Vijaya Bank, payment was made to or received from KMFL.

(g) The company did not maintain any register or record to show the receipt or delivery of securities under ready forward deals. Thus, it was not ascertainable whether the securities were actually received or not.

8. Funds collected as inter-corporate deposits from public sector units, like IRFC, Oil India Ltd., Pawan Hans Ltd., Air India, KRIBHCO, RCF and Goa Shipyard, were placed by the company with customers of Indian Bank on the basis of a letter of comfort issued by the latter. Indian Bank, in such cases, reduced the drawing power on the date of placement of such deposits and on due dates, the client's accounts were debited and payment made to IMBSL. For issuing the letter of comfort, Indian Bank received from its subsidiary, service charges at one per cent on the average weekly balance outstanding of such deposits. Indian Bank had thus contravened RBI instructions issued in April 1974 and reiterated in May 1983 and March 1984 in terms of which issuance of guarantees covering inter-company deposits/loans was prohibited. The entire operations were carried out at Bombay on an informal/oral basis. Proper records were not maintained even though huge funds were deployed in this manner. Such placements of funds with clients of Indian Bank amounted to (i) indirect lending by Indian Bank, (ii) indirect acceptance of deposits by Indian Bank, and (iii) avoidance of maintenance of SLR/CRR by Indian Bank. IMBSL hence assisted its parent organisation, Indian Bank, in circumventing RBI guidelines.

X. Indian Bank Mutual Fund

The Indian Bank Mutual Fund (IBMF) was set up in November 1989 with the approval of the Reserve Bank of India. Indian Bank as the settler and principal trustee contributed a sum of Rs.0.25 crore to the corpus of the Trust. The Mutual Fund has raised substantial funds amounting to Rs.483.60 crores through eight schemes since its inception in November 1989. The major operations of the Fund are carried out in its corporate office located in Bombay. The Fund is headed by a wholetime President, who is also the Executive

Trustee. He also heads the Investment Committee.

2. Broker-wise distribution of business in capital market instruments, such as PSU bonds and Units, between 1 April 1991 and 31 March 1992 is given below:

(Rs.in crores)

Sr.No.	Name of the broker	Amount#	Percentage
1.	Kotak Mahindra Finance Ltd. (KMFL)	335.50	26.57
2.	Batliwala & Karani	272.65	21.59
3.	Harshad S. Mehta	259.58	20.56
4.	Chandrakala & Co.	159.01	12.59
5.	Asit C. Mehta	116.25	9.22
6.	Direct	19.01	1.50
7.	Others	100.60	7.97
		1262.60	100.00

Excludes transactions in equities and debentures.

3. The Investment Committee was not maintaining, prior to 1 August 1992, any record or minutes of the decisions taken to purchase or sell securities in the secondary market; nor was there a policy framework for undertaking securities transactions. It was not, therefore, possible to know the basis for its decisions.

4. The Fund failed to maintain "arms length" relationship with the sponsor/principal Trustee, viz. Indian Bank, as required by the RBI. In call money lending, the Fund charged a lower rate of interest to Indian Bank. A few examples are given at the bottom of this page.

During the year 1991-92, as much as Rs.7397.85 crores out of Rs.8311.00 crores were lent to Indian Bank in call money, thus depriving the Fund of higher income.

5. A scrutiny of the security transactions undertaken by the Fund during the period 1 April 1991 to 31 May 1992 revealed the undernoted irregularities.

(a) The Fund had undertaken 275 ready forward transactions in securities/PSU bonds/Commercial Papers and Certificates of Deposit for Rs.554.90 crores with banks and financial institutions in violation of RBI guidelines.

(b) The Fund had issued 69 "Receipts" for sale of securities during this period, which are not in the IBA format for Bank Receipts. (It is not authorised to issue Bank Receipts).

(c) In a number of ready forward deals entered into with banks, the RBI cheques issued by the Fund were credited to the brokers' accounts with the counterparty banks (e.g. ANZ Grindlays Bank, UCO

(Rs.in crores)

Sr. No.	Date	Amount	Name of the borrower	Rate (%)
1.	4.12.90	15.00	Indian Bank	11.00
	4.12.90	5.00	American Express	11.75
2.	29.1.91	22.00	Indian Bank	12.25
	29.1.91	10.00	Corporation Bank	12.50
3.	13.5.91	9.00	Indian Bank	14.00
	13.5.91	17.00	Bank of Maharashtra	14.25
4.	14.5.91	10.00	Indian Bank	20.50
	14.5.91	54.00	State Bank of India	54.00
5.	20.5.91	49.00	Indian Bank	42.00
	20.5.91	7.00	State Bank of India	45.10

Bank, Syndicate Bank, Bank of Karad, State Bank of India and Bank of India). Between August 1991 and March 1992 Rs.116.86 crores, Rs.12.99 crores and Rs.21.47 crores were so credited respectively to the accounts of Harshad S. Mehta (State Bank of India and ANZ Grindlays Bank), KMFL (Syndicate Bank), and Batliwala & Karani (Banque Indosuez and Bank of Karad), although the deals were with the counterparty banks as per the Fund's records.

(d) On 5 March 1992, the Fund entered into a ready forward deal with Syndicate Bank through KMFL for purchasing commercial papers of two companies. The RBI cheques for Rs.7.97 crores and Rs.5.02 crores were credited to KMFL's account under the Fund's instructions. The deal was reversed on 9 March 1992 on receipt of RBI cheque issued by Syndicate Bank, by debit to KMFL's account. The Fund has subsequently clarified that the deal was actually with KMFL and not with Syndicate Bank. Such a ready forward deal with KMFL or for that matter, Syndicate Bank, which placed the finance company in funds for 4 days, is not permissible under RBI guidelines.

(e) On 31 January 1991, the Fund purchased from Bank of Karad 11.5% GOI Loan 2015 for Rs.14 crores (face value) through broker Batliwala & Karani (B & K). The SGL transfer form received from Bank of Karad bounced due to insufficient balance. The deal was then reversed on 9 February 1991 on receipt of payment vide RBI cheque issued by Bank of Karad. Examination of the books of Bank of Karad revealed that the overdraft account of B & K had been credited with Rs.14.26 crores on 31 January 1991 and after using the funds for 8 days, the broker returned the sum of Rs.14.30 crores by instructing Bank of Karad to issue an RBI cheque.

6. It was also observed that on several occasions, the Fund entered into ready forward deals with the Indbank Merchant Banking Services Limited against the security of non-covertible debentures of Reliance Industries Ltd. which was tantamount to borrowing of funds. This was in violation of RBI guidelines. Some instances of such transactions are given below :

(Rs.in crores)

Date	Purchase/sale	Amount
21.2.1992	Sale	20.00
24.2.1992	Purchase	20.00
24.2.1992	Sale	24.79
26.2.1992	Purchase	24.79
3.3.1992	Sale	4.49
10.3.1992	Purchase	4.49

7. In primary market operations, it was observed that the Fund had subscribed to shares of various companies out of promoter's quota on private placement basis. The Fund also entered into an arrangement with the promoters to buy back these shares on the expiry of three years at a pre-determined price which would ensure a minimum assured rate of return and is presently holding 15.33 lakh shares of 23 companies for Rs.15.53 crores purchased during the period from 1 January 1991 to 31 May 1992.

XI. Deutsche Bank

Deutsche Bank has branches at Bombay and New Delhi, which are functioning since October 1980 and April 1989.

2. The Bombay branch of the bank entered into a large number of ready forward transactions in PSU bonds and Units of UTI. Many of these transactions were also with non-bank clients including firms and companies for short periods. Out of the total turnover of Rs.6,982.67 crores in securities transactions of the branch during the period from 1 April 1991 to 30 May 1992, ready forward transactions in PSU bonds and Units aggregated Rs.4,586.36 crores (65.7 per cent). Of this, the total amount of ready forward transactions with companies amounted to Rs.363.24 crores. These deals were in violation of the RBI prohibition on banks undertaking ready forward transactions with non-bank clients as also the PMS guidelines and the RBI directives on interest rates on deposits. The bank has explained that it "acted as an intermediary between the customer and the inter-bank market" in these deals and "customers

have normally sought this service when they have desired an alternative to making inter-corporate deposits". In the process, the bank, in fact, borrowed large amounts without having to maintain the SLR and CRR on such funds. Some of the companies with whom ready forward deals in PSU bonds and Units had been entered into by the branch and the aggregate amounts deployed by them during the period from 1 April 1991 to 30 May 1992 were as under:

(Rs.in crores)

i)	Hindustan Lever Ltd.	66.15
ii)	Larsen & Toubro Ltd.	5.00
iii)	Modern Woollen Ltd.	9.34
iv)	Lynde Process Technologies	11.70
v)	Special Steels	8.50
vi)	Reliance Capital and Finance Trust Ltd.	4.40

3. Other irregularities observed in the securities transactions of the bank's branch at Bombay are given below :

(a) Transactions on account of a broker client viz. M/s.A.R. Financial Services were routed through the bank's own SGL account by issuing its SGL transfer forms for sales and accepting SGL transfer forms for purchases on account of the broker.

(b) The branch entered into ready forward transactions in Government securities against exchange of BRs, when SGL facility was available for Government securities.

(c) The branch entered into ready forward transactions in Government securities with non-bank clients.

(d) In the case of part purchases under ready forward deals, the branch was cancelling the original amounts in its BRs and was incorporating the balance amounts.

(e) The bank was issuing and receiving BRs on behalf of its associate company, viz. DB Financial Services (India) Ltd., in respect of the latter's transactions. The deficiencies observed in this arrangements are discussed in a separate chapter on the company.

(f) In one transaction, the bank appears to have "borrowed" Units for Rs. 10 crores (face value) from a non-bank client on 7 April 1992 by a ready forward transaction (of which the first leg was a purchase), which were subsequently "returned" to the client on 28 May 1992 when the transaction was reversed. The purchase and sale rates being Rs.15.00 and Rs.15.44, the bank derived an income of Rs. 44 lakhs which works out to a return of 21 per cent, apart from any advantage derived by it by the use of the Units in the intervening period of 51 days.

4. (a) The New Delhi branch of the bank had been providing "Custodian Services' to some of its clients. The clients who were interested in availing of such facilities entered into an agreement with the branch known as "Safe Custody Agreement" in terms of which the clients appointed the bank as the custodian of their investments and placed their funds at the disposal of the bank. The clients paid a fee or commission for the services, which was around three per cent of the turnover. Such investments were mainly in bills of exchange. When clients authorised the branch to make investments, the branch debited clients' current accounts and purchased bills of exchange of various parties, some of whom were not the customers of the bank. The amounts invested were credited to an account called "Endorsements Account". When the bills were discounted, they were accounted for in an account known as "Collective Endorsement Account" which was shown in the balance sheet as a contra item under contingent liabilities. No separate account in respect of either each investor or the drawer or the drawee is maintained, but a monthly computer print-out giving these details is prepared. On the due dates, the entries were reversed and fresh bills were purchased unless the investors sought refund of the deposit. In case the investor requested the bank for refund of the amount before the due date, the branch switched the transaction in favour of another investor.

(b) In some of the cases, the branch had created bills of exchange by itself drawing bills on its clients towards electricity charges and payment was made by charging it to the Investor's Account.

(c) The manner in which the branch undertook to make investments on behalf of its clients mainly in bills of exchange violated RBI guidelines on PMS.

(d) The branch has discontinued this facility from September 1992 after receipt of Reserve Bank circular dated 27 July 1992 on bill discounting.

XII. DB Financial Services (India) Ltd.

1.1 DB Financial Services (India) Ltd. (DBFSL), was formed after taking over the erstwhile Comfund Investment Ltd. and it commenced its operations in December 1989. The company has a paid-up capital of Rs.1.00 crore, of which 30 per cent is subscribed by Deutsche Bank, 24 per cent by Brooke Bond India Ltd., a company of Unilever Group and the balance 46 per cent by employees of Deutsche Bank and Unilever Group companies. The company, which has its registered office in Bangalore, opened an office in Bombay in March 1991 to carry on money market operations and securities trading and servicing of customers with respect to leasing, hire-purchase and financial consultancy services. Both the Chief Executive Officer and a senior official of Deutsche Bank in India were Directors on the company's Board.

1.2 The company (DBFSL) raised funds for its trading initially by accepting inter-corporate deposits. On 4 April 1991, Deutsche Bank sanctioned to the company initially for 70 days an overdraft limit of Rs.3.00 crores and allowed this facility to continue thereafter.

1.3 The total turnover (both purchases and sales) in securities transactions of the company during the period 1 April 1991 to 31 July 1992 amounted to Rs.15,094.31 crores in 1177 deals, of which the transactions put through brokers accounted for Rs.10,358.02 crores (68.6 per cent). In respect of a number of sale transactions, cost memos issued to counterparty banks and institutions were not available for verification. The brokers' notes and sale memos of counterparties in respect of some purchase transactions of the company were also not available for scrutiny. The company traded mostly in PSU bonds and Units of UTI. Apart from trading in these bonds and Units, the company also traded in shares and debentures of certain companies. The total value of such transactions in shares and debentures amounted to Rs.689.06 crores. The brokers who handled the bulk (60.6 per cent) of the company's business were Asit C. Mehta (Rs.3840.64 crores), D.S. Purbhoodas & Company (Rs.2415.43 crores), Ashwin Dand (Rs.2154.23 crores) and Excel & Company (Rs.734.75 crores).

1.4 The company traded in securities on its own account as well as on account of certain clients. Most of these clients are associate companies of Unilever Group and/or have their Director/s on the Board of DBFSL. DBFSL did not hold on its record resolutions passed by the Boards of some of these companies covering (i) the placement of funds with it for investment purpose (ii) type of securities in which the companies wished to invest, and (iii) minimum period for which funds were to be invested, etc. The purchases and sales of securities on behalf of certain companies were recorded by DBFSL in its books as deals with these companies as its counterparties and no BRs were issued. On the dates of receipt of funds in round sums from these companies, DBFSL advised them that it had purchased certain securities on their behalf. On the transaction lists, purchase of securities as advised to the companies was, however, shown as a sale of securities to these companies. The excess amount/shortfall involved in the sale of security transaction vis-a-vis funds received was refunded to or recovered from the companies separately. On reversal of the transactions by way of purchase of the same securities from these companies at rates higher than the ones at which securities were sold earlier, DBFSL advised the companies that it had sold the securities on their behalf and was remitting the sale proceeds to them.

1.5 The particulars of funds of various companies received by DBFSL under the guise of security transactions and average yield passed on to them are indicated hereunder :

(Rs.in crores)

Name of the company	Period	Sales	Purchases	Yield (%)
Hindustan Lever Ltd.	30.8.1991 to 17.2.1992	68.55	79.43	14 to 18
Ind Exports Ltd.	16.7.1991 to 15.5.1992	14.32	14.48	14 to 26
Housing Development Finance Corporation (HDFC)	12.8.1991 to 11.5.1992	538.44	568.83	13 to 20
Videocon Ltd.	21.5.1991 to 11.5.1992	25.95	30.92	13 to 25.8

Incidentally, the Chairman of HDFC was a Director of the company from 21 December 1990 and also its Chairman since then and there was a possible conflict of interest. He resigned from the Board of the company in September 1992.

1.6 Apart from accepting funds for investment from Videocon Appliances Ltd. (VAL) and Videocon Ltd. (VL) under the cover of securities transactions, DBFSL assisted these companies either directly by purchasing 12.5% Videocon International Ltd. fully convertible debentures from VAL and VL on sellback basis, or indirectly by dealing on their behalf in these debentures with different counterparty banks and finance companies on buyback basis. The funds raised from counterparties through such deals were passed on to the above companies on the dates of receipt. On the date of reversal of the deals, DBFSL repaid the principal together with the cost to the counterparties, for which funds were received from VAL and VL. In short, DBFSL undertook funding accommodation to VAL and VL through its books. For routing such transactions, DBFSL at times collected a small arbitrage from these companies. During the period July 1991 to April 1992, DBFSL arranged funding for these companies to the extent of Rs.133.42 crores. In order to meet a purchase commitment of 50 lakh Units @ Rs.15.00 (ost of Rs.7.50 crores) on 19 May 1992 under a ready forward transaction with Citibank, DBFSL had to borrow the required amount from VL on clean basis where DBFSL had to borrow the required amount from VL on clean basis where DBFSL had not shown the funds received from VL in its books. Detailed comments on this transaction are given separately in paragraph 5 of this chapter.

2. Dealings with Deutsche Bank

2.1 The scrutiny of securities transactions between DBFSL and Deutsche Bank revealed the following :

(a) DBFSL's security transactions were on ready forward basis. DBFSL received funds from Deutsche Bank on most occasions through sale of securities in the first leg of the transactions.

(b) At times, the cost of funds to DBFSL (return for deutsche Bank) was very high ranging from 21 per cent to 76 per cent. Instances are given below:

Date of transaction	Sale/ Purchase	Security	Face value (Rs.in crores)	Rate Rs.	Settlement amount(Rs. in lakhs)	No.of days	Cost/ Return percent
5.5.1992	Sale	Units	7.5	15.49	1161.75 }	1	45
6.5.1992	Purchase	Units	7.5	15.5090	1162.50 }		
20.4.1992	Sale	9% IRFC bonds	6.0	85.00	526.27 }	1	21
21.4.1992	Purchase	9% IRFC bonds	6.0	85.0258	526.58 }		
28.4.1992	Sale	9% IRFC bonds	11.0	90.65	1004.47 }	1	76
29.4.1992	Purchase	9% IRFC bonds	11.0	90.8155	1006.57 }		
28.4.1992	Sale	9% IRFC bonds	6.0	85.25	528.96 }	1	76
29.4.1992	Purchase	9% IRFC bonds	6.0	85.4090	530.06 }		

It will be seen that the security 9% IRFC bonds was traded by Deutsche Bank on 28 April 1992 at two different rates viz. Rs.90.65 and Rs.85.25 which apparently were not in alighnment with market rates.

2.2 During the period 1 April 1991 to 31 May 1992, Deutsche Bank entered into 93 purchase transactions amounting to Rs.686.13 crores and 101 ale transactions for Rs.866.50 crores with DBFSL which constituted about 10 per cent of the total transactions of the latter. The entire trading was on ready forward basis and was in violation of Reserve Bank's directives prohibiting banks from entering into such arrangements with non-bank clients.

2.3 As already stated, Deutsche Bank has a shareholding of 30 per cent (Rs.30.00 lakhs) in DBFSL and acts as its custodian for the latter's securities operations. It is also a banker to DBFSL. Deutsche Bank and sanctioned an overdraft facility of Rs.3.00 crores to DBFSL mainly to meet the working capital requirement of the company. The documents executed by the company for this limit were a demand promissory note for Rs.3.00 crores and a Board resolution. Several temporary overdrawals had been allowed to enable the company to meet its commitments. (The maximum outstanding was a high as Rs.69.53 crores as on 27 Junly 1992). As DBFSL incurred huge losses of Rs.58.38 crores as on 31 December 1992 on account of trading in securities,. Deutsche Bank stopped charging interest on the company's overdraft account from 1 October 1992 as requested by DBFSL. On 9 November 1992. DBFSL made a request to Deutsche Bank to write off 50 per cent of the principal of the excess outstandings amounting Rs.27.54 crores and refund interest charged upto 30 September 1992 amounting Rs.2.60 crores. Initially, Deutsche Bank did not accede to DBFSL's request. However, in December 1992 Deutsche Bank wrote off a debit balance of Rs.24.00 crores in the company's overdraft account i.e. Rs.21.40 crores being the principal amount and Rs.2.60 crores being the interest charged upto 30 September 1992. DBFSL's outstanding overdraft balance with Deutsche Bank as on 31 December 1992 was Rs.40.51 crores (net of Rs.24.00 crores written off by Deutsche Bank).

2.4 As part of continuing rescue operations, Deutsche Bank entered into an agreement with DBFSL on 28 July 1992 to purchase on 31 July 1992, 23.17 crores Units @Rs.14.30 from DBFSL with an option to the company to buy back the Units from Deutsche Bank on or before 28 February 1993 at the same rate of Rs.14.30. This purchase agreement was, in effect, a funding operation to meet the DBFSL's commitment on 31 July 1992 on purchases (representing deliveries under forward purchase deals made on various dates) of 27.50 crore Units from Canfina, Bank of America (BoA), Citibank and Standard Chartered Bank (Stanchart) and sale of 4.333 crore Units to six parties. On exercising the option the company received from Deutsche Bank, an amount of Rs.9.39 crores representing the difference in rates in settlement of Units transaction done by Deutsche Bank on behalf of company. After paying Rs.4.82 crores to Deutsche Bank towards services (i.e. charges at 12 paise per month per Unit on the balance Units held at the end of each month), the company made a net gain of Rs.4.57 crores on its Units sold to Deutsche Bank.

3. Powers of the dealer and methods of operation

3.1 The entire securities and money market operations at Bombay were left in the hands of the dealer. Although certain guidelines have been issued and limits have been fixed for the dealer, she exceeded the delegated powers on a number of occasions. Trading decisions taken by her were also not subjected to closer scrutiny. The reconciliation of BRs issued/ received and outstanding was to be undertaken on a monthly basis. This was never attempted except that a statement of BRs outstanding as at the end of March 1992 was furnished to the company. The dealer reported to the Chief Executive Officer (CEO), and the Management Committee consisting of three members including the CEO was the only other authority which was reviewing the securities trading business. There was no proper back-up section, with a segregation of duties between dealing and settlements. The company did not also have a formal internal audit system. Although the Management Committee met thrice in 1991 and again on three occasions during the period 1 January to 15 May 1992, it did not find any irregularity in the securities transactions. However, at the meeting held on 26 May 1992, certain irregularities were reported and accordingly Deutsche Bank arranged for investigation of DBFSL's affairs by its own officials. The investigation revealed, inter alia, that the dealer had been maintaining a more detailed listing of transactions on her personal computer. This did not form part of the company's record and was maintained exclusively for personal use of the dealer. No officer of the company was aware of the exact date since when this personal computer was in use.

3.2 Some of the irregularities noticed in the working of Investment Banking are as under :

(a) The dealer took far larger positions in securities transactions than what was permitted. The limits placed on dealing through brokers and the exposure limits for banks and finance companies as well as aggregate limits under various securities were not adhered to. For example, the excess exposure was over four times the limit in the case of Canfina on 5 May 1992 and nearly eight times the limit in the case of Citibank and Stanchart on the same date.

(b) Under the arrangement, Deutsche Bank acted as a custodian of physical securities of DBFSL and issued and received BRs and bankers cheques as per instructions issued to the custodian (Deutsche Bank) by the company (DBFSL). There were instances of instructions issued by the company contrary to the actual transactions recorded in its books. For deals done between the bank and DBFSL, no BRs were issued or securities transferred. For securities transactions with Deutsche Bank, the DBFSL's dealer issued letters signed singly, authorising debits to DBFSL's account which was not in accordance with the account mandate. So also were instructions received from DBFSL's dealer for receipt and delivery of securities, receipt and issue of BRs, and cash receive/pay instructions for securities transactions. In other words, it was simply a "one woman show" in DBFSL.

(c) The statements of outstanding BRs (issued/ received) and outstanding ready forward transactions awaiting reversals were not periodically prepared and placed before the Management Committee or Board. These were also not insisted upon.

(d) The dealer was allowed to do "Forward Trading". No record was produced to show that at any time the information on the exact position of forward trading was called for by the top management.

(e) The dealer was in the habit of fudging the quantum of security and deal rate to match with the proceeds received or paid so that the trading losses incurred in the transactions were concealed. On the personal computer, the quantum of securities not reflected in the transactions recorded was shown as "disguised". For instance, on 31 March 1992, 27 lakh Units were sold to a customer @Rs.14.80 (book value Rs.3,99,60,000). The proceeds were received on the same day. However, while preparing the deal ticket/ voucher, the sale transaction was split into 7 lakh Units on company's own account and 15 lakh Units on client's account. Neither a BR was issued nor was scrips delivered to the customer on the date of transaction. The entry for the balance 5 lakh Units was taken in the books belatedly on 31 May 1992 through a journal entry according to which the balance 5 lakh Units were sold on company's own account.

(f) At times the dealer had split the large purchase transactions into smaller lots, for the purposes of record to avoid detection of her transgression of delegated powers and to conceal the higher exposures.

3.3 Irregularities under ready forward transactions

DBFSL had no system of keeping control over the period, yield and cost of ready forward transactions undertaken. At times even when the company needed funds to meet its own commitments, it had entered into certain ready forward purchase transactions of securities which have, in the ultimate analysis, proved to be disadvantageous to the company. On 9 April 1992, DBFSL lent funds under a ready forward transaction in PSU bonds to Canfina (Rs.97.42 crores against Rs.100 crores face value 17% NPC bonds). The deal was for 90 days and yield on the funds to DBFSL was 18.5 per cent. DBFSL had not covered the purchase of 17% NPC bonds of Rs.100 crores for the entire period. Having thus blocked its funds, it had to raise funds for its own requirements intermittently at a higher cost. While the company received from Canfina by way of yield Rs.4.39 crores, it had to pay an interest cost of Rs.9.56 crores on its borrowing made from various counterparties including Deutsche Bank at interest rates ranging between 15 per cent and 50.25 per cent per annum. In order not to attract the attention of the top management the dealer split the transaction with Canfina into five smaller lots.

4. Deals in Units of UTI

4.1 Of the total turnover in securities transactions of the company during the period 1 April 1991 to 31 July 1992 at Rs.15,094.31 crores, the transactions in Units amounted to Rs.11,310.18 crores (74.9 per cent). The dealer started entering into forward purchases and sales of Units in a big way from January 1992, and large positions were taken on various days from February through to mid-April. On 25 April 1992, a large open position was taken for ultimate delivery as of 5 May 1992.

4.2 As per the records maintained by the dealer, the forward position taken by the company in Units as at 30 April 1992 was as under:

It had sold forward 211.50 crore Units of the aggregate value of Rs.3,132.56 crores for settlement on 5 May 1992. As against this, it had made forward purchases of 192 crore Units for an aggregate value of Rs.2,865.53 crores. The forward purchases included one ready forward deal for 10 crore Units taken up on 29 April 1992. Thus, there was a short sale of 29.50 crore Units (value Rs.267.03 crores). Two brokers viz. Asit C. Mehta and D.S. Purbhoodas & Co., accounted for about 80 per cent of the Unit deals. On 5 May 1992, the company adjusted the forward deals in Units broker-wise and booked an outright purchase of 43.05 crore Units (value Rs.642.12 crores) and outright sale of 71.25 crore Units (value Rs.1044.24 crores) leaving a net uncovered position of 28.2 crore Units (value Rs.402.12 crores). This gap was covered on the same day by booking two ready forward deals as explained in the following paragraph.

4.3 The personal record maintained by the dealer indicated that the short position in Units was met by concluding on 5 May 1992 two ready forward purchase deals of (a) 21.5 crore Units with Stanchart and (b) 7 crore Units with Canfina. The investigation of the irregularities and subsequent correspondence on record show that the ready forward purchase deal of 21.5 crore Units (value Rs.300.00 crores) was actually for 20 crore Units and the name of the counterparty recorded in the company's books as Stanchart was incorrect.

4.4 According to the broker Asit C. Mehta's letter dated 29 May 1992 and the letter dated 30 May 1992 from Reliance Capital and Finance Trust Ltd. (RCFT), the details of the first ready forward deal are as under:

(a) (i) The broker Asit C. Mehta had contracted on 28 and 29 April 1992 two ready forward purchase deals on behalf of the company for 10 crore Units each, starting from 5 May 1992, to be reversed on 4 May 1993 and 20 May 1992.

(ii) The base rate of sale of Units was Rs.15 per Unit and 20 crore Units (value Rs.300.00 crores) were delivered on 5 May 1992 to the DBFSL on behalf of the broker's client RCFT. The delivery of 20 crore Units as per delivery instructions, was arranged through Stanchart. DBFSL used this lot of 20 crore Units to partly meet its delivery commitment under its sale transaction of 23 crore Units @ Rs.14.3835 with Stanchart on the same date i.e. 5 May 1992. For the balance of 3 crore Units undelivered, DBFSL issued (through Deutsche Bank) its BR No.265 dated 5 May 1992 for the face value of Rs.30 crores in favour of Stanchart.

(iii) As per understanding reached between DBFSL, the broker and RCFT, 10 crore Units were to be sold back by DBFSL to RCFT on 4 May 1993 at the rate of Rs.15.43 net to DBFSL. DBFSL was entitled on these Units to dividend benefits of only upto 19 per cent out of the dividends declared by UTI for the year ending June 1992. If any dividend higher than 19 per cent was declared by UTI, the difference was to be paid to RCFT by DBFSL within 30 days from the date of dividend declaration. All other benefits such as rights and bonus on 10 crore Units (if allowed by UTI) were to go to RCFT.

(iv) The purchase of balance 10 crore Units was to be reversed by DBFSL on 20 May 1992 calculated @31.5 per cent per annum.

(v) The delivery of Units was by physical scrips.

(vi) DBFSL had not received the cost memo from Stanchart and delivery note from broker Asit C. Mehta. The terms of understanding other than reversal at the rate of Rs.15.43 (net) and date of reversal i.e. 4 May 1993 could not be confirmed in the absence of any record in the company's books. For record, only a cost memo internally prepared was retained in the file.

(vii) The company did not have any record of distinctive numbers of the 20 crore Units believed to have been delivered to it by the broker through Stanchart on account of RCFT. The record at DBFSL did not reveal the manner in which its purchase consideration of Rs.300 crores was passed on to RCFT.

(viii) At Stanchart, records did not show the sale deal of 20 crore Units (value Rs.300 crores) to DBFSL on RCFT account on 5 May 1992. However, Stanchart had recorded three sale deals on its own account for an aggregate number of 20 crore Units to DBFSL on the same day for which there were no corresponding purchase entries in the books of the latter. As stated earlier, in the books of DBFSL there was one entry for purchase of 20 crore Units from Stanchart (altered to 21.5 crore Units). The details of the sale deals as recorded in Stanchart's books are as at bottom of this page.

(ix) Cost memos, broker notes and delivery orders in respect of these transactions were not available at Stanchart. Stanchart had netted the amount of Rs.300 crores on 20 crore Units at Rs.15 from the amount of Rs.330.8987 crores payable on 23 crore Units purchased

Date	Quantity of Units sold (crores)	Rate Rs.	Counterparty	Name of the broker	Sale consideration (Rs.in crores)
i) 5.5.92	10.00	15.00	DBFSL	Asit C.Mehta	150.00
ii) -do-	6.00	15.00	-do-	-do-	90.00
iii) -do-	4.00	15.5575@	-do-	L.K. Pandey	62.23
	20.00				302.23

@ Delivery rate for Stanchart was Rs.15 per Unit by it from DBFSL. It accepted from DBFSL BR No.265 for 3 crore Units for the residual amount of Rs.30.8987 crores. An amount of Rs.2.23 crores representing the difference in the contract and delivery rate in the thrid transaction was received by a bankers' cheque issued by Fort branch of Syndicate Bank on account of Dhyan Investments.

(b) In the books of DBFSL, deals recorded and subsequent settlements were as under :

(i) The company's transaction list and purchase deal ticket (CP 326) show the name of the counterparty as Stanchart instead of RCFT.

(ii) The quantum of Units purchased was shown as 21.5 crore Units instead of 20 crore Units though what was contracted for through the broker Asit C. Mehta was 20 crore Units. The purchase rate was shown as @Rs.13.953488 on 21.5 crore Units as against the actual contracted rate of Rs.15 on 20 crore Units.

(iii) The total purchase consideration of Rs.300.00 crores was netted from the sale proceeds of Rs.330.8987 crores due to DBFSL from Stanchart on the same date i.e. 5 May 1992. DBFSL received a net amount of Rs.30.8987 crores from Stanchart representing the difference between its purchase cost and sale consideration of Units in the two deals.

(iv) By inflating the number of Units by 1.5 crore, the dealer apparently wished to show that there was overall gain from all forward deals in Units concluded sale of these 1.5 crore Units. It would appear that the dealer fudged the records to conceal or defer the trading losses arising particularly in Units deals booked on forward basis in the earlier months.

(v) In another case, the dealer had inflated the spot Units position as on 5 May 1992 by booking a fictitious purchase of 1.65 crore Units to disguise the losses incurred by the company. Of the 1.65 crore Units, purchase of 1.5 crore Units was included in the purchase transaction referred to in item (ii) above. In regard to the purchase of 0.15 crore Units, the transaction list shows that DBFSL paid to Stanchart an amount of Rs.2.15 crores for purchase of 0.15 crore Units directly at the rate of Rs.14.3333 per Unit. The company did not have on its record, sale memo of Stanchart . The mode of delivery of 0.15 crore Units was neither recorded nor was a BR from Stanchart actually received.

(vi) On scrutiny, it was observed that the dealer had disguised through this fictitious purchase transaction the trading loss on matching forward purchase and sale contracts of 6 crore Units each with Stanchart concluded through broker Excel & Co. There were three forward purchases of 2 crore Units each and three forward sales of 2 crore Units on different dates from 24 January 1992 to 7 April 1992 where the company had incurred a net loss of Rs.2.15 crores. The dealer did not book this loss in the accounts as on 5 May 1992 straight away but instead covered this loss by recording an outright spot purchase of 0.15 crore Units from Stanchart.

(c) In regard to the two ready forward deals of 10 crore Units each purported to have been concluded on 5 May 1992 with RCFT as counterparty through broker Asit C. Mehta, the settlement arrived at was as under:-

(i) DBFSL did not have in its custody 10 crore Units to undertake the sale deal (reversal) with the counterparty on 20 May 1992. RCFT and broker Asit C. Mehta have acknowledged that DBFSL gave physical delivery of 2 crore Units on 18 May 1992. There is no transaction for sale of 2 crore Units with RCFT in the books of DBFSL. The company has, however, booked a sale of 2 crore Units to American Express Bank @Rs.15.1683 through broker Asit C. Mehta. Sale memo from American Express Bank and contract note from Asit C. Mehta were not on record. The company received sale proceeds of Rs.30.342 crores inclusive of excess amount of Rs.54,000 payable to the broker by cheque dated 18 May 1992 from Oman International Bank. On 20 May 1992, DBFSL did not deliver the balance 8 crore Units but instead arrived at a settlement with RCFT on 30 May 1992 according to which it was agreed that in consideration of cancellation of the agreement to deliver 8 crore Units, DBFSL will pay to RCFT compensation for non-delivery of Units, a sum of Re.0.55 per Unit being the price difference as on that date. On 8 crore Units, DBFSL paid an aggregate amount of Rs.4.40 crores to RCFT on 1 June 1992.

(ii) With regard to the delivery of 10 crore units to be delivered on 4 May 1993 @ Rs.15.43 the DBFSL also deemed it fit to cancel the reversal (sale) of the ready forward deal. In consideration thereof, DBFSL agreed to pay an aggregate sum of Rs.19.00 crores to RCFT.

(iii) A pay order for an aggregate amount of Rs.23.40 crores representing the cost of compensation towards cancellation of the sale of 8 crore Units not delivered as on 20 May 1992 and 10 crore Units to be delivered in May 1993 was issued to RCFT on 1 June 1992.

(iv) Subsequent to declaration of 25 per cent dividend on Units by UTI, for the year ended June 1992 the company in keeping with the terms of understanding (as mentioned at [a(iii) above] paid a further sum of Rs.5 crores to RCFT on 27 July 1992.

(v) There were no notes recorded to indicate the basis on which the decision was taken to cancel the ready forward reversal deal to the extent of 18 crore Units and to make a total payment of Rs.28.40 crores to RCFT.

(d) The aggregate loss incurred from the trading deals in Units involving Stanchart and RCFT on 5 May 1992 is estimated at Rs.39.1604 crores, as under.

(i) The company utilised the 20 crore Units purchased from RCFT on 5 May 1992 (on ready forward basis) to set off its delivery commitment of 23.00 crore Units to Stanchart on the outright sale deal on the same day.

(ii) The break-up of trading loss is detailed below :

		(Rs.in crores)
	Purchase cost of 20 crore Units from Stanchart (RCFT) @Rs.15 on 5 May 1992	300.00
Less	Sale proceeds of 2 crore Units received @Rs.15.1683 on 18 May 1992	30.3366
		269.6634
Add	Payout to RCFT on 1 June 1992 and 27 July 1992 towards difference in Unit costs/ compensation towards cancellation of balance delivery of 18 crore Units unfulfilled commitment under ready forward deals.	28.40
	Total outlay	298.0634
	Sale proceeds received from Stanchart on 18 crore Units (out of 23 crore) @Rs.14.3835 on 5 May 1992	258.903
	Trading loss on purchase and sale of 18 crore Units	39.1604

4.5 On 5 May 1992, DBFSL incurred losses of Rs. 4.48 crores while unwinding its forward deals in Units with counterparties viz., Citibank, Canfina and Stanchart. In its ready forward purchase deal of seven crore Units with Canfina on the same day, DBFSL incurred losses of Rs. 2.88 crores on the reversal leg of the transaction settled on 21 May 1992.

5. Clean borrowing of Rs.7.50 crores from M/s. Videocon Ltd.

5.1 To meet the various commitments to deliver physical scrips or for reversal of ready forward obligations in May 1992, the dealer fudged the record in the case of the transaction described below.

5.2 The company had sold 50 lakh Units to a customer on three different dates viz. 3 January 1992 (12 lakh Units), 6 January 1992 (8 lakh Units) and 25 March 1992 (30 lakh Units) and had issued BRs thereagainst. The relative BRs were received back from the customer duly discharged on 7 May 1992. However, no delivery of the Units was undertaken. In order to make delivery of the Units, the dealer recorded a fictitious sale of 50 lakh Units to the same customer on 19 May 1992 and to show receipt of the sale proceeds thereof a clean loan of Rs.7.50 crores was obtained from V.L. This loan was not recorded as the company's liability in its books. However, the fictitious sale entry and the receipt of the sum of Rs.7.50 crores enabled the dealer to issue instructions to the custodian viz. Deutsche Bank to deliver 50 lakh Units to the customer on 19 May 1992, and thus fulfil the commitments under the three sales. The amount of Rs.7.50 crores obtained from V.L. together with the interest of Rs.5.31 lakhs for the period from 19 May 1992 to 5 June 1992 (at call money rates) was paid to V.L. treating the aggregate amount of Rs.7.5531 crores as a trading loss.

6. Working results of the company

The company changed its financial year from 1 October - 30 September to 1 April - 31 March in 1992 in September 1992. As per the provisional unaudited accounts of the company for the 9 months period ended 31 December 1992, it suffered an aggregate loss of Rs.58.38 crores. After adjusting a portion of the company's dues to Deutsche Bank to the extent of Rs.24.00 crores, (which was written off by Deutsche Bank) and also taking into account its carried forward profit of Rs.0.64 crore as on 31 March 1992, the company ended up with a net loss of Rs.33.74 crores as on 31 December 1992. This has totally eroded the paid-up capital of the company at Rs.1.00 crore as on that date resulting in its negative net worth at Rs.32.74 crores.

7. Conclusion

7.1 The findings clearly show that (DBFSL) had not taken care to introduce proper systems and controls and develop an independent back-up section for its securities transactions. The top management failed totally in applying the brakes on the reckless trading activities of the dealer. The absence of control enabled the dealer to fudge the records and thereby conceal the losses.

7.2 The company's net loss as at the end of December 1992 was Rs.57.74 crores (without taking into consideration the company's dues of Rs.24.00 crores written off by Deutsche Bank). Even after write off of its dues of Rs.24.00 crores by Deutsche Bank, the company still owed an amount of Rs.40.51 crores (88.3 per cent of the outside liabilities) to Deutsche Bank as on 31 December 1992.

7.3 The company had become a large and aggressive player in Units deals. The forward deals in Units proved to be detrimental to the interest of the company. This could not have escaped the attention of the CEO and a Director of the company who not only signed cheques on the company's account but also had an opportunity to review the day-to-day transactions, which were submitted a in consolidated form to the Management Committee. There was no explanation as to how the dealer was allowed to accumulate losses on forward deals in the period January-April 1992 and to take an overbought position of 27.50 crore Units as on 31 July 1992. The then CEO and the dealer were not available for clarifications, having been allowed to resign during July/ August 1992. The Board of the company had in fact sounded a note of caution in its meeting held on 10 February 1992 with respect to trading in Units and PSU bonds "in view of the anticipated changes in fiscal laws and regulations on the anvil".

XIII. National Housing Bank

The Committee in its second Report (chapter VI) had covered certain features in the securities transactions of National Housing Bank (NHB). The observations based on a further scrutiny carried out are furnished in the following paragraphs.

2. Ready forward deals vis-a-vis call money lendings.

2.1 During the period October 1991 to February 1992, NHB had undertaken certain purported securities transactions as detailed below in which funds were initially raised by it through sale of Units or PSU bonds from State Bank of India (SBI). The funds so raised were simultaneously lent to other banks by way of entering into purchase deals of the same securities. The deals were generally reversed within a period of 1 to 3 days.

Period (From - To)	Particulars of securities sold to SBI	Amount received (Rs.in crores)	Interest paid to SBI (Rs. in lakhs)	Securities purchased from	
				Name of the Bank	Amount paid (Rs.in crs.)
1.	2.	3.	4.	5.	6.
1. 19.10.91 to 21.10.91 22.10.91	9% IRFC bonds	300.00	45.82	Indian Bank	300.00
2. 24.10.91 to 25.10.91	9% IRFC bonds	118.00	5.09	United Bank of India	118.00
3. 28.10.91 to 29.10.91 4.11.91	i) 9% IRFC bonds (reversed on 29.10.91) ii)9% IRFC bonds (reversed on 4.11.91)	150.00 85.00	31.11	i)Indian Bank ii)Indian Bank	150.00 (reversed on 29.10.91) 100.00 (reversed on 4.11.91)
4. 29.10.91 to 30.10.91	Units	142.00	5.15	United Bank of India	142.00
5. 30.10.91 to 31.10.91	Units	110.00	2.86	UCO Bank	110.00
6. 18.11.91 to 20.11.91	Units	80.00	15.11	i)Allahabad Bank ii)Indian Bank	80.00 (reversed on 19.11.91) 80.00 (purchased on 19.11.91 and reversed on 20.11.91)
7. 20.11.91 to 22.11.91	i)Units ii)Units	78.00 21.00	13.67 3.16	i)Allahabad Bank ii)Bank of America	80.00 21.00
8. 2.12.91 to 3.12.91	Units	38.00	1.24	Indian Overseas Bank	38.00
9. 22.02.92 to 24.02.92	Units	110.00	5.12	Indian Bank	110.00

2.2 From scrutiny of the records relating to these transactions at NHB and the counterparty banks, the following facts have emerged.

(a) The records at SBI showed that it had not undertaken these securities deal with NHB in its own investment account.

(b) The relative receipts and payments have been put through in the current account of Harshad S. Mehta (HSM) in the books of SBI.

(c) In the books of the counterparty banks, receipts and payment of funds, have been shown as call money borrowings and repayment thereof and not sale and purchase of securities to or from NHB.

(d) In all these cases call deposit receipts have been issued by the counterparty borrowing banks and on repayment of the borrowings they have received back the relative receipts duly discharged by the officials of the NHB. In the case of transaction at No.6 with Indian Bank on 19 November 1991 and at No.7 with Allahabad Bank on 20 November 1991 call deposit recepits issued are for Rs.140.00 crores and Rs.166.00 crores respectively as the amounts indicated in column 6 above were clubbed with regular call money lendings of NHB to these banks on those dated. In the case of the transaction at No.7 with Bank of America on 20 November 1991 for Rs.21.00 crores, although there is evidence to indicate that a call deposit receipt has been issued, the discharged receipt is not available on the record of that bank.

(e) The entire accounting of the purchase and sale transactions in NHB's books was fictitious. As these transactions have been accounted for as call money borrowings by counterpaty banks and not as sale of securities and as they have issued call deposit receipts to NHB, no actual sale of securities was made by NHB to SBI as shown in the books of NHB.

(f) NHB is permitted to nly lend but not to borrow in the call money market. Apparently to overcome this restriction, transactions have been shown as security transactions by NHB.

(g) The transactions clearly indicate that the modus operandi was adopted to enable HSM to deploy the funds available with him in the call money market as he is not permitted to participate directly in the call money market. In the process HSM earned an income of Rs.128.33 lakhs within a short period (i.e. in 2 or 3 days in respect of each deal) through these transactions.

2.3 Out of the amount of Rs.300.00 crores received by NHB from SBI on 19 October 1991 (item 1 of the Table) an amount of Rs.188.00 crores was adjusted on 21 October 1991 by a purchase transaction and the balance amount of Rs.112.00 crores was reversed only on 22 October 1991. However, as the entire amount of Rs.300.00 crores lent to Indian Bank was received back by NHB on 21 October 1991 itself, NHB had to record a "sale" transaction with Indian bank for Rs.300.00 crores only. As NHB was not holding sufficient balance in PSU bonds on that date this had resulted in NHB's books showing an oversold position in PSU bonds to the extent of Rs.85.69 crores on 21 October 1991.

3. Transactions with State Bank of Saurashtra

3.1 NHB had lent to State Bank of Saurashtra (SBS) undernoted amounts as call deposits.

Date	Amount lent (Rs. in) crores)	Date of reversal	Rate of Interest %	Amount of interest received from SBS (Rs. in lakhs)
5.7.91	25.00	26.7.91	24.5	33.56
13.7.91	47.75	-do-	28.0	47.62
18.7.91	50.00	-do-	28.0	30.68
				111.86

NHB had also received during the same period from SBS the undemoted amounts.

(Rs. in crores)

Date	Amount borrowed	Nature of borrowal	Date of reversal	Rate of interest (%)
5.7.91	25.00	Sale of bill	5.8.91	23
13.7.91	47.75	Sale of SRHDs* -Rs.39.75 crores Sale of Units - Rs.8.00 crores	11.10.91	18
18.7.91	49.86	Sale of bill	26.7.91	12.5

(* Special Rural Housing Debentures)

(The transaction of Rs.47.75 crores is recorded as sale of SRDHs and Units in the books of NHB. In the books of SBS, however, it is recorded as a rediscounting of bill transaction).

3.2 Out of the amount of Rs.111.86 lakhs received by NHB as interest from SBS, only an amount of Rs.79.34 lakhs was taken to income account. The amount of Rs.79.34 lakhs was worked out at the rates of 23 per cent, 18.5 per cent and 13.5 per cent presumably to aligh the rates with the rates charged by SBS on amount lent by it. The balance amount of Rs.32.52 lakhs was initially held in Sundry Deposit account by NHB.

3.3 The balance amount was paid to SBI on 12 August 1991 (by cheque No.159772) although the excess interest was considered by NHB as refundable to SBS. There was also no indication of any underly8ng transaction in this regard with SBI in the records of NHB. At SBI the amount was credited to the current account of HSM.

3.4 In a number of transactions with SBS the particulars of transactions relating to nature of security and/ or nature of transaction itslef as reported in the books of NHB and SBS differ. Further, in some cases amounts have been received from or paid to SBI, even though the counterparty was mentioned as SBS in NHB books.

4. **Transactions in the Savings Bank account of Shri Deepak Mehta at SBI Bombay (Main) branch**

4.1 NHB had issued three cheques agreegating Rs.24.49 lakhs in favour of SBI relating to certain security transactions as detailed below.

(a) **Cheque No.173926 dated 1 February 1992 for Rs.8.99 lakhs**

As per NHB records the cheque relates to excess amount received from SBI in respect of certain PSU bonds and Units sold to ti by NHB on 29 and 31 January 1992. The amount initially held in sundry deposit account was paid to SBI on 1 February 1992.

(b) **Cheque No.212157 dated 21 February 1992 for Rs.2.50 lakhs**

NHB had to pay to SBI a total amount of Rs.47.975 crores on 21 February 1992 representing cost of Treasury Bills of face value Rs.50.00 crores purchased by it. The amount was paid by two cheques for Rs.47.95 crores and Rs.2.50 lakhs.

(c) **Cheque No.212167 dated 22 February 1992 for Rs.13.00 lakhs**

NHB had to pay to SBI total amount of Rs.152.12 crores representing cost of Government securities (described as GOI Loan 2007 and 2008) purchased from it. The amount was paid by two cheques for Rs.151.99 crores and Rs.13.00 lakhs.

4.2 During the CBI investigation at SBI, Bombay (Main) branch it transpired that the proceeds of the cheques have been credited to the Savings Bank account of one Shri Deepak Mehta (a close relative of HSM), on the strength of three forwarding letters accompanying the cheques, signed by two officials of NHB. Further investigation revealed that the signatures on the forwarding letters were forged. The amount credited to Deepak Mehta's account has been reportedly used for purchase of shares etc. by him. The matter is being investigated by CBI.

The transactions referred to at item (b) and (c) form part of disputed transactions of SBI with NHB and the remaining portion of the cost of securities was credited to the account of HSM as indicated in paragraph 4 (b) of Chapter VI of the second Report of the Committee. As regards the transaction at (a), the same is apparently put through the account of HSM, as the relative deals have not been undertaken by SBI on its own investment account.

5. Transactions with other banks/institutions

5.1 Certain other features observed in the securities transactions of NHB with banks and institutions are given below.

5.2 As per NHB's books a large number of transactions in PSU bonds and Units were booked in the name of Syndicate Bank. Further scrutiny revealed that majority of these transactions have been routed through Syndicate Bank on behalf of Fairgrowth Financial Services Ltd. (FGFSL). Many of these transactions were originating sales of NHB reflecting borrowing of funds by NHB.

5.3 (a) NHB had undertaken certain transactions in Government securities wherein it purchased securities of 11.5% GOI Loan 2010 from certain banks and sold them to certain other banks (or to the same bank in a few cases), on the same day. On five such occasions NHB routed through its books during January to March 1992 aggregate purchases of Rs.209.64 crores and sales of Rs.207.32 crores thereby incurring a loss of Rs.2.32 crores. This loss was reimbursed to it by FGFSL by means of cheques drawn on Syndicate Bank, in each group of transactions. The background to these payments by FGFSL is not ascertainable.

(b) In another transaction in this security, NHB short sold to the extent of Rs.20 crores (face value) on 18 April 1992 to Andhra Bank (Rs.15 crores) and Banque Indosuez (Rs.5.00 crores) and remained short until 20 April 1992 when it purchased the said security from Syndicate Bank.

5.4 In the case of transactions of NHB with UCO Bank, 19 out of 24 transactions during the period 1 April 1991 to 30 March 1992 have been put through in the current account of HSM in the UCO Bank. In many cases payments were received from or made to SBI, eventhough counterparty as recorded in NHB books was UCO Bank.

5.5 As per NHB's records it had 95 deals in PSU bonds and Units etc. with SBI Capital Markets Ltd. (SBI Caps) during the period April 1991 to May 1992. The scrutiny of records of SBI Caps has revealed that out of these as many as 46 deals do not appear in the books of SBI Caps. The deals with SBI Caps have been settled by issue or receipt of RBI cheques by Bombay (Main) branch of SBI. Since the transactions are not reflected in SBI Caps and there were no such deals with SBI Caps and no such transactions with SBI either, it is clear that these were put through in the account of HSM at the SBI Bombay (Main) branch. Many of the transactions are originating sales in NHB indicating borrowing of funds by NHB from HSM.

XIV. Bank of America

Various irregularities observed in the securities transactions of Bank of America (BoA) during the period April 1991 to May 1992 were brought out with instances in the third Report of the Committee (chapter V). Further scrutiny of the securities transactions of this bank revealed some more irregularities which have been detailed in the following paragraphs.

2. Short sale of GOI securities

On 6 April 1992 BoA sold to Citibank, SBI and Standard Chartered Bank (Stanchart) securities of 8.25% GOI Loan 1995 of aggregate face value of Rs. 310.00 crores by issuing SGL transfer forms when its effective balance in the above securities (after taking into acount the bouncing of certain inward SGL transfer forms as advised to it by the PDO on 3 April itself) was only Rs.40,44,82,500.00. This has resulted in a net short sale of Rs.269,55,17,500.00 in this security.

3. Portfolio Management Scheme (PMS)

3.1 During the period under reference, the bank had three PMS clients as under:

(Rupees in crores)

	Name of PMS client	PMS client since	Amount placed with the bank	Amount paid back	Return (%)
1.	Unit Trust of India	October 1990	100.00	114.00	14.00
2.	Indian Railway Finance Corporation	May 1991	10.00	11.67	16.68
3.	Peerless General Finance & Investment Ltd.	July 1991	25.00	29.53	18.11

3.2 From the records, it was observed that the bank had invested the entire PMS funds in its own investment account only and earnings on PMS funds were made available to the clients by undertaking a series of sale and purchase transactions on certain dates in a month with its own investment account with abnormal variation in the sale and purchase prices of the securities. The manner in which these transactions were undertaken by the bank giving huge earnings to PMS clients accounts in certain months is indicative of the bank's prior commitment of an assured return on PMS funds, or its intention of parking a share of the bank's profit for the month in PMS account to be withdrawn later. For instance, in the PMS account of Peerless General Finance & Investment Ltd., the bank showed earnings in the range of Rs.0.34 crore in July 1991 to Rs.16.16 crores in March 1992. The bank adjusted the profit earning in such a way that on maturity of the contract, it could pay to the company aggregate amount of Rs.4.53 crores only. The bank officials could not clarify the matter.

3.3 Apart from violating RBI guidelines on PMS by accepting short-term funds from PSUs and corporate bodies as brought out in the third Report, the bank has also deviated from other PMS guidelines such as PMS funds to be accepted by the bank entirely at the customer's risk without guaranteeing either directly or indirectly a predetermined return, and the transactions between the bank's investment account and the PMS clients being undertaken strictly at market rates.

4. Deployment of short-term funds of PSUs and corporate bodies for securities transactions

4.1 It was pointed out in the third Report of the Committee that BoA used the mechanism of ready forward deals in PSU bonds and Units for deploying short-term funds of PSUs and corporate bodies. Further scrutiny of the deals entered into by BoA for deploying such funds revealed that as on 25 April 1992, the forward liability on account of the ready forward transactions in PSU bonds and Units amounted to Rs. 431.50 crores, out of which the liability on account of IOC, PFC and IRFC alone amounted to Rs. 151.18 crores, Rs. 76.58 crores and Rs. 42.74 crores respectively. In other words, the short-term funds accepted by the bank from PSUs and corporate bodies through ready forward deals in PSU bonds and Units and invested in securities in its investment portfolio amounted to Rs. 431.50 crores which accounted for 49% of the bank's investments (Rs. 881.00 crores) as on 31 March 1992.

4.2 Transactions of this nature enabled BoA to earn large profits as could be seen from the following:

(Rupees in crores)

	31-03-1991	31-03-1992	% increase
1. Deposits	731	1169	59.9
2. Advances	972	894	(-) 8.0
3. Total investments	259	881	240.0
- of which SLR investments	239	346	44.8
4. Gross profit of the bank	62.24	136.09	118.7
5. Profit from securities transactions	12.40	56.84	358.4
6. % of (5) to (4)	19.9	41.8	

5. Off the books (OB) deals

Apart from OB deals of ready forward nature undertaken by BoA referred to in the third Report of the Committee, it was observed that the bank was also acting as intermediary between two counterparties for ready sale and purchase transactions concluded on the same day. At times these transactions were done through the brokers also. In such transactions done through the brokers, instead of merely paying brokerage to the brokers, the bank in some cases had passed on to or recovered from the brokers the entire difference between purchase and sale prices of the securities suggesting that the bank could be undertaking these transactions also on behalf of the brokers. The bank could not give any satisfactory explanation for the practice adopted by it.

6. Dummy forward deals with the brokers

6.1 As already mentioned in the third Report of the Committee BoA has been accommodating the brokers by allowing them to take forward positions through the OB deal mechanism. Such forward deals booked through the brokers had never been confirmed by the counterparty indicated in the deal. Hence the forward liability in respect of these dummy forward deals was being controlled in the BoA's books in the name of the concerned broker whereas in the case of forward deals entered into by BoA directly with banks/non-bank clients, this liability was controlled in the name of the counterparty bank/ non-bank client.

6.2 The bank had fixed specific forward exposure limits for selected brokers for monitoring its forward exposures against these brokers. Such forward exposures taken by the bank on behalf of these brokers as on 30 April 1992 aggregated Rs.6549.19 crores as against permitted aggregate broker exposure limits of Rs. 940.00 crores only. It was observed that for arriving at the aggregate forward exposure position in respect of each broker every day, the bank was netting the forward purchases and sales figures instead of adding them together, resulting in a lower exposure position. In the case of forward deals entered into by the bank directly, the forward liability of the counterparty (bank and non-bank clients) was correctly arrived at by aggregating the sale and purchase figures instead of netting. Thus, BoA was following two different standards for working out its forward exposure position.

6.3 Controlling the forward exposure liability against brokers on netting basis, it was reported, had the approval of BoA's country office at New Delhi and also of the Head of the Capital Markets, Asia Division, Hongkong. By netting its exposure against brokers, BoA was accommodating the brokers to take forward position to any extent and without any value limit thus violating its own guidelines. For example, as against an exposure limit of Rs.50.00 crores allowed in respect of Bhupen Champaklal Devidas, the aggregate of forward purchases and sales exposure in his name as on 30 April 1992 was Rs.1099.48 crores whereas the netted position as controlled in the system was only Rs.75.50 crores. Similarly the aggregate (actual) forward position allowed to Hiten P. Dalal, as against a limit of Rs.10.00 crores, as on 30 April 1992 was a whopping Rs. 1040.79 crores whereas the same as controlled in the system was (-) Rs.582.97 crores only.

6.4 When the irregularities in the securities transactions came to light, the forward liability on account of 41 such forward deals (dummy deals) valued at Rs.1521.50 crores controlled in the names of brokers like Harshad S. Mehta, Bhupen C. Devidas, M/s.V.B. Desai and N.K.Aggarwala & Co., devolved on BoA and the bank had to take these into its position as these dummy deals were disowned by the counterparties concerned (dummy) mentioned in the deal. This amply proves that these were mere broker positions. The bank has estimated the impact of these dishonoured contracts at a net loss of nearly Rs.21 crores.

7. Exchange of SGL transfer forms

In respect of many purchase and sale transactions in Government securities the bank had used SGL transfer form as 'BR' and the transactions were settled by mere exchange of SGL transfer forms (on the same day or after a few days) without lodgement with the PDO. It was also observed that the SGL transfer forms were used by the bank as 'BR' for netting the transactions. In some cases SGL transfer forms issued by BoA/ other counterparty banks and bounced on lodgement with PDO were also used for settlement of transactions by mere exchange.

8. Violations of IBA instructions on Bank Receipts

Apart from the fact that the bank was issuing its BRs and accepting BRs of other banks for netting of its transactions as indicated in the third Report of the Committee, it was also not observing the instructions contained in IBA circular dated 6 May 1991 regarding issue of BRs, in many respects. It was also observed that during the period from April 1991 to December 1991, the bank had issued various BRs to counterparty banks having the same serial number. The nature and value of securities under each BR were different but this irregularity went unnoticed for a long time. The control on issue of BRs was thus lax.

9. Deals without brokers' contract notes

It was observed that in respect of many deals spot as well as forward, in all types of securities booked by the bank through Bhupen Champaklal Devidas, Hiten P. Dalal and N.K.Aggarwala & Co., the brokers' contract notes were not found on the bank's records and transactions were concluded on the basis of delivery notes issued by the brokers. A good number of such deals were settled through BRs and were undertaken through B.C. Devidas.

XV. Canbank Financial Services Ltd.

1.1 Reference was made in the fourth Report of the Committee issued in March 1993 to the securities transactions of Canbank Financial Services Ltd. (Canfina). A further scrutiny of the transactions has been made and the findings are recorded in subsequent paragraphs.

1.2 Canfina traded in Government securities on the basis of BRs without insisting on or issuing SGL transfer forms. BRs were exchanged for BRs. RBI instructions not to deal in Government securities with non-bank clients on ready forward basis were not adhered to. Securities including Government securities were sold at rates which were not market related.

1.3 In respect of several purchases, where the rates indicated in the cost memos received from the counterparties were lower than the contracted rates, Canfina made payment at the rate as per cost memo. The difference in amount was passed on to the broker or adjusted against payments due from him. In cases where rates indicated in the cost memos were higher than the contracted rates, Canfina paid the higher amount to the counterparty and recovered the difference from the broker. Similarly in respect of its sales, when Canfina received less than the contracted amount from the counterparty, the difference was recovered from the broker. In a number of purchase and sale transactions the actual payment or receipt was to or from a counterparty other than the one named in the relative contracts. In certain cases, Canfina had accepted adjustment of purchase and sale proceeds involving the same or different counterparty banks, brokers and securities through the account of a broker maintained at the counterparty bank or third bank. There were several instances where Canfina had made excess payments for its purchases or received short payments in respect of its sales. In some of these cases the amount involved was significant. Such excess payments or short receipts were recovered or adjusted after a period, thereby accommodating the brokers on an interest free basis.

1.4 In disregard of RBI guidelines, Canfina undertook in its clients' accounts ready forward transactions in PSU bonds, debentures and Units for a period ranging from one day to six months and over and in some cases on open basis. By undertaking ready forward deals on sellback or buyback basis, Canfina lent or raised funds in the market. The market operations of Canfina indicated that 90 per cent of its ready forward deals were on buyback basis. The company raised substantial funds through such deals mainly to make repayments to the clients who placed funds with Canfina under its PMS/ Corporate Investment Advisory Services (CIAS) and to honour its commitments under the reverse legs of earlier buyback deals. There was no system of preparing periodically the list of outstanding ready forward commitments for being placed before the top management. In respect of some of the ready forward deals, the rate of interest at which the reversal purchase deal was undertaken was much higher than the rate indicated in the dealer's pad, thereby causing loss to the company.

1.5 (a) Canfina permitted the broker common to security deals involving different counterparties and scrips to net its outstanding buyback transactions and received from or paid the netted amount to him by simultaneously undertaking fresh sale deal through him on the date the transactions were netted. These deals had thus allowed the broker to assume the role of counterparty even though the record showed him as broker. In such deals, Canfina accepted from the broker and not from the counterparty its outstanding sale BR (duly discharged) without passing on the repurchase consideration directly to the counterparty named in Canfina's discharged BR. It then issued fresh BRs in the name/s of counterparty/ies named by the broker even when the named counterparty did not make payment of the sale proceeds of the securities named in those BRs to Canfina.

(b) There were eight netted transactions where Canfina entered into 17 purchase and 11 sale deals of different securities with different counterparty banks. Of these, four netted transactions each were concluded at Bombay and Calcutta. While Harshad S. Mehta (HSM) was broker to the Bombay transactions, Rahul & Company were either the broker or the counterparty in respect of the four netted deals at Calcutta. Sale/cost memos in most cases were not issued/received in the above transactions.

(c) In one of the netted transactions, Canfina had, as per its records, taken up on 27 August 1991 through common broker HSM three purchase (Rs.100.97 crores) and one sale (Rs.98.06 crores) transactions with four different counterparties, namely American Express Bank, Canbank Mutual Fund (CBMF), State Bank of India and SBI Caps of 9% HUDCO bonds, 9% NLC bonds, Units and 9% IRFC bonds respectively. Of the four transactions, three purchases made by Canfina were its buyback deals and the fresh sale transaction in 9% IRFC bonds (face value - Rs.100.00 crores) was on ready forward basis. Canfina got back, duly discharged, its two outstanding sale BRs both dated 12 July 1991 issued in favour of American Express and CBMF and one outstanding sale BR dated 31 July 1991 issued in the name of State Bank of India from broker HSM. For its sale of 9% IRFC bonds of Rs.100.00 crores, Canfina handed over to broker HSM its sale BR dated 27 August 1991 issued in favour of SBI Caps. Canfina neither passed on buyback consideration to the three counterparty banks nor received sale consideration from SBI Caps. It paid the net amount of Rs.2,90,93,810.68 to the broker by way of its cheque drawn in favour of State Bank of India. The record of CBMF indicated that there was no deal with Canfina on 27 August 1991.

2.1 Mention has been made in the fourth Report of the Committee about the various ways by which Canfina had placed certain brokers in funds. Canfina bought securities directly from various brokers on 93 occasions (Rs.1078.74 crores) during the period April 1991 - May 1992. Of these, in 13 cases identified so far (as per table given on page 218) Canfina's purchase was on sellback basis.

Under these deals, Canfina virtually lent an aggregate amount of Rs.133.41 crores to certain brokers; the prominent of whom were Rahul & Co. (Rs.71.88 crores), C. Mackrtich (Rs.50.51 crores) and Hiten P. Dalal (Rs.11.02 crores). In three cases, the securities shown to have been received were Cancigo units which were not transferable. In 10 such deals, there is no evidence of any security having been received. Canfina's funds remained with the brokers for a period of two days to four and half months and were received back by it subsequently together with yield at varying rates. In effect these were in the nature of clean loans.

2.2 (a) Canfina had, as per the dealer's pad, made a purchase transaction for Rs.17.29 crores on 10 October 1991 directly with CBMF. The description of the security mentioned in the dealer's pad is "14% RIL". The rate of purchase and mode of delivery have not been indicated. Although only one transaction for Rs.17.29 crores to the Bombay (Tamarind Lane) branch of Canara Bank. There is no record to show that any security was received by the company. The transaction did not appear in the books of CBMF.

(b) As per the correspondence between the CBMF and Canara Bank the amounts of Rs.8.99 crores and Rs.8.30 crores were released to brokers Pallav Sheth and Ketan Parikh respectively by CBMF at the instance of Canfina. A note made in the column 'Nature

Statement showing the purchase of security from broker on ready forward basis where the broker was funded by Canfina

Sr. No.	Date of transaction	Particulars of security		Name of broker	Rate (Rs.)	Book value (Rs. in crs.)	Date of reversal	Rate (Rs.)	Book value (Rs. in crs.)
		Face value (Rs.in crs.)	Scrip						
1.	25.4.1991	7.00	13% MTNL	Rahul & Co.	97.75	7.01	6.5.1991	98.35	7.08
2.	20.5.1991	0.70	Units-64	H.P. Dalal	14.5	1.02	23.5.1991	14.53	1.02
3.	1.8.1991	5.00	-do-	Rahul & Co.	13.3	6.65	14.8.1991	13.64	6.82
4.	1.10.1991	4.00	-do-	C.Mackertich	13.4	5.36	26.11.1991	13.94	5.58
5.	3.12.1991	10.00	12.5% Tata Chemicals NCD	H.P. Dalal	100.00	10.00	5.12.1991	100.124	10.01
6.	18.12.1991	2.00	Cancigo	Rahul & Co.	100.00	2.00	30.12.1991	102.8891	2.06
7	23.12.1991	3.75	Canstar	Rahul & Co.	110.00	4.125	8.5.1992	110.00	4.125
8.	29.1.1992	5.00	-do-	-do-	100.00	5.00	28.4.1992	104.2534	5.21
9.	18.2.1992	2.00	Candouble	Rahul & Co.	125.00	2.50	3.4.1992 }	127.60	1.276
							18.4.1992 }	128.60	1.286
10.	12.3.1992	13.00	Cancigo	Rahul & Co.	116.50	15.145	28.4.1992	119.423	15.52
11.	2.4.1992	20.00	Units-64	C.Mackertich	15.00	30.00	27.4.1992	15.19	30.38
12.	3.4.1992	31.0	9% IRFC 1.4	Rahul & Co.	95.00	29.45	2.6.1992	87.0	26.97
13.	9.4.1992	10.0	Units-64	C.Mackertich	15.15	15.15	27.4.1992	15.29	15.29
						133.41			

of Transactions' in the dealer's pad in Canfina indicates that the amount of Rs.8.99 crores was to be reversed after 15 days at a yield of 24 percent annum to Canfina. No such indication is available in respect of the balance amount. The reversal sale transaction in the above security was noted in the dealer's pad on 31 March 1992 i.e. 5 months and 23 days later.

(c) The manner in which this aggregate amount of Rs.17.29 crores was adjusted is indicated below.

(i) On 31 March 1992, M/s. V.B. Desai had tendered to Canara Bank, Bombay, 11 cheques for an ggregate amount of Rs.70.78 crores drawn in favour of Canara Bank by various banks. The adjustment of the amounts in the books of Canfina's registered office and the available information collected from the records of UCO Bank indicated that its Bombay (Hamam Street) branch has issued a cheque for Rs.24.90 crores in favour of Canara Bank (A/c. Canfina) by debiting M/s. V.B. Desai's current account as per the broker's letter to the bank on 31 March1992. For the purpose of issuing cheque in favour of Canara Bank, UCO Bank had funded the current account of M/s. V.B. Desai by discounting on 31 March 1992 five dheques for a total amount of Rs.25.00 crores deposited by the latter drawn in his favour by give HSM group companies on their accouts with Grindlays Bank, Bombay. Detailed comments on this have been given in the chapter on UCO Bank in this report.

(ii) Out of the amount of Rs.70.78 crores, Canfina had as per its record recovered the amounts of Rs.17.00 crores and Rs.12.00 crores lent to brokers Manubhai Maneklal and Shrenik Jhaveri under the cover of 14% NCDs (reference to which appears in chapter III paragraph 4.3 of the Committee's fourth Report) together with interest and adjusted the amount of Rs.17.29 crores lent on 10 October 1991 under "14% RIL" without any yield to the company. After adjustments in respect of certain other transactions, the balance amount of

Rs.6.073 crores was released to the broker Pallav Sheth on 2 April 1992. No interest on the amount of Rs.17.29 crores was received on 31 March 1992 and no documentary proof was made available by Canfina to show that the interest was recovered subsequently.

(iii) The reasons for remitting the balance amount of Rs.6,073 crores to Pallav Sheth remained unexplained although this amount was payable to CBMF as per the accounting entry passed in Canfina's records on 31 March 1992.

3.1 There were a few deals where Canfina had purchased and sold the same security at the same rates involving no loss or gain to it from the deals. These aappeared to be deals to accommodate brokers to the transactions. Canfina could not explain the need for taking such transactions on its record.

3.2 Canfina had lent its funds to broker N.K. Aggarwala & Co. (NKA) where it neither received the named security nor collected the BR from the named seller. For example, on 31 October 1992, Canfina had released on amount of Rs.5.86 crores purportedly to purchase 13% NTPC bonds of face value Rs.5.75 crores (as per transaction list) from "Naresh/Hongkong". The diary maintained in the New Delhi Office of Canfina indicated that money was lent to "Naresh/Hongkong". The amount of Rs.5.88 crores was received by Canfina on 6 November 1991 by debit to the broker's account with Hongkong Bank, New Delhi.

3.3 On 2 November 1991, Canfina sold 9% IRFC bonds of the face value of Rs.100 crores to BoA, through NKA. Canfina's cost memo indicated the rate as Rs.95 and it received an amount of Rs.95.789 croes from BoA Bombay. As per BoA's records, its purchase of the security was at Rs.91. As such Canfina paid back Rs.4 crores to BoA at New Delhi. In the normal course, Canfina should have recovered the amount of Rs.4 crores from the broker on the same day or the broker should have paid the money to BoA. To release Rs.4 crores to BoA, Canfina recorded a dummy purchase transaction of 9% NTPC bonds in its transaction list for Rs.4 crores (@Rs.100). In the dealer's dairy there is no description of security on 2 November 1991. As per diary maintained at New Delhi office of Canfina and dealers pad at Registered Office Canfina received back an amount of Rs.4.1863 crores on 17 December 1991 from NKA. The receipt of money on 17 December 1991 was gain covered by recording another dummy sale entry of 9% NTPC bonds of Rs.4 crores to the broker. It is evident that Canfina had funded the broker to the extent of Rs4 crores for one month and 15 days for which fictitious purchase and sale transactions were recorded in the books.

4. The method of maintaining records, dealer's pad and passing accounting entries in respect of adjustment of Canfina's funds under the purchase and sale transactions indicated that Canfina's security operations were essentially at the behest of brokers and Canfina did not look to the counterparty banks for execution of the deals.

XVI. Bank of Karad Ltd. (In liquidation)

A reference has been made in the third Report of the Committee (chapter VII) to the investment operations undertaken by Bank of Karad Ltd. (in liquidation) (BoK). On the basis of the scrutiny conducted subsequently, certain further irregularities have been observed in the investment transactions of the bank as also in those entered into by the bank on behalf of its broker-clients. Some of these are discussed in this Chapter.

2. Head Office transactions

2.1 The total turnover (sales and purchases) of securities transactions in bank's own Investment Account for the period April 1991 to May 1992 was Rs.334.72 crores (face value). The security deals were carried out by the bank mainly with its broker-clients, the main among them being Abhay D. Narottam (ADN), who accounted for 73.4 per cent of the bank's total turnover during the period. The scrutiny of security deals effected on bank's own Investment Account revealed certain irregularities, the more important of which are given below :

2.2 The rates at which deals were effected had no relevance with the prevailing market rates. There were certain deals in the same securities, with the same broker and on the same day, where the rates were heavily in favour of the bank and the difference in the buying and selling rates was very wide resulting in huge loss to the broker. The special favour shown by brokers to the bank was apparently because of the help extended in turn by the bank to the brokers in putting through their security deals disregarding the rules, systems and procedures. A few such instances are given below :

Date of transaction	Security	Particulars	Face value (Rs.in crores)	Rate
28.1.1992	9.5% GOI Loan 2008	Bought from Excel & Co.	2.90	84.09
28.1.1992	-do-	Sold to Excel & Co.	2.90	89.09
6.4.1992	11% Exim 2003	Bought from ADN	1.00	96.00
6.4.1992	-do-	Sold to ADN	1.00	98.28
6.4.1992	7.5% IFC 1997	Bought from ADN	0.75	94.00
6.4.1992	-do-	Sold to ADN	0.75	99.4556
6.4.1992	7.5% IDBI 1997	Bought from ADN	0.15	94.00
6.4.1992	-do-	Sold to ADN	0.15	101.28
6.4.1992	11.5% GOI Loan 2008	Bought from ADN	0.63	95.00
6.4.1992	-do-	Sold to ADN	0.63	98.0888

It may be observed from the table that the deals were simultaneous purchase and sale relating to the same broker, by which the payments made by the broker appear to have been brought into the books of the bank.

2.3 The bank purchased bonds, shares and debentures not qualifying for SLR purposes, from its broker clients viz., ADN and Excel & Co. and funded the brokers. The bank even borrowed funds in the call market for the purpose. However, the funds borrowed in the call market were not included in the bank's demand and time liabilities. Instead of showing these as its own borrowings, the funds were credited to the brokers' account directly.

2.4 The funds borrowed in the call market were also utilised for purchasing bonds which were resold subsequently. The bank incurred losses in such deals. The rationale behind such deals was not clear. A few such instances are given below:

(a) (i) The bank borrowed Rs.14.85 crores on 26 March 1991 and Rs.5.30 crores on 27 March 1991 @18.5% from Canbank Mutual Fund (CBMF) and utilised the funds for purchasing tax free 9% PSU bonds worth Rs.20.22 crores (face value Rs.19.00 crores) from CBMF on the same day, on its own Investment Account. The bonds were sold back to CBMF on 5 April 1991 and the sale proceeds were utilised to repay the funds borrowed and interest of Rs.8.92 lakhs accrued thereon. The securities transactions were not recorded in the HO Investment ledger maintained at the branch though advised to the HO for passing necessary responding entries. While the bonds did not qualify for SLR purposes, the call borrowings made for their purchase added to the bank's DTL on which it had to maintain CRR and SLR. Besides, the borrowing of funds in the call market was at a higher rate of interest than the coupon rate on the bonds. In a note placed before the Board on 21 September 1991, it was clarified that investment in these bonds was made under the impression that the bonds qualified for the purpose of SLR. The Board simply noted it and took no serious view of the lapse on the part of the official responsible for taking the decision which put the bank to a net loss of Rs.4.60 lakhs.

(ii) While the bank borrowed Rs.14.85 crores in the call market at 18.5 per cent on 26 March 1991, it had lent Rs.15.00 crores to UCO Bank on the same day at a lower rate of 18 per cent.

(iii) The bank was to receive interest of Rs.85.50 lakhs on the bonds for the half years ended 27/29 March, 1991 and 1 April 1991 from the concerned bond issuers. However, it is observed that the interest was received from ADN. An amount of Rs.22.50 lakhs was received from ADN vide his cheque dated 3 April 1991 drawn on his Savings Bank account and debited on 4 April 1991, Rs.31.50 lakhs was received by debit to his A/c.No.201 on 5 April 1991 and the balance Rs.31.50 lakhs was received through 17 warrants (mentioned as D/W i.e. dividend warrants in the bank's clearing register but, in fact, seemed to be interest warrants), of which 6 warrants for Rs.4.50 lakhs each were drawn on Bombay (Bandra-Kalanagar) branch of United Bank of India and the remaining 11(9 for Rs.45,000.00 each and 2 for Rs.22,500.00 each) on Bombay (Parel) branch of Punjab National Bank. Whether the relative bonds were in the possession of the broker and/or were standing in his name (so that he could claim interest on the bonds from the concerned PSUs) was not ascertainable.

(iv) The bank had, as per its records, received physical delivery of the bonds from CBMF at the time of their purchase in March 1991. As such, the bonds should have been delivered back to CBMF at the time of resale in April 1991. Instead, the bank issued its 5 BRs (3389 to 3393) to CBMF. Three of these BRs were received back from CBMF on 24 July 1991 and the other two on 28 September 1991. Enquiries with CBMF showed that the three BRs released on 24 July 1991 were returned by it to BoK against receipt of an RBI cheque for Rs.13.28 crores from BoK and the remaining two BRs were released on 28 September 1991 on receiving an RBI cheque for Rs.1.03 crores as the net amount of certain deals, from Andhra Bank. The cheque for Rs.13.28 crores was issued by BoK by debiting ADN's account. This leads to the inference that the bank had not actually received physical delivery of bonds.

(v) The investment of Rs.20.22 crores in PSU bonds and another amount of Rs.14.91 lakhs in equity shares of certain private sector companies on the same day i.e. 27 March 1991 by the bank contravened the RBI restriction on banks making such investments beyond the stipulated norm. The bank's total investments of Rs.19.54 crores (face value) far exceeded the permissible amount of Rs.15.00 lakhs for the year 1991-92.

(b) The bank raised call borrowings of Rs.30 crores from CBMF on 27 February 1991 and utilised the funds on the same day for purchasing 9% MTNL bonds of the face value of Rs.30 crores from Canfina at Rs.101 for Rs.31.59 crores. The bank received delivery of the bonds from Canfina and collected half-yearly interest of Rs.1.35 crores due thereon on interest due date i.e. 6 March 1991. On 7 March 1991, the bank sold the bonds to CBMF at Rs.98.35 for Rs.29.51 crores under its BR No.3155 which was received back duly discharged on 30 March 1991. The sale proceeds were utilised to repay the call borrowings together with interest of Rs.10.52 lakhs accrued thereon upto 6 March 1991. It is observed that the bank sustained a loss of Rs.82.99 lakhs in the above deals as shown below :

			(Rs.in lakhs)
Purchase price of bonds			3158.71
Less	:	Sale price of bonds	2951.24
	:	Loss on bond transactions	207.47
Add	:	Interest paid on call borrowings	10.52
			217.99
Less	:	Half-yearly interest received on bonds	135.00
		Net loss	82.99

Even considering that interest on these bonds was tax-free, the bank stood to lose a substantial amount on these deals. The rationale behind investing money borrowed at a higher rate of interest in these low-yielding bonds was not clear.

3. Brokers' Transactions

3.1 There was manipulation and falsification of records in BoK pertaining to its broker-clients' securities transactions. None of the books i.e. brokers' securities ledgers, Subsidiary General Ledger (Mirror) Account, BRs Issued and Received Register etc. gave a true and correct position of the transactions put through on behalf of the bank's broker-clients. No authentic record of transactions entered into on day-to-day basis furnishing information like names of broker-clients on whose behalf transactions were undertaken, nomenclature of securities purchased or sold, face value, names of counterparties, and total amount paid or received for the transactions was maintained so as to give a total picture of the transactions put through on any particular day. A large number of transactions were not recorded at all in the securities ledgers. Wherever the transactions were recorded, many of these were not recorded on the dates when the transactions were actually undertaken. Especially in cases where sales were effected without the brokers having any balance or sufficient balance of the securities sold, the posting of sales transactions in the brokers' securities ledgers was either not done or it was deferred until the brokers had arranged for suitable backing for the sale transactions. In several cases where transactions were recorded, the relative debit or credit entries were not available in the brokers' current accounts/overdraft accounts. Such transactions seemed to be either dummy deals or the brokers might have received the funds from the counterparties into their accounts maintained with some other banks or paid the amounts out of such accounts. There were also cases where brokers had sold as well as purchased various securities to and from the same counterparties on the same day and received or paid the net difference in the cost of sales and purchases. Details of securities involved in such transactions where netting was done were not recorded in the relative vouchers with the result the transactions to which the net amount pertained could not be identified. In the case of a few transactions between two brokers of the bank, while one leg of the transaction appeared in one broker's security ledger, the other leg of the transaction was not found recorded in the other broker's ledger.

3.2 In a number of cases BRs were not issued in chronological order. BRs shown in the securities ledger as having been received from counterparties were not entered in BRs Received Register in all the cases. Similarly, all the SGL transfer forms issued and received were not recorded in the SGL (Mirror) account maintained at the branch. As a result, the SGL (Mirror) account did not show correct balance. Whenever there was a difference with the SGL Account statement received from the RBI (PDO), the balance was changed to that as appearing in RBI's statement without making any effort to reconcile the balance and locate the difference.

3.3 (a) (i) On 13 April 1991, the bank purchased 9% IRFC bonds from Citibank and sold 9% PFC bonds to Citibank, both for the face value of Rs.20 crores on behalf of ADN. On 2 May 1991, the bank resold the 9% IRFC bonds to Citibank and simultaneously repurchased 1 crore Units of UTI sold on 27 April 1991 to that bank. The net difference of Rs.5.22 crores in the cost of two deals received from Citibank was credited to ADN's account.

(ii) The transaction dated 13 April 1991 relating to sale of 9% PFC bonds was reversed on 10 May 1991 by repurchasing the bonds. The funds required to reverse the transaction were raised by selling 9% IRFC bonds. Since ADN did not possess 9% IRFC bonds, the sale transaction was not recorded in his securities ledger.

(iii) The sale transaction dated 10 May 1991 referred to in (ii) above was reversed on 14 May 1991 through repurchase of 9% IRFC bonds. The funds amounting to Rs.20 crores paid to Citibank for reversing the transaction were raised by ADN by selling 9% IRFC bonds for Rs.20 crores (face value) to CBMF on the same day.

(iv) All the above transactions were effected by the counterparties under their BRs. BoK effected the sales without having any balance of 9% IRFC or 9% PFC bonds and Units of UTI in the broker's securities account. As per bank's record, the BR issued to CBMF was received back on 28 November 1991. CBMF, when contacted to ascertain whether it released the BR against delivery of bonds or receipt of funds, could not give any convincing reply. It only maintained that since its accounts were duly reconciled, the BR in question was no more outstanding.

(b) As per ADN's securities ledger, the bank purchased 11.5% GOI Loan 2010 of the face value aggregating Rs.99 crores (including Rs.69 crores from Stanchart) on 26 August 1991 and simultaneously sold the securities aggregating Rs.62 crores (Rs.50 crores + Rs.12 crores) to Stanchart on the same day and Rs.37 crores on 23 October 1991. However, it is observed that the posting of transactions in the broker's securities ledger was manipulated inasmuch as the purchase of securities for Rs.69 crores from Stanchart was actually made on 14 October 1991 while the sale of securities for Rs.50 crores to the said bank was effected on 14 June 1991. The sale to Stanchart was effected without the broker having any balance of the securities. As such, the posting of the sale transaction in the broker's security ledger was deferred while that of the purchase transaction was preponed to 26 August 1991 so as to show that sales matched purchases.

(c) Bhupendra Champaklal Devidas (BCD) purchased 11.5% GOI Loan 2010 of the face value Rs.15 crores from Excel & Co. and simultaneously sold it to

Bank of Madura on 30 November 1991. While Excel & Co.'s current account showed receipt of sale proceeds from BCD, its securities ledger did not show any such sale to BCD. BCD's sale to Bank of Madura was without any backing as there was no balance available in its securities account where the purchase of the security was not reflected.

(d) On 17 June 1991, the bank purchased from various parties and simultaneously sold to different parties 11.5% GOI Loan 2010 of the face value aggregating Rs.184.75 crores and Rs.182 crores respectively on behalf of Excel & Co. These transactions included purchase and sale of securities for Rs.30 crores each from and to Karur Vysya Bank. It was observed that the purchase from Karur Vysya Bank was made on 21 June 1991 but recorded in the broker's securities ledger on 17 June 1991 to represent that the sales were adequately covered by the available balance. As such, the broker's actual total purchases on 17 June 1991 excluding the purchase of Rs.30 crores from Karur Vysya Bank worked out to Rs.154.75 crores only as against its total sales of Rs.182 crores, thus resulting in an oversold position of Rs.27.25 crores for the broker. The oversold position was regularised on 1 July 1991.

(e) The bank sold 11.5% GOI Loan 2007 of the face value of Rs.10 crores to State Bank of Saurashtra on 13 July 1991 on behalf of Excel & Co. under its BR No.3410 without the broker having any balance of the securities with it. The posting of the sale transaction in the broker's securities ledger was deferred until 27 July 1991 when the broker purchased the securities for an equivalent amount from ADN without making payment therefor. Incidentally, ADN himself did not have the securities with him on 27 July 1991. In his case too, the bank resorted to manipulation in the posting of the transaction inasmuch as the securities repurchased from Punjab National Bank on 29 July 1991 were shown as purchased on 27 July 1991 in the broker's securities ledger.

(f) The bank purchased 11.5% GOI Loan 2010 of the aggregate face value Rs.22.50 crores on 19 October 1991 on behalf of Excel & Co. and simultaneously sold the securities of the total face value of Rs.33 crores on the same day resulting in an oversold position of Rs.10.50 crores for the broker. In order to show that the sales on 19 October 1991 were fully covered by the balance available, the purchases aggregating Rs.18 crores made on 2 November 1991 were recorded on 19 October 1991 in the broker's securities ledger.

(g) As per the securities ledger, Chandrakala & Co., a broker-client of the bank, purchased 11.5% GOI Loan 2010 of the face value aggregating Rs.33.35 crores from various parties including that for Rs.3.35 crores from BCD on 8 February 1992 and simultaneously sold the same to Bank of Madura. While the broker's securities ledger as well as current account showed the purchase from and relative payment to BCD on 8 February 1992, BCD's securities ledger showed the sale to the broker on 10 February 1992. BCD had purchased the securities from Bank of America (BoA) on 10 February 1992.

3.4 In several cases there was no evidence of movement of securities. Only BRs/SGL transfer forms issued at the time of sale were exchanged at the time of reversal of transactions through repurchase of underlying securities indicating that they were mere financing transactions in the garb of securities transactions. A few such instances are given below :

(a) The bank purchased 11.5% GOI Loan 2011 of the face value Rs.14.50 crores from Stanchart on 22 February 1992 on behalf of Excel & Co. and received back its own SGL transfer form from the counterparty bank as per remarks in the cost memo received from Stanchart. BoK's record did not show when this SGL transfer form was issued by it to Stanchart. It was observed that the broker also did not have the above security in the securities ledger.

(b) On 18 July 1991, the bank purchased 11.5% GOI Loan 2010 of the face value Rs.5.00 crores from State Bank of Mysore "free" on behalf of Excel & Co. and received back its own SGL transfer form from the counterparty bank. The particulars of the transaction in respect of which BoK issued this SGL transfer form was issued to the counterparty bank were not available.

(c) On 18 May 1991, BoK sold 11.5% GOI Loan 2010 of the face value of Rs.82.54 crores to Andhra Bank @97.75 for Rs.83.80 crores on behalf of ADN. The broker had no balance of the security as on the date of sale and as such the sale transaction was not recorded in ADN's securities ledger until 25 May 1991 by which date ADN had arranged for suitable cover through purchase of security of the same GOI Loan of the face value Rs.85.00 crores on various dates. Despite there being no balance of the security with the broker as on the date of sale, the bank issued two SGL transfer forms for Rs.40.00 crores and Rs.42.54 crores to Andhra Bank on 18 May 1991, of which the former was duly lodged with and honoured by RBI. The other SGL transfer form for Rs.42.54 crores was found filed in original in BoK's file with the words "return back" written thereon. BoK had purchased 11.5% GOI Loan 2010 of the face value of Rs.50.00 crores from Andhra Bank on 20 May 1991, against which Andhra Bank delivered back BoK's SGL for Rs.42.54 crores to it and issued its own SGL transfer form for the balance of Rs.7.46 crores.

3.5 There were a number of transactions which indicated the nexus between ADN and other brokers like Haresh K. Dalal, Excel & Co., BCD and Dhanraj Mills Pvt.Ltd. A few such instances are as below :

(a) On 4 May 1991, the bank sold 11.5% IDBI 2010 bonds of the face value Rs.8.00 crores to Indian Overseas Bank on behalf of Excel & Co. and issued BR No.3294. The sale proceeds received from Indian Overseas Bank were credited to Excel & Co.'s current account. The transaction was reversed on 18 May 1991 and the BR was received back duly discharged. The payment made towards repurchase of bonds was debited to ADN's account. Both the sale and purchase transactions were not recorded in the brokers' securities ledgers.

(b) The bank sold 11.5% IDBI 2010 bonds of the face value Rs.5.00 crores to Indian Overseas Bank @Rs.97.50 for Rs.4.92 crores on behalf of Excel & Co. on 1 June 1991 and repurchased the same @99.8583 for Rs.4.97 crores on 1 July 1991. The BR No.3353 issued at the time of sale was received back when the bonds were repurchased. While the sale proceeds received from Indian Overseas Bank were credited to Excel & Co.'s current account, the payment made towards repurchase of bonds was debited to ADN's account. The transactions were not recorded in the brokers' securities ledgers.

(c) (i) On 1 July 1991, the bank sold 11.5% GOI Loan 2009 of the face value Rs.15.00 crores to State Bank of Saurashtra on behalf of ADN under its BR No.3377 without having any balance of the security with the broker. The sale proceeds received from State Bank of Saurashtra were credited to ADN's account.

(ii) The transaction was reversed on 13 July 1991. Since ADN did not have sufficient funds to pay to State Bank of Saurashtra, the transaction dated 1 July 1991 was split into two, i.e. Rs.5.00 crores and Rs.10.00 crores. The bank repurchased the security of the face value Rs.5.00 crores by debit to ADN's account and issued a fresh BR No.3402 for Rs.10.00 crores treating it as a fresh sale to State Bank of Saurashtra.

(iii) When the sale transaction dated 13 July 1991 for Rs.10.00 crores (underlying BR No.3402) was squared up on 10 August 1991, ADN continued to be under financial strain. As such, Excel & Co. came to his rescue and facilitated reversal of the transaction which was again split into two i.e. Rs.2.00 crores and Rs.8.00 crores. The bank repurchased the security of the face value Rs.2.00 crores by debit to Excel & Co.'s current account and issued a fresh BR No.3441 in lieu of the balance of Rs.8.00 crores to State Bank of Saurashtra.

(iv) The transaction dated 10 August 1991 for Rs.8.00 crores (underlying BR No.3441) was squared up on 26 August 1991 through repurchase of the security by debit to Excel & Co.'s current account and the relative BR was received back.

(v) With a view to settle the accounts of the two brokers, on 26 August 1991 the bank received instructions from (i) ADN to purchase 11.5% GOI Loan 2009 security of the face value Rs.8.00 crores from Excel & Co. and (ii) Excel & Co. for selling the same loan for Rs.2.00 crores (face value) to ADN. The proceeds of both the transactions amounting to Rs.10.19 crores were transferred by the bank to Excel & Co.'s current account by debiting ADN's account.

(d) (i) On 1 July 1991, Excel & Co. desired to purchase 11.5% GOI Loan 2007 of the face value Rs.10.00 crores from BoK itself and sell the security simultaneously to Bank of Commerce and Credit International (BCCI). Since BoK did not have the security in question with it, the broker's purchase transaction was not put through. However, the bank effected the sale transaction despite there being no balance of the security with Excel & Co. and credited the sale proceeds amounting to Rs.10.22 crores received from BCCI to Excel & Co.'s current account. The bank issued its SGL transfer form to BCCI in respect of the above sale. Having been issued against non-existent security, the SGL transfer form bounced when lodged by BCCI with RBI on 3 July 1991.

(ii) The broker's sale transaction with BCCI was reversed on 19 July 1991 through repurchase of the security against payment of Rs.10.24 crores by debit to Excel & Co.'s current account, and the bounced SGL transfer form was received back. The funds required to be paid to BCCI were raised by Excel & Co. from Punjab National Bank (PNB) by selling to that bank the said security for Rs.10.25 crores against issue of BoK's BR No.3412. The transaction with PNB was reversed on 27 July 1991 and the BR No.3412 was received back. Since Excel & Co. did not have sufficient funds to pay to PNB and reverse the transaction, ADN came to its rescue and made the payment to PNB. ADN thereafter sold the security to Excel & Co. "free" on the same day by delivering to Excel & Co. BR No.3412 received by it from PNB.

(e) On 1 July 1991, the bank purchased 86 lakh Units from BoA @Rs.13.16240 for Rs.11.32 crores on behalf of BCD and on the same day sold the Units to Hongkong Bank for Rs.13.03 crores @Rs.15.15. The BR No.411 of Hongkong Bank stated to have been received on 7 June 1991 was returned to it. Both the debit and credit in BCD's account on account of the purchase and sale transactions were reversed on 8 July 1991 by transfer to Excel & Co.'s current account as these were reported to have been accounted for in BCD's account wrongly. In this connection, it is observed that :

(i) The bank had on its record delivery orders No.2795 and 3326 of BCD instructing it to purchase and sell the Units from/to the concerned banks. The delivery orders were unsigned as was the case with delivery orders received from BCD in some other transactions.

(ii) No delivery orders from Excel & Co. were held on bank's record in respect of the above transactions. Also, as per Excel & Co.'s securities ledger maintained by the bank, Excel & Co. had no investment in Units.

(iii) In case the transactions in question were really on Excel & Co.'s account, it would have objected to wrong accounting of the funds which deprived Excel & Co. of the use of Rs.170.93 lakhs (net of purchase and sale prices) for a week but there was nothing on record to suggest that Excel & Co. did so.

(iv) BCD's securities ledger showed that BoK had received a BR from BoA in respect of the purchase of Units. However, the bank's BRs Received Register did not show receipt of any such BR from BoA.

(v) The BRs Received Register of the bank did not show receipt of any BR from Hongkong Bank on 7 June 1991 nor was there any purchase of Units either by BCD or by Excel & Co. from Hongkong Bank on that date as per their securities ledgers.

(f) ADN instructed BoK on 1 June 1991 to issue a cheque favouring Citibank for Rs.304.95 lakhs with a memo to the said bank to adjust the amount towards difference on 11.5% Loan 2010 securities for Rs.107.00 crores - A/c.H.P. Dalal.

3.6 The bank effected a number of purchase and sale deals with BoA on behalf of its broker-client, BCD, in the same security, for the same face value and on the same day wherein BCD either incurred a huge loss or earned a marginal profit. In none of these deals actual delivery of securities took place. BoK purchased the bonds or securities from BoA which merely issued its BRs to the bank and the latter in turn delivered them back to BoA duly discharged on the same day when the transactions were squared up through sale by the bank. Thus, there was only exchange of BRs. Apparently these transactions were not genuine and were artificially structured to enable the broker to pay the difference in amounts to the counterparty banks and account the same in their books of accounts. The details of such transactions have been given in Chapter V of the third Report of the Committee.

3.7 In the case of ADN also transactions of the above type where the broker stood to lose heavily were observed. A few such transactions are given below :

(a) On 21 October 1991, BoK sold 9% IRFC bonds of the face value Rs.200.00 crores to Canfina @Rs.90.00 for Rs.180.99 crores on behalf of ADN vide BR No.3462 issued against BR No.015 obtained "free" by ADN from Metropolitan Co-operative Bank (MCB). MCB's BR had no backing and was procured mainly for the purpose of raising funds through BoK. BoK's BR issued on the strength of MCB's BR was, therefore, of no worth. The bonds were repurchased from Canfina on 8 January 1992 at Rs.92.32 and the bank's BR No.3462 was received back. ADN took "self" delivery of the above BR and MCB's BR No.015 was returned to him. The broker lost Rs.4.64 crores in the deals with Canfina.

(b) On 29 October 1991, the bank bought 9% IRFC bonds of the face value of Rs.25.00 crores from Citibank @Rs.97.25 on behalf of ADN and on the same day sold the bonds to Stanchart @RS.90.00 thus resulting in a loss of Rs.1.81 crores (approximately) to the broker.

(c) As mentioned in chapter IV [paragraph 5 (b)] of the third Report of the Committee, on 31 October 1991, the bank bought on behalf of ADN 9% IRFC bonds of the face value of Rs.350.00 crores from Citibank @Rs.101.00 for Rs.356.09 crores and on the same day sold the bonds of the face value Rs.150.00 crores each @Rs.90.00 and Rs.94.00 back to Citibank and Rs.50.00 crores to Stanchart @Rs.95.00 aggregating Rs.326.09 crores. The BR received from Citibank at the time of purchase of bonds was delivered back to Citibank at the time of resale thereof. Thus, the broker lost Rs.30.00 crores in the deals. Since the deals were undertaken on behalf of ADN, he incurred a total loss of Rs.36.45 crores in the above 3 purchase and sale deals.

4. (i) The securities ledger of Dhanraj Mills Pvt.Ltd. (DMPL) was not maintained properly inasmuch as instances were noticed where the broker's current account showed payments towards purchase of securities but the relative purchases were not recorded in the broker's securities ledger.

(ii) There was net transfer of huge funds from DMPL's account to some brokers on account of both securities and non-securities transactions. The more significant inflow and outflow of funds into and from the broker's account during the period April 1991 to May 1992 are shown below :

(Rs.in crores)

	Total		Net	
	Inflow	Outflow	Inflow	Outflow
ADN	0.10	9.89	-	9.79
Excel & Co.	8.98	13.30	-	4.32
Bhupen Champaklal Devidas	18.91	0.23	18.68	-
Kenilworth Investment Co. Pvt. Ltd.	0.39	18.71	-	18.32
State Bank of Hyderabad	0.50	5.92	-	5.42
Bank of India	20.02	0.10	19.92	-

5. Off the book transactions

The number of unrecorded (i.e.off the book) transactions entered into between April 1991 and May 1992 as per the statement prepared by the bank is 197 involving an aggregate amount of Rs.3724.60 crores (face value). Of these, 126 transactions (forming 64 per cent of the total transactions) for Rs.3133.64 crores (forming 84.1 per cent of the total amount) pertained to ADN alone. However, it is observed that this figure did not include all the unrecorded transactions and the volume of off the book transactions was very large. A few of these unrecorded transactions are given below :

(a) (i) The bank entered into the following sale and purchase transactions with Stanchart on 14 October 1991 on behalf of ADN.

A. Sale to Stanchart

(Rs.in crores)

Particulars of securities	**Face value**	**Rate**	**Amount**	**Mode of delivery of securities**
i) 11.5% IDBI 2011	50.00	99.75	50.62	BR No.3455
ii) 10% GOI Loan 2014	50.00	88.45	45.63	BR No.3456
			96.25	

B. Purchase from Stanchart

Particulars of securities	Face value	Rate	Amount	Mode of delivery of securities
i) 11.5% GOI Loan 2010	69.00	101.00	96.01	BR No.1365 for Rs.49.00 crores and BoK SGL transfer form for Rs.20 crores.
ii) 11.5% GOI Loan 2006	10.44	101.16		BoK's SGL dated 17.6.1991 for Rs.10.44 crores.
iii) 9.75% IFCI 1998	8.00	100.10		BR No.1362
iv) 9.75% IDBI 1998	5.00	100.10		BR No.1361

The net difference of Rs.23.68 lakhs received from Stanchart was credited to ADN's account.

(ii) None of the above transactions except sale of 10% GOI Loan 2014 was recorded in ADN's securities ledger. The bank did not have on its record ADN's delivery order regarding sale of 11.5% IDBI 2011 bonds nor any balance of the said bonds. The bank was yet to meet its liability to Stanchart under BR No. 3455 which was still outstanding. As regards 10% GOI Loan 2014 security it is observed from the transactions as recorded in the broker's securities ledger tht the security was bought "self" by ADN "free" on 14 October 1991. On the same day, the security was sold to Stanchart under the bak's BR No. 3456 and repurchased (again "free") on 7 February 1992.

(iii) The "free" repurchase of BR No.3456 on 7 February 1992 was incorrect. As mentioned in paragraph 5(1)(b) of chapter II of the fourth Report of the Committee. BoK sold Units of the face value of Rs.60 crores @ Rs.13.30 for Rs.79.80 crores to Stanchart on 4 January 1992 and simultaneously repurchased 10% GOI Loan 2014 of the face value Rs.50 crores for Rs.42.16 crores on the same day from Stanchart against receipt of its own BR No.3456 issued on 14 October 1991. The bank received Rs.37.64 crores from Stanchart towards net difference of the above deals which was credited to ADN's current account. Thus, it would be observed that the bank had falsified the broker's securities ledger by showing the security as having been repurchased on 7 February 1992 though the transaction was reversed on 4 January 1992. Incidentally, the transaction relating to sale of Units to Stanchart was not recorded in the broker's securities ledger.

(b) (i) On 14 October 1991, the bank sold 11.5% GOI Loan 2010 of the face value Rs.181 crores and 11.5% GOI Loan 2011 of the face value Rs.5.60 crores to Stanchart for an aggregate amount of Rs.185.49 crores and simultaneously purchased bonds of various PSUs aggregating Rs.189.44 crores (face value) from it for an aggregate amount of Rs.185.57 crores on behalf of ADN. The bank issued SGL transfer form in respect of its sale of 11.5% GOI Loan 2010 whereas the mode of delivery of 11.5% GOI Loan 2011 is not known as nothing in this regard is available either on Stanchart's record or BoK's record. The bank received 17 BRs (from

BR No.1366 to 1382) from Stanchart in respect of its purchases of PSU bonds which were returned consequent upon resale of the bonds to Stanchart on 15 October 1991 (underlying BR No.1381) and 16 October 1991 (other underlying 16 BRs).

(ii) The transactions were not recorded in the broker's securities ledger maintained by the bank. The sale of GOI securities by the bank was without any backing as ADN did not have any balance of these securities with him. Stanchart was reported to have received Rs.5,00,135.64 from BoK towards the net difference in the purchase and sale deals. However, BoK's record as well as ADN's account showed no such payment to Stanchart on 14 October 1991.

(c) (i) The bank sold bonds of various PSUs and Units of the aggregate face value Rs.136.50 crores to Stanchart on 31 March 1992 and the sale proceeds of Rs.132.61 crores received from the counterparty bank were credited to ADN's current account. ADN utilised the sale proceeds on the same day for purchasing shares and debentures of various companies (i.e. RIL - 6000 shares, Essar Gujarat - 9000 shares, 12.5% PCD of RIL, 15% Ballarpur Paper Industries - debentures worth Rs.63.17 crores, Zero Coupon Bonds SPIC - 96472, etc.) from Citibank. Both the sale and purchase transactions were not recorded in ADN's securities ledger. However, the bank had on its record Citibank's cost memos regarding the sale of above referred shares and debentures which were addressed to Hiten P. Dalal (HPD). Thus, it would be seen that although the shares and debentures in question were sold by Citibank to HPD, the payment therefor was made by BoK by debit to ADN's current account.

(ii) The bonds and Units sold on 31 March 1992 to Stanchart were repurchased by the bank on 3 April 1992 and the cost thereof amounting to Rs.132.72 crores was debited to ADN's current account. The particulars of bonds and Units repurchased and the mode of delivery thereof are given below :

Particulars of bonds/Units	Face value (Rs. in crores)	Mode of delivery
i) 9% HUDCO bonds	50.00	Delivered physically
ii) 13% NPCL bonds	45.00	BR No.2136
iii) 13% CIL bonds	23:50	BR No.2137
iv) Units of UTI 1.8 crores	18.00	BR No.2135

(iii) The bonds and Units underlying the above referred three BRs were again sold to Stanchart on 28 April 1992 along with 9% HUDCO bonds of the face value Rs.25 crores. However, ADN did not receive the sale proceeds from Stanchart as these were adjusted by Stanchart towards HPD's dues to it, as mentioned in paragraph 8.11 (b) of chapter II of the fourth Report of the Committee.

(iv) The shares and debentures purchased from Citibank on 31 March 1992 were resold on 3 April 1992 and sale proceeds aggregating Rs.131.41 crores received from Citibank were credited to ADN's account.

The transactions dated 3 April 1992, too, were not recorded in ADN's securities ledger.

(d) The bank sold 11.5% GOI Loan 2011 of the face value Rs.60 crores to Stanchart @Rs.96 for Rs.58.74 crores and simultaneously purchased 9% MTNL bonds of the face value Rs.34 crores and 9% HUDCO bonds of the face value Rs.15 crores at Rs.92.05 for an aggregate amount of Rs.45.61 crores from Stanchart on 24 October 1991 on ADN's behalf. The net difference of Rs.13.13 crores received from Stanchart was credited to ADN's account. Both the above sale and purchase transactions were not recorded in ADN's securities ledger nor were his delivery orders directing the bank to sell and purchase the securities and bonds in question held on bank's record. The mode of delivery of the securities and bonds also was not available either at Stanchart or BoK. While the cost memos received from Stanchart were held, the bank's own cost memo, if any, sent to Stanchart was not available. A small piece of paper with no signatures or initials thereon and containing insufficient information regarding the transactions was found filed in the bank's file.

(e) (i) The bank sold 11.5% GOI Loan 2011 of the face value Rs.59 crores @95.73 for Rs.57.62 crores and simultaneously purchased 4 crore Units at Rs.13.50 for Rs.54 crores from Stanchart on 25 October 1991 on ADN's account. Thus, BoK was to receive the balance amount of Rs.361.57 lakhs from Stanchart. However, a rough work-sheet available on the bank's record showed an amount of Rs.272.32 lakhs as having been adjusted against that amount leaving a balance of Rs.89.25 lakhs which was duly received by the bank from Stanchart vide bankers cheque dated 28 October 1991 and credited to ADN's account on 30 October 1991 clubbed with another amount of Rs.65.33 lakhs received from Stanchart vide banker's cheque dated 29 October on account of transactions dated 28 October 1991 referred to at item (f) below. The amount of Rs.272.32 lakhs represented the amount receivable by Stanchart from HPD on account of certain deals which Stanchart had effected with BoA through HPD. Stanchart adjusted this amount against Rs.361.57 lakh payable to ADN reportedly as per instructions of HPD/ADN.

(ii) The above transactions were not recorded in ADN's securities ledger nor were his delivery orders available on bank's record. However, the cost memo in respect of sale of Units by Stanchart to BoK was available in the file.

(f) (i) The bank put through the undernoted purchase and sale transactions with Stanchart on 19 and 28 October 1991 on behalf of ADN.

Purchase from Stanchart

(Rs.in crores)

Date of transaction	Particulars of securities/bonds	Face Value	Rate (Rs.)	Amount	Net difference Received	Net difference Paid	Banker's cheque No. and date
19.10.1991	11.5% GOI Loan 2007	74.00}	101.40	262.08	-	-	-
	-do-	90.00}					
	-do-	90.00}					
28.10.1991	9% - 13% PSU bonds and Units	143.63	-	189.95	-	-	-

Sale to Stanchart

Date of transaction	Particulars of securities/bonds	Face Value	Rate (Rs.)	Amount	Net difference Received	Net difference Paid	Banker's cheque No. and date
19.10.1991	11.5% GOI Loan 2010	114.00	N.A. }	263.22	1.14	-	226379
	11.5% GOI Loan 2007	140.00 }	96.72 }				19.10.1991
	-do-	15.00 }	}				
28.10.1991	12% GOI Loan 2011	100.00	100.00 }	190.61	0.65	-	226538
	11.5% GOI Loan 2011	92.00	96.30 }				29.10.199

N.A. - Not available

(ii) The difference in the sale and purchase prices received from Stanchart was credited to ADN's account on 28 October and 30 October 1991 respectively. The transactions were not recorded in ADN's securities ledger.

(iii) The record at Stanchart showed that Stanchart had issued SGLtransfer forms to BOK in respect of its sale on 19 October 1991. BoK, out of its sale of 11.5% GOI Loan 2007 security of the face value Rs.155.00 crores. repurchased securities of the face value Rs.131.50 crores and Rs.9.50 crores from Stanchart on 11 and 10 December 1991 respectively without giving delivery leaving a balance of Rs.14.00 crores (face value), the transaction value being Rs.13.54 crores. This transaction is appearing paragraph 3.3 (h) (ii) of chapter 11 of the fourth Report.

(g) The bank sold 11.5% GOI Loan 2010 of the face value Rs.58.00 crores at Rs.100.98 to Grindlays Bank on 18 April 1991 on ADN's account under its BR No.3270. The sale proceeds amounting to Rs.60.34 crores were credited to ADN's account. On the same day, the bank purchased 13% SCICI bonds of the face value Rs.38.00 crores @ Rs.100.3360 for Rs.38.36 crores and 13% MTNL bonds of the face value Rs.20.00 crores at Rs.99.2550 for Rs.20.27 crores from Grindlays Bank and debited the cost thereof to ADN's account. Grindlays Bank delivered SCICI bonds and a BR in respect of MTNL bonds to the bank. The MTNL bonds were resold to Grindlays Bank in two instalments of Rs.10.00 crores (face value) each on 26 April and 2 May 1991 respectively against delivery of the relative BR back to Grindlays Bank. While the bond transactions were duly recorded in ADN's security ledger, the transaction relating to sale of GOI securities was not recorded therein, perhaps because ADN had no balance of the security in his account and as such the sale and the BR issued by BoK were without any backing. Although, ADN's delivery order dated 18 April 1991 did not mention so, the sale of 11.5% GOI Loan 2010 security to Grindlays Bank seemed to be on ready forward basis as the security was repurchased by the bank on 7 June 1991 against payment of Rs.61.27 crores to the said bank by debit to ADN's account and BR No. 3270 issued on 18 April 1991 was received back.

6. **Bank's total exposure**

In all 43 BRs and seven SGL transfer forms for an aggregate amount of Rs.930.84 crores issued by BoK are outstanding as on date, out of which nine BRs and four SGL transfer forms for amounts aggregating Rs.852.09 crores issued on behalf of ADN had no backing whatsoever, whereas the remaining 34 BRs and three SGL transfer forms totalling Rs.78.75 crores were backed by BRs of other banks and financial institutions or the securities lying with the bank/in its SGL account maintained with the PDO. The counterparty-wise break-up of BRs/SGL transfer forms having no backing is as below:

(Rs.in crores)

Counterparty	No.of BRs/SGL transfer forms	Amount
Stanchart	7	354.70
Canfina	3	374.35
Canbank Mutual Fund	2	103.83
Allahabad Bank	1	19.21
Total	13	852.09

XVII. Hongkong and Shanghai Banking Corporation Ltd.

A. New Delhi branch

1. Hongkong and Shanghai Banking Corporation Ltd. (Hongkong Bank) formulated a scheme called "Client Investment Scheme" (CIS) in April 1991 confined only to its New Delhi branch. The bank could not make available a copy of the scheme as the relative document is stated to be not traceable either at the Corporate Office at Bombay or at the New Delhi branch. The broad features of the scheme, as stated by the bank were as under:

(a) On the specific instructions of clients, funds placed by them would be utilised for investments in Units, PSU bonds and Central Government securities.

(b) The purchase and sale values of these securities were to be determined through the market, if necessary, through brokers.

(c) Securities (BRs, physicals) would be obtained for all purchases and kept in safe custody.

(d) The purchases and sales of securities were on clients' account and at their risk; and

(e) The dealing officer would confirm the deals to the clients in writing.

2.1 During the period April 1991 to May 1992, the New Delhi branch of the bank entered into 216 purchase transactions for a total contract value of Rs.2286.94 crores and 200 sale transactions valued at Rs.2103.10 crores. Of the 216 purchase transactions, 200 were on ready forward basis and the remaining 16 on spot basis where the bank delivered securities to the clients. The dealer collected management fee at his discretion as no instructions were issued by the bank in this regard. During the above period a sum of Rs.2.01 crores was earned by Hongkong Bank as management fee.

2.2 The bank relied heavily on broker Naresh K. Aggarwala & Co. (NKA) for effecting the transactions under the scheme as could be seen from the broker-wise distribution of business during the period from 1 April 1991 to 31 May 1992 given below :

Sr. No	Broker	No.of transactions	% of total transactions	Contract value (sale + purchase) (Rs. in crores)	% of total business
1.	N.K. Aggarwala & Co. (NKA)	298	71.6	3517.78	80.1
2.	Prasad & Co.	68	16.4	630.72	14.4
3.	Batliwala & Karani	18	4.3	70.86	1.6
4.	Hemdev	17	4.1	84.56	1.9
5.	B.D. Aggarwal	13	3.1	80.52	1.8
6.	Others	2	0.5	5.60	0.2
		416	100.0	4390.04	100.0

3.1 The clients listed under the scheme were some of the PSUs like Gas Authority of India, Power Finance Corporation, KRIBHCO, IFFCO, Container Corporation of India, National Film Development Corporation, Maruti Udyog Ltd., some private sector organisations and individuals. A few banks and bank subsidiaries, viz., Grindlays, Stanchart, PNB Mutual Fund, PNB Caps, Canfina and SBI Caps have also been listed as clients in the list. However, on enquiry, these banks have stated that they had entered into purchase/sale transactions with Hongkong Bank and were not clients of the bank under the scheme.

3.2 Though the New Delhi branch of the bank handled a substantial volume of funds with turnover of about Rs. 4,400 crores, no proper records were maintained, nor was there a system of reporting/monitoring transactions put through by the dealer, either at the New Delhi branch or at the Corporate Office of the bank in Bombay. The deal slips were not prepared, cost memos were not issued/delivered to counterparties for its sales. Such documents were only occasionally received from counterparties for the bank's purchases on behalf of its clients. No register for BRs was maintained to show movement of BRs received, issued or exchanged. No investment register was maintained to show receipt of client's funds, the corresponding sale/purchase of securities and earnings therefrom. The dealer was required to give written confirmation of purchases made on behalf of clients by way of letters addressed to them. Copies of such letters were not available on record in several cases. The bank's Investment Strategist in his note on the investigation carried out after the outbreak of information about widespread irregularities in securities transactions commented that "the records available are inadequate to carry out a full investigation at this stage"

3.3 Under CIS, the bank was required to perform "agency" function of buying and selling securities on behalf of its clients in a non-discretionary manner as per the latter's instructions. In actual practice, the dealer indicated the security to be purchased and the rate and the client confirmed the transaction. The rate quoted did not have any relevance to the market value. Similarly, the rate quoted to the client at the time of reversal of the transaction was also at off market rate. This rate was arrived at by adding the interest element to the purchase rate. The interest element was determined by call money market rates during the period. In effect, the scheme was more in the nature of a lending operation.

4. A scrutiny of the limited available records relating to the scheme at the branch revealed the following features/irregularities.

4.1 The essence of the CIS revolved around the broker(s) arranging funds of public/private/co-operative sectors and some individuals for lending under the cover of security transactions. The only role played by Hongkong Bank was to lend its name and provide documentary support, wherever necessary. For example, where banks or financial subsidiaries appear as "clients", a Hongkong Bank's BR was demanded by the bank's client and hence issued. For such services rendered, the bank did not collect any fee or service charges at fixed rate from the clients but appropriated as fee/commission certain amounts by way of difference in the rate of sale on reversal and the actual rate at which reversal was done. There is no definite pattern in the amount appropriated by the bank in the different deals.

4.2 In certain cases Hongkong Bank did not obtain BR for its purchases. In some cases the funds appear to have been lent on "clean" basis as the availability of securities was not ensured. For example, Hongkong Bank purchased on 13 May 1991 from StanChart, New Delhi, 9% HUDCO bonds of face value Rs.5 crores for a consideration of Rs.5.08 crores. The bank did not obtain any BR from Stanchart. The deal was reversed on 12 June 1991 with Canbank Mutual Fund (CBMF) on receipt of Rs.5.18 crores although the deal was with Stanchart.

4.3 The bank has also acted as a routing bank for the clients' transactions of Stanchart, New Delhi. Under this, the clients placed funds with Stanchart, New Delhi under its Corporate Cash Deployment Services scheme (CCDS) for purchase of securities. Stanchart, New Delhi purchased the securities from Hongkong Bank, New Delhi which showed Stanchart as its client under CIS. As per the records available, Hongkong Bank, New Delhi was shown as having purchased securities from Stanchart, Bombay for which it received BRs issued by Stanchart, New Delhi on behalf of Stanchart, Bombay. On the basis of these BRs, Hongkong Bank in turn issued BRs to Stanchart, New Delhi. The Hongkong Bank, New Delhi received bankers cheques from Stanchart, New Delhi for the amount of the securities purchased and in turn issued its own pay orders for the same amount in favour of Stanchart, New Delhi. In a statement given by Stanchart, New Delhi, listing the transactions of sale of securities by Stanchart, Bombay to Hongkong Bank, New Delhi, the bank has remarked against the transactions as under :

"No broker note. Name of broker not mentioned in Deal Slip. (However, broker would have been Hiten Dalal)".

5. Transactions with Naresh K. Aggarwala & Co. (NKA)

5.1 The bank has acted as a routing bank for broker NKA. There were several instances where pay orders issued by different banks favouring Hongkong Bank were credited to NKA's current account maintained at Hongkong Bank, New Delhi branch, although there was no accompanying memo or letter from the issuing bank for the credit of the proceeds of the pay order to NKA's account. However, no claim have arisen on Hongkong Bank as a result of such credits. Similarly, debits were raised in the said current account at the instance of the bank's Merchant Banking Division (MBD) and pay orders were issued favouring other banks. The bank was unable to produce any letter/cheque issued by the account holder NKA authorising such debits. Such routing enabled the broker to have his account credited to the extent of differences arising from selling and buying rates of two other banks he would have brought together in a deal. For instance, an amount of Rs.27.30 crores received from Grindlays on 13 January 1991 was credited to NKA's account and thereafter a payment order for Rs.26.90 crores issued favouring Canara Bank. The broker hence netted Rs.0.40 crore. In fact a perusal of the operation of the account gives an impression that it was operated by the bank's MBD rather than the account holder. A few examples are given below :

(a) On 13 January 1992, a pay order issued by Grindlays, Delhi for Rs.27.30 crores was credited by Hongkong Bank to NKA's account without any advice from the issuing bank. The books of Grindlays, Delhi showed that the payment was for purchase of Units of face value Rs.20 crores @13.65 from Hongkong Bank through NKA. Grindlays, Delhi branch could not produce any document to support the transaction. The transaction did not appear in the books of Hongkong Bank, New Delhi. Hongkong Bank did not issue any cost memo or BR in this regard. The said deal was reversed on 5 May 1992 in the books of Grindlays on receipt of pay order issued by Hongkong Bank by debiting NKA's account. No satisfactory explanation was forthcoming from the bank for making the debit to the broker's account in the absence of any letter/cheque from the account holder.

(b) On 20 February 1992, a banker's cheque issued by Canara Bank for Rs.84.90 crores favouring Hongkong Bank was credited to NKA's account without receiving any advice. On the same day, a pay order favouring Citibank was issued for Rs.84.30 crores leaving Rs.0.60 crore in the account. In the books of Citibank, three deals appear for the value of Rs.84.30 crores wherein Hongkong Bank is shown as counterparty bank. These deals are not however reflected in Hongkong Bank's records.

(c) On 4 November 1991 a pay order issued by Canara Bank for Rs.8.64 crores favouring Hongkong Bank was credited into NKA's account without any advice from the issuing bank. A scrutiny of the records of CBMF revealed that it had issued its BR No.2231 on 13 June 1991 for its sale of 13% NTPC bonds of the face value of Rs.13.50 crores to Hongkong Bank. This BR, as per the records of CBMF, was liquidated in parts. On 24 September 1991 CBMF purchased the said bonds of value Rs.5.75 crores and reduced the value of the BR No.2231. The remaining bonds of face value Rs.7.75 crores were purchased on 4 November 1991 for a consideration of Rs.7.99 crores as per the records of CBMF. There was hence a remittance of excess funds by CBMF. Thus, Hongkong Bank refunded a sum of Rs.0.65 crore on 4 November 1991 through a pay order issued by debit to NKA's account. However, as per Hongkong Bank's records instead of liquidation in two stages (as shown in the CBMF records), it had shown reversal in three stages i.e. on 24 September 1991 of the face value Rs.5.75 crores, on 1 October 1991 of the face value Rs.5.75 crores, and finally on 4 November 1991 of the remaining face value Rs.2 crores. The records of Hongkong Bank do not corroborate receipt of Rs. 8.64 crores by it on 4 November 1991. Enquiries at Hongkong Bank regarding this variation revealed that the client i.e. IFFCO on whose behalf the asset was held, had to be paid. Therefore, the existing asset was allotted to a new client i.e. Grindlays by showing a sale of the asset on 1 October 1991. Further, the repayment to Grindlays due on 31 October 1991 was arranged by NKA from Canfina, New Delhi through a ready forward deal for 6 days wherein Hongkong Bank was shown as counterparty though this transaction did not figure in the books of Hongkong Bank. This deal was reversed in Canfina's books after receipt of a pay order issued by Hongkong Bank by debit to NKA's account. Thus the pay order received for the reversal of a transaction between Hongkong Bank and CBMF got credited into broker's account.

5.2 The bank also funded the broker NKA by way of crediting the differences between the rates at which the securities were actually bought from the selling bank and the rates quoted to the client for whom it was purchasing the said securities. Hence, knowingly, Hongkong Bank subverted the role envisaged of the broker, i.e. of merely bringing the selling and buying bank together. Such differences in rates paid to NKA were not by way of brokerage as the bank has certified that it did not pay any brokerage in any of the transactions. This enabled the broker to use such funds at will. Some instances of crediting differences to NKA's account are given below :

(i) On 7 April 1992, Hongkong Bank purchased on behalf of client Grindlays 9% IRFC bonds of face value Rs.33 crores for Rs.30 crores from Stanchart. As per records of Stanchart, the contract value was Rs.29.75 crores and Hongkong Bank paid accordingly. The excess of Rs.0.25 crore received from Grindlays was credited to NKA's account.

(ii) On 5 February 1992 Hongkong Bank purchased on behalf of two of its clients 9% IRFC bonds of face value Rs.8 crores @94 for Rs.7.52 crores from BoA. The BR received from BoA stated that it had received Rs.7.35 crores for the said deal. The difference of Rs.0.17 crores was credited to NKA's account.

5.3 It was also observed that the bank funded NKA by occasionally wrongly crediting the account with huge sums. Some instances of wrong credits and their reversals are given below :

(Rs.in lakhs)

Date	**Wrong credit**	**Date of rectification**
20.2.1992	200.00	25.2.1992
31.3.1992	4.56	6.4.1992 and 2.5.1992
7.4.1992	25.12	22.4.1992
22.4.1992	4.72	25.4.1992
22.4.1992	18.40	5.6.1992

The bank has thus extended "clean" interest free funds to NKA for periods ranging from 5 to 45 days.

5.4 Hongkong Bank funded NKA by showing the broker as counterparty and credited the broker's account with the value of securities purchased on behalf of its clients. The bank did not receive any securities or BRs from the broker in these cases. At other times, though a bank is shown as counterparty, payments were made to or received from the broker's current accounts maintained with other banks. In these cases, too Hongkong Bank did not receive the securities or BRs and cost memos from the selling banks. Some instances are given below:

(a) On 29 August 1991, Hongkong Bank purchased on behalf of KRIBHCO and IFFCO 13% CIL bonds of face value Rs.4.25 crores from CBMF. The bank had shown in its statement that it received BR No.2100 from CBMF. This was incorrect as BR No.2100 for Rs.18.5 crores face value was received by Hongkong Bank on 26 April 1991 and discharged on 27 May 1991. The deal on 29 August 1991 does not figure in CBMF's books. The deal was reversed on 27 November 1991 and 30 December 1991 by sale of the securities to CBMF and NKA for Rs.2 crores and Rs.2.25 crores respectively. The payment for the sale of face value Rs.2.25 crores 13% CIL bonds on 30 December 1991 came from NKA's current account.

(b) On 18 November 1991, Hongkong Bank purchased for IFFCO from CBMF 13% CIL bonds of face value Rs.13.5 crores and 13% NPC bonds of face value Rs.7 crores for a total consideration of Rs.19.12 crores which was passed on to CBMF and received CBMF's BR Nos.2491 and 2741 respectively. These bonds were sold to Stanchart on 18 December 1991 by discharging both the BRs received from CBMF and handing these over to Stanchart. However, Hongkong Bank has shown in its transaction statement that it had a purchase on 17 December 1991 from CBMF of 13% CIL bonds of face value Rs.13.5 crores (for client PFC) and 13% NPC bonds of face value Rs.9 crores against CBMF BR Nos.2741 and 2491 which were already in the possession of Hongkong Bank and discharged by it on 18 December 1991. Thus, there were two purchases shown in Hongkong Bank's books against the same set of BRs. The reversals of the 17 December 1991 purchases were made on 16 March 1992 by selling 13% CIL bonds face value Rs.13.5 crores and 13% NPC bonds of face value Rs.2 crores to NKA. The balance security of 13% NPC bonds of face value Rs.7 crores was sold to Stanchart on 20 March 1992. The combined contract value for these reversals was Rs.23.22 crores. The mode of delivery of the securities in both the cases is not ascertainable from the Hongkong Bank records.

(c) On 28 September 1991 the bank received a sum of Rs.13.50 crores from its clients PNB Caps and Maruti Udyog Ltd. The bank, as per its records, invested this amount in Units of UTI of face value of Rs.10 crores purchased from BoA through the broker NKA @13.50 for a consideration of Rs.13.50 crores. The bank issued a pay order for the said amount favouring BoA. The bank received neither a BR nor physicals from the counterparty bank (BoA). There was no broker's note available on the records for this transaction.

The pay order in question was credited into the current account of the broker NKA maintained with BoA, New Delhi. The enquiry at BoA revealed that there was no such transaction with Hongkong Bank and it could not produce any advice from Hongkong Bank for crediting the amount into the account of the concerned broker.

In the books of Hongkong Bank, the transaction was reversed in parts. On 28 October 1991 the bank showed a sale of Units of face value of Rs.6 crores @13.75 for a consideration of Rs.8.25 crores to ABN Amro Bank. The enquiry with ABN Amro Bank revealed that it had no such transaction with Hongkong Bank and it had issued a pay order for Rs.8.25 crores favouring Hongkong Bank by debit to the current account of the broker (NKA) maintained with it.

The remaining Units of Face value of Rs.4 crores, as per the records of the bank were sold on 27 December 1991 to Canfina @13.65 for a consideration of Rs.5.46 crores. Though the bank received a pay order issued by Canara Bank, the said deal did not figure in the books of Canfina.

(d) On 10 April 1992, Hongkong Bank purchased on behalf of its clients three assets, namely 13% CIL bonds of face value Rs.13.5 crores, 9% HUDCO bonds of face value Rs.5 crores and Cantriple Units of face value Rs.10 crores for an aggregate sum of Rs.29.12 crores. The asset 13% CIL bonds was reportedly purchased from CBMF and a receipt of CBMF BR No.2491 dated 18 November 1991 was shown against this purchase. For the other two purchases bank had indicated receipt of physical securities without mentioning the counterparty. In all these transactions NKA was the broker. On the same day a credit of Rs.29.12 crores was afforded in the current account of NKA by the bank. Further the scrutiny of the records of CBMF revealed that there was no such transaction with Hongkong Bank on the said date. The BR in question was issued in some other deal on 18 November 1991 and stood discharged on 18 December 1991. All the said transactions were reversed on 11 May 1992 by Hongkong Bank after receipt of a pay order issued by Canara Bank for a sum of Rs.30.10 crores and a cheque from NKA for Rs.0.15 crore. These transactions, in effect, were nothing but "clean" lending to the broker under the cover of sale and purchase of securities.

6. Disputed transactions

6.1 As on 1 June 1992, the bank had the undernoted disputed deals :

(a) On 3 September 1991, the bank purchased for its client KRIBHCO 13% DVC bonds of face value Rs.3 crores from CBMF through broker NKA for a consideration of Rs.2.27 crores. The bank received CBMF's BR No.2714 dated 3 September 1991 in this regard. On 30 December 1991, the BR was stated to have been discharged by Hongkong Bank and given to broker NKA for onward transmission to CBMF for a swap with another asset of the same face value and amount. According to CBMF, on 20 November 1991, it had purchased 13% DVC bonds of face value Rs.25 crores from ABFSL through Hiten P. Dalal (HPD). ABFSL had lodged bonds of face value Rs.22 crores and for the balance Rs.3 crores it had returned to CBMF its own BR No.2714. The return to CBMF of its BR No.2714 by ABFSL could have been only after 30 December 1991, since Hongkong Bank as per its records had parted with the BR to NKA only on that date. The matter is under dispute.

(b) On 11 December 1991, Hongkong Bank purchased 13% NPTC bonds from Stanchart of face value Rs.10 crores against its BR No.1646. According to Hongkong Bank the BR was discharged and returned to Stanchart through NKA for an asset swap in the last week of December 1991 as the interest payment was falling due on 1 January 1992. The purchase of the bonds on 11 December 1991 did not however figure in the statement of deals submitted by Hongkong Bank although it had passed on the consideration amount to Stanchart on that date. On the other hand, liability on account of a part of the BR (face value Rs.8 crores) was reversed by Stanchart on 24 April 1992 by remitting a sum of Rs.7.88 crores and the balance bonds of the face value Rs.2 crores with a transaction value of Rs.1.68 crores are under dispute.

6.2 On 5 May 1991, Hongkong Bank purchased from Canfina, Canstock units for Rs.1.66 crores against its BR No.116. Canfina confirmed the BR but has refused to honour the same till its dispute for 13% CIL bonds is settled (paragraph 12.21, Chapter III of the fourth Report).

6.3 Besides, Hongkong Bank was also involved in disputes with Stanchart/Canfina with regard to the undernoted deals.

Bonds	Face Value (Rs. in crores)	Reported in fourth Report at
i) 9% IRFC	27.5	para 7(d), chapter II
ii) 13% NPC	16.5	para 3.3 (d), chapter II
iii) 13% CIL	13.5	para 3.3 (g), chapter II
iv) 9% PFC/NLC	5.0	para 3.1 (f), chapter II
v) 13% CIL	18.0	para 12.21 (b), chapter III

6.4 The bank stopped accepting funds under the CIS on 27 May 1992. It has subsequently reversed the outstanding transactions and paid the investor clients the purchase consideration including the unrecorded assured rate of return and taken bonds of the face value of Rs.160 crores in its own investment account. These bonds are carried in its books at Rs.149.31 crores. The bank will have to reckon with the depreciation in the value of the bonds.

7. Conclusion

As indicated earlier, immediately after the irregularities in the securities transactions surfaced, the bank's Corporate Office conducted an investigation into operations of the CIS. The investigation appeared to have been confined to outstanding commitments and resolution thereof. As seen from a copy of the note dated 18 May 1992 submitted to the bank's Chief Executive Officer, the following points emerged :

(a) In general it would appear that the dealer had exceeded his authority and has not acted strictly in terms of the guidelines.

(b) In some of the cases, payments for the purchase of the securities although required to be made to the counterparty banks, had been made to the broker. In such cases, the broker had given letters to the effect that the securities had been sold by him to the bank and would be delivered as soon as they were ready for delivery.

(c) BRs were not always received by the bank on the same day as the payment date. In a few cases BRs were released to brokers/banks for asset swaps, repayment, etc., in advance without obtaining any acknowledgement for the same.

(d) The bank was used as routing bank in some of the transactions.

The report pointed out that records available were inadequate to carry out further investigation at this stage (in May 1992). Thus, while the bank had noticed serious irregularities in the operations of the scheme, it did not seem to have felt the need for carrying out a detailed scrutiny.

B. Corporate Office, Bombay

8. Hongkong Bank had investments in Government securities, other trustee securities, non-trustee securities and Units of UTI aggregating Rs.616.84 crores at book value as on 31 March 1992. The turnover in its investment account between 1 April 1991 and 29 May 1992 amounted to Rs.16,852.49 crores. About 51 per cent of the business totalling Rs.8601.36 crores was routed through two brokers viz. HPD and NKA.

9. Investment Account

A scrutiny of the deals transacted by the bank revealed that -

(a) the bank issued BRs and accepted BRs of other banks while trading in GOI securities for which SGL facility is available.

(b) the bank often settled the bounced SGL deals by netting between three or more banks affected by such bounced SGL transfer forms. For example, Hongkong Bank purchased on 30 November 1991 Rs.20 crores (face value) 12% GOI Loan 2011 from American Express Bank and received its SGL transfer form. On the same day, Hongkong Bank sold Rs.25 crores (face value) of the same security to State Bank of Saurashtra (SBS) which lodged Hongkong Bank's SGL transfer form at PDO a few days later. The same bounced as Hongkong Bank had not lodged American Express Bank's SGL transfer form with the PDO. The transaction was then settled between the three banks by payment for Rs.5 crores of the above security by Hongkong Bank to SBS and for Rs.20 crores by American Express Bank to SBS.

(c) the BRs issued were not on security paper.

(d) the BRs issued as well as BRs received were kept pending for periods exceeding 90 days.

(e) the bank entered into several buyback deals in PSU bonds and Units with banks as well as financial institutions.

10. Portfolio Management Scheme

The Portfolio Management Scheme (PMS) formulated by the bank envisaged, besides approved instruments, investment in trade bills and retention of the money in cash with the bank in times of tight money market which was not in accordance with RBI guidelines. The bank assured returns to the clients though no written assurances of returns were given. As on 30 May 1992 the bank had 26 PMS accounts, the clients being drawn from private corporate sector, trusts and individuals and the total of PMS funds placed by the 14 clients aggregated Rs.14.69 crores.

10.1 On a scrutiny of records it was noticed that on 16 August 1991, Hongkong Bank sold Rs.3.45 crores (face value) 9% NTPC bonds @100.44 to PMS clients from its Investment Account. The entry was subsequently reversed on 19 August 1991 at the same rate. Again on 15 May 1992 the bank sold to PMS clients Rs.4 crores (face value) Government Treasury Bills @100 and bought them back at the same rate on 18 May 1992. The bank thus utilised funds of PMS clients for 3 days without passing on the benefit of either the accrued interest at coupon rates or the discount to them. It was also observed that the bank in some cases invested funds received from PMS clients after a gap of 10-15 days as detailed below :

(Rs.in lakhs)

Client	Amount received	Date on which received	Date of first investment
1.Milkfood Ltd.	250.00	25.6.1991	11.7.1991
2.American Church	30.00	26.6.1991	11.7.1991
3.Jasmer Singh	10.50	26.11.1991	10.12.1991

The sales to the clients were invariably made from the holdings of the bank and securities so purchased for PMS clients were not segregated, as only book entries were made. Reversals or purchases were made by the bank from the PMS clients at rates often contrived to give certain yields to the PMS clients. For example, on 20 April 1992, the bank sold 13% NPC bonds @93 and purchased it from them @94.64. The same bonds were purchased by the bank on the same date at varying rates from its clients viz. at 93, 94.64, 94.80 and 95.11.

XVIII. Citibank

1.1 Reference was made in the third Report of the Committee issued in August 1992 to the securities transactions of Citibank on behalf of its PMS clients. A further scrutiny of the transactions has been made and the findings are recorded in subsequent paragraphs.

1.2 During the period from 1 April 1991 to 23 May 1992, an aggregate of 21,682 transactions was entered into on behalf of PMS clients for an aggregate value of Rs.2,13,983 crores. As at 31 March 1992, the total funds held on behalf of PMS clients and the investment of those funds were as follows :

(Rs.in crores)

Nature of investment	Amount invested	Percentage
Equity shares *	257.87	19.97
PSU bonds	188.01	14.56
Units	476.67	36.91
Others	353.64	27.38
Uninvested	15.30	1.18
	1291.49	100.00

* The bank had been holding equity to the extent of 90 per cent and over in the case of certain PMS customers such as Air India, Pawan Hans Ltd., Tourism Finance Corporation of India Ltd., Varahagiri Investment & Finance (P) Ltd., Manali Investment Finance (P) Ltd., Sakthi Sugars Ltd., H.M.M. Ltd., Smithkline Beecham, Thiru Arooram Sugars, etc.

1.3 (a) According to Citibank, IDBI held in IDBI A/c.No.2 and IDBI A/c.No.5 with Citibank as on 18 September 1991 and 24 December 1991 Rs.30.8095 crores and Rs.15.9222 crores respectively under PMS. The funds for these accounts were provided out of the sale proceeds of Units of the face value Rs.21.50 crores and Rs.11.15 crores respectively, purchased by Citibank from IDBI. However, as per IDBI records there was no sale but the Units were just deposited by IDBI with Citibank.

(b) From a note provided by Citibank to IDBI it appears that notwithstanding the documentation, the real substance of the transaction was that IDBI converted its investment in PSU bonds into Units and these Units were "loaned" to Citibank for an indicated return of one per cent per annum.

(c) (i) Under this scheme, between 15 April 1991 and 24 July 1992, Citibank received under PMS accounts in the aggregate Units numbering 29.933 crores from IDBI, GRASIM, Hindalco, HDFC, ITI, TELCO, Smithkline Beecham and Coromandel Fertilisers Ltd. with total principal inflows at Rs.411.21 crores.

(ii) On receipt of the Units, Citibank recorded a purchase of the Units at the ruling rate and credited the proceeds to PMS account opened in the customers' names. Simultaneously, out of the balance in the PMS account the Units were re-purchased for the customer. In effect, therefore, the Units which were held by the customer in his own investment portfolio were now held by him as an investment of his PMS account.

(iii) Citibank used the Units in the PMS accounts to make a series of transactions on ready forward basis whereby funds were generated and profits booked ensuring that at the termination of the arrangement, the PMS account was invested in Units.

(iv) At all times, the Units remained registered in the customers' names and the dividend was directly collected by the customer.

(d) The transactions in the accounts have been so arranged as to ensure that the return to the customer was marginally in excess of one per cent.

1.4 Bombay Stock Exchange (BSE) had placed with Citibank an aggregate amount of Rs.12 crores under PMS. These funds were finally withdrawn as to Rs.7 crores on 6 May 1992 and Rs.5 crores on 7 August 1992. The withdrawal on 7 August 1992 was effected by Citibank liquidating the assets by transferring the same to the account of another PMS client. However, the rates at which this transfer was made were not in conformity with ruling market rates as shown below :

Security	No.of shares	Sale Rate (Rs.)	Market Rate (Rs.)	Difference (Rs.)
Clutch Auto	10,600	25.00	32.50 - 35.00	79,500.00
DCL Polyester	3,500	39.50	41.00 - 43.75	5,250.00
Great Eastern	60,000	115.00	132.50 - 138.75	10,50,000.00
India Glycol	7,700	94.30	112.50 - 117.50	1,40,140.00
Prestige H.M. Poly.	14,000	25.00	29.00 - 35.00	56,000.00
				13,30,890.00

1.5 There are a number of cases where the PMS accounts were overdrawn. A few instances are given below:

Date	PMS client	Amount overdrawn (Rs. in lakhs)
(1)	(2)	(3)
30.8.1991	Bombay Stock Exchange	70.95
5.5.1992	Grasim Ltd. A/c. No.1*	2131.02
	Grasim Ltd. A/c. No.2*	2135.49
	Grasim Ltd. A/c. No.3	2415.72
	Grasim Ltd. A/c. No.4*	1484.67
		8166.90
2.7.1992	Grasim Ltd. A/c. No.4	486.20
16.7.1992	-do-	541.63
20.7.1992	-do-	821.64
21.7.1992	-do-	923.27

* The above accounts were overdrawn almost continuously during June 1992. In case of A/c. No.1, the overdrafts were over Rs.2,000 lakhs from 22 June to 29 June 1992, while in case of A/c. No.2, during the same period, overdrafts were over Rs.8,150 lakhs. A/c. No.4 was overdrawn to a maximum extent of Rs.1,692.60 lakhs as on 26 June 1992.

1.6 Grasim Ltd. maintained 4 PMS accounts. As shown above, the accounts were overdrawn on 5 May 1992 for an aggregate amount of Rs.81.67 crores. This overdrawing arose because of large transactions in Units aggregating to Rs.1847 crores. Moreover, the rates at which the transactions were made in the different accounts also showed significant variances as indicated below:

Account No.	Sale Rate (Rs.)	Purchase Rate (Rs.)	Profit/(Loss) for the day (Rs. in crores)
1.	14.45875 to 14.9200	15.0875 to 15.5525	(21.33)
2.	15.1500 to 15.5400	14.68822 to 14.9150	7.75
3.	14.9050 to 15.85375	14.4513 to 15.0825	16.25
		Net	2.67

It is obvious that these transactions were put through to ensure that the returns in three accounts approximated to the indicated rate of return.

1.7 On 5 May 1992, Citibank sold to Stanchart an aggregate of 23 crore Units through broker Hiten P. Dalal (HPD). According to the cost memo the sale was at Rs.15.018 per Unit. Out of the total sale of 23 crore Units, sale of 13.5 crore Units was on account of PMS clients and the sale of the balance 9.5 crore Units was on its own investment account. However, the transactions in respect of the PMS clients were booked @Rs.14.9497 per Unit whereas the transaction in respect of its own investment account was booked @Rs.15.115 per Unit. The details are given below :

On account of	No.of Units (In lakhs)	Rate recorded (Rs.)	Sale rate (Rs.)	Difference (Rs.in lakhs)
Grasim Ltd.A/c.No.2	500	14.9497	15.018	(34.150)
Grasim Ltd.A/c.No.3	550	14.9497	15.018	(37.565)
IDBI	100	14.9497	15.018	(6.830)
ICICI	100	14.9497	15.018	(6.830)
Hindalco	100	14.9497	15.018	(6.830)
Citibank's Investment Account	950	15.1150	15.018	92.205

Citibank has, therefore, taken credit for Rs.92.205 lakhs at the cost of their PMS clients.

1.8 Citibank had two PMS accounts in the names of Indian Sugar and General Industry Export Import Corporation Ltd. (ISGIEC) and Indian Sugar Mills Association (ISMA) in which it had accepted an aggregate amount of Rs.10.74 crores. The entire funds available in these accounts were invested on 20 August 1992 in BOI Mutual Fund units which had been bought @Rs.177.30 per unit from another PMS client. The 'bench mark' returns indicated to the client were 18.50 per cent but on expiry of the 'lock-in' period Citibank was unable to return to the clients the amount invested together with the bench mark return. It, therefore, delivered to the clients, 4,45,000 units of BOI Mutual Fund at a rate of Rs.195 per unit and the balance in cash. These transactions have been challenged by the clients, particularly the purchase of units @Rs.177.30 which is alleged to be an arbitrarily fixed rate in the absence of a quotation on that date. Earlier, on 26 June 1992 the bank had purchased from an external counterparty viz. Mansoon Trading Co. 9% IRFC bonds of face value Rs.1.00 crore @Rs.100/- as against the then prevailing market rate of Rs.80 - 85 and sold the same on 30 June 1992 @Rs.86/- thereby creating losses in the account.

1.9 (a) In the Committee's third Report reference has been made (in paragraph 7 of chapter IV) to certain transactions in GIC Rise I and Rise II units whereby Citibank sold the units to brokers, Stewart & Co. and C.Mackertich who in turn resold the units to Canfina and made profits as shown below :

(Rs.in crores)

Date	Broker	Unit	Face Value	Profit
8.4.1992	Stewart & Co.	GIC Rise II	25.00	14.00
11.4.1992	Stewart & Co.	GIC Rise I	28.55	17:38
8.4.1992	C.Mackertich	GIC Rise II	25.00	14.00
11.4.1992	C.Mackertich	GIC Rise I	28.55	17.38
20.4.1992	C.Mackertich	GIC Rise II	25.00	23.50
				86.26

(b) Further scrutiny has shown that on 5 June 1992, Citibank purchased from C.Mackertich on behalf of Grasim Ltd., GIC Rise I units of the face value Rs.7.10 crores @Rs.25 per unit. The debit of the relative purchase considerations of Rs.17.75 crores resulted in an overdraft in the account of the client. On 19 June 1992, the bank sold the same units to an external party @Rs.10.68 per unit. Therefore, a loss of Rs.10.17 crores accrued to the account of the PMS client. The broker, C.Mackertich used the sale proceeds of Rs.17.75 crores covering the sale of GIC Rise I units for making payment to Allahabad Bank in respect of a BR issued by BoK (in liquidation). Further investigations also revealed that the bank had undertaken transactions in GIC Rise II as per particulars furnished below :

Date/Type of transaction	Fiduciary customer	Counterparty	Rate (Rs.)	Proceeds (Rs.in crores)
GIC Rise II Units				
10.6.1992 Sale F.V.Rs.17.50 crs.	Grasim Ltd. A/c.No.2	Allahabad Bank	24.00	42.00
30.7.1992 Sale F.V.Rs.4.50 crs.	IDBI A/c.	Dummy counterparty	11.00	4.95
4.8.1992 Sale F.V.Rs.1.00 crore	-do-	-do-	11.00	1.10
8.8.1992 Sale F.V.Rs.1.50 crs.	Grasim Ltd. A/c.No.4	-do-	11.00	1.65
11.9.1992 Sale F.V.Rs.0.50 crore	-do-	-do-	11.00	0.55

From the above it is clear that the transactions had been put through at varying rates thereby causing losses to fiduciary clients.

1.10 (a) On 13 April 1992, Citibank purchased from broker HPD, Cantriple units of face value Rs.15 crores @Rs.50 per unit. However, there are a number of transactions around this date where the rates have varied between Rs.10 and Rs.26 per unit. Thus, the broker HPD derived undue benefit at the cost of the concerned fiduciary client.

(b) In settlement of various deals the bank has received substantial sums aggregating Rs.20.46 crores by way of differences from the broker HPD.

2. Citibank has entered into several sale and purchase transactions with PSUs on behalf of its PMS clients. The transactions have been mainly in Units and PSU bonds. In several cases, in respect of these transactions BRs were issued but no physical delivery was effected and the BRs were returned on reversal of the transactions.

3.1 There are a number of transactions between Citibank and Andhra Bank. It has been established that Andhra Bank was a 'routing' bank for broker HPD. A large number of such transactions were one day transactions, that is, they were purchase and sale transactions in the same security of the same face value on the same day but with difference in the purchase and sale rates. Between 10 July 1991 and 6 April 1992, there were 29 such transactions for an aggregate purchase value of Rs.1888.06 crores and an aggregate sale value of Rs.1892.18 crores yielding to Citibank a profit of Rs.4.12 crores. One such transaction may be noted. On 6 April 1992, 11.5% GOI Loan 2010 of face value Rs.120 crores was purchased at Rs.90 and sold at Rs.92 yielding a profit of Rs.2.4 crores. In the books of Andhra Bank, the sale proceeds and purchase consideration were credited and debited to the account of HPD.

3.2 In several cases, the cost memo received from Andhra Bank clearly mentioned that the transactions were on account of broker HPD. However, even with this knowledge, Citibank recorded these transactions as the counterparty being Andhra Bank and not HPD.

3.3 A substantial portion of bank's business with Andhra Bank was in the form of ready forward transactions which were nothing but lending or borrowing operations of the bank to or from HPD. The bank had entered into some forward sale and purchase contracts with Andhra Bank as counterparty through the broker HPD and these contracts were settled by the bank either by issuing BRs against inadequate current holdings or by exchanging SGL transfer forms, which generally bounced, with Andhra Bank or with Stanchart by changing the counterparty bank; however, these forward contracts were not recorded in Andhra Bank's books.

3.4 The bank had entered into ready forward transactions in Units with its PMS customers which had been routed through another intermediary bank for a fee. A few such instances are given below :

Name of intermediary	**Face Value of Units (Rs.in crores)**	**First leg**		**Second leg**	
		Bought from PMS client on	**Sold to Citibank on**	**Bought from Citibank on**	**Sold back to PMS client on**
1. Andhra Bank	50.00	24.3.1992 @14.6075 for Rs.73.04 crs.	24.3.1992 @14.6085 for Rs.73.04 crs.	30.3.1992 @14.66 for Rs.73.30 crs.	30.3.1992 @14.66 for Rs.73.30 crs.
2. Bank of India	150.00	8.11.1991 @13.46 for Rs.201.90 crs.	8.11.1991 @13.47 for Rs.202.05 crs.	12.11.1991 @13.4975 for Rs.202.46 crs.	12.11.1991 @13.5075 for Rs.202.61 crs.

In case of item no. (1) above, PMS customer paid Rs.26.25 lakhs over a period of 6 days to Citibank on Rs. 73.04 crores equivalent to 21.65 per cent per annum through Andhra Bank.

In case of item No. (2) above, PMS customer paid Rs. 71.25 lakhs over a period of 4 days to Citibank on Rs. 201.90 crores equivalent to 32.09 per cent per annum through Bank of India, which was paid a fee of Rs.30 lakhs by Citibank.

The above ready forward transactions with PMS customers through an intermediary bank are really ready forward transactions with non-bank counterparties and consequently are in contravention of the RBI guidelines.

3.5 As on 30 June 1992 the bank has purchased from fiduciary clients 13% taxable bonds and 9% tax-free bonds of the aggregate face value of Rs.321.83 crores @ Rs.2 below the corresponding market rates furnished by a broker resulting in a loss of Rs.6.44 crores to fiduciary clients.

4.1 On 17 March 1992, there was a hike in the coupon rate of Government securities resulting in a significant fall in the market value of securities.

4.2 Citibank had entered into several contracts with brokers for sale and purchase of 11.5% GOI Loan 2010 for delivery on 21 March 1992. The aggregate face value of purchase contracts was Rs.125 crores and of sale contracts was Rs.260 crores. There were inadequate balances in the investment account for this security and therefore, Citibank had an oversold position of about Rs.135 crores.

4.3 Except for a sale contract of Rs.25 crores, the forward contracts were not appearing in Citibank's records of forward contracts. After the coupon hike Citibank covered its short position at the reduced market rates and made a profit of over Rs.3.18 crores.

4.4 (a) Citibank bought on cash basis from Stanchart, SGL transfer forms covering 11.5% GOI Loan 2010 of the face value Rs.240.00 crores @Rs.96.00 (rate recorded in Stanchart's books as Rs.98.00) on 30 November 1991 through the broker HPD and entered into a forward sale contract on the same day with Andhra Bank through the same broker for delivery on 2 December 1991 @Rs.94.72. SGL transfer form received by Citibank from Stanchart was lodged by it with PDO, RBI on 30 November 1991, which bounced due to inadequate balance of Stanchart at PDO; however, date of bouncing of this SGL transfer form could not be ascertained from Citibank's records as the bank is not maintaining proper records of objection memos received from RBI.

(b) On 2 December 1991 (i.e. delivery date) Citibank sold to Andhra Bank this security @Rs.96.07 instead of at the contract rate of Rs.94.72; however, no approval was obtained from higher authorities for change of rates. Citibank issued its SGL transfer form to Andhra Bank which was lodged by the latter bank with PDO on 2 December 1991 and which bounced due to inadequate balance of Citibank at PDO. Citibank earned profit of Rs.27.16 lakhs [Rs.230,41,83,628.00 (sale proceeds) - Rs.230,14,67,503.56 (purchase cost)] in these deals.

(c) A scrutiny of Andhra Bank books revealed that the bank had sold this security on the same day (i.e. 2 December 1991) to Stanchart on behalf of the broker HPD and issued its SGL transfer form No.1587 bearing initials HPD. This SGL transfer form in the lower portion does not contain signatures of the authorised signatories of Stanchart as a buyer and that of the witness and it was endorsed on the back by the Manager, to that bank; however, the same was not lodged with PDO by Stanchart. Proceeds received from Stanchart by Andhra Bank and paid to Citibank on 2 December 1991 were credited and debited respectively to HPD's current account maintained at Andhra Bank.

(d) Finally, bounced SGL transfer forms of Stanchart and Citibank and SGL transfer form of Andhra Bank (not lodged with PDO) were exchanged by these banks among themselves on 31 December 1991.

(e) A scrutiny of Stanchart books reveals that it has sold on 30 November 1991 11.5% GOI Loan 2010 of face value Rs.10.00 crores to Citibank (in the account of one of the fiduciary clients) @Rs.98.00; Citibank recorded the contract rate at Rs.96.00 mentioning the name of the broker as HPD. Thus Citibank purchased from Stanchart in all 11.5% GOI Loan 2010 of face value Rs.250.00 crores and gave bankers cheques amounting to Rs.250,15,95,112.81 (Rs.240,15,31,308.70 + Rs.10,00,63,804.11) both dated 30 November 1991 to Stanchart. Stanchart has not received, either from HPD or any other broker or institution, the sum of Rs.5.00 crores represented by the rate difference of Rs.2/- (98-96) although Stanchart has prepared a debit voucher dated 30 November 1991 debiting ITD Interbank P.O. received from Citibank. Thus although Stanchart has booked a profit of Rs.46.16 lakhs ultimately it resulted in an effective loss of Rs.4.54 crores.

5 The following overdue forward contracts covering SLR securities are outstanding in the books of the Citibank.

Sr. No.	Date/Deal No.	Security/Type of transaction/ face value (Rs.)	Counterparty/ broker (Rs.)	Delivery date as per contract	Remarks
1.	31.3.1992 515	12% U.P. Loan 2011 Purchase Rs.19.00 crores	Allahabad Bank Stewart & Co.	22.4.1992	Rate @Rs.97.50 contract note not available.
2.	31.3.1992 516	12% GOI Loan 2011 Purchase Rs.10.00 crores	-do-	-do-	Rate @Rs.100.00 contract note not available.
3.	31.3.1992 517	11.5% UP Loan 2010 Purchase Rs.12.00 crores	-do-	-do-	Rate @Rs.96.00

In all the above cases, the bank does not hold confirmations from the counterparty.

6.1 There are a large number of ready forward transactions, other than in SLR securities in violation of RBI guidelines. Some examples are given in subsequent paragraphs.

(i) On 12 February 1992, Citibank entered into a fourteen month buyback arrangement with SBI apital Markets Ltd. covering PSU bonds of face value Rs.59.50 crores with asset change facility.

(ii) On 16 October 1991, Citibank entered into ready forward contracts with Stanchart for PSU bonds, SCICI bonds and HUDCO bonds for an aggregate value of Rs.199.44 crores through the broker HPD. These were only 60 day loaning arrangements with an interest rate of 16.5 per cent loaded into the contracts.

(iii) On 29 May 1991, Citibank entered into ready forward contracts with Canbank Mutual Fund for PSU bonds of an aggregate face value Rs.111 crores through broker HPD. These were 2 day loaning arrangements with an interest rate of 40 per cent built into the contracts.

(iv) On 27 March 1992, Citibank entered into a ready forward contract with Bombay Stock Exchange in PSU bonds and Non Convertible Debentures, for an aggregate value of Rs.76.10 crores. These were 68 day borrowing arrangements with an interest rate of 28 per cent built into the contracts.

7. Shri A. Ghosh, Deputy Governor, RBI's letter dated 26 July 1991 to the Chairman/Chief Executives of banks specifically stated that "under no circumstances, the bank should hold an oversold position in any security". Citibank has violated this directive on a number of occasions by maintaining oversold positions for substantial amounts for varying periods upto a maximum of over five months in Central and State Government securities and guaranteed bonds by resorting to roll-overs. In the bank's investment account it had been undertaking ready forward deals in Units even though they are prohibited by RBI.

8. Citibank entered into a number of forward contracts in respect of its PMS clients. These contracts were recorded in a PC (data-base) operated by the traders and were not entered in the main frame computer system. Thus the knowledge of these contracts was confined to the treasury group comprising the treasury head, local currency head, treasury in-charge and the traders. Consequently, the back-up and operations departments remained unaware of these contracts nor were the same subjected to audit. Thus, as per the print-out furnished by the then local currency head, forward commitments aggregating Rs.14,757.72crores booked during 1990-91

and till 29 June 1992 on the PC (data-base) were not brought into the main frame computer system. Information regarding these unsettled contracts and certain particulars regarding the inhouse transactions are not given to fiduciary clients, thereby impairing transparency.

On account of impairment/erosion of the corpus and/or returns, the bank entered into deeds of settlement with various PMS clients and in the process the bank has suffered a loss of Rs.105.95 crores, which is being accounted for in the bank's balance sheet for the year ended 31 March 1993. Identification and crystallisation of losses for the next financial years is in progress. Thus the bank has mismanaged the fiduciary customers' accounts.

XIX. Andhra Bank

1. Reference has been made in the Third Report of the Committee (Chapter VI) to the investment operations etc. undertaken by the Bombay (Fort) branch of Andhra Bank. On the basis of a scrutiny conducted subsequently, certain further irregularities/features have been observed in the investment transactions of the bank as also in those put through by the branch on behalf of broker clients. Some of these are discussed in this chapter.

2. Transactions in securities on Head Office Investment Account

2.1 As already reported a verification of securities at the branch had revealed that the branch was not holding 11.5% NHB bonds 2009 (2nd series) for Rs.200 lakhs. The branch has since been advised by NHB that two bonds of Rs.100 lakhs each issued by it and remaining with it have been seized by the CBI alongwith some other records and are in CBI custody.

2.2 During the course of verification of the stock of cheque books on 9 November 1992 by the bank's internal inspectors, 10 bundles of shares of various companies standing in the names of Harshad S. Mehta group concerns were found in the cupboard meant for Current Accounts Department. These shares were not accounted for in the books of the branch. CBI has seized the shares. As per the inventory, the total face value of these shares amounted to Rs.62.72 lakhs; the market value thereof as on 9 November 1992 worked out to Rs.1611.30 lakhs.

2.3 In a number of cases, the rates at which the transactions have been actually put through by the branch were different from the rates contracted for by its Head Office and advised to the branch. The difference was either credited or debited to the brokers' accounts. However, in the Head Office account, the transactions were reflected at the rates contracted by them. In the daily statements of security transactions sent to Head Office by the branch, generally contracted rates have been advised and not the rates at which the purchases/sales have been actually effected. Some instances where the difference in rates were noticed are given below :

(Amounts in rupees)

Date of transaction	Security	Face Value (Rs.in crores)	Contracted rate	Actual rate	Difference credited/ debited to broker's a/c.	Name of the broker
Purchases						
07.09.1991	11.5% GOI Loan 2010	5	99.8696	98.9675	4,51,050.00 (Cr.)	Puran & Purnima
18.12.1991	-do-	16.98	98.35	96.85	25,46,850.00 (Cr.)	H.P.Dalal (HPD)
20.11.1991	-do-	5	99.56	97.00	12,80,000.00 (Cr.)	V.B.Desai
06.12.1991	10.5% COI Loan 2014	15.70	92.40	94.00	25,12,000.00 (Dr.)	-do-
22.02.1992	11.5% GOI Loan 2010	25	97.25	96.50	18,75,000.00 (Cr.)	G.N. Hegde

Date of transaction	Security	Face Value (Rs.in crores)	Contracted rate	Actual rate	Difference credited/ debited to broker's a/c.	Name of the broker
Sales						
20.11.1991	11% IFCI 2001 (45th series)	4	99.61	97.20)	12,05,000.00 (Dr.)	V.B. Desai
-do-	11% IFCI 2001 (44th Series)	1	99.61	97.20)		
06.12.1991	9.75% IFCI 1998	15.70	97.70	94.00	58,09,000.00 (Dr.)	-do-
11.12.1991	11.5% GOI Loan 2008	15	100.21	99.53	10,20,000.00 (Dr.)	Mukesh Babu
18.12.1991	10.2% GOI Loan 1993	16.98	100.55	99.05*	25,46,850.00 (Dr.)	HPD
08.02.1992	11.5% GOI Loan 2010	8	98.25	95.1406	24,87,520.00 (Dr.)	V.B. Desai
18.04.1992	182 days Treasury Bills	10.00	96.355	96.3708	15,800.00 (Cr.)	Mukesh Babu

* Cost memo was issued @ the rate of 100.55 (settlement amount - Rs.17,63,00,595.66) whereas banker's cheque received from the counterparty, viz. ANZ Grindlays Bank, was for Rs.17,37,53,745.67 i.e.@ the rate of 99.05, which was the rate indicated by the broker in the delivery order to Andhra Bank. In Grindlays record, there is no contract/delivery note from its broker HPD and the contracted rate of 99.05 was agreed over telephone between itself and the broker.

3. **Transactions on account of broker-clients**

3.1 As mentioned in the Third Report, Andhra Bank issued SGL transfer forms for its sales against SGL transfer forms received from other banks for its purchase, on account of broker-clients transactions in Government securities. However, where sales and purchases have been effected with the same banks on the same day, it issued SGL transer forms for its sales and received back the same SGL transfer forms for its purchases. This amounted to creating an oversold position at the time of sale although it was squared on the same day. These transactions have resulted in gain to the counterparty banks. In the clients' holding register, the entries for the purchase transactons have been shown before those of sales. These transactions have not been reflected in the PDO books. Instances are given below:

(a) On 20 April 1991, Andhra Bank sold to Bank of America 11.5% GOI Loan 2010 of face value Rs.35 crores on account of HPD @ 101.02 by issuing its SGL transfer form No.1081; it bought back the same security of face value Rs.25 crores @ 101.17 and of face value Rs.10 crores @ 101.12 and received back its SGL transfer form from Bank of America. In this transaction Bank of America made a profit of Rs.4.75 lakhs.

(b) On 22 April 1991, Andhra Bank sold to Canfina 11.5% GOI Loan 2009 of face value Rs.10 crores on account of HDP @ 101.25 by issuing split SGL transfer forms Nos.1103 (Rs.7.21 crores) and 1104 (Rs2.79 crores); it bought back the same security of face value Rs.10 crores @ 101.50 from Canfina, against which the SGL transfer forms issued by it were received back from Canfina. The profit to Canfina in this transaction was Rs.2.50 lakhs.

(c) On 18 April 1992, Andhra Bank sold to ANZ Grindlays Bank 11.5% GOI Loan 2010 of face value Rs.40 crores on account of Batliwala & Karani @ 90.50 by issuing its SGL transfer form No.0100 and bought back the same security of face value Rs.20 crores @ 90.60 and the balance Rs.10 crores @ 91.012. The bank received back the same SGL transfer form issued by it from ANZ Grindlays Bank. The profit to ANZ Grindlays Bank in this transaction was Rs.12.24 lakhs.

(d) Apparently, these "structured" transactions were undertaken at the instance of the broker for settling his dues to the counterparty banks.

3.2 On 18 April 1992, Andhra Bank purchased 11.5% GOI Loan 2010 of aggregate face value Rs.130 crores from various banks on account of B.C. Devidas and sold the same to difference banks on the same day. Out of Rs.130 crores, securities of face value Rs.75 crores were purchased from Stanchart for which Andhra Bank received a BR instead of SGL transfer form. However, while selling the lot, Andhra Bank issued its SGL transfer forms against the BR. The BR was substituted by SGL transfer form by Stanchart only on 21 April 1992. The said SGL transfer form from Stanchart bounced 3 times on 22 April 1992, 2 May 1992 and 9 May 1992 and finally Andhra Bank got credit only on 15 May 1992. During the interregnum, the bank had taken a positionon behalf of the broker.

3.3 A series of transactions in 11.5% GOI Loan 2006 of face value Rs.20 crores by Andhra Bank and others without actual backing of security were reported inthe Committee's fourth Report vide Chapter IV, paragraph 8.3. A similar set of transactions was also noticed in 11.5% GOI Loan 2007 of face value Rs.56 crores. The details thereof are summarised below :

(i) On April 1991, Andhra Bank purchased 11.5% GOI Loan 2007 of face value Rs.72.74 crores on account of HPD from CBMF (Settlement amount Rs.72.90 crores) and the latter issued its 2 SGL transfer forms for Rs.16.74 crores and Rs.56 crores to it. Andhra Bank got credit for Rs.16.74 crores in its SGL account with the PDO of RBI but the second SGL transfer form for Rs.56 crores lodged with the PDO on 12 April 1991 bounced. Although this was relodged three times subsequently (20 April 1991, 2 May 1991 and 13 May 1991), the bank did not get credit for want of sufficient balance in the seller's account. However, the above security was traded by Andhra Bank on account of the broker HDP on the basis of these SGL transfer forms, as per the table given below:

Date	Purchased from/ Face Value	Rate	Date	Sold to Face Value	Rate	Remarks
			05.04.1991	Canara Bank (Rs.50 crores)	99.75	Andhra Bank issued 2 SGL transfer forms Nos.1004 and 1005 for Rs.32.50 crs. and Rs.75.50 crs.
				Stanchart (Rs.22.74 crs.)	100.35	Andhra Bank issued SGL transfer form No.1003
01.06.1991	Canara Bank (Rs.50 crs.) Canara Bank (Rs.25 crs.)	102.1607)) 1004.0045)	01.06.1991	Stanchart (Rs.75 crs.)	100.75	Andhra Bank received back its SGL transfer forms Nos.1004 Rs.50 crs. Fresh SGL transfer form received for Rs.25 crs. from Canara Bank, Andhra bank issued fresh SGL Nos. 1230 and 1231 for Rs.55.77 crs. and Rs..19.23 crs. to Stanchart.
25.07.1991	Stanchart (Rs.45 crs.)	100.95				SGL No.1230 for Rs.55.77 crs. was received and Andhra Bank issued fresh SGL transfer form
25.07.1991	CBMF (Rs.10 crs.)	102.00				for Rs.10.77 crs. to Stanchart, CBMF's SGL transfer form for Rs.10 crs. and Stanchart SGL
01.08.1991	Stanchart (Rs.1 crore)	101.15				transfer form for Rs.1 crore received.

(ii) On 2 August 1991, Andhra Bank sold the same security of face value RS.56 crores back to HPD "free" for which the SGL transfer form for Rs.56 crores received from CBMF on 5 April 1991 was returned to him. This SGL transfer form issued by CBMF on 5 April 1991 to 'Andhra Bank was on the basis of a purchase transaction with Stanchart of the same security of face value Rs.56 crores @ 101.25 on 20 March 1991. According to CBMF it did not get SGL transfer form or BR for this purchase from Stanchart, as in the case of the deal in 11.5% GOI Loan 2006 of face value Rs.20 crores discussed earlier.

(iii) It will thus be seen that Stanchart did not deliver the securities for a total amount of face value Rs.76 crores (i.e Rs.20 crores of 11.5% GOI Loan 2006 and Rs.56 crores of 11.5% GOI Loan 2007) for its sale to CBMF on 20 March 1991. However, CBMF sold securities to this extent by issuing its own SGL transfer forms without holding the same, merely on the basis of its purchase transactions with Stanchart. Based on these SGL transfer forms, a series of transactions were made for HPD through Andhra Bank till 2 August 1991. Finally, SGL transfer forms received by Andhra Bank for its purchases from Grindlays (Rs.20 crores) and CBMF (Rs.56 crores) were got back by HPD from Andhra Bank on 2 August 1991. How these were disposed of by him is not known. According to CBMF, the issue regarding non-receipt of SGL transfer forms from Stanchart was not pursued by it since there were no claims from ANZ Grindlays bank and Andhra Bank. On checking up the matter with Stanchart, it was observed that it had sold 11.5% GOI Loan 2006 of face value Rs.22 crores and 11.5% GOI Loan 2007 of face value Rs.56 crores on 20 March 1991 to CBMF vide its deal slips Nos.3847 and 3848 and delivery had been shown therein as "SGL". However, no satisfactory explanation was forthcoming from the bank regarding non-issue of SGL transfer forms for these sales to CBMF. Photocopies of two SGL transfer forms covering the above two sales (originals are stated to have been seized by CBI) available in Stanchart did not bear the signatures of Stanchart officials although these were signed by CBMF officials as "transferee". CBMF is doubtful about the genuineness of the SGL transfer forms and it denies having received these forms from Stanchart on 20 March 1991 or any time thereafter. CBMF has since served on Stanchart legal notices for delivery of securities or repayment along with interest.

4. Conclusion

4.1 The bank did not follow most of the guidelines issued by the Reserve Bank in its circular D.O. letter dated 26 July 1991. Several SGL transfer forms received and lodged at the PDO of the Reserve Bank bounced for want of sufficient balance in the sellers' accounts. Several SGL transfer forms issued by the bank in favour of other banks also bounced for the same reason. These were not reported by the Bombay (Fort) branch to the Reserve Bank. The bank was returning SGL transfer forms or BRs to the issuing banks while selling the securities back to them; and also delivering BRs of one bank duly discharged to another bank. The Head Office of the bank and Zonal Office at Bombay did not monitor the reporting system. As per the data compiled by the branch itself, there were 130 cases of SGL transfer forms issued by it involving Rs.2438.27 crores bounced during the period April 1991 to June 1992.

4.2 There was inadequate supervision over the operations of the Funds Department at the Bombay branch by both the Head Office and the Zonal Office at Bombay. Head Office had not ascertained the reasons for the difference between the contracted rates and the actual rates at which the transactions were effected, as also the reasons for crediting/debiting the difference to the brokers' accounts.

4.3 There was no system of physical verification of securities on Head Office account at the branch. Zonal Office, Bombay had not carried out any such exercise although it was required to do so once in a quarter as per Head Office instructions. Zonal Office also did not scrutinise the securities transactions taking place at the Bombay branch through the daily statements, for the purpose of reporting the deficiencies, if any, to Head Office as per the latter's instructions. The absence of similar physical verification of clients' holding or reconciliation of SGL balances on their account has already been mentioned in the Committee's third Report.

4.4 The branch had credited to broker's account (HPD) on a number of occasions bankers' cheques drawn in its favour. No covering letters/instructions from the issuing banks were available in some cases.

5.1 A reference has been made by the Committee to the scrutiny of Hiten P.Dalal's (HPD) current account maintained with Andhra Bank, in its third Report vide paragraph 6 of Chapter VII. The analysis of HPD's current account for the period 1 April 1991 to 30 May 1992 indicates payments and receipts from/to the account as under:

(Rupees in crores)

Payments		Receipts	
		Opening balance	0.49
(a) Bankers cheques issued by Andhra Bank to other banks covering security transactions undertaken by it on account of the broker	5,990.75	(a) Bankers cheques received from other banks covering security transactions on account of the broker	5,606.67
(b) Bankers cheques issued by Andhra Bank for which there were no security transactions in its books	1,769.49	(b) Bankers cheques received and credited for which there were no security transactions in its books	2,402.00
(c) Personal cheques issued/ transfers made Banks - 476.80 ABFSL- 865.60	1,342.40	(c) Transfers from the accounts of: ABFSL - 1,024.19 other brokers - 75.23	1,099.42
(d) Personal cheques issued/ transfers made to/in favour of other brokers	160.19	(d) Other receipts	214.65
(e) Other payments including cash withdrawals	59.92		
(f) Closing balance	0.48		
	9,323.23		9,323.23

Note: In respect of some large value security transactions (purchases and sales effected on the same day), the total value thereof has been shown as debits and credits in the accounts although bankers cheques actually issued/received were only for the net amounts.

5.2 Out of the total payments and receipts at Rs. 15,768.91 crores by means of bankers cheques, the payments to and receipts from thefollowing banks accounted for Rs. 13,356.12 crores (constituting 84.7%) as under :

(Rupees in crores)

Bank	Amount
Stanchart	3,444.01
Canara Bank and its subsidiaries	2,892.17
Citibank	2,712.39
Bank of America	1,697.05
Grindlays	1,324.13
Bank of Karad	1,286.37
	13,356.12

The remaining 15.3% was on account of various other banks. Apart from the bankers cheques, HPD had made payments aggregating Rs.476.80 crores by means of personal cheques to various banks. Of this, payments made to Stanchart, Citibank, Grindlays Bank and Canara Bank/its subsidiaries were to the extent of Rs.462.21 crores. Payments by means of personal cheques to banks were mainly intended for purchase of shares and debentures. HPD had also made payments by means of personal cheques totally Rs.58.50 crores to various firms, companies and individuals which included a number of investment and finance companies. He had also made payments to other brokers totalling RS.160.19 crores. The purposes for which these payments to firms, companies, brokers and individuals were made are not known. The total cash withdrawn amounted to Rs.1.42 crores and single withdrawals of Rs.5 lakhs and above were noticed on a number of days. There were also three such single withdrawals of Rs.10 lakhs and above.

5.3 After commencement of business by teh branch of ABFSL at Bombay in August 1991, the total value of transactions entered into by HPD with this company as reflected in his current account (receipts and payments from/to ABFSL) amounted to Rs.1,889.79 crores. More than 40% of the transactions of ABFSL in Bombay was with HPD.

5.4 As per records available at Andhra Bank, the securities transactions undertaken by the bank on account of HPD resulted in a shortfall of about Rs.300 crores (the total value of purchases and sales being around Rs.10,700 crores and Rs.10,400.crores respectively). Certain purchases and sales have been shown as 'free' or 'self' for which no payments were made and received. Out of the shortfall of Rs.300 crores, an aggregate amount of Rs.96.61 crores represented the loss absorbed by HPD on account of simultaneous purchase and sale transactions on the same day concluded with BoA (Rs.84.53 crores), Stanchart (Rs.10.46 crores) and Citibank (Rs.1.62 crores). The excess outflow of Rs.300 crores stated above was possibly made good out of the net inflow to the extent of Rs.474.04 crores into his account from other brokers by way of transfer of funds. It may be mentioned that HPD received a net amount of Rs.559 crores from BoK by means of bankers cheques for which there were no securities transactions at Andhra Bank. These bankers' cheques were issued by BoK by debit to the account of the broker A.D.Narottam. The sum of Rs.474.04 crores being the net inflow of funds from brokers has been arrived at after taking into account receipts from and payments to various brokers.

6.1 An attempt has also been made to trace the use of funds aggregating Rs.2,246.29 crores (i.e. personal cheques issued favouring various banks - Rs.476.80 crores and the bankers cheques issued not covering securities transactions in Andhra Bank - Rs.1,769.49 crores). Out of Rs. 2,246.29 crores, HPD used Rs.1,337.94 crores for the following purposes as per the scrutiny conducted so far at six banks/subsidiaries:

(Rupees in crores)

a)	Towards differences in contracted rates and actual delivery rates	407.83
b)	Towards purchase of equity shares/ debentures/units of Mutual Funds	433.51
c)	Bankers cheques issued favouring other banks which were found credited to some other brokers accounts	153.95
d)	Towards purchase of PSU bonds/GOI securities	313.91
e)	Towards payment of interest on bonds/ securities	28.74
		1,337.94

6.2. It is not known whether HPD disposed of the assets acquired at (b) and (d) above subsequently or these continue to be held by him.

7. Compilation of the above data involved scrutiny of a large number of vouchers and other records at various banks and was done manually. Consequently, some variations in the figures arrived at cannot be ruled out.

8. Andhra Bank Financial Services Ltd.

8.1 In the fourth Report of the Committee (vide paragraphs 16.1 to 16.4 - Chapter V) certain 'back-to-back' transactions, which took place between April 1992 and October 1992, between HPD, Andhra Bank Financial Services Ltd and Shri N. Krishna Mohan, Managing Director of Goldstar Steel & Alloys Ltd (GSAL) were mentioned.

8.2 It was reported by ABFSL earlier that the 'loan' of Rs.2 crores with due interest was repaid on 26 October 1992. On further enquiry it is observed that Shri Krishna Mohan repaid a total sum of Rs.2,22,15,140.00 through five cheques, which were realised by ABFSL between 10 October 1992 and 26 October 1992. The source for the repayment of the loan is traced mainly to three refund orders dated 23 July 1992 for an aggregate amount of Rs.2,20,14,790.00 issued by GSAL, which were debited to 'GSAL - Refund Orders A/c' with State Bank of India (Industrial Finance Branch), Hyderabad. It is observed that the refund orders account with the branch was running in overdraft. Reconciliation of the 'Refund Orders Account' between SBI, Industrial Finance Branch, Hyderabad, Karvy Consultants P. Ltd., Registrars to the right issue of GSAL and the company is stated to be still in progress.

XX. UCO Bank

1.1 Findings on the scrutiny of certain bills discounting transactions of UCO Bank (UCO) were incorporated in chapter 7(IV) of the Committee's first interim Report issued in May 1992.

1.2 Scrutiny of the securities transactions

UCO's investment transactions are mainly undertaken at its Bombay (Hamam Street) branch. The bank's total turnover (purchases and sales) in securities transactions during the period 1 April 1991 to 23 May 1992 was Rs. 28,906 crores of which the transactions entered into through the broker, Harshad S. Mehta (HSM) alone amounted to Rs. 10,100 crores. The Bombay branch has undertaken purchases and sales of various securities on the bank's investment portfolio as also on behalf of a number of clients including brokers. The transactions on behalf of Head Office are done on the basis of telex/telephonic instructions received from Head Office in Calcutta by raising debits or credits in the Head Office account whereas those on behalf of clients are made as per the clients' instructions by debiting or crediting their current accounts maintained with the branch, without any reporting to Head Office in this regard. The Bombay branch operated two SGL accounts with PDO (RBI) viz. 032 for bank's own investments and 065 for broker clients.

2. Transactions in securities on account of Head Office Investment Account

2.1 The Head Office of the bank in Calcutta enters into contracts directly with brokers for purchases and sales of securities and advises the Bombay branch to execute the contracts. A scrutiny of the securities deals revealed certain irregularities and some of the major findings are discussed below.

2.2 Crediting of securities purchased for bank's own investment account into brokers' SGL Account

(a) On 5 April 1991, UCO purchased for its own investment account, 11.5% GOI Loan 2009 of face value Rs. 20 crores from Indian Bank and it received a BR which was replaced by an SGL transfer form on 12 April 1991. The SGL transfer form was lodged with PDO on 13 April 1991 for credit to SGL account No. 065 maintained for broker-clients instead of SGL account No. 032 of UCO's investment account and also obtained credit in the broker-clients' account. Thereafter, a number of transactions in the above loan took place on account of broker-clients and UCO issued its SGL transfer forms on behalf of the clients. After a lapse of more than six months, the discrepancy in crediting wrongly to the SGL account intended for brokers was discovered on 25 October 1991. The difference was located in the holdings of the broker, HSM and he was asked to make good the same. However, the balance in the broker's account was only Rs. 3 crores. HSM, therefore, brought an SGL transfer form for Rs. 17 crores in respect of the security, issued by State Bank of Saurashtra (SBS) and the position was rectified on 28 October 1991 by transferring securities of face value Rs. 20 crores from brokers' SGL account to UCO's investment SGL account with PDO. It may be mentioned that the SGL transfer form for Rs. 17 crores was issued by SBS on the strength of an SGL transfer form for similar amount issued by State Bank of India (SBI) to SBS as mentioned in chapter IX paragraph 6 (a) of the Committee's second Report and hence UCO had not made any payment in this regard to SBS on behalf of the broker. The bank had thus issued SGL transfer forms on account of HSM without ensuring that the broker had sufficient balance to his credit and the broker has also taken advantage of the discrepancy and traded in the loan freely without actually holding the security. This has amounted to UCO's extending a clean loan free of interest for a period of about six months to HSM for Rs. 17 crores i.e., the value of security not available in the account.

(b) It was further seen that there were transfers of securities from SGL account 065 meant for brokers to SGL account 032 i.e., bank's own investment account on certain other occasions also as shown below:

Particulars of Security	Face Value (Rs.in crores)	Date of transfer from SGL 065 to 032
11.5% GOI Loan 2008	20	29-4-1991
11.5% GOI Loan 2007	15	4-6-1991
11.5% GOI Loan 2009	2	18-7-1991

From the available records, no purchases of these securities from the brokers by the bank could be established to support these transfers. The bank has expressed its ignorance about the circumstances under which these transfers were effected. In the light of the similar transfer of security of the face value Rs. 20 crores effected on 28 October 1991 (discussed in the earlier paragraph), these three transfers to the extent of Rs. 37 crores also suggest that they were in rectification of 'clean loans' to the brokers given earlier.

(c) Shortfalls in Statutory Liquidity Ratio (SLR) on account of diversion of securities to brokers' account

It was observed that several SGL transfer forms issued by UCO in respect of sales of 11.5% GOI Loan 2009 on behalf of broker-clients during 5 April 1991 to 28 October 1991 were cleared by the PDO only because of the fact that the balance in the SGL account No. 065 in respect of the above loan had been inflated by affording a wrong credit as stated in paragraph 2.2. But for the wrong credit, there would have been huge deficits in the loan account on certain days as shown below:

(Rs.in crores)

Particulars of SGL transfer form issued — In favour of/on behalf of		Face Value	Date of debit to SGL A/c. No.065	Closing balance after excluding Rs.20 crores wrongly credited to SGL A/c.No.065
1.	Punjab National Bank (Batliwala & Karani)	25	16.4.1991	(—) 5 16.4.91 to 21.4.91)
2.	-do-	25	23.4.1991	(—) 15 23.4.91 to 5.5.91)
3.	State Bank of Hyderabad (Harshad S. Mehta)	5	3.7.1991 }	(—) 15 3.7.91 to 27.10.91)
4.	State Bank of Saurashtra (Harshad S. Mehta)	10	3.7.1991 }	

Note: The sale proceeds in regard to the above were credited to the current accounts of the brokers.

Since Bombay (Hamam Street) branch mislodged the purchase into the brokers' SGL account and further allowed the brokers to sell the same and credited the brokers current accounts with the sale proceeds, the securities to the extent of such sales were not available either in the bank's own SGL account or its broker clients' SGL account. The Head Office of the bank however included the value of entire securities worth Rs. 20 crores for the purpose of its SLR which when excluded from the bank's SLR holdings resulted in UCO Bank having defaulted in the maintenance of SLR requirements, as under, on many an occasion :

(Rs. in crores)

Period	SLR required to be maintained	SLR actually maintained (after adjusting the sales made in excess of the balance in SGL A/c No. 065 as mentioned above)	Deficit in liquid assets
23-04-91 to 02-05-91	2,302.45	2,297.34	5.11
03-05-91	2,302.45	2,296.89	5.56
04-05-91 to 05-05-91	2,295.04	2,293.26	1.78
23-08-91	2,272.76	2,263.28	9.48
24-08-91 to 05-09-91	2,269.10	2,252.30	16.80
06-09-91	2,269.10	2,254.62	14.48
07-09-91 to 19-09-91	2,269.75	2,260.18	9.57
20-09-91	2,269.75	2,261.32	8.43
21-09-91 to 02-10-91	2,276.73	2,260.92	15.81
03-10-91	2,276.73	2,274.92	1.81
04-10-91	2,276.73	2,275.07	1.66

2.3 Crediting of interest to brokers' account

(a) The Head Office of the bank entered into ready forward contracts with brokers directly and in a large number of cases, the rates for purchases and sales of securities fixed were the same (level rates). In such cases, the interest on the flow of funds is worked out at predetermined ready forward rates but the reversal rate is not calculated on this basis. The exact manner of settlement of reversal amounts is discussed in the examples given below. It may be observed that in the first case, where there is a sale of security and an inflow of funds (borrowing), and the rate of interest on the funds is higher than the coupon rate, the difference is passed on to the broker concerned as "balance amount" or "additional amount". Likewise, in the second case, where the first leg of the deal is a purchase (lending), and the rate of interest on the outlay of funds involved is lower than the coupon rate, the difference is again paid to the broker as 'additional amount'. The bank has no system of obtaining confirmation of contracts from counterparty banks and hence, the brokers quoted rates to the counterparty banks which were often different from the rates entered into by them with UCO. A few instances where the difference in interest was passed on to the brokers are given below:

(Amount in lakhs of rupees)

Particulars of Security and face value	Date of purchase/ repurchase (rate and purchase consideration)	Date of sale/ resale (rate and sale proceeds)	Total amount receivable/ repayable and the rate of interest charged	Name of broker/ counterparty bank	Amount passed on to broker
1. 11.5% GOI Loan 2008 Rs.25 crs.	14.12.1991 98.85 2483.87 (RP)	30.11.1991 98.85 2475.46 (S)	2491.12 16.5%	Sharada & Co. Bank of Madura	7.25
2. 11.5% GOI Loan 2007 Rs.15 crs.	11.1.1992 99.20 1522.63 (P)	25.1.1992 99.20 1527.68 (RS)	1527.15 7.75%	Batliwala & Karani United Bank of India	0.53

(b) In the first transaction above, which amounted to a borrowing, the Head Office entered into a ready forward contract with the broker Sharada & Co. to sell on 30 NOvember 1991, 11.5% GOI Loan 2008 of face value Rs.25 crores @ 98.85 and repurchase the same at the same rate of 95.85 on 14 December 1991 and advised the Bombay (Hamam Street) branch to contact the broker to execute the deal. As per the instructions of Head Office, the branch had to receive on behalf of the Head Office Rs.24,75,45,807.78 on 30 November 1991 as the sale proceeds of the security as per details given on the next page.

Sale proceeds of 11.5% GOI 2008 @ Rs.98.85, face value Rs.25 crores		Rs.24,71,25,000.00
Add interest from 23-11-91 to 29-11-91 i.e. 7 days	Rs. 5,59,027.78	
Less Incometax @ 24.725%	Rs. 1,38,220.00	Rs. 4,20,807.78
Total inflow of funds (Borrowing)		Rs. 24,75,45,807.78

As the security was repurchased on 14 December 1991, (repayment of the amount borrowed), the Head Office arrived at the repayment amount after loading interest at 16.5% p.a. for the period 30 November 1991 to 13 December 1991 on the funds borrowed as shown below:

Amount borrowed on 30-11-91		Rs. 24,75,45,807.78
Add interest @ 16.5% for 14 days		Rs. 15,66,659.77
Total amount repayable by the bank	(A)	Rs. 24,91,12,467.55

As per the contract with the broker, the repurchase price was Rs.24,83,87,424.33 which was arrived at as under:

Repurchased price of 11.5% GOI Loan 2008 of face value Rs.25 crores @ 98.85		Rs. 24,71,25,000.00
Add interest from 23.11.91 to 13.12.91 i.e. for 21 day	Rs.16,77,083.33	
Less Income tax @ 24.725%	Rs. 4,14,649.00	
		Rs. 12,62,424,33
	(B)	Rs. 24,83,87,424.33

As the amount of repurchase price at (B) above was less than the amount calculated to be repayable as at (A) above, the Head Office asked the branch to pay the amount at (B) as the cost of security as also pay the difference at Rs. 7,25,043.22 as "additional amount" and debit the total amount i.e. Rs. 24,91,12,467.55 to Head Office account. Head Office did not give the name of the payee for these amounts. The branch credited this additional amount of Rs. 7,25,043.22 to the broker's current account. It was, however, observed that though the broker was successful in selling the security on 30 November 1991 to the counterparty bank viz. Bank of Madura, at 98.85 i.e. Rs.24,75,45,807.78, it could repurchase the security in two lots from that bank on 14 December 1991 at an average rate of 99.09 i.e. Rs.24,89,93,674.33 only, as against the amount of Rs.24,83,87,424.33 (B), thereby incurring a loss of Rs. 6,06,250.00 in the second leg of the transaction. Thus, the broker's net gain in the whole transaction was reduced to Rs.1,18,793.22 (i.e. Rs.7,25,043.22 minus Rs. 6,06,250.00).

(c) In the second transaction, which is in the nature of lending by UCO, the bank contracted with the broker Batliwala & Karani to buy 11.5% GOI Loan 2007 of the face value Rs. 15 crores on 11 January 1992 @ 99.20, the total cost after adjustment of interest being Rs. 15,22,62,650/- (A). As per the contract, the security was to be sold back at the same rate viz. 99.20 on 25 January 1992 and the total sale proceeds including interest on the security worked out to Rs. 15,27,67,619.33 (B). The Head Office of the Bank, however, reckoned interest at 7.75% per annum on the outflow of funds as at (A) above for the period 11 January 1992 to 24 January 1992 and arrived at the amount recoverable on 25 January 1992 on resale of the security at Rs. 15,27,15,266.37 (C). UCO, therefore, passed on the amount of Rs. 52,352.96 being the difference between the contracted sale proceeds and the amount calculated to be recovered on 25 January 1992 {i.e. (B)-(C)}, to the broker by credit to his current account.

(i) It was observed that although the broker purchased the security on 11 January 1992 from the counterparty bank at the same rate contracted with UCO, the broker sold the security back on 25 January 1992 to the counterparty bank at 99.1651 and UCO realised an amount of Rs. 15,27,15,269.33 (D) only, from the counterparty bank. UCO, therefore, debited the broker's account with an amount of Rs. 52,350.00 (B - D) on 25 January 1992.

(ii) In this process, UCO was not able to derive even the coupon rate in full for the period of its holding the security as the rate of interest charged on the outflow of funds was lower than the coupon rate.

(iii) Though the entire funds outlay in these transactions is that of the bank, the broker took a share of the interest charged on the funds.

2.4 Crediting of difference in rates to brokers' account

(a) It was observed that the Bombay (Hamam Street) branch purchased or sold securities at rates determined by the brokers instead of at the rates contracted and advised by Head Office and received or issued the cost memos as per the brokers' directions. However, in all such cases, the Head Office was debited or credited for the amounts already advised by Head Office and the difference if any, was paid to the brokers, without intimating the Head Office about the same. A few instances in this regard are given below:

A. Purchase

(Rs. in crores)

Date	Security and face value	Rate of purchase and purchase consideration advised by HO	Rate of actual purchase and purchase consider-ation paid to counterparty bank	Name of the broker and counterparty bank	Amount paid to broker
28.12.91	10.5%GOI Loan 2014	88.45	87.45	Sharada & Co.	0.15
	Rs.15 crores	13.4618	13.3118	Bank of Karad	
B. Sale					
28.12.91	11.5% GOI Loan 2010	94.25	96.88	Sharada & Co.	0.66
	Rs.25 crores	23.6647	24.3223	Bank of America	

(b) In the first transaction, the branch debited the Head Office with the entire amount of Rs.13.4618 crores as the cost of the security and passed on the difference of Rs.15.00 lakhs (excess of contract value over delivery value) to the broker by credit to his current account. On the day of reversal i.e. 11 January 1992, the broker could resell the security for UCO at 88.40 only (i.e. Rs.13.5031 crores) as against 88.45 (Rs.13.5046 crores) contracted, thereby reimbursing the bank for the excess of contract value over delivery value i.e. Rs.0.15 lakh by UCO on 11 UJanuary 1992 as explained in the previous paragraph. Thus the broker's net gain in this ready forward transaction amounted to Rs.14.87 lakhs. It was further observed that the amount Rs.13.3118 crores paid by UCO to Bank of Karad (BoK) and Rs.13.3118 crores received by it from that bank were credited and debited respectively to the broker's current account at BoK. Since the above sale and purchase made by BoK were on behalf of its broker-client viz. Sharad & Co., the broker has not only enjoyed the funds lent by UCO under this ready forwad deal but also received the difference in prices for his benefit.

(c) In the second transaction, UCO had contracted with the broker to purchase the security on 18 December 1991 @ 94.25 and pay the purchase consideration of Rs.23.5805 crores and also resell the same on 28 December 1991 at the same rate i.e. 94.25 and realise the amount of Rs.23.6647 crores. While in UCO, this was a ready forward transaction, it was concluded with two different counterparties i.e. purchase from BoK and sale to BoA. It was also stipulated that an amount of Rs.0.63 lakh be recovered by UCO as "additional amount" on 28 December 1991 on reversal of the ready forward transaction (as discussed in paragraph 2.3). The broker had purchased the security for UCO at a total cost of

Rs.23.5805 crores on 18 December 1991 i.e. there was no difference in contract and delivery rates. On 28 December 1991, howevber, the broker resold the security at 96.8804 (Rs.24.3223 crores) instead of at the rate 94.25 (Rs.23.6647 crores) contracted with UCO. The excess of delivery value over contract value i.e. Rs.65.76 lakhs was paid to the broker. After UCO's recovering the "additional amount" of Rs.0.63 lakh as stated above, the broker, made a gain Rs.65.13 lakhs. It was further observed that the amount of Rs.23.5805 crores being the sale proceeds received by BoK from UCO was credited to the current account of Excel & Co. maintained at BoK, indicating that the securities were sold by BoK on behalf of its broker-client Excel & Co.

(d) On 25 November 1991, the Bombay branch made an outright purchase of 11.5% GOI Loan 2010 of the face value Rs.3,39,25,000 from Grindlays Bank at the rate of Rs.101 as contracted by Head Office, the settlement amount after making necessary adjustments towards interest being Rs.3,56,02,107.06. Accordingly, the branch debited Head Office for the amount with a corresponding credit to the current account of the broker Puran Moorjani, through whom the contract was booked. However, as per the cost memo of Grindlays Bank, the securities were sold to UCO at the rate of Rs.97, the total cost including interest being Rs.3,42,45,107.06 which was debited to the broker's current account and a cheque was issued to Grindlays Bank. The net result of passing the entries through broker's account as mentioned above was that the broker got an excess credit of Rs.13,57,000 to his current account.

2.5 Ready forward deal with State Bank of India/Grindlays Bank

(i) (a) On 28 March 1992, UCO bought through HSM, 11.5% GOI Loan 2008 and 11.5% GOI Loan 2009 of face value Rs.25 crores and Rs.75 crores, respectively and cheques dated 28 March 1992 for Rs.23,25,14,432.89 and Rs.69,89,86,065.33 respectively were also issued to the counterparty bank viz. SBI. There was no cost memo issued by SBI in this regard. As per the contract, the securities were to be sold back on 6 April 1992, the buying and selling rate being Rs.90.00. In ready forward deals, executed at level rates, the practice of the bank is to fix a rate of interest on the outflow or inflow of funds depending on whether the bank is a lender or borrower (i.e. buyer or seller of securities). However, in this case, significant variation was made from this practice inasmuch as the rate on bank's outflow of funds through purchase of securities was fixed at 5 per cent over the bank's average cost of borrowing from the money market. It was stated that the linking of interest rate to the cost of borrowing from money market was made for the reason that HSM had offered to procure call money funds for the bank. The bank had obtained call money funds aggregating Rs.710.80 crores during 28 March 1992 to 5 April 1992 from various banks through HSM and the average cost was 28.35 per cent per annum. Thus, interest at 33.35 per cent per annum was to be recovered on the outgo of Rs.100 crores. The deal, which was to be completed on 6 April 1992 by a sale by UCO, was carried forward to 17 April 1992, and continued to be linked to the cost of money market funds to be procured through HSM. During the period 6 April 1992 to 17 April 1992, call money procured through HSM's intervention from various banks totalled Rs.1000 crores at an average interest of 16.4 per cent per annum. Thus, the rate of interest on the relative outgo of funds to the tune of Rs.100 crores, was reduced to 21.4 per cent.

(ii) The transaction was partially completed as outright sale on 18 April 1992 by sale of securities of face value Rs.50 crores through the broker M/s. V.B. Desai instead of HSM to the counterparty viz. Grindlays Bank, instead of SBI as shown below:-

11.5% GOI Loan 2008, face value Rs.25 crores @90.17343 and 11.5% GOI Loan 2009, face value Rs.25 crores @90.17475. UCO had also received the sale proceeds amounting Rs.23,41,50,315.11 and Rs.23,46,34,614.00 respectively from Grindlays Bank on 18 April 1992. UCO's branch has, however reported to its Head Office, the sale of these securities @90.00 each i.e. at the original sale price for the ready forward transactions and credited Head Office for Rs.23,37,16,740.11 and Rs.23,41,97,664.00 only, respectively, the difference in amounts having been credited to HSM's current account maintained with UCO.

(iii) The contract for sale of balance amount of the security, viz. Rs.50 crores was ultimately cancelled by UCO on 31 August 1992. The bank has thus not recovered any interest from the broker or counterparty bank on the amount provided by it on 28 March 1992.

(iv) It was further observed that as per the sales register of SBI, there were no sales of the securities in question to UCO on 28 March 1992. However, as per the entries in the PDO's books, these securities were debited in the SGL account No.004 relating to SBI's Investment Account with corresponding credit to UCO's SGL account on 30 March 1992. This has resulted in the SBI's balances with PDO being lower by Rs.100 crores as compared to the balances in its investment ledger on that day.

(v) The two bankers' cheques received from UCO on 28 March 1992 along with certain other cheques were, however, realised by SBI and the funds utilised by it for issuing its own cheques/RBI cheques in favour of certain other banks and NHB on that day as shown below :-

Cheques received by SBI on 28 March 1992

Amount (Rs.)	Received from
23,25,14,432.89	UCO
69,89,86,065.33	UCO
17,31,325.00	N.A.
93,32,31,823.22	

Cheques issued by SBI on 28 March 1992

Amount (Rs.)	In favour of
48,73,09,588.44	Syndicate Bank
20,02,125.00	Bank of America
38,96,961.64	Grindlays Bank
36,00,23,148.14	NHB
8,00,00,000.00	NHB
93,32,31,823.22	

(vi) The above information is based on the waste book maintained by SBI and it has reported that both the cheques received and the cheques issued are not supported by any investment transaction of the SBI. SBI has pleaded ignorance of the purpose for which the cheques were received by it and the parties who tendered them. SBI is also not aware why the proceeds of the cheques were utilised in the manner in which was done.

(vii) Syndicate Bank had received the cheque from SBI in consideration for its sale of the following securities to SBI on 28 March 1992 reportedly through the broker, HSM.

1)	9% IRFC bonds face value Rs.30 crores @92.24792	Rs.28,99,84,855.89
2)	17% NTPC bonds face value Rs.20 crores @95.58839	Rs.19,73,24,732.55
		Rs.48,73,09,588.44

Syndicate Bank has not issued any BR or delivered any security to SBI in regard to the above sales "pending confirmation from SBI with regard to the transactions". The cheques issued to NHB also related to purchase of certain securities by SBI from NHB as per the records at NHB. However, there was no movement of securities in this regard also. The amount of Rs.38.97 lakhs paid to Grindlays Bank was credited to HSM's current account maintained with that bank on 31 March 1992.

(viii) It may be seen that the securities in the SBI's investment account at PDO had been got unauthorisedly sold off by the broker HSM. Neither the funds received from UCO nor the securities purchased therewith from Syndicate Bank could so far been appropriated by SBI. As far as UCO is concerned, it has not so far received any interest on the funds lent.

2.6 Transactions with National Housing Bank/PNB Capital Services Ltd.

2.6.1 (a) On 28 March 1992 UCO subscribed to 17% bonds issued by Power Finance Corporation (PFC) of the face value Rs.150 crores, at par, on its investment account. The bank was under obligation to sell 40 per cent of the bonds (i.e. bonds for face value Rs.60 crores) over the counter as per the condition stipulated by the Controller of Capital Issues.

(b) On the same day PFC invested the entire subscription amount of Rs.150 crores received from UCO with that bank itself under the Portfolio Management Scheme (PMS). The bank in turn sold the same PFC bonds from its investment account on the same day to PFC itself under the PMS.

(c) On 30 March 1992, the bank sold these bonds (on behalf of its PMS client) to PNB Capital Services Ltd. (PNB Caps) at the rate of 97 per cent and received a sum of Rs.145.64 crores thereby incurring a loss of Rs.4.36 crores. PNB Caps sold the bonds on the same day to Punjab National Bank at the purchase price.

(d) The sale proceeds of Rs.145.64 crores received by UCO were on the same day invested with National Housing Bank (NHB) in 17% NTPC bonds of face value Rs.71.00 crores (cost Rs.70.64 crores) and Units of the face value Rs.50.00 crores (cost Rs.75.00 crores).

(e) As per NHB's record, the entire deal was for NTPC bonds though it had given two separate BRs for NTPC bonds and Units to UCO. NHB in turn had purchased the bonds from State Bank of India (cost Rs.90.46 crores) and Stanchart (Cost Rs.55.18 crores).

(f) The deal relating to sale of PFC bonds to PNB Caps and the deal relating to purchase of bonds and Units from NHB were made through the intermediation of broker HSM.

(g) As indicated in Chapter II (paragraph 2) of the second Report of the Committee, the amounts paid by NHB to SBI and Stanchart for its purchases had been credited to the accounts of HSM and Growmore Research & Assets Management Co. Ltd. (GRAM), respectively.

(h) As NHB was not in a position to deliver the securities, it has refunded the principal amounts of the deals to UCO in two instalments of Rs. 90.45 crores and Rs. 55.18 crores, on 6 July 1992 and 24 December 1992. The interest due on the amount was refunded by NHB to UCO on 30 March 1993 at a negotiated rate of 12 per cent.

(i) PFC is yet to issue the bonds or even the letter of allotment to UCO for the subscription made by UCO on 28 March 1992. Therefore, the bonds are yet to be delivered by UCO to PNB Caps. UCO is yet to repay the PMS funds of Rs. 150 crores to PFC which matured for repayment after lock-in period of one year, on 28 March 1993, pending resolution of the disagreement between itself and PFC on the return to be given to PFC under PMS.

(j) It is observed that the decisions relating to - (i) subscription to PFC bonds, (ii) undertaking PMS transactions on behalf of PFC, (iii) sale of bonds to PNB Caps and (iv) investment of funds with NHB were taken with the approval of the Chairman and Managing Director (CMD) and were put up to the Board for post-facto approval. The Board notes were however silent on certain important aspects of the deals viz. -

(1) the bank had incurred a loss of Rs.4.36 crores on sale of PFC bonds to PNB Caps,

(2) that the bonds were held by the bank in the PMS account and the loss has been parked there,

(3) the manner in which it proposes to make good the loss,

(4) No mention was made in the Board note dated 8 April 1992 relating to PMS transactions dated 8 April 1992 that the PFC bonds had already been sold to PNB Caps and funds invested with NHB. The note relating to these transactions was put up to the Board only on 12 May 1992 when it became apparent to the bank that NHB was not in a position to honour the deal,

(5) although the investment of the funds with NHB was to the tune of Rs.145.64 crores, the details regarding the expected yield etc. have not been given.

(k) The manner in which the transactions were hurriedly put through indicates that these deals were a part of a total arrangement whereby funds were made available to HSM.

2.6.2 On 8 February 1992, the Bombay (Hamam Street) branch of UCO purchased 11.5% GOI Loan 2010 of face value Rs.50 crores from NHB through HSM. As per the cost memo of NHB, the value of security @ 100 including interest was Rs.50,68,53,161.67. The branch had, however, issued an RBI cheque for Rs.48,68,53,161.67 only based on another unsigned cost memo in which the rate was shown as 96. The security was sold back to NHB on 22 February 1992 at 95.92480 and the BR was returned to NHB. UCO received an amount of Rs.48,81,60,393.78 from NHB as against the agreed sale proceeds of Rs.48,85,36,393.78. Hence, the shortfall of Rs.3,76,000 was debited to HSM's current account.

2.7 Payment of Rs.1.50 crores by HSM through the bank's CMD

On 22 April 1992, Shri K.Margabanthu, the then CMD of UCO received a cheque No.049043 dated

22 April 1992 for Rs.1.50 crores drawn on Grindlays Bank from HSM and handed it over to the then Zonal Manager of Bombay Zonal Office with instructions to credit the proceeds to Head Office account as the amount represented commission on security transactions undertaken by UCO on behalf of HSM. However, the credit advice prepared by Nariman Point branch stated that the amount represents profit on security dealings received from HSM. Since the transaction was not clear, the Head Office did not respond to the credit advice till 30 September 1992, when the amount was credited to Sundry Creditors account. The CBI is investigating the transaction.

3. Transactions on behalf of broker-clients

3.1 The Bombay (Hamam Street) branch had undertaken various purchases and sales of securities, bonds, Units, and shares during the period June 1987 to May 1991 on behalf of 19 broker-clients without following any norms. As per the memorandum of the bank's Vigilance Department put up to the bank's Board in August 1991, the Bombay (Hamam Street) branch had undertaken these risky operations on a massive scale without the controlling offices having come to know of them. During an investigation carried out by the General Managers of the bank in May 1991, they found that several brokers of the branch had procured huge funds from various PSUs under PMS prior to April 1991 and credited those funds to their own accounts in UCO. The brokers then acquired securities with these funds from mutual funds, foreign banks and financial institutions, etc. These brokers requested the institutional sellers to issue BRs in lieu of securities so purchased in favour of UCO. Subsequently, the brokers made UCO issue its own BRs against the above BRs and handed over UCO's BRs to the investors from whom funds were originally tapped by them. It was also observed by the investigating officials that in all these cases of BRs so issued by UCO, it did not hold any security in its name and the entire deals were ultimately those of the brokers and UCO's services were utilised by them for collection of funds and issue of BRs. The bank, however, received commission for its services. The investigation further revealed that during 1988-1991, Shri V.N. Deosthali, an officer in Scale I at the Bombay branch signed all the BRs, singly. The officer was also found to have unauthorisedly accepted portfolio funds to the tune of Rs.100 crores directly from PFC at rates fixed by himself. The officer was found to have issued cost memos on the basis of some contracts purported to have been entered into between some broker-clients and financial institutions and receiving cheques from those institutions and crediting the same to brokers' account. It was observed from the letter dated 24 December 1991 written by UCO to CBI that the bank had reported these irregularities to CBI in October 1991.

3.2 The branch, therefore, stopped the transactions on behalf of brokers on 8 May 1991. However, it resumed the operations in April 1992, reportedly on profitability grounds. The only refinements suggested in the new arrangement were that the dealings were to be restricted to three brokers viz. HSM, M/s. V.B. Desai and Batliwala & Karani and that the BRs should be issued subject to certain restrictions and that each broker should keep with the bank a minimum deposit of rupees one crore at all times. As per a note recorded by DGM on 18 March 1992, the bank's then CMD had issued oral instructions to restart switch deals on behalf of brokers, immediately. Therefore, the operations resumed on 6 April 1992 on behalf of HSM with the bank purchasing or selling Government securities on HSM's behalf by operating the SGL account No.065 for the purpose, correspondingly debiting or crediting his current account.

3.3 Transactions on behalf of HSM

(a) On 6 April 1992, the Bombay branch bought securities worth Rs.205 crores (mainly 11.5% GOI Loan 2010) from various banks and sold them to various banks, as instructed by HSM, on his account. After crediting his current account in respect of these sales and debiting it for the purchases, there was a debit balance of Rs.39.07 crores in his current account on 6 April 1992. This was, however, adjusted on 6 April 1992 itself by crediting to the current account of HSM an amount of Rs.40 crores received from NHB on that day through UCO's branch at D.N. Road, Bombay. It may be mentioned that the amount of Rs.40 crores provided by NHB was presumably a call money lending to UCO. But UCO did not issue any receipt for it. The amount which landed initially at D.N. Road branch of UCO (which handled call money operations of the bank) was immediately transferred to UCO's Hamam Street branch and credited to HSM's current account without any written instruction from NHB to this effect. The overdraft in the current account was caused on account of the fact that UCO issued an SGL transfer form, reportedly on behalf of HSM, for Rs.50 crores to SBI on 6 April 1992 in respect of 11.5% GOI Loan 2010 without obtaining any payment for the same, for credit to HSM's current account. This transaction is not supported by any cost memo/delivery instructions in writing etc. from the broker. While the payment from SBI for this sale to it is still outstanding, the call money borrowing was repaid to NHB on 16 April 1992 through Grindlays by HSM as detailed in paragraph 8(b) of chapter VI of the second Report of the Committee.

(b) On 6 April 1992, the branch bought 11.5% GOI Loan 2010 of face value Rs.135 crores (cost Rs.127.21 crores) from Bank of Madura (BoM) and sold the same security of face value Rs.70 crores (cost Rs.69.74 crores) back to that bank on the same day and the net amount (Rs.57.47 crores) of the cost of purchases and sales was paid to BoM by debit to HSM's account. The security was purchased from BoM at an average rate of 91.4 and sold back at an average rate of 96.9 to it bringing in approximately a profit of Rs.3.50 crores to the broker.

(c) On 18 April 1992, the branch again bought and sold 11.5% GOI Loan 2010 for Rs.180 crores(face value) each on behalf of HSM. It was observed that an SGL transfer form in respect of this security of the face value Rs.155 crores obtained from DFHI by UCO on 18 April 1992 bounced several times at PDO and the same was, therefore, taken back by DFHI and two back-dated SGL transfer forms, one for Rs.130 crores and another for Rs.25 crores were issued by DFHI. The SGL transfer forms were ultimately credited to the SGL account of broker-clients on 12 May 1992.

3.4 It may be mentioned that the above transactions on 6 April 1992 and 18 April 1992 undertaken by UCO on behalf of HSM after a lapse of nearly one year were only to help the broker in his business. The SGL transfer forms brought by the broker for the purchases made from various banks, for credit to SGL account No.065 bounced. This has resulted in bouncing of the SGL transfer forms issued by UCO on behalf of the broker to other banks. The securities bought by UCO from DFHI on behalf of HSM were sold to BoM which in turn sold the same to Karur Vysya Bank and Banque Indosuez from whom DFHI bought the securities originally, all the purchases and sales made by them being on the same day. The SGL transfer forms issued by all of them bounced indicating that none of them held adequate amount of security in their SGL accounts at the PDO on that date.

3.5 Reconciliation of SGL account maintained on behalf of broker-clients

The Bombay (Hamam Street) branch of the bank has not maintained an investment mirror account for the purchase and sales made on behalf of the broker-clients and continued to receive and issue SGL transfer forms on behalf of the broker-clients without any periodical reconciliation having been done at any point of time.

3.6 The branch had received several SGL transfer forms on account of broker-clients for credit to the SGL account No.065 and issued SGL transfer forms for debit to that account even after 8 May 1991, when the transactions on behalf of broker-clients were stopped by the bank. Some of these SGL transfer forms were not supported by any financial transactions and the branch has not received or paid any amount or credited or debited the current account of brokers on account of the same. These were reported to be for squaring up old outstanding transactions entered into on the basis of records maintained at the level of brokers. The explanation of the bank reads as under :

> "The SGLs were received by us after 8 May 1991 i.e. after the date of stoppage of switch transactions as per Head Office instructions on behalf of broker-clients, free of cost now. These SGLs were received against exchange of BRs held by us for which payments had been made in the past debiting relative brokers account. However, we are not able to co-relate the amount of SGL received now and payments made earlier. This is due to clubbing of two or more contracts. The particulars regarding rates of payment, exact amount of payment etc. are not on our records as these payments are made by the brokers through other banks."

The above explanation clearly reveals the kind of hold the brokers had on UCO.

3.7 It was observed that an SGL transfer form dated 26 August 1991 for Rs.38 crores in respect of 11.5% GOI Loan 2015 purported to have been signed by one of the officials of UCO Bank, Bombay branch viz. Shri M.V. Shidhaye and located at NHB was reported to be a forged one. This SGL transfer form was shown as having been issued from SGL A/c.No.065 meant for brokers but there was no entry in the books of UCO on that date relating to the transaction. CBI is investigating the matter as reported in the Committee's second Report vide paragraph 6(b)(v) of Chapter VI.

3.8 The Bombay branch was holding a number of original SGL transfer forms purported to have been issued to various banks during December 1990 to December 1991. On examination of some of these SGL transfer forms, it was observed that some of them bore the stamp and signatures of the counterparty banks. Some of them were discharged by the counterparty banks with remarks, "payments received". These SGL transfer forms were issued out of SGL account No.065 and the circumstances under which they were held back are not explained. The CBI has seized these SGL transfer forms for further investigation.

3.9 Funding of HSM through issue of BRs by UCO

(a) On 16 April 1991, UCO issued a BR No.110 to Corporation Bank showing sale of 11.5% GOI Loan 2010 of face value Rs.25 crores on behalf of the broker, HSM and credited the sale proceeds of Rs.26,00,89,431.89 received by pay order of Corporation Bank dated 16 April 1991, to his current account. Again on the same day, it showed a sale of the same class of security of face value Rs.10 crores to Corporation Bank and issued a BR No.112. The amount of Rs.10,40,55,772.56 received by pay order from Corporation Bank was also credited to HSM's current account. The BRs were returned by Corporation Bank on 4 May 1991 and instead of delivering any security, UCO refunded an amount of Rs.36,64,79,723.45 to Corporation Bank vide its cheque dated 4 May 1991 by debiting the broker's current account. Thus, UCO could arrange funds to the tune of Rs.36.41 crores for a period of 18 days @ 13 per cent per annum to the broker.

(b) Again on 16 April 1991, UCO issued a BR No.111 to SBI Mutual Fund showing sale of 9% HUDCO bonds of face value Rs.25 crores and the amount received for this from SBI by its cheque dated 16 April 1991 for Rs.25 crores was credited to HSM's current account on 16 April 1991. The BR was returned by the Fund on 20 April 1991 and an amount of Rs.25,09,31,627.05 (vide cheque for Rs.28,09,97,381.30 which included the above amount) was paid to it by debiting HSM's account on that day. The rate of interest in this case worked out to 34 per cent per annum.

(c) By merely exchanging BRs showing transactions in securities and entering into ready forward deals with counterparties, UCO had placed funds in the hands of the broker for short periods.

4. Current accounts of brokers

4.1 (a) The Bombay branch is maintaining current accounts of 19 brokers, the notable among them being HSM and M/s.V.B. Desai. The accounts are maintained mainly for the purpose of raising debits and credits thereon to account for purchases and sales of securities by the bank, on their behalf. The volume of operations in the current account of HSM was huge. The monthly turnover (debits and credits) during January - April 1991 in this account ranged between Rs.2,949.88 crores and Rs.5,593.98 crores. This had come down to almost "nil" by March 1992 after the transactions in securities on behalf of broker-clients were stopped by UCO. Later, the operations picked up in April 1992 when the switch deals on behalf of HSM were resumed. The account was, however, frozen by CBI in May 1992 and the balance therein transferred to Custodian, Special Court as per his instructions dated 9 November 1992.

(b) There are a large number of credits and debits for huge amounts to the brokers' accounts which are not supported by any transactions in securities undertaken on behalf of those brokers. They are mostly transfer of funds from one bank to another and one broker to another. The Bombay branch was in the habit of crediting to the accounts bankers cheques drawn in favour of UCO and brought in by the brokers, on the basis of written instructions in this regard from the concerned brokers.

4.2 Call money lending/borrowing by HSM through UCO

(a) On 5 August 1991 and 6 August 1991, two cheques for Rs.54 crores and Rs.75 crores, issued by SBS in favour of UCO were credited to the current account of HSM with UCO, under the instructions of HSM. On checking with counterparty bank, it was ascertained that the above amounts represented call money lendings by SBS to UCO at 9.5 per cent per annum interest. Likewise, on 5 July 1991 and 6 July 1991, UCO issued two cheques for Rs.34 crores and Rs.40 crores respectively in favour of SBS by debiting the amounts to the current account of HSM under his instructions. The above amounts had landed in SBS as call money borrowings by that bank from UCO at 36 per cent per annum. The amounts borrowed from SBS were repaid on 6 August 1991 and 7 August 1991 with interest by UCO by debit to HSM's current account. Further, the amounts borrowed by SBS from UCO were refunded by that bank on 8 August 1991 and UCO credited the amounts to HSM's current account. In the books of UCO, the transactions did not represent any call money operations but only transfer of funds from and to HSM. In the books of SBS, the amounts paid to UCO are shown as call money lendings and the amounts received from UCO are shown as call money borrowings.

(b) It may be mentioned that SBS had ostensibly lent call money to UCO but the funds had been used by the broker at low rates. The broker has also lent funds to SBS at high call rates.

4.3 Cheque purchase facility for M/s.V.B, Desai

On 31 March 1992, the Bombay (Hamam Street) branch purchased five cheques aggregating Rs.25 crores drawn in favour of the broker, M/s.V.B. Desai, by five companies in HSM Group, viz. Velvet Holdings (P) Ltd., Growmore Leasing and Investment (P) Ltd., Treasure Holdings (P) Ltd., Topaz Holdings (P) Ltd. and Zest Holdings (P) Ltd. and the amount of Rs.25 crores was credited to M/s. V.B. Desai's account with UCO. On the same day, an amount of Rs.24.90 crores, out of the above Rs.25 crores, was withdrawn by the broker for the purpose of payments to Canfina in respect of securities purchased by him from it. UCO recovered an amount of Rs.8.22 lakhs by way of interest at 60 per cent for two days. The above cheques were presented in clearing by UCO on 2 April 1992. The drawee bank viz. Grindlays Bank made the payment by debiting the current accounts of the five companies, resulting in overdrafts in the accounts with Grindlays Bank. These overdrafts were cleared on 3 April 1992 by crediting cheques issued by HSM in favour of these companies, out of his account with Grindlays Bank. UCO (Hamam Street branch) in its letter dated 2 April 1992 signed by Senior Manager and addressed to Zonal Office, Bombay has advised "as per the telephonic message received through Mr.Prabhu, AGM, Nariman Point branch and subsequent telephonic conversation with Mr.B. Roy Chowdhury, DGM we have purchased cheque for Rs.25 crores on account of M/s. V.B. Desai and received interest at the rate of 60 per cent for 2 days."

4.4 Crediting of cheques to HSM's account

(a) UCO credited the undernoted cheques drawn in its favour by Canara Bank (A/c.Canfina) into the current account of HSM as per his instructions. In the books of UCO, there were no underlying security deals in support of the receipt of the amounts. However, as per the books of Canfina, the cheques related to payments for securities purchased by Canfina from UCO. The details of cheques received and the transactions in the books of Canfina are given below :

(Rs. in crores)

Canfina's Cheque No. and date		Amount of cheque	Particulars of securities shown as having been purchased by Canfina from UCO (as per Canfina's books)		
			Security	Face value	Cost price
1.	077312 5.7.91	75.88	13% NPC bonds	25.00	25.54
			9% IRFC bonds	9.00	9.19
			9% PFC bonds	40.00	41.15
2.	077769 2.8.91	31.45	13% NTPC bonds	32.00	31.45
3.	077787 6.8.91	50.91	13% NTPC bonds	50.00)	10.30
				)	40.61
4.	077793 7.8.91	83.86	9% IRFC bonds	60.00	59.19
			-do-	25.00	24.67

In respect of purchases at items 1, 2 and 3 by Canfina, it received back three BRs issued by it earlier when the same securities were sold to UCO. However, the BRs in question were issued in favour of HSM instead of UCO and Canfina received back these BRs duly discharged by HSM himself. As regards the purchase of 9% IRFC bonds costing Rs.59.19 crores made by Canfina on 7 August 1991 (item 4 above) it received back its BR issued to UCO earlier on 6 August 1991 when the same security was sold to it. On 6 August 1991, UCO had issued a cheque No.956361 for Rs.60,07,89,041.10 in favour of Canfina by debiting the current account of HSM as per his instructions. As per the books of Canfina, the payment was against the Canfina's sale of 9% IRFC bonds of face value Rs.60 crores on 6 August 1991. This BR received back by Canfina on 7 August 1991 was having an endorsement on the reverse for having been discharged by UCO. The above amounts received from Canfina and credited to HSM's account were largely utilised by the broker for lending call money to/repaying call money borrowed from State Bank of Saurashtra as mentioned in para 4.2 earlier.

(b) UCO has received a cheque No.938287 dated 5 August 1991 for Rs.5,31,80,000 from BoM which was also credited to HSM's account. Likewise, it had issued a cheque No.954770 dated 6 July 1991 for Rs.5,30,20,000 in favour of BoM by debiting the current account of HSM. There are no security transactions relating to the above cheques in the books of UCO and the debit/credit to the current account of HSM as stated above are reported to have been done as per the broker's instructions. It was, however, ascertained from BoM that the above cheques represented payments relating to securities purchased from/sold to UCO by BoM. BoM had also issued a BR No.73/91 dated 6 July 1991 for Rs.5,30,20,000.00 evidencing sale of 40 lakhs Units to UCO and UCO discharged the same and returned it to BoM on 5 August 1991 showing repurchase of securities by BoM.

UCO has, however, explained that it was not a party to any of the transactions in securities mentioned above with Canfina or BoM and that it had not received/discharged any BRs as explained. The BRs issued to UCO by Canfina and BoM as stated above are reported to have been discharged by forging the signatures of an official of UCO Bank.

5. Procedural irregularities

5.1 The system followed by UCO in regard to transactions in securities was fraught with risk. There were no separate dealing and back-up sections and the same set of officers often issued SGL transfer forms and cheques and prepared the vouchers. In the case of purchases, the brokers brought the cost memos, SGL transfer forms and BRs from the counterparty banks and the bank handed over the bankers' cheques or pay orders drawn in favour of seller banks to the brokers. Similarly, in the case of sales, the brokers furnished pay orders or cheques of the counterparty banks in exchange of SGL transfer forms, cost memos etc. delivered to them by the Bombay (Hamam Street) branch.

5.2 In certain cases, the first leg of the ready forward transactions was done at rates which were not in alignment with market rates exposing the bank to price risk in the event of counterparty not reversing the transactions. In several cases, the SGL transfer forms issued by Bombay branch bounced from PDO due to insufficient balance in the SGL accounts. This was mainly on account of bouncing of SGL transfer forms received from other banks. The Bombay branch has no system of informing RBI of such bouncing of SGL transfer forms as required under RBI guidelines. In several cases, the SGL transfer forms and BRs in respect of Government securities received on purchases were discharged and returned on the reversal dates of ready forward transactions. In certain cases, financial transctions were done without exchange of SGL transfer forms or any other documents and the difference in the contract and delivery values in the deals was paid to brokers. The cheques drawn in favour of UCO were credited to the brokers' accounts in the case of sales made on their behalf and cheques were issued in favour of counterparty banks for purchases made for them. In certain cases crediting of cheques to HSM's account was done as per his written instructions but no instructions in this regard from cheques issuing banks were received.

5.3 The Bombay branch is not keeping proper records relating to security deals. 'Kutcha' registers intended for recording purchases and sales of securities are not properly written up and many transactions entered into as per Head Office telex/telephonic instructions are not entered in the register. The branch was not holding any contract notes since they are held at Head Office. The investment registers maintained at the Bombay branch are not posted on a day-to-day basis. The cost memos, delivery orders etc. are not arranged properly and some are not traceable. The SGL transfer forms are in stencil sheets and are not serially numbered. Many of them are issued under single signature. Many vouchers relating to security transactions as also those for transfer of funds from or to current accounts of brokers and issue of cheques on their behalf are not giving essential details. Many of the securities transactions on bank's investment account are routed through brokers' current accounts. The Bombay branch has not maintained BRs issued or BRs received registers.. The registers for SGL forms issued/received do not contain the particulars of credits and debits obtained from RBI. The credit and debit advices, objection memos etc. of RBI relating to SGL transactions are not properly filed/ not traceable. No reconciliation of SGL account intended for broker-clients has so far been done and the branch is not aware of the extent of client-wise holdings at any point of time.

XXI. General

As mentioned in the fourth Report, the Committee has confined its work to an examination of the findings of the scrutiny already undertaken by the RBI inspecting officers under the direction of the Committee and report thereon.

2. While the Committee has tried to cover all the banks/ institutions whose irregularities in securities transactions as in the opinion of the Committee should find a place in its Reports, it would like to mention about the following two noticeable omissions. In the case of Fairgrowth Financial Services Ltd. (FGFSL) which was one of the most important players in the securities market and whose links with Andhra Bank Financial Services Ltd. have revealed a large number of irregularities, though the Committee would have liked to comment on its operations in its Reports, it has not been able to do so as the enquiries have not been completed. Similarly, in case of State Bank of India (SBI), the Committee's findings in its first and second Reports were largely confined to the bank's investment portfolio and its transactions with National Housing Bank and its relations with broker Harshad S. Mehta and a detailed examination of its securities transactions has not been completed. In both the cases, the records have been seized by the CBI and access to such records has proved cumbersome and time consuming. As this Report could not be delayed any further, the Committee has reluctantly decided to issue this Report without the investigations in the securities transactions of SBI and FGFSL being completed.

3. Shri Y.H. Malegam is a partner in the firm of Chartered Accountants which has carried out the audit of the Bank of America's Indian branches for the year ended 31 March 1992. He has not, therefore, participated in the enquiry into the transactions of that bank or in the discussions of the Committee in respect thereof nor is he a party to items contained in the Report of the Committee as specifically referring to Bank of America.

4. Along with this Report, the Committee is also releasing its final Report containing an overview of the irregularities in securities transactions of banks and institutions and its final recommendations.

R.Janakiraman
Chairman

Y.H. Malegam — **V.G. Hegde**

C.P. Ramaswami — **E.N. Renison**

Vimala Visvanathan
Member-Secretary

BOMBAY
Date : 29th April 1993

Sixth & Final Report

April 1993

I. Introductory

The Committee was constituted on 30 April 1992 by the Governor, Reserve Bank of India (RBI) to investigate into the securities transactions of banks and financial institutions. The members of the Committee were Shri R.Janakiraman, Deputy Governor of the RBI as the Chairman and Shri Y.H. Malegam, Chartered Accountant and Shri V.G. Hegde, Principal Legal Adviser, RBI, as members and Kum.V. Visvanathan, Executive Director, RBI as Member-Secretary. Shri C.P. Ramaswami, Deputy Director, Income Tax (Investigation) and Shri E.N. Renison, retired Additional Director, Central Bureau of Investigation (CBI) were co-opted as members of the Committee on the basis of nominations made by the Income Tax Department and the CBI.

2. The terms of reference of the Committee were to :-

(a) enquire into the extent of non-compliance by banks and financial institutions with the guidelines of the RBI regarding securities transactions including transactions in PSU bonds, Units, etc.;

(b) enquire into the inadequacies in systems and procedures in force in these institutions generally and the extent of use of Bank Receipts (BRs) which have been in vogue in regard to the transactions in Government securities and other instruments;

(c) suggest such corrective steps as may be necessary to have a more efficient and accountable system in the future;

(d) examine and determine the extent of malpractices, if any, indulged in by officials of banks and financial institutions, where their funds have been allowed to be used for speculative transactions by brokers and other intermediaries and whether undue benefits have been thereby derived by brokers and others through unauthorised access to borrowed funds of the banks/ financial institutions and fix responsibility therefor and recommend the action to be taken; and

(e) scrutinise the procedure adopted by the Public Debt Offices (PDOs) of the RBI in regard to the maintenance of SGL accounts and other related matters and suggest remedial measures to tone up the responsiveness of the system.

3. The Committee's detailed findings are contained in the five Reports issued by it in May 1992, July 1992, August 1992, March 1993 and April 1993. This Report of the Committee summarises these findings on a global basis and offers its final recommendations.

II. Approach

The immediate need for the formation of the Committee was the information received by the RBI that there was a massive shortfall in the securities holding of the State Bank of India (SBI) and that a broker had been called upon to make good the shortfall as also the information that some banks were undertaking large-scale transactions in Government securities through the medium of brokers, which transactions were violative of RBI guidelines.

2. However, immediately after the Committee was constituted, it recognised that the malaise was far more widespread than was originally believed and it was necessary to quickly determine the size of the problem exposure of the banks and institutions (hereinafter collectively referred to as banks). It, therefore, arranged for a "round table" meeting of all the banks where BRs held by the banks could be tallied with the BRs admitted to have been issued by the corresponding banks. Simultaneously, banks were required to reconcile their investment portfolio with the securities, PDO balances, SGL transfer forms, and BRs held and issued by them.

3. The Committee also requested the officials of the RBI to carry out a detailed examination of the securities transactions of the banks with particular emphasis on the aspects covered by the Committee's terms of reference and provided guidance to the officers as regards the area and mode of enquiry. The reports of the officers were examined by the Committee and discussions held, where considered necessary, with individual officers. Based on this examination and discussions, the Committee, when required asked for additional examination.

4. Recognising the need for early remedial action, the Committee issued its first Report on 31 May 1992. This Report contained the Committee's preliminary findings, including its estimate of the probable problem exposure as also its preliminary

recommendations. The Committee understands action has already been taken by RBI on several of these preliminary recommendations.

5. The scrutiny of individual securities transactions of banks is an enormous task. During the period between 1 April 1991 and 23 May 1992 alone for which details were submitted by the banks, the total number of transactions recorded by them exceeded 87,000 in number. It was, therefore, decided to generally restrict the examination to transactions entered into by banks after 31 March 1991 even though there is evidence to show that the irregularities have also taken place in respect of transactions entered into before that date.

6. The total number of banks whose securities transactions have been examined is 180 consisting of 75 scheduled commercial banks, 10 subsidiaries of banks, 81 urban co-operative banks, the National Housing Bank and 13 non-bank financial companies. Of these, detailed findings have been reported in respect of 32 banks. In respect of 146 banks, either no irregularities have been observed or the irregularities observed are not significant enough to warrant separate mention in the Committee's Reports but the irregularities have been communicated by RBI to the banks for necessary action. In the case of two non-bank financial companies, the scrutiny is not yet complete.

7. In its work, the Committee has tried to trace the transactions as between different banks by simultaneously examining the transaction in the records of both counterparties. It has also examined the bank accounts of the major brokers involved in the transactions with a view to analysing the receipt and disbursement of funds. It has, however, been hampered in this examination by the fact that it has no access to the brokers' books of account nor has it the power to call and examine these brokers or third parties.

8. The Committee noted that even while it was carrying on its examination, simultaneous investigations were in progress by the CBI and the Income Tax Department. While the Committee's powers were restricted to an examination of the records and officers of banks, these agencies had much wider powers including the power to conduct raids and carry out searches as also to examine persons other than banks and their officers. They also had powers to prosecute offenders. In August 1992, a Joint Parliamentary Committee (JPC) with very wide powers was also appointed. The Committee, therefore, decided that its primary role should be to identify the irregularities as revealed by its examination of the records of the banks and through its Reports, which were being made public, to bring them to the attention of these other agencies who would examine the transactions in greater detail, if necessary by co-ordinating this information with the other information obtained by such agencies through raids, searches and interrogation of bank officials as also non-bank persons.

9. While the appointment of these different agencies was necessary it has to be recognised that the involvement of these several agencies has to some extent hampered the work of the Committee. This was unavoidable as all these agencies needed to draw, among others, on the resources of the departments of RBI dealing with this work and have access to the same records and individuals in banks. In many cases, the records of the banks are in the custody of some of these agencies and access to such records by the Committee has proved difficult and time-consuming.

III. Environment

To understand the nature and extent of the irregularities in the securities transactions of banks, it is necessary to understand the environment in which these irregularities took place. The significant features of this environment are given in subsequent paragraphs.

2. (a) There were large investible funds with the corporate sector, particularly with Public Sector Units (PSUs). With the gradual withdrawal of budgetary support from the Government, the PSUs alone raised Rs.20,700 crores by the issue of bonds between 1 April 1986 and 31 March 1992.

(b) The large public issues made by the PSUs did not find a ready market. These PSUs therefore made arrangements with banks whereby the banks subscribed for a significant part of the issues and in turn, the PSUs placed the funds raised by the issues with the banks who subscribed to the issues. For example, Canfina subscribed to PSU bonds on 10 occasions during 1991-92 for an aggregate amount of Rs.2182.18 crores on private placement basis, and of this, Rs.2122.80 crores was placed with it by the PSUs. UCO Bank had subscribed an amount of Rs.150 crores to Power Finance Corporation (PFC) bonds in March 1992, which was placed by PFC with UCO Bank for portfolio management.

(c) As many of the bonds issued by PSUs were tax free, they along with Units under the Unit-64 Scheme of the Unit Trust of India (UTI), which also provided tax benefits under Section 80M of the Income Tax Act, were mainly held by corporate entities including banks. Thus, as on 30 June 1992, the total funds invested by banks alone both on their own account and on behalf of PMS clients in PSU bonds and Units aggregated to almost Rs.11,583 crores (face value).

(d) However, while these large investible funds were available with the corporate sector, the opportunities for short-term investment of these funds were restricted. There did not exist a significant money market in which these funds could be invested and the call money market was restricted to banks and specified financial institutions.

(e) While companies in the private sector could invest in inter-corporate deposits, these were perceived as a risky form of investment for large amounts. PSUs were generally prohibited by administrative guidelines from investing in inter-corporate deposits. For deposits with banks there were ceilings on the rates of interest which varied according to monetary policy, the maximum rate of interest which banks were allowed to pay being 13 per cent since April 1992 on deposits beyond 46 days and up to three years or more. Though the ceiling on interest rates did not apply to Certificates of Deposit (CDs) issued by banks, each deposit had to be for a minimum value of Rs.1 crore (lowered to Rs.50 lakhs in 1990) and there was a monetary ceiling on the aggregate amount of CDs which could be issued by a bank.

(f) On the other hand, the stock market was booming. The sensitive index of the Bombay Stock Exchange had risen from 956.11 on 25 January 1991 to 4467.32 on 22 April 1992 and the average 'badla rates' at which stock brokers borrowed funds had during that period ranged from 7.8 per cent to 59.1 per cent.

(g) Banks, particularly the foreign banks, were, therefore, quick to identify 'arbitrage' opportunities whereby funds could be borrowed cheap and lent dear.

3. To exploit these arbitrage opportunities, banks needed to circumvent existing regulations. The most significant of these regulations were as under :-

(a) As mentioned above, banks were not permitted to offer rates of interest which were in excess of the stipulated rates. On the other hand, PSUs needed to service the bonds issued and therefore, needed a return on the funds placed with the banks at a rate higher than the coupon rate on the bonds.

(b) Banks were required to maintain a significant portion of their deposits in cash or in specified securities or with RBI. During most of the relevant time, the Cash Reserve Ratio (CRR) was 25 per cent of the incremental deposits and the Statutory Liquidity Ratio (SLR) was 38.5 per cent of the deposits. Thus, 63.5 per cent of the deposits earned either no interest or interest which was considerably lower than the market rates and only 36.5 per cent of the deposits was available for commercial lending. Even out of this, almost 40 per cent in respect of nationalised banks and private sector banks and a lower percentage for foreign banks was required to be lent to the priority sector earning only a concessional rate of interest.

(c) Banks were required to maintain reserve requirements (CRR and SLR) on call and notice money borrowings, which added significantly to the cost of borrowing such funds.

(d) Banks were permitted to accept funds from the corporate sector under Portfolio Management Schemes (PMS) where the depositor could earn higher returns but the acceptance of these funds was subject to the following restrictions :

(i) there was a minimum 'lock-in' period of one year;

(ii) the bank was to act as an agent of the depositor to make investments on his behalf and the risk of the investment was to remain with the depositor; and

(iii) the bank could not share in the profits or losses made by the depositor out of the investment of the funds and could only charge a fee (fixed or as a percentage).

(e) Banks could enter into ready forward transactions in securities only with other banks and only in respect of Government and other approved securities.

(f) The yield on banks' investments in Government securities under the SLR prescription was much below the prevailing market rates on long-term debt instruments, and banks felt the need to improve the yield both through trading in these securities (at artificial rates) and through the mechanism of ready forward transactions.

4. BRs were being used on a greatly extended scale for the following reasons :-

(a) In respect of sale and purchase transactions in Government securities, normally the sale would be supported by delivery of SGL transfer forms. These are orders issued on the PDO to transfer the securities from the account of the seller to the account of the purchaser. However, the incidence of dishonour of SGL transfer forms had increased due to a number of reasons. The PDO records were maintained manually and on some occasions there was delay in intimating the fact of dishonour. Therefore, for ready forward transactions, banks increasingly resorted to the issue of BRs rather than SGL transfer forms

(b) SGL account facilities in the PDOs were granted region-wise. Thus, if the securities were held in the SGL account with one regional PDO and the sale was made in another region, it was not possible to issue an SGL transfer form without first transferring the securities from one PDO to the other. Although the transfers could be effected by telegram/telex, in these circumstances a BR needed to be issued even for transactions in Government securities.

(c) SGL facilities were restricted to Government securities. For purchase and sale of other securities, e.g. Units or PSU bonds, it was necessary to effect physical delivery of the bonds, along with transfer forms. In many cases of PSU bonds, the actual issue of scrips was delayed for several years and the holders' evidence of ownership was only an 'allotment letter'. The seller therefore, could not make delivery of part of the bonds covered by the 'allotment letter' until the scrips were issued. Even where bonds were available, exact delivery could not be made if the scrips were not available in denominations which permitted exact delivery. Finally, for large transactions, physical delivery could be cumbersome in respect of ready forward transactions which were intended to be reversed within a short period of time. Therefore, in all such cases BRs were increasingly resorted to.

5. Thus the stage was set for an era of irregular dealings in money disguised as securities transactions. There was a triple coincidence of wants; first, the PSUs who, after the withdrawal of the Government budgetary support, had to raise funds massively in the market and had short term liquidity on their hands, wanted an avenue of investment yielding more than the coupon rate on the bonds they had issued. Secondly, the stock market was booming and the 'bulls' desperately needed funds to finance their overbought positions, never mind the high badla rates. Thirdly, bankers who had accepted high cost funds from PSUs saw that the only avenue which yielded the anticipated high returns was financing the stock brokers in a booming market. What was needed was to devise some 'innovative' techniques to circumvent the regulations.

6. To circumvent the regulations, banks needed the assistance of brokers and therefore a close nexus had developed between certain brokers and certain banks. This was aggravated by the fact that operating managers were under pressure to greatly increase the profitability of banks. While in the case of foreign banks this arose out of the growth of intense competition, in the case of nationalised banks, there was a growing awareness that their overall performance compared very unfavourably with the performance of foreign banks and steps were needed to improve the 'bottom line' of their published results.

IV. Findings

The examination of the securities transactions of the different banks has revealed a fairly consistent pattern of irregularities in most of the banks with local variants. It is also evident that these irregularities have largely arisen out of attempts to circumvent RBI regulations.

2. The main source of funds for the irregular transactions has been the corporate sector and particularly the PSUs. These bodies were unable to place their funds with banks in the form of deposits because of the ceiling on interest rates. The device used to circumvent this regulation was therefore the PMS and allied schemes.

3. There were two broad schemes which were used :-

(a) Under the PMS, funds were placed by the corporate sector with banks and their merchant banking subsidiaries with a lock-in period of one year. However, contrary to the RBI regulations, there was an understanding with the clients to give them an assured rate of return though the documentation showed that the investment was at the clients' risk.

(b) Under a second set of schemes [for example "Corporate Cash Deployment Service Scheme" (CCDS) in the case of Standard Chartered Bank (Stanchart)], the banks received funds from the corporate sector in the form of proceeds of securities sold to customers which securities were repurchased from the customer after a specified period at a rate which gave to the customer a specified rate of return.

4. The magnitude of the funds made available under these schemes can be seen from the summary table at the bottom of this page.

The figures of aggregate funds accepted are both for PMS and the other schemes. Whereas PMS has a lock-in period of one year, under other schemes the same funds may have been rolled over and therefore, the figures may be inflated. However, the figures of funds outstanding on 30 June 1992 show that two banks alone, namely Canfina and Citibank, accounted for almost 60 per cent of the outstanding amounts.

5. (a) The table on the next page gives the composition of the investments made out of PMS and other schemes funds and outstanding as on 31 December 1991 and 30 June 1992. The aggregate figure does not exactly tally

(Rs. in crores)

Name of the bank	Aggregate funds accepted 1.1.1991 to 31.12.1991	Aggregate funds accepted 1.1.1992 to 30.6.1992	Funds outstanding as on 30.6.1992	Percentage
Canbank Financial Services Ltd.	7282.34	7638.81	2095.20	36.46
Stanchart	4259.61	9201.99	166.81	2.90
Hongkong Bank	1559.10	792.85	90.38	1.57
Andhra Bank Financial Services Ltd.	1135.91	1569.23	506.79	8.82
Citibank	843.06	676.97	1334.59	23.22
BOI Finance	517.72	641.85	195.90	3.41
Indbank Merchant Banking Services Ltd.	505.70	489.60	489.60	8.52
Others	619.54	942.68	867.43	15.10
	16722.98	21953.98	5746.70	100.00

with the aggregate figures given in paragraph 4 above because the figure is inclusive of profit or loss in the portfolio.

(Rs.in crores)

	As on 31.12.1991 Amount	Per-centage	As on30.6.1992 Amount	Per-centage
Government securities	66.74	1.13	11.50	0.20
PSU bonds	2734.74	46.21	1327.98	23.07
Company shares and debentures	736.43	12.44	1365.70	23.72
UTI and Mutual Fund Units	1172.76	19.82	1998.01	34.70
Others	1105.89	18.69	927.79	16.12
Undeployed	101.16	1.71	126.23	2.19
	5917.72	100.00	5757.21	100.00

(b) It will be seen that as much as 66.03 per cent on 31 December 1991 and 57.77 per cent on 30 June 1992 was invested in PSU bonds and Units. The investment in PSU bonds alone on 30 June 1992 was Rs.1328 crores. The aggregate value at acquisition ccst of PSU bonds held by the banks as part of their own portfolio and in PMS and other schemes was Rs.10,681 crores (face value Rs.11,583 crores). The Nadkarni Committee on "Trading in public sector bonds and units of mutual funds" has estimated the aggregate face value of PSU bonds issued between 1986-87 and March 1992 and outstanding; at Rs.20,550 crores. Therefore, 56.36 per cent of all PSU bonds issued and outstanding were held by banks both on their own account and on PMS account. On a rough estimate there is a depreciation of about Rs.804 crores (i.e. 7.5 per cent) in the value of bonds held by banks in their own account and in PMS and other schemes.

(c) The Committee believes that due to this large concentration and due to a lack of demand, banks have found it difficult to sell these bonds and return the funds to PMS clients on the termination of the 'lock-in' period in respect of PMS and the reversal date for other schemes.

6. A number of irregularities developed in the operations of the PMS schemes. Some of these are explained below :-

(a) There was a clear difference in perception between the customer who placed funds with the bank and the bank itself. The former believed that the PMS and other similar schemes were "deposit substitutes" though the mode of operations and documentation were designed to circumvent RBI guidelines (which was perceived as no concern of the customer). The bank contended, to protect itself against the charge of a violation of RBI guidelines, that it acted only as an agent of the customer and that all transactions were at customers' risk. This difference in perception was deliberately encouraged by the banks which quoted to the customer an 'indicated' rate of return on his funds.

(b) In many cases, no details were furnished to the customer of the operations in the PMS account beyond a year-end statement.

(c) The funds collected under PMS and similar schemes were made available to brokers under ready forward transactions. Though such contracts were violative of RBI guidelines, banks (e.g. Citibank) have claimed that the RBI guidelines did not apply to transactions on behalf of PMS clients.

(d) Under the PMS, the bank presumably was acting as the agent of the customer. Therefore, all investments made by the bank under the PMS were in fact investments made by the customer and should be within the provisions of the law applicable to the customer, for example, whether the client could invest in shares. No attempt was made to see whether these provisions were observed.

(e) There is evidence to show that when the actual earning in PMS accounts was substantially higher than the indicated rate of return, transactions were made in PMS accounts at artificial rates to siphon off the excess earnings and retain earnings close to the indicated rates. Major instances noticed have been given in the Reports of the Committee containing the detailed findings.

(f) There is also evidence (e.g. in Citibank) to show that where composite sales were made of securities held partly in PMS accounts and partly in the bank's own investment portfolio, sale proceeds were credited to PMS accounts at rates which were lower than the composite sale rate and credited to the bank's own investment account at rates which were higher than the composite sale rate. Thus, an excess profit for the bank was recorded at the cost of PMS clients.

(g) In some cases (e.g. Citibank) customers' Units were 'loaned' to the banks. The bank thereafter presumably purchased the Units and deposited the sale proceeds in PMS accounts. The funds so placed were operated upon by the banks to make ready forward transactions in securities, and at the 'accounting-year end' of the customer and also the maturity of the 'loan', the PMS funds presumably remained invested in the original Units. At all times the Units remained in the name of the customer who received the dividend. For this 'loaning' the bank generated a return to the customer of not less than 1 per cent of the face value of the securities. However, a substantial portion of the income in the PMS account was siphoned off to the credit of the bank. The total amount of funds so generated on PMS account by Citibank was Rs.411.21 crores.

7. A number of irregularities have also taken place in respect of schemes which were designed to circumvent the rigours of the PMS. For example :-

(a) RBI guidelines did not permit banks to enter into ready forward transactions with parties other than banks and also did not permit such transactions to be entered into in respect of securities other than Government and other approved securities. All banks which had such schemes obviously violated both these guidelines.

(b) In most cases, there is no evidence to show that securities which were presumed to have been sold and for which sale proceeds were received by the bank, were in fact delivered or even separately kept in trust for the clients.

(c) In some cases (e.g. Andhra Bank Financial Services Ltd.) there are instances where at the time of alleged sale of securities, even the securities were not identified in the security receipts issued.

8. The major banks which have operated these schemes and violated RBI regulations were : -

Standard Chartered Bank
Canbank Financial Services Ltd.
Citibank N.A.
Andhra Bank Financial Services Ltd.
ANZ Grindlays Bank p.l.c.
Syndicate Bank
Vijaya Bank
Bank of America
Hongkong and Shanghai Banking Corporation Ltd.

9. (a) The funds collected by banks as also their own funds could be lent to brokers only in accordance with RBI guidelines. To circumvent these guidelines, the funds were lent in the guise of ready forward transactions. As mentioned above, ready forward transactions could be entered into only with banks and only in respect of Government securities. To circumvent the first stipulation, transactions were recorded as made with counterparty banks but the beneficiaries of these transactions were certain brokers. To accomplish this, certain banks acted as 'routing' banks for brokers.

(b) The 'routing' banks purchased securities in their own name and sold securities in their own name without indicating that they were acting for the brokers. Where securities were not readily available, they even issued their own BRs. The cost of the purchase was debited to the broker's account and the sale proceeds were credited to the broker's account.

The major 'routing' banks and the brokers for whom they acted are as under:

Bank	Brokers
Andhra Bank	i) Hiten P. Dalal ii) Batliwala & Karani iii) M/s.V.B. Desai iv) N.K. Aggarwala & Co. v) Mukesh Babu
Bank of Karad Ltd.	i) A.D. Narottam ii) Excel & Co. iii)Bhupen Champaklal Devidas iv) Darashaw and Co.
State Bank of India	Harshad S. Mehta.
UCO Bank	Harshad S. Mehta
State Bank of Saurashtra	Harshad S. Mehta
Bank of Madura	Chandrakala & Co.
Karnataka Bank Syndicate Bank	} Fairgrowth Financial } Services Ltd. and } } Fairgrowth Investments Ltd.
Vijaya Bank	Kotak Mahindra Finance Ltd. and Komaf Financial Services Ltd.

10. Brokers also arranged contracts with banks where the name of a bank was given as a counterparty selling bank without the knowledge of the bank concerned. The proceeds received from the purchasing bank in the form of bankers' cheques in the name of the alleged counterparty bank were credited by that bank to the broker's account by virtue of an existing arrangement. Thus, the purchasing bank was unaware that it was in fact dealing with a broker and not with a counterparty bank. When delivery was not effected for securities for which payments had been made, liability was denied by the bank whose name was shown as the counterparty bank. A significant part of the problem exposure has arisen on this account. Some of the brokers and the banks with whom they had such arrangements were as under :

Broker	Bank
Harshad S. Mehta	State Bank of India State Bank of Saurashtra UCO Bank ANZ Grindlays Bank
Hiten P. Dalal	Andhra Bank
N.K. Aggarwala & Co.	Hongkong & Shanghai Banking Corporation Ltd.

11. The role of a broker is to act as an intermediary between the purchasing bank and the selling bank. However, in a large number of cases, brokers started dealing on their own account. This is reflected in the fact that there were wide variations between the rates at which the transactions were recorded by the purchasing bank and the rates at which the transactions were recorded by the selling bank and the difference in rates running sometimes into crores of rupees were recovered from or paid to brokers. Major instances have been noticed in the following banks :

Bank	Broker
Canfina	Hiten P. Dalal C.Mackertich Rahul & Co.
Citibank	A.D. Narottam B.S. Gandhi
Bank of America	A.D. Narottam Hiten P. Dalal B.S. Gandhi Bhupen Champaklal Devidas Syndicate Bank Kishore Narottamdas Amarchand
Standard Chartered Bank	Hiten P. Dalal
Hongkong and Shanghai Banking Corporation Ltd.	N.K. Aggarwala & Co.

Bank of Madura Ltd.	Chandrakala & Co.
Bank of Karad Ltd.	A.D. Narottam Excel & Co.

12. There is evidence to show that in many cases, banks have carried brokers' positions, that is, they have entered into informal contracts where the risk is carried by the broker but the bank has used its own investment portfolio and invested its own funds and for which service it has been given a fixed rate of return. The most blatant case is the arrangement between Stanchart and broker Hiten P. Dalal whereby Stanchart made available its funds and securities to earn a guaranteed return of 15 per cent on the funds invested.

13. The rates at which transactions in the same securities on the same date have been recorded by different banks have significantly varied and even in respect of the same bank, transactions in the same securities on the same date have been at different rates. It is obvious that in many cases, artificial rates have been used to record transactions for the following reasons :-

(a) There are no official quotations for Units or for PSU bonds.

(b) Where a ready forward transaction is made, the difference between the purchase rate and sale rate reflects the agreed return on the use of funds and necessarily therefore, either the purchase or the sale must be at a rate different from the real value of the security.

(c) There are several transactions which are artificial transactions. For example:

(i) Where differences are payable to or recoverable from a broker, the difference is accounted for by a purchase and sale transaction recorded on the same day but with a difference between the purchase and sale rates.

(ii) Where profits are to be credited to or taken away from PMS clients, there would be a purchase or sale in the PMS account at a rate which is different from the true rate.

(iii) Where for tax or other reasons, it is desired to change the holding rate of a security, cross-transactions are made between the same counterparties at desired rates which may be different from the true rates. One of the important motivations for doing this was the method by which SLR requirements were calculated. For the purpose of SLR the investments are to be valued at cost or face value whichever is lower. Therefore, through a series of related transactions, e.g. double ready forward transactions between banks, the holding cost of both securities would be raised, with consequent benefit in the calculation of SLR positions of both the banks.

14. To give effect to these complex arrangements to account for differences with brokers or PMS clients as also to adjust holding values, a number of artificial transactions have been recorded by the banks with or without the connivance of brokers and in most cases without the actual transfer of securities. Some of the most blatant instances noticed have been in the case of Stanchart and Citibank.

15. (a) A very large proportion of the transactions entered into by the banks have been ready forward and double ready forward transactions. In a ready forward transaction there is a present purchase or a present sale of a security tied with a forward sale or a forward purchase of the same security with the same counterparty. The purpose behind the transaction is not to buy or sell the security but to temporarily create finance by selling the security which finance is repaid when the sale is reversed in the second leg of the transaction. In a double ready forward transaction, two securities are simultaneously bought and sold on a ready forward basis. The purpose behind such a transaction is not to create liquidity but rather to temporarily exchange the investment portfolios and in the process alter the holding rates of the securities.

(b) It is believed that some leading brokers were speculating heavily on the possibility of a hike in the coupon rates on Government securities. As such a hike would lead to a reduction in market rates of the securities, they had short-sold these securities, mainly 11.5% GOI Loan 2010. When the hike did not materialise for some time, the brokers were unable to liquidate their positions. It is possible that a number of ready forward and double ready forward deals in such securities were designed to enable the brokers to carry forward their positions till the hike materialised.

(c) As mentioned earlier, banks were permitted to enter into ready forward transactions only in SLR securities (i.e. investments in which SLR requirements had to be maintained) and secondly, such transactions could be entered into only with other banks. In almost all cases, banks have violated the first regulation and have entered into ready forward transactions in respect of non-SLR securities like Units and PSU bonds. Some of the banks have also violated the second regulation and have sought to camouflage this violation by ingenious means. Thus, in the case of Bank of America (BoA) there were a number of transactions known as "Off the Books" deals. Under these deals, BoA accepted funds from customers at pre-determined rates of return for specific periods. These were recorded as spot sales of securities, mainly PSU bonds and Units, to the customers. Simultaneously a forward purchase of the same securities and for the same amount was recorded with a counterparty bank, in most cases, Canbank Financial Services Ltd. (Canfina) or UCO Bank. These were in fact dummy deals. On the maturity of the deposit, the funds were returned to the customer by recording a re-purchase of the security and the dummy forward purchase was reversed.

(d) Normally, even in a ready forward transaction, each leg of the transaction should be accompanied by actual delivery of securities or SGL transfer forms. However, in most cases, there is no evidence to show that actual delivery of securities or SGL transfer forms was effected but on the contrary, there is evidence to suggest that BRs were issued and the same BRs were returned on reversal of the transaction. In many cases where SGL transfer forms were issued, there was apparently a tacit understanding between the parties not to present the SGL transfer forms at the PDO but to return them to the seller on the reversal of the ready forward deal. In a number of cases this raises a doubt whether underlying securities for the transaction existed at all. It will be appreciated that the ready forward transaction was in essence a financing transaction and if this transaction was not supported by underlying securities, the transaction was no more than an unsecured loan of funds.

16. (a) The BR is intended to be a document which acknowledges receipt of funds for the sale of a security and which confirms that the issuer has undertaken to deliver the specified securities to the purchaser and pending such delivery is holding the securities in trust for the purchaser. Indian Banks' Association (IBA) had prescribed a standard format for the BR and also prescribed BR rules and a format for a monthly statement of BRs held and issued. These formats and rules were notified to the Chief Executives of all member banks vide IBA letter dated 6 May 1991. A copy of this letter and its enclosures are given in the Annexure to the first Report of the Committee issued in May 1992.

(b) These rules inter alia provided that :-

(i) The BR should be issued only in the prescribed form.

(ii) Normally no BR should be issued where SGL facility is available.

(iii) A separate BR should be issued for each type of security.

(iv) The BR is non-transferable.

(v) BRs should be issued serially numbered on security paper.

(vi) BRs must be exchanged with actual scrips as early as possible and in any case within 90 days of issue.

(vii) BRs should be signed by two authorised signatories whose signatures should be registered with the buyer bank to verify the signatures.

(viii) BRs could be accepted by purchasing banks only if they were issued by the following institutions -

- All member banks of IBA

- All-India financial institutions like IDBI, IFCI, ICICI, NABARD, UTI, GIC, LIC

- Public sector undertakings

- Other institutions specified by IBA/RBI.

(c) In most banks the IBA guidelines were observed only in their breach. In particular, BRs were not issued on security paper or in the prescribed form and more significantly were not exchanged with actual scrips but were returned for cancellation on reversal of the original transactions or even against independent transactions of equivalent value. There are several instances where BRs were treated as negotiable instruments and transferred by endorsement and even instances when in support of purchases, BRs issued not by counterparty banks but by 'third parties' were accepted.

17. The fact that funding transactions of banks increasingly took the guise of securities transactions is evident from the sharp increase which took place in the investment income of banks as shown below for some of the major banks :

Bank	**Investment Income (Rs.in crores)**	
	1990-1991	**1991-1992**
i) ANZ Grindlays Bank p.l.c.	92.34	144.94
ii) Citibank N.A.	50.38	128.27
iii) Standard Chartered Bank	43.93	81.24
iv) Hongkong & Shanghai Banking Corporation Ltd.	39.41	58.83
v) Bank of America	22.91	66.94
vi) ABN Amro Bank N.V.	5.75	12.68
vii) State Bank of India	1854.71	2028.50
viii) Punjab National Bank	520.56	645.44
ix) Bank of India	452.74	530.46
x) Canara Bank	439.18	504.08
xi) Bank of Baroda	381.58	453.55
xii) Union Bank of India	255.37	305.33
xiii) Oriental Bank of Commerce	104.35	125.90
xiv) Corporation Bank	60.99	77.91
xv) The Federal Bank Ltd.	27.90	38.51
xvi) The Bank of Rajasthan Ltd.	26.94	33.80
xvii) The United Western Bank Ltd.	16.13	20.51
xviii) Bank of Madura Ltd.	14.49	17.96

18. On 26 July 1991, Shri A.Ghosh, Deputy Governor, RBI wrote to the Chairmen/Chief Executives of all commercial banks expressing great concern at the fact that certain banks had engaged in types of transactions in securities which were prohibited. This letter is given in the Annexure to the first Report of the Committee issued in May 1992. This letter specifically stated that banks were not permitted to hold an oversold position in any security. There is evidence to show that this regulation was violated in many cases. Some of the banks where large oversold positions were noticed and mentioned in the detailed findings given in earlier Reports of the Committee are Citibank, Canfina and Bank of America.

19. (a) There was a close nexus between certain brokers and certain banks which enabled the brokers to have unauthorised access to funds as also undertake unauthorised transactions to their advantage.

(b) Broker Harshad S. Mehta (HSM) had a strong nexus with the State Bank of India (SBI) and some of its subsidiary banks like State Bank of Saurashtra as also with its merchant banking subsidiary, SBI Capital Markets Ltd. (SBI Caps). During the period from 1 April 1991 to 31 March 1992, the value of SBI's transactions in Government securities aggregated Rs. 48,562 crores and of these, transactions of an aggregate value of Rs.17,300 crores (i.e. 35.6 per cent) were booked through HSM alone. Similarly in the case of SBI Caps, out of 643 contracts between 1 December 1991 and 31 March 1992, 152 contracts (i.e. 23.64 per cent) were booked through HSM alone. In many cases, though these banks were named as counterparties by other banks, in fact the transactions were actually on HSM's own account and payments and receipts were debited and credited to HSM's account with SBI. Even the SGL account of SBI with the PDO was operated by SBI virtually as if it was HSM's own investment account in the PDO. Finally, in many cases, SGL transfer forms and BRs appear to have been issued by SBI at the behest of HSM and for his benefit.

(c) HSM also appears to have had a similar nexus with the National Housing Bank (NHB), ANZ Grindlays Bank (Grindlays Bank) and UCO Bank. In the case of NHB, a large number of transactions were at the behest of HSM entered into on a "back to back" basis. Between July 1991 and April 1992 there were

12 such ready forward deals in Government securities for an aggregate value of Rs.653.06 crores. In many of these deals, no securities or SGL transfer forms were received by NHB and though the deals are recorded as being with SBI, in fact the amounts paid by NHB have been credited to HSM's account with SBI. Similarly, in respect of 15 contracts for an aggregate value of Rs.511.66 crores recorded by NHB as being with Grindlays Bank, the payments of Rs.489.75 crores made by NHB have in fact been credited to HSM's account in Grindlays Bank. In the case of UCO Bank, HSM has been financed through the purchase of accommodation bills. In one case alone, referred to in the first Report of the Committee, UCO Bank purchased for the benefit of HSM, accommodation bills of Rs.49.42 crores and later provided funds to HSM to retire the bills by purchasing shares for a total consideration of Rs.49.50 crores.

(d) Broker Hiten P. Dalal (HPD) had a close nexus with Stanchart and with Citibank and through broker A.D. Narottam (ADN) with the Bank of Karad Ltd. (BoK) and Metropolitan Co-operative Bank Ltd. (MCB). A large volume of Stanchart's transactions have been with or through HPD. These transactions have been under an arrangement whereby, in order to obtain a guaranteed return from HPD on its investments, Stanchart has in fact totally surrendered to HPD its discretion regarding dealings in securities and has acted entirely under the direction of HPD. It has also used its own funds to actually carry the broker's position in forward contracts. There is also evidence to show that on occasions, when Stanchart's dealers had made huge losses in dealing on Stanchart's account, HPD has bailed out the dealers by absorbing some of the losses. Though the transactions of BoK and MCB have largely been on account of ADN, there is sufficient evidence to show that the beneficiary of these transactions has been HPD. A large number of transactions of Citibank have been through HPD. Many of these transactions were with Andhra Bank and the real counterparty in these transactions was HPD. There is evidence to suggest that Citibank was aware of this position. There are also a number of transactions entered into by Citibank with BoK and other counterparty banks where there are significant differences between the rates at which the contracts were recorded by Citibank and the rates at which the contracts were recorded by the counterparty banks. Most of these contracts have been put through by HPD and the differences have been paid out of ADN's account with BoK.

(e) There also appears to have been a nexus between brokers Stewart and Co. and C. Mackertich (both of whom are inter-connected) and Citibank. Thus, in a series of transactions for the sale and purchase of GIC Rise I and Rise II units, on or around the same dates (referred to in the third Report of the Committee) these brokers earned profits of Rs.31.38 crores and Rs.54.88 crores respectively without any investment of funds. They were also the brokers, whose associate concern M/s.Y.S.N. Shares and Securities was involved in a deal whereby Allahabad Bank, under a prior arrangement with the broker, bid for and acquired two bundles of shares of PSUs and sold the bundles to the broker who in turn sold one of the bundles to Citibank for one of its fiduciary clients.

(f) Brokers HPD and C.Mackertich also had a nexus with Canfina. A number of controversial transactions of Canfina referred to in the second Report of the Committee have been entered into through these brokers.

(g) Brokers M/s.V.B. Desai and HSM also had a nexus with Allbank Finance Ltd. (AFL), a wholly-owned subsidiary of Allahabad Bank. As reported in the second Report of the Committee, the amounts collected as inter-corporate deposits by AFL have been made available to these brokers through ready forward deals.

(h) Broker N.K. Aggarwala & Co. (NKA) had a nexus with Hongkong and Shanghai Banking Corporation Ltd. Between 1 April 1991 and 31 May 1992, the New Delhi branch of Hongkong Bank entered into 416 transactions through brokers for an aggregate value of Rs.4390.94 crores. Of these, 71.63 per cent in number and 80.11 per cent in value were through NKA. Pay orders drawn in favour of Hongkong Bank have been credited to NKA's account and there are a number of instances where transactions recorded as being with other counterparties have in fact been with NKA.

20. Apart from the nexus between brokers and banks, there was a nexus between different banks whereby one bank would be used as a source of funds and the

other bank was used as a disburser of the funds. Most of the funds were obtained from PSUs, possibly through the intervention of brokers, who in turn were the beneficiaries of the funds disbursed. Such a nexus can be seen between Vijaya Bank and Citibank and between Andhra Bank Financial Services Ltd. (ABFSL) and Fairgrowth Financial Services Ltd. (FGFSL). In the former case, most of the PMS funds collected by Vijaya Bank were made available to Citibank. In the latter case, almost all the funds collected by ABFSL were made available to FGFSL or to broker HPD. In fact, even before ABFSL was formed and started functioning, Andhra Bank and FGFSL appear to have agreed that ABFSL would merely act as a conduit for the diversion of funds from PSUs to FGFSL.

21. (a) A key element in the perpetration of the irregularities was the BR. As mentioned earlier, the guidelines for the issue of BRs laid down by the IBA were observed more in their breach. In fact, the RBI circular of 26 July 1991 referred to earlier specifically prohibits banks from issuing BRs on behalf of their constituents including brokers. It also enjoins on banks to be circumspect while acting as agents of their broker clients while carrying out transactions in securities on behalf of brokers.

(b) Moreover, arising out of the close nexus between the brokers and the banks, BRs were used to generate transactions which had no security backing. Thus, the guise of security transactions was given to what were in fact pure financing transactions without even the backing of an underlying security. In many cases (e.g. in the case of SBI), by omission or perhaps by design no record was maintained of BRs issued. In other cases there is clear evidence to show that BRs supported by BRs were issued at the request of brokers. The third Report of the Committee lists a number of cases where BRs were so issued by BoK and MCB at the behest of broker ADN and for the benefit of brokers HPD and other brokers. Similarly, BRs appear to have been issued by SBI for the benefit of broker HSM.

(c) As has already been pointed out BRs were almost used as negotiable instruments and transferred from bank to bank and 'third party' BRs were accepted by banks.

(d) These lax practices gave considerable scope to banks and brokers to indulge in a number of irregularities in the guise of securities transactions. The indiscriminate use of BRs without security backing created a kind of paper money which circulated from bank to bank like a stage army of soldiers and provided an opportunity to brokers to avail of funds of increasingly larger amounts.

22. (a) A second key element in the perpetration of the irregularities was the complete breakdown of internal control in a number of banks.

(b) It is an essential element of internal control in securities transactions that there should be a clear segregation between the front office and the back office. The front office consists of the dealers who actually negotiate the deals. The back office has the responsibility to complete the paper work, receive and effect delivery of the securities, and receive the proceeds and authorise payment. Thirdly, there is the accounting section which records the transactions and reconciles the investment accounts.

(c) In a number of banks this segregation of duties did not exist or was not operative. Thus, in NHB, (as pointed out in the Committee's second Report) Shri C.Ravikumar, Assistant General Manager functioned like a one-man orchestra. He was not only the dealer but also one of the signatories to the cheques and all the back-up functions were with Shri S.Suresh Babu, Assistant Manager who reported to Shri Ravikumar and acted under his instructions. In the SBI, the segregation of duties did not operate in practice. A special facility of collection and credit of bankers' cheques issued in favour of SBI and issue of bankers' cheques by SBI as per his instructions was extended by SBI to HSM in the Investment Division of the Bombay Main branch which facilitated irregular operations of HSM. Shri R.Sitaraman, Officer in Scale I, virtually looked after his interests single-handedly. Similarly, in Stanchart (as pointed out in the fourth Report of the Committee) there have been significant violations of internal control procedures. The deliveries were effected without receiving sale proceeds, payments were made without receiving securities, BRs or SGL transfer forms, and even where BRs were received, discharged receipts were handed over to the broker to be exchanged against bonds and there was inadequate follow-up to ensure that bonds were in fact ultimately delivered to Stanchart.

(d) In almost all banks a market practice developed whereby there was no independent confirmation of contracts between counterparty banks and in many cases, deliveries of securities, BRs and SGL transfer forms were made to and received from brokers, and even cheques for settlement of dues were given to or received from brokers. Incidentally this resulted in brokers delaying delivery of securities, BRs and SGL transfer forms as also cheques for settlement.

23. A third key element in the perpetration of the irregularities was the fact that brokers were increasingly dealing on their own account and carrying positions. This was one of the reasons for the differences between the rates at which the same contract was booked by two counterparty banks and the large differences paid to or received from brokers.

24. A fourth key element was the failure to periodically reconcile the investment accounts. Thus, as pointed out in the first Report of the Committee when RBI asked SBI on 2 April 1992 to furnish to RBI a statement of investments held by it on 31 March 1992, it was informed that a statement only as at the end of January 1992 was available. Similarly, in its second Report issued in July 1992, the Committee had to report that reconciliation of investments as at 31 March 1992 had in respect of certain banks not been completed by the date of the Report. In the absence of this periodic reconciliation, gaps in the investment portfolio remained undetected.

25. (a) As a consequence of the various features mentioned earlier, 'holes' had developed in the investment portfolio of banks. These holes remained undetected because presumably the portfolio was supported by SGL transfer forms or BRs which were on hand or which were to be delivered by brokers and it was not realised that the SGL transfer forms or BRs were not backed by securities. In effect a huge 'teeming and lading' operation had developed, the deliveries to be effected and payments to be made under one set of transactions being met by the creation of a new set of transactions again supported by SGL transfer forms and BRs not backed by securities. Thus, like a game of musical chairs, this 'hole' in the overall investment portfolio of banks was transferred from bank to bank and was detected only when the music stopped.

(b) The event which triggered this stoppage was the enquiries into the securities transactions of banks started by the RBI in January 1992 and which in April 1992 revealed a short-fall of Rs.649 crores in the investment portfolio of SBI which could be traced to broker HSM. Under pressure from SBI, HSM made payment between 13 April 1992 and 24 April 1992 of Rs.574.76 crores through payment orders received from Grindlays Bank, Rs.47.76 crores through a banker's cheque from Syndicate Bank, and Rs.0.20 crore by adjustment of interest on 182 days Treasury Bills. HSM perhaps believed that with these payments the 'shortfall' would be buried. Unfortunately for him, the shortfall refused to remain buried. As a result of RBI's further scrutiny, it was established that HSM's account in Grindlays Bank which enabled him to make payment of Rs.574.76 crores was in fact funded to the extent of Rs.489.75 crores by seven cheques drawn by the NHB in favour of Grindlays Bank and credited to HSM's account. Irrespective of these payments underlying securities had not been delivered.

(c) The discovery of the shortfall in SBI and the subsequent disclosure of the payments by NHB created a crisis in the securities market whereby other brokers also were not able to hide the 'holes' in the investments of some banks by replacement deals. Thus, in the case of Stanchart fictitious sale transactions were booked to clear part of the purchases not supported by delivery of securities and fresh purchases were made backed by BRs issued by MCB not supported by securities. Both BoK and MCB are under liquidation proceedings. They were found to have issued BRs and SGL transfer forms without security backing and the holders of such BRs and SGL transfer forms have been exposed to loss. Similarly, FGFSL was not in a position to deliver securities to ABFSL. It tried to cover this shortfall by the delivery of scrips in respect of Units and 'allotment letters' in respect of HUDCO bonds and NPTC bonds. On verification of these scrips and 'allotment letters' by the officers of RBI, these were found to be forged/fabricated.

26. The findings detailed in the earlier Reports of

the Committee have now established that the gross problem exposure of banks can be placed at Rs.4,024.45 crores made up as under :-

	(Rs.in crores)
1. Total value of investments made by banks for which they do not hold any securities, SGL transfer forms or BRs -	
(a) National Housing Bank (as detailed in the second Report of the Committee)	1271.20
(b) State Bank of Saurashtra (as detailed in the second Report of the Committee)	174.93
(c) SBI Capital Markets Ltd. (as detailed in the second Report of the Committee)	121.36
(d) Standard Chartered Bank (as detailed in the fourth Report of the Committee)	506.61
(e) Canbank Financial Services Ltd. (as detailed in the fourth Report of the Committee)	188.47
	2262.57
2. Total exposure against BRs/SGL transfer forms issued by Bank of Karad Ltd. or Metropolitan Co-operative Bank Ltd. (for which there appears to be no security backing) -	
(a) Canbank Financial Services Ltd. (as detailed in the fourth Report of the Committee)	438.66
(b) Canbank Mutual Fund (as detailed in the second Report of the Committee)	102.97
(c) Standard Chartered Bank (as detailed in the fourth Report of the Committee)	931.84
	1473.47
3. Other items -	
(a) Standard Chartered Bank (as detailed in items (d), (e) and (f) of paragraph 7 of chapter II of the fourth Report of the Committee)	43.69
(b) Canbank Financial Services Ltd. (as detailed in item 4 of paragraph 2.1 of chapter III of the fourth Report of the Committee)	39.60
(c) Andhra Bank Financial Services Ltd. in respect of securities found to be forged/fabricated (as detailed in paragraph 13(b) of chapter V of the fourth Report of the Committee)	205.12
	288.41
Gross problem exposure (Total of items 1 + 2 + 3 above)	4024.45

Against this gross problem exposure, the following have to be considered.

(a) Stanchart had reportedly received from broker HPD securities at which a value of Rs.350 crores was initially placed. This includes Cantriple units on which alone the depreciation in value is estimated at around Rs.150 crores.

(b) In respect of forged/fabricated securities lodged by FGFSL with ABFSL, ABFSL had received from FGFSL securities valued at Rs.101.59 crores before FGFSL was notified under the Special Court (Trial of Offences relating to Transactions in Securities) Act, 1992 and securities of Rs.112.29 crores after the notification.

(c) In respect of some of the brokers, in whose accounts monies for the above transactions have been credited, certain securities have been found lying with other banks.

(d) The above gross problem exposure does not include the depreciation/loss suffered by several banks by reason of the fact that ready forward transactions in securities (including on account of PMS and similar schemes) could not be reversed and the banks were left holding securities which had depreciated in value, as also losses which may occur in the settlement of matters which are in dispute.

V. Statistical Analysis

On the basis of information furnished by banks, the Committee has attempted a statistical analysis of the securities transactions of banks during the period from 1 April 1991 to 23 May 1992. These details are given in the following paragraphs.

2. The aggregate value of transactions is as under:

Type of transaction	Aggregate face value (Rs.in crores)	Percentage
Ready Forward	5,67,165	44.12
Outright	69,192	5.38
Others	6,49,192	50.50
	12,85,549	100.00

In several cases, where commitments to repurchase or resell the securities have not been documented, but are matters of 'understanding' between the parties, the transactions have been reported by the banks as 'others' and not as ready forward. Therefore, the percentage of ready forward transactions is actually much more than what is indicated above. What is however significant is that transactions reported as 'outright' purchases or sales account for only 5.38 per cent of the total value of transactions.

3. The above transactions when analysed by nature of security show the following :

Nature of security	No.of transactions	Aggregate face value (Rs.in crores)	Percentage of aggregate value
Government securities	31,417	6,07,627	47.27
PSU bonds	35,352	4,94,415	38.46
Units	11,957	1,56,976	12.21
Others	8,545	26,531	2.06
	87,271	12,85,549	100.00

4. A broker-wise analysis of the transactions is as under :

(Rs.in crores)

Broker	No.of transactions	Aggregate face value	Percentage to aggregate face value
Direct	33,282	5,41,945.39	42.16
Hiten P. Dalal	6,253	1,27,504.04	9.92
Harshad S. Mehta	2,607	68,839.24	5.35
Somayajulu & co.	1,961	48,344.28	3.76
Batliwala & Karani	3,873	43,857.03	3.41
N.K. Aggarwala & Co.	1,833	43,698.83	3.40
M/s.V.B. Desai & Associates	2,501	40,196.87	3.13
C.Mackertich	1,824	37,684.93	2.93
D.S. Purbhoodas & Co.	1,651	36,067.98	2.81
Asit C. Mehta	2,273	34,867.46	2.71
Bhupen Champaklal Devidas	1,619	34,264.07	2.67
Darshaw & Co.	1,663	24,930.90	1.94
Hemdev & Co.	1,308	19,179.64	1.49
Excel & Co.	1,417	18,032.36	1.40
P.R.Subramanyam & Co.	841	12,110.68	0.94
B.D. Agarwal	830	10,460.83	0.81
Chandrakala & Co.	943	9,972.51	0.78
G.N. Hegde	746	9,886.44	0.77
A.R.Financial Services Ltd.	611	9,287.67	0.72
Mukesh Babu	780	9,110.39	0.71
Aswin Dand	430	8,860.00	0.69
Kotak Mahindra & Co.	867	8,655.28	0.67
Stewart & Co.	487	8,502.28	0.66
A.D. Narottam	600	7,693.68	0.60
L.K. Pandey	405	5,179.42	0.40
Others	15,666	66,417.03	5.17
	87,271	12,85,549.23	100.00

It will be seen that only three brokers accounted for 31.29 per cent of the transactions booked through brokers. Moreover, out of the transactions shown as direct, there were many transactions with 'routing' banks where the counterparties were in fact the brokers. Besides, in some banks although the bulk of these transactions were shown as direct, these were in fact entered into through brokers.

5. A bank-wise analysis of the transactions is as under :

(Rs.in crores)

Bank	Aggregate face value	Percentage to aggregate face value
Citibank	2,15,179	16.74
Standard Chartered Bank	1,88,034	14.63
Bank of America	1,59,478	12.41
ANZ Grindlays Bank	93,958	7.31
Canbank Financial Services Ltd.	90,282	7.02
American Express Bank	69,191	5.38
State Bank of India	54,343	4.23
Andhra Bank	42,135	3.28
SBI Capital Markets Ltd.	32,971	2.56
UCO Bank	28,906	2.25
Canara Bank	27,879	2.17
Bank of Madura Ltd.	25,729	2.00
Others	2,57,464	20.02
	12,85,549	100.00

Thus three banks alone accounted for 43.78 per cent of the transactions.

6. An analysis of the transactions as between transactions on "own" account and others is given below :

(Rs.in crores)

	No.of transact-ions	Aggregate face value	Percentage to aggregate face value
Own account	50,002	8,65,449	67.32
PMS clients	31,656	3,40,303	26.47
Others including brokers	5,613	79,797	6.21
	87,271	12,85,549	100.00

7.An analysis of the transactions which were not on 'own' account, by major banks is given below :

(Rs.in crores)

Bank	Transactions on behalf of PMS clients			Transactions on behalf of others		
	No.	Face value	Percentage	No.	Face value	Percentage
Citibank	21,682	2,13,983	62.88	-	-	-
Canfina	4,242	90,282	26.53	-	-	-
Andhra Bank	-	-	-	1,142	26,449	33.15
UCO Bank	-	-	-	940	22,635	28.37
Stanchart	1,340	20,975	6.16	-	-	-
Bank of Karad	-	-	-	1,671	15,423	19.33
Bank of America	615	7,832	2.31	-	-	-
Bank of Madura	-	-	-	726	7,256	9.09
ANZ Grindlays	3,154	5,615	1.65	-	-	-
ABFSL	-	-	-	661	5,541	6.94
Others	623	1,616	0.47	473	2,493	3.12
	31,656	3,40,303	100.00	5,613	79,797	100.00

This analysis clearly identifies the major 'routing' banks.

VI. Brokers' Accounts

The particulars of the aggregate problem exposure detailed in earlier Reports of the Committee give in most cases details of the accounts (including brokers' accounts) where the payments made for investments purchased (and forming part of the exposure) have been credited. The Committee has also made an attempt to trace the diversion of funds into brokers' accounts and to determine the ultimate disposal of funds.

2. Since the scrutiny of securities transactions had revealed that in the case of a number of banks, losses had been funded out of broker ADN's account with BoK and broker HPD's account with Andhra Bank, a detailed analysis of these accounts was carried out. This analysis showed that the funds raised by ADN through BRs issued by BoK (and outstanding on date) have been used to the extent of Rs.559 crores to fund HPD and to the extent of Rs.74 crores to fund other brokers. There was also a net outflow of Rs.209 crores arising out of difference between the aggregate receipts and payments covering securities transactions with various banks. Similarly, the analysis of HPD's account with Andhra Bank on the basis of verification so far made at six banks and subsidiaries has shown that over Rs.433 crores has been used for the purchase of shares, debentures, Units of Mutual Funds and approximately Rs.408 crores has been used to fund losses of banks in securities transactions. Details of the analysis have been given in the fifth Report of the Committee.

3. However, while the Committee has been able to analyse the entries in some of the accounts maintained by brokers with banks, it has not been very successful in determining the ultimate disposal of funds, mainly for the following reasons :

(a) Brokers maintain accounts in several banks and there is a constant movement of funds between different accounts and between associate concerns.

(b) The source and destination of funds can be determined only by a detailed scrutiny of the vouchers on the basis of which entries have been made in the bank accounts. In a number of banks the relevant records have been seized by the CBI and access to such records is cumbersome and time-consuming.

(c) To understand the nature of a receipt or payment and its purpose it is necessary to examine the books of accounts and records of the broker and to examine him. These powers were not available with the Committee.

4. The Committee believes that a meaningful enquiry in this regard can only be made by a co-ordinated effort between the different investigating agencies. Much of the work already done by the RBI at the instance of the Committee would be of great assistance in such an effort.

VII. Why were the irregularities not detected?

The Committee has tried to determine why, given the wide-spread nature of the irregularities, they were not detected earlier. Some of the possible reasons are given in subsequent paragraphs.

2. The control mechanism to ensure that a bank's operations are conducted with prudence rests on three major parties, namely the bank's management, the supervisory authorities and the bank's external auditors.

3. (a) The primary responsibility for the conduct of a bank's business rests with the bank's management supervised by its Board of Directors. Management discharges this responsibility partly by ensuring (i) that appropriate policies in major areas of operations are precisely laid down (ii) that there are professionally competent persons to manage key positions within the bank (iii) that there are proper control systems (iv) that statutory and regulatory directives are observed (v) that the operations are conducted with due regard to prudence and (vi) that there exists an adequate system of internal audit and internal inspection and that this system is functioning.

(b) The nature of the irregularities which have been revealed by the Committee's findings shows that though in many cases professionally competent persons were manning key positions and though control systems had been laid down, these had been by-passed. The nexus which had developed between the dealers and other officers of the banks on the one hand and the brokers on the other and a desire on the part of treasury departments to maximise earnings had enabled the concerned officers to over-ride the system. If a proper internal audit and internal inspection system had been functioning, this over-ride would have been detected but internal audit appears to be one of the weakest links in the control system within banks. This is an activity which is considered within banks as not being intellectually stimulating or conducive to professional advancement within the bank and the department is often inadequately staffed.

(c) Perhaps the most important factor for the bank management's failure to prevent the irregularities was their attitudinal approach to the problem. Bank managements could not have been unaware that RBI regulations were being violated, particularly in spirit if not in terms of the letter of the regulations. That they turned a Nelson's eye to these violations is clear and could have been due to the following reasons :

(i) Regulations were considered as being technical in nature and the true rationale for the regulations was not appreciated. Therefore, compliance with the regulations was being given no greater importance than say a motorist's compliance with parking regulations. It was easier to park in a 'no parking' zone and pay the fine than to have the inconvenience of searching for a parking space.

(ii) Comfort was taken from the widespread breach of certain regulations, e.g. those applicable to ready forward transactions. A so-called market practice was considered more important than RBI regulations.

(iii) Senior management saw their treasury departments making increasingly larger profits and chose not to enquire too deeply as to how these profits were made for fear of rocking the boat.

(d) Symptomatic of this approach of the management is the fact that when in Shri A.Ghosh, Deputy Governor, RBI's letter dated 26 July 1991 (referred to earlier), RBI asked banks "to frame and implement a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices" and later asked for specific confirmation that this had been done, banks readily gave such confirmations even though violations of RBI guidelines continued. Similarly, the foreign banks gave assurances of full compliance with the PMS guidelines of the RBI in early 1991, while they continued to violate them.

4. (a) The role of the supervisory authority, namely RBI, is to protect the interests of bank depositors, to safeguard the soundness and stability of the banking system and ensure compliance with monetary or exchange rate policies.

(b) In the discharge of this role, RBI has issued a number of directives, either in the form of circulars or D.O. letters addressed to the Chairmen and Chief Executives of banks or occasionally by verbal communication at meetings with the Governor. In many instances parts of such communications previously issued have been modified by subsequent communications and many of the communications have remained in force for a large number of years. There is not therefore available a readily accessible comprehensive record in which RBI directives are contained and which can be referred to. This creates the possibility of banks and/or their officers by omission or design claiming ignorance of specific directives and makes supervision within the bank also difficult.

(c) RBI ensures compliance with its directives both by on-site inspections and by the collection and interpretation of regular reporting returns and other statistical data. However, given the fact that there are 80 banks (with over 46,000 branches) required to be inspected by RBI, the resources of RBI are obviously overstretched. Thus, RBI inspected branches of foreign banks and private sector banks only once in two years and public sector banks only once in four years. In addition, for public sector banks it carried out an Annual Financial Review, without inspection and based on secondary data like annual accounts, Board notes, etc.

(d) In carrying out its inspections, RBI has given major emphasis to the quality of banks' assets and particularly to the adequacy of provisions for doubtful debts. This is understandable considering the rapidly deteriorating quality of these assets in the Indian banking system and the need to formulate and comply with internationally acceptable prudential norms of income recognition, provisioning and capital adequacy. Consequently, sufficient importance was perhaps not given to the treasury function and particularly to the individual transactions for sale and purchase of securities.

(e) Inspections of individual banks are carried out by RBI in isolation, that is, by examination of the records of that bank alone. Many of the irregularities noticed by the Committee have been detected only because of a system of simultaneous inspection of related banks as directed by the Committee, that is, entries relating to a single contract in the bank being correlated with entries relating to the same contract in the counterparty bank.

(f) RBI inspection is not an audit of individual transactions based on scrutiny of vouchers. It is, therefore, not a substitute for audit, which is an internal function of banks.

(g) Many of the foreign banks have sophisticated E.D.P. systems for recording of transactions. Access to records maintained on the electronic systems and understanding of the same need specialised knowledge of such systems in general and of the system used in particular. Perhaps this knowledge was not always available with the inspecting officers. The Committee has also found some instances where a part of the bank's record was maintained on a parallel system and knowledge of this record was restricted even within the bank to a few individuals.

(h) Despite the above difficulties, RBI had detected some of the irregularities outlined in the Committee's Reports. Thus, in 1989-90, a detailed scrutiny of PMS transactions by banks revealed many irregularities. These irregularities were pointed out to the banks and revised guidelines issued by RBI through a circular dated 18 January 1991. At the instance of the Governor, RBI, a quick scrutiny of securities transactions of some of the public sector banks was made in the first quarter of 1991 to find out whether banks were undertaking sale transactions in securities through the medium of BRs, with buyback arrangements, without actually holding such securities and whether the banks were putting through transactions in securities for the benefit of brokers otherwise not warranted by business considerations. This study did establish (i) the predominance of ready forward transactions (ii) the existence of double ready forward deals (iii) window dressing through inter-bank transactions at rates which have no relevance to market rates (iv) extensive use of BRs and (v) assistance to brokers to take up temporary positions by issue of BRs on their behalf. It was as a result of this study that Shri A.Ghosh, Deputy Governor's letter dated 26 July 1991 was issued. This letter, in addition to proscribing certain practices, specifically cautioned the banks in respect of transactions as agents of their broker clients. In December 1991 and January 1992, RBI carried out specific inspection of the securities transactions of three 'routing' banks, namely, Bank of Karad Ltd., Bank of Madura Ltd. and Andhra Bank, but before action could be taken it was overtaken by events.

(i) In retrospect, it is obvious that while being aware of the violations of its directives by certain individual banks, RBI was not aware of or did not appreciate the all pervasive nature of the malady. It treated these as technical violations for which the individual banks should be reprimanded and the banking system as a whole cautioned but it did not comprehend the total picture whereby certain brokers had in fact captured the securities operations of certain major banks and had directed the conduct of these operations to their own maximum benefit. Perhaps, RBI was also hampered by the absence of a good market intelligence system which might have given some indication of what was actually happening. It was looking at the problem as possible violations of compliance of reserve requirements and interest rate directives and it had no inkling that banks' funds were being diverted by brokers for their stock market operations in the guise of securities transactions.

5. (a) The primary objective of an audit by an external auditor is to enable him to express an opinion as to whether the financial statements of the bank give a "true and fair" view. Given the large volume of transactions in a bank, a detailed audit of all transactions is not only time-consuming and extremely expensive but also wholly impracticable. The auditor therefore, relies upon the internal control system existing in a bank. He needs to test and evaluate the system but this testing and evaluation is for the limited purpose of deciding to what extent he can rely upon the system to ensure the accuracy of the accounting records and the security of its assets.

(b) Essentially therefore, the auditor's examination of a bank's accounting and other records is designed to obtain satisfaction regarding the income and expenditure of the bank, the correctness of the liabilities and the quality of the assets. A large part of his work is connected with the verification of the assets, particularly the investments and advances, and the adequacy of provisions and a considerably lesser part with the examination of individual transactions.

(c) The external auditor's duties are governed by Section 30 of the Banking Regulation Act, 1949. This section requires that the auditor "shall have the powers of, exercise the functions vested in, and discharge the duties and be subject to the liabilities and penalties imposed on, auditors of companies by Section 227 of the Companies Act, 1956". The section further provides that "in addition to the matters which under the aforesaid Act the auditor is required to state in his report, he shall, in the case of a banking company incorporated in India, state in his report, -

(i) whether or not the information and explanations required by him have been found to be satisfactory;

(ii) whether or not the transactions of the company which have come to his notice have been within the
powers of the company;

(iii) whether or not the returns received from branch offices of the company have been found adequate for the purposes of his audit;

(iv) whether the profit and loss account shows a true balance of profit or loss for the period covered by such account; and

(v) any other matter which he considers should be brought to the notice of the shareholders of the company."

(d) Sub-section (1B) of Section 30 specifically provides that "where the Reserve Bank is of opinion that it is necessary in the public interest or in the interests of the banking company or its depositors so to do, it may at any time by order direct the auditor of the banking company to conduct a special audit of the accounts of the banking company in relation to any transactions or class of transactions specified in the order and the auditor shall comply with such directions and make a report of such audit to the Reserve Bank and forward a copy thereof to the company."

(e) In respect of nationalised banks, the auditors' duties are governed by Section 10 of the Banking Companies (Acquisition and Transfer of Undertakings) Acts 1970 and 1980. This section is similar to Section 30 of the Banking Regulation Act, 1949.

(f) For the audit of nationalised banks, there also exists a Bank Audit Committee consisting of representatives of RBI, the Institute of Chartered Accountants of India and nominees (by rotation) of some public sector banks. This Committee meets periodically and discusses the manner in which audits of such banks are to be carried out. Arising out of such discussions, a format of a "long-form" audit report has been prescribed and auditors of nationalised banks are required, on completion of each year's audit, to submit a report in this format to RBI.

(g) The appointment of auditors in respect of public sector banks is made by the banks under the direction of the RBI and in the case of private sector banks and branches of foreign banks is approved by the RBI.

6. (a) The irregularities noticed by the Committee fall into two broad categories namely (i) violation of RBI guidelines and (ii) other irregularities.

(b) In so far as violation of RBI guidelines is concerned, external auditors did not perceive it as part of their duties either to examine transactions with a view to identify such violations or to report upon the same. No doubt this perception was influenced by the fact that :-

(i) this is not a duty cast upon them under Section 30 of the Banking Regulation Act, 1949;

(ii) no directive in this regard has been issued by RBI under sub-section (1B) of Section 30; and

(iii) no such directive has been issued even in respect of nationalised banks through the Bank Audit Committee nor was any mention made of the same in the format of the long-form audit report.

(c) In so far as other irregularities are concerned, these irregularities can again be divided into two parts namely, those relating to individual transactions and those relating to the existence and quality of investments at the balance sheet date.

(d) In so far as individual transactions are concerned, the auditors as mentioned above do not examine all transactions. An examination of the transactions would have revealed that the rates at which some of the transactions were made were unrealistic but in the absence of suspicion it would be difficult to notice this since firstly the bulk of the transactions were ready forward deals where one leg of the transactions necessarily has to be at a rate different from the market rate and secondly, a large part of the transactions were in PSU bonds and Units for which market quotations are not available. Moreover, the irregularity in many of the transactions has been detected only by a simultaneous examination of the records of the counterparty banks which clearly was not possible in an audit.

(e) In so far as the existence and quality of investments at the balance sheet date are concerned, the auditors clearly had a duty to verify the existence and quality. This required a reconciliation of the investment account, physical inspection of securities on hand, confirmations of counterparty banks for BRs issued by such banks and on hand, confirmation of SGL balances with the PDO, and control and reconciliation of BRs issued by the bank. The audits for the year ended 31 March 1992 were completed after the irregularities were detected but if irregularities regarding the existence and quality of investments had existed as at 31 March 1991 and had not been detected (particularly the existence of BRs which were long overdue) the external auditors must accept responsibility.

(f) In determining to what extent external auditors could have detected the irregularities, two other factors must be recognised :-

(i) The appointment of auditors was either made under the direction of or approved by, RBI. In most cases, these appointments were made very late in the accounting year and banks were required to file audited accounts with the RBI within three months of the close of the year. The short time available with the auditors was fully utilised in complying with their statutory duties and particularly with the verification of assets and adequacy of provisions and no time would be available for a detailed examination of individual transactions.

(ii) An audit is different from an inspection or an investigation. Whereas the former is concerned with expressing an opinion on the overall "true and fair" view of the financial statements, the latter is concerned with an in-depth examination of a few selected transactions. Moreover, in the case of an audit, within the restrictions of time and resources available, he has to examine the whole area of a bank's financial operations whereas an inspection or investigation is not limited by time or coverage.

7. It does however appear that the irregularities could perhaps have been detected earlier if there had been greater co-ordination between the different controlling agencies. In many countries such close links already exist or are currently under study. In a joint statement issued by the Bank Supervisors' Committee (comprising representatives of the central banks and supervisory authorities of the Group of Ten countries, formed under the auspices of the Bank of International Settlements, Basle) and the International Auditing Practices Committee of the International Federation of Accountants, New York, the basis for such a relationship has been spelt out. The statement states that auditors can assist bank supervisors in specific supervisory tasks within a framework which is based on the following criteria:

(a) the basic responsibility for supplying complete and accurate information to the Supervisor must remain with the bank management;

(b) the normal relationship between the auditor and his client must be safeguarded;

(c) before concluding any arrangements with the Supervisor, the auditor should consider whether any conflicts of interest may arise;

(d) the supervisory requirements must be specific and clearly defined in relation to the information required;

(e) the tasks which the auditor is asked by the Supervisor to perform need to be within his competence, both technical and practical;

(f) the auditor's task for the Supervisor must have a rational basis, that is, except in special circumstances, the task must be complementary to his regular audit work and one which can be performed more economically or more expeditiously than by the Supervisor, either because of the auditor's specialised skills or because duplication is thereby avoided; and

(g) certain aspects of confidentiality need to be protected, in particular the confidentiality of information obtained by the auditor through his professional relationship with other clients and not available to the bank or the public.

8. There were many players in the securities market all of whom were not subject to inspection by RBI. The Department of Banking Operations and Development (DBOD) inspected only the banks and subsidiaries of banks, including their mutual funds. Non-banking financial companies were inspected by the Department of Financial Companies but this inspection was restricted to their function of acceptance of deposits. These companies fall into two categories, namely companies where banks have no shareholding e.g. Fairgrowth Financial Services Ltd., and companies where banks have shareholding not exceeding 30 per cent like Esanda Finanz & Leasing Ltd. (where ANZ Grindlays Bank has a shareholding of 30 per cent) and D.B. Financial Services (India) Ltd. (where Deutsche Bank has a shareholding of 30 per cent). Even in the latter class of companies there was no provision for inspection by DBOD. Finally, there were the financial institutions which were not subject to inspection. Therefore only a section of the securities market was subject to inspection by RBI.

VIII. Public Debt Office of the RBI

One of the terms of reference of the Committee was to "scrutinise the procedure adopted by Public Debt Offices (PDOs) of the RBI in regard to the maintenance of SGL accounts and other related matters and suggest remedial measures to tone up the responsiveness of the system".

2. The detailed findings of the Committee are reported in its first and third Reports. The major findings are summarised in subsequent paragraphs.

3. The PDO is a central depository for all types of Government securities except Treasury Bills. The main activities of the Subsidiary General Ledger Section of the PDO are -

(a) the maintenance of Subsidiary General Ledger (SGL) accounts in the names of banks, financial institutions, corporate bodies, provident funds, brokers, trusts, etc.;

(b) the examination of securities tendered for credit to SGL account, issue of scrips by debit to SGL account and transfer of SGL balances from one account to another on the basis of transfer deeds submitted by SGL account holders;

(c) the transfer of balances to other regional PDOs and the acceptance of transfer from other regional PDOs as per advices of holders;

(d) payment of half-yearly interest and redemption dues to account holders; and

(e) furnishing balances statements to account holders periodically.

4. The records of the PDO were manually maintained and the functioning of the PDO was generally satisfactory except for the following :-

(a) though all SGL transfer forms received on a given day were generally disposed of the same day, there was some delay in the preparation and despatch of objection memos;

(b) no statements showing the debits and credits to SGL accounts were submitted to banks except for a half-yearly statement of balances. This statement of balances was also made available to the account holders as on any other day, on request; and

(c) scroll numbers given at the receipt counter and recorded on the SGL transfer forms were not cross-referenced either in the ledger or in the day-book.

5. The indiscriminate use of BRs in place of SGL transfer forms has been justified by some banks on the ground that the dishonour of SGL transfer forms for lack of adequate balance in the seller's account was not intimated to the banks in time and therefore, they were not in a position to control the issue of their own SGL transfer forms. While this may be true to some extent, this cannot by itself justify the enormous increase in the use of BRs. Moreover, PDOs maintain accounts only in respect of Government securities. The bulk of securities transactions in number have been in respect of PSU bonds and Units for which PDO accounts could not have been operated. Furthermore, even with respect to SGL transfer forms, in a number of cases, these were either not lodged at all with the PDO or were lodged after a substantial time-lag.

6. The absence of a procedure to provide detailed statements of transactions in the accounts to the holders has however hampered regular reconciliation of investment balances and to that extent contributed to the failure in early detection of the irregularities.

7. In its first Report the Committee had made certain recommendations regarding the functioning of PDOs, in particular the computerisation of its records. Partial implementation of these recommendations has been reported in the Committee's third Report.

IX. Recommendations

Based on its preliminary findings the Committee had made certain recommendations in its first Report. Thereafter, the Committee has re-examined the matter and makes its final recommendations in succeeding paragraphs. For the sake of completeness, these recommendations include the recommendations made in the first Report.

2. The diversion of funds to brokers through securities transactions has been largely engineered through the process of ready forward security transactions. Since there is no permanent purchase or transfer of investments in such cases, there is no real need to effect the actual transfer of scrips or to deposit SGL transfer forms with the PDO. In most cases these transactions have been supported by BRs or by SGL transfer forms not intended to be deposited with the PDO. Often the BRs and the SGL transfer forms do not appear to be supported by underlying securities. The ready forward transaction in substance is a financing transaction and not a security transaction and therefore is possible only when one leg of the transaction is at a rate which is at variance with the market rate. Finally, circumvention of the 'lock-in' period in respect of PMS has been achieved through such deals with customers. The Committee would therefore, recommend that until adequate safeguards are devised, all ready forward transactions be barred.

3. A key factor in the perpetration of the irregularities has been the system of Bank Receipts (BRs). The issue of BRs should be an exception rather than the rule. To achieve this end, the Committee makes the following recommendations :

(a) There must be a central depository for all securities in which a bank normally deals. At present, the PDO is a depository only for Government securities. In its first Report the Committee had made a recommendation that a central depository should be created for other securities like PSU bonds, Units, etc. The Committee has noted that following upon its recommendations a Committee was constituted under the chairmanship of Shri S.S. Nadkarni, Chairman, Industrial Development Bank of India (IDBI) and that Committee has submitted its report. Its recommendation for setting up of a central depository has been accepted and is in the process of implementation.

(b) There should be no delay in recording the transfers in the PDO and in communicating objection memos to the banks concerned. These and other recommendations regarding the functioning of the PDOs were made in the first Report of the Committee. The Committee has noted that action in this behalf has already been taken by RBI.

(c) Steps should be taken to ensure that PSUs and other institutions speedily issue scrips in exchange for 'allotment letters' so that physical delivery of the scrips can be facilitated, where such scrips are not deposited in the central depository.

4. Irregularities have also been facilitated because banks have not strictly adhered to IBA guidelines for issue of BRs and because proper controls have not been maintained in this regard. The Committee would therefore recommend that :

(a) BR rules formulated by IBA and enclosed with its letter dated 6 May 1991 addressed to the Chief Executives of all member banks be strictly enforced.

(b) Like cheques, BRs should have a validity period of 30 days and if not redeemed within that time, the BR should be deemed to be dishonoured and the fact of dishonour should immediately be notified to RBI for penal action.

(c) Similarly, a BR should normally be redeemed only by actual delivery of securities and not by cancellation of the transaction or by set-off against another transaction. If a bank is not able to redeem its BR by actual delivery, it should obtain the prior approval of RBI for settlement in any other manner and RBI should take penal action if it is not satisfied regarding the circumstances in which delivery cannot be effected.

(d) There should be proper systems in each bank for the custody of unused BR forms and for control on their utilisation and the existence and operation of these controls must be reviewed periodically by internal audit, bank supervisors and external auditors.

5. An equally important factor which has allowed the irregularities to develop has been the fact that brokers have acted on their own account and banks have provided facilities for this purpose. The Committee would make the following recommendations in this regard :

(a) Only "approved" persons should be allowed to operate as bank brokers. This approval must be given by an independent authority like RBI, Securities and Exchange Board of India (SEBI) or a similar body and there must be well-defined criteria for the grant of approval. All brokers should remain registered with this body which must have the power to refuse registration or cancel registration, if already granted, to a broker who is guilty of professional misconduct.

(b) There must be a clear distinction between brokers and traders and persons who are registered as approved brokers should be prohibited from trading in securities on their own account either by themselves or through associated concerns. Such a distinction already exists, in many stock exchanges abroad between brokers and jobbers.

(c) Registered brokers and their associated concerns must be debarred from carrying on other activities, particularly as share brokers, merchant bankers, etc.

(d) Banks should be required to lay down internal "prudential" criteria for dealing with the approved brokers whom they may decide to empanel for their security transactions. These should include exposure limits for transactions, for individual brokers, as also for counterparty banks. Compliance with these criteria should be reported to the RBI.

(e) Brokers' notes should indicate the name of the counterparty and also indicate separately the brokerage charged.

(f) There must be a compulsory practice for all contracts between banks to be supported by exchange of written confirmations of the contract. This will ensure that the name of the true counterparty is disclosed to both contracting parties.

(g) When the bank undertakes a transaction on behalf of its client, all documentation should clearly disclose the name of the party on whose behalf it has been acting.

(h) The existing prohibition on banks issuing cheques drawn on their account with RBI for third party transactions should be strictly enforced. Such payments should be made through normal instruments like bankers' cheques, drafts or a transfer advice which clearly discloses the identity of the person on whose behalf the transfer is made.

(i) No cheques or other instruments drawn in favour of a bank should be credited to customers' accounts unless there is a clear written mandate from the drawer to do so.

6. Much of the funding of the irregularities has been through funds placed with the banks under PMS and similar schemes. The Committee makes the following recommendations in this behalf :

(a) Banks should not be given general power to operate PMS and similar schemes but should be specifically authorised to do so. Proper criteria should be devised on the basis of which this authorisation would be given. One of the most important criteria to be devised should be the physical segregation of these activities from the normal banking activities and independent control of the operations and custody of the assets.

(b) PMS activities of a bank should be treated as similar to trustee activities and separate accounts and records should be maintained for the same.

(c) All PMS accounts must be subject to a separate audit by the banks' statutory auditors.

(d) Full details of all transactions in PMS accounts must be provided to customers.

(e) There should be no transactions, direct or indirect, between the bank and its PMS clients or between two PMS accounts as it is difficult to establish whether such transactions were at 'arms length'. Alternatively, there must be established an independent authority in each bank whose prior concurrence would be obtained before such transactions are entered into.

(f) There should be totally independent custody of investments held on behalf of PMS clients and investments held by the bank on its "own" account.

(g) The existing guidelines of RBI regarding PMS accounts should be strictly enforced.

7. The Committee has noticed several instances

where securities transactions have been at rates which are different from ruling market rates. As explained earlier, these transactions could have been entered into to alter the holding rate of investments or to book profits on sale of investments, which profits would get reversed after the year-end on reversal of the transactions through a forward purchase. Current RBI guidelines require banks to determine the market value of investments which form part of the bank's balance sheet but no account is taken of forward purchases and sales. The Committee would recommend that in preparing their annual accounts banks be required to take account of all forward sales and purchases of investments and to provide for the loss, if any, when the rates of such forward sale and purchase contracts are compared with ruling market rates. If this is done, any artificial profits booked would get neutralised.

8. The perpetration of irregularities and the non-detection of the same have been largely brought about by inadequate internal control in banks regarding securities transactions and the inadequacy of the internal inspection system. The Committee would recommend that in each bank an immediate review be made, if necessary with outside professional help, of the adequacy of the internal control system relating to security transactions, and remedial steps needed to be taken expeditiously.

9. The Committee's findings have shown that transactions between banks and their merchant banking subsidiaries have often not been at 'arms length' to the detriment of the interests of the customers of such subsidiaries. It has also been seen that in respect of such subsidiaries, the parent banks have exercised custodial functions and a minimum of control and information is available with the subsidiary. The Committee would recommend that RBI re-examine the operations of these subsidiaries and their relationship with their parent banks.

10. As mentioned earlier, RBI directives are not conveniently documented in a single publication but are contained in various forms of notifications like circulars, D.O. letters, etc. There are also frequent piece-meal modifications. This makes access to and comprehension of such directions difficult. The Committee recommends that all RBI directives be collected in a loose-leaf publication service wherein all modifications are effected through the replacement of sheets and proper indexing is available. This will ensure that all directives are available in a single document which can be kept uptodate and which can be easily accessed.

11. RBI had through its inspections noticed irregularities in some of the banks but was unable to appreciate the magnitude of the irregularities in the banking system as a whole or the implications thereof on a global basis. Perhaps this was due to an inability on the part of RBI to supplement its information of the operations of banks with information regarding other segments of the economy, e.g. the stock market, and also because it did not adequately correlate the information obtained from different banks. In this context, the Committee would make the following recommendations :

(a) RBI should modify its inspection procedures whereby transactions in the bank being inspected are cross-verified with the record of these transactions as appearing in the counterparty banks.

(b) RBI should strengthen its organisation responsible for market intelligence.

12. Though the National Housing Bank is a wholly-owned subsidiary of RBI there are not at present any institutional arrangements for the inspection of its operations. In its first Report the Committee had recommended that these arrangements be made at an early date. The Committee urges that this should be put in place expeditiously.

13. The Committee believes that given the large number of banks and their branches, RBI or even the new Supervisory Board which is envisaged will not have the resources to adequately carry out on-site inspection of the banks. The Committee therefore, recommends that in line with the procedure followed by supervisory authorities in many other countries, more formal arrangements be made for a closer co-ordination between the accountancy profession and the supervisory authorities whereby the former can assist the latter in the discharge of their supervisory responsibilities. The basis on which these links could be developed has been discussed in paragraph 7 of chapter VII of this Report.

14. At present, the auditors are appointed in all categories of banks (nationalised, private sector and foreign) for one year at a time. Although the auditors are generally allowed to be re-appointed for a further period, upto four years in all, this makes for a certain amount of uncertainty in the continuance of the auditors for audit of the same banks. More importantly, it is only in the second and subsequent years that the auditors are able to undertake the audit with greater precision and efficiency, with better knowledge of and familiarity gained with the accounting procedures and systems in the concerned banks. The Committee would therefore recommend that RBI approve the appointments of auditors for a three-year term. In banks, where a number of audit firms are appointed each year based on the size of operations, it could be ensured that not less than two of them have, at any annual audit, been involved in the audit for one year or more as part of the three year term.

15. The Committee has explained in paragraphs 1 to 3 of chapter VI of this Report the difficulties faced by it in trying to trace the diversion of funds into brokers' accounts and to determine the ultimate disposal of funds. A considerable amount of data has been collected by the inspecting officers of RBI under the direction of the Committee. It remains to correlate this data with the records seized from the brokers by the CBI and Income Tax Department or available with the brokers and to examine the brokers and other third parties. The Committee recommends that the RBI officers co-ordinate their efforts with the other investigating agencies which have the powers of search, seizure and examination to trace the ultimate destination of the funds diverted.

16. The Committee has identified one of the reasons for artificial transactions in securities as the desire to enhance the holding rate of securities in order to obtain a benefit in the computation of SLR. The Committee would recommend that for SLR calculations all investments should be valued at market value only. If because of the depreciation in market values in relation to cost, this would require a significantly larger investment by banks in SLR securities, RBI might consider a reduction in the rate of SLR.

17. Use of computer system by banks has become very common. In the changing banking scenario, while it may be inevitable for banks to computerise their operations, at the same time, such a system could also be exploited by certain unscrupulous dealers or other operating staff to hide certain irregularities from their top managements and the Supervisors, so long as the top managements and Supervisors do not have sufficient knowledge of the computer systems in use and have access to data available in the system. It was observed by the Committee that in certain banks (e.g. Grindlays Bank and Citibank) certain vital details relating to securities transactions were available only with the dealers in their personal computers and the back-up staff had no access to them. The Committee is, therefore, of the view that the inspecting officers of the Reserve Bank should have sufficient knowledge of the computer systems in operation in the individual banks. To enable the inspecting officers to have pre-knowledge of the system in place before they take up the inspection, the banks, whenever they computerise any of their operations; should be required to inform the Reserve Bank with the following details :

(i) the type of system in use;

(ii) the coverage of the data that are stored in the system and the output that are generated; and

(iii) the Operating Manual of the system.

Super accessibility available in the software should be accessible to the inspecting officers of the Reserve Bank.

X. General

The Committee's terms of reference were largely restricted to the examination of the securities transactions of banks. However, the Committee has identified that there has also been diversion of funds through other means, for example, call money transactions and the discounting of bills. Thus, large payments such as call money placed with other banks, have been found to be credited to individual brokers' accounts. On due date, these alleged call loans have been repaid by payment out of brokers' accounts in the same or other banks. The Committee has also noticed cases where brokers' funds have been placed in the call money market under banks' names. Similarly, banks have rediscounted bills of exchange held by other banks but the proceeds and repayments have been routed through brokers' accounts. Given its terms of reference, the Committee has not however, made a detailed examination of banks' transactions of this nature.

2. The large size of the PSUs' bond issues, when the funds raised bore little or no relation to the needs of their capital projects undei implementation, had forced the PSUs to shop around for attractive avenues for deployment of the large surplus funds. This was one of the major contributory factors for the large-scale irregularitics in the securities transactions of banks. The Committee would recommend that the funds requirements of PSUs be assessed more realistically and their access to the market staggered suitably, so that the surplus liquidity with the PSUs is kept to the minimum and for short periods only.

3. The Committee has noticed instances where banks had in February 1992, bid for and acquired bundles of shares of Public Sector Enterprises (PSEs) and which bundles were later sold to brokers, though one of the terms and conditions of the offer under which these bundles were acquired stated that the banks were 'free to offload their shareholding in these PSEs through the normal stock exchange transactions'. The details of these transactions are given in the second and fifth Reports of the Committee. It is for the Government of India to examine whether these sales by banks were actually violative of the condition requiring the buyers to sell the shares through the stock exchanges.

4. The Committee's terms of reference require it to fix responsibility for the malpractices and to recommend the action to be taken. The large number of irregular transactions and wide involvement of different banks has made it impossible for the Committee to deal with this term of reference. To do so would require a detailed enquiry into each such transaction and an examination of the individual officers concerned. The resources and time available with the Committee are not adequate for this purpose. The Committee therefore, has in its several Reports identified the transactions and would recommend that the managements of the individual banks hold an enquiry in the major transactions and take such disciplinary action as is appropriate. RBI may also look into the responsibility of the top management of banks for the irregular practices.

5. The investigations of the irregularities in the securities transactions of banks is an endless task. The Committee has in its Reports covered the most important items but there is considerable additional material which has been identified by the inspecting officers and which no doubt will be used by RBI to take such action as it considers appropriate. There are however, two noticeable omissions which must be mentioned. One of the most important players in the securities market is Fairgrowth Financial Services Ltd. (FGFSL). FGFSL is not a bank or even a subsidiary of a bank but its links with Andhra Bank Financial Services Ltd. have revealed a large number of irregularities. The Committee would have liked to comment on its operations in its Reports but the enquiries in respect of FGFSL have not been completed. Reference has been made to the State Bank of India (SBI) in the first and second Reports of the Committee. This reference is largely confined to its investment portfolio and its transactions with National Housing Bank and its relations with broker Harshad S. Mehta. However, a detailed examination of its securities transactions has not been completed. Both in the case of FGFSL and SBI many of the records have been seized by the CBI and access to such records has proved cumbersome and time-consuming. As this Report could not be delayed any further, the Committee has reluctantly decided to issue this Report without the investigations in the securities transactions of these two banks being completed.

6. Shri Y.H. Malegam is a partner in the firm of Chartered Accountants which has carried out the audit of the Bank of America's Indian branches for the year ended 31 March 1992. He has not, therefore, participated in the enquiry into the transactions of that bank or in the discussions of the Committee in respect thereof nor is he a party to items contained in the Report of the Committee as specifically referring to Bank of America.

7. The work of the Committee would have been impossible without the willing co-operation and assistance of Shri N.D. Parameswaran, Chief Officer, Department of Banking Operations and Development,

Reserve Bank of India and the officers and staff of the department. They have worked with great dedication and put in long hours in very difficult circumstances to examine the records of the banks and identify the transactions which form the basis of the Committee's Reports. The Committee would like to record its appreciation of the work done by them and its gratitude for the assistance they have provided to the Committee in its work.

R.Janakiraman
Chairman

Y.H. Malegam **V.G. Hegde**

C.P. Ramaswami **E.N. Renison**

Vimala Visvanathan
Member-Secretary

BOMBAY
Date : 29th April 1993