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STANDING COMMITTEE ON FINANCE (2005-2006)

FOURTEENTH LOK SABHA

MINISTRY OF FINANCE
(DEPARTMENTS OF ECONOMIC AFFAIRS, EXPENDITURE AND DISINVESTMENT)

DEMANDS FOR GRANTS
(2004-2005)

[Action taken by the Government on the recommendations contained in the First Report of the Standing Committee on Finance on Demands for Grants (2004-2005) of the Ministry of Finance (Departments of Economic Affairs, Expenditure and Disinvestment)]

TWENTY THIRD REPORT

LOK SABHA SECRETARIAT
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1. Dr. (Smt.) P.K. Sandhu	—	*Additional Secretary*
2. Shri R.K. Jain	—	*Deputy Secretary*
3. Shri T.G. Chandrashekhar	—	*Under Secretary*

INTRODUCTION

I, Chairman of the Standing Committee on Finance having been authorized by the Committee to submit the Report on their behalf present this Twenty-Third Report on action taken by Government on the recommendations contained in the First Report of the Committee (Fourteenth Lok Sabha) on Demands for Grants (2004-2005) of the Ministry of Finance (Departments of Economic Affairs, Expenditure and Disinvestment).

2. The Report was presented to Lok Sabha/laid in Rajya Sabha on 20 August, 2004. The Government furnished the written replies indicating action taken on the recommendations in batches on 19 October 2004, 20 October 2004, 25 January 2005, 8 February 2005 and 3 March 2005 respectively. The draft action taken report was considered and adopted by the Committee at their sitting held on 22nd August, 2005.

3. An analysis of action taken by Government on the recommendations contained in the First Report (Fourteenth Lok Sabha) of the Committee is given in the Appendix.

4. For facility of reference observations/recommendations of the Committee have been printed in thick type in the body of the Report.

NEW DELHI;
25 *August*, 2005
03 *Bhadra*, 1927 *(Saka)*

MAJ. GEN. (RETD.) B.C. KHANDURI,
Chairman,
Standing Committee on Finance.

CHAPTER I

REPORT

1.1 This Report of the Standing Committee on Finance deals with Action taken by Government on the recommendations/observations contained in their First Report (14th Lok Sabha) on Demands for Grants (2004-2005) of the Ministry of Finance (Departments of Economic Affairs, Expenditure and Disinvestment) which was presented to Lok Sabha and laid in Rajya Sabha on 20.8.04.

1.2 Action taken notes have been received from the Government in respect of all the recommendations contained in the Report. These have been analysed and categorized as follows:

(i) Recommendations/observations that have been accepted by the Government:

Recommendation Nos. 1, 2, 6, 8, 9, 13

(Para Nos. 21, 22, 23, 24, 25, 26, 35, 36, 61, 83, 84, 85, 87, 99, 100, 138)

(Total 16) (Chapter II)

(ii) Recommendations/observations which the Committee do not desire to pursue in view of Government's replies:

Recommendation Nos. 3, 4, 5, 9, 10, 12

(Para Nos. 40, 41, 45, 46, 55, 101, 109, 110, 111, 135)

(Total 10) (Chapter III)

(iii) Recommendations/observations in respect of which replies of Government have not been accepted by the Committee:

Recommendation Nos. 1, 5, 7, 8, 11

(Para Nos. 27, 56, 74, 75, 76, 84, 85, 86, 124, 125, 126)

(Total 11) (Chapter IV)

(iv) Recommendations/observations in respect of which final reply of the Government is still awaited

(Nil) (Chapter (V)

1.3 The Committee desire that replies in respect of the recommendations contained in Chapter I should be furnished to the Committee expeditiously.

1.4 The Committee will now deal with the action taken by the Government on some of their recommendations.

Inflation

Recommendation (No. 1, Para No. 27)

The Committee were of the view that inflation had hit the senior citizens the most and they desired the Government to ensure that there were attractive saving schemes for them. Tax free RBI bonds, offering annual interest of 6.5% was one such instrument which enabled people to park their savings, however, the same had since been withdrawn. It had resulted in causing much distress, particularly to the senior citizens many of whom were availing this facility. The Committee, therefore, recommended the Government to consider reintroducing these tax free bonds, apart from the scheme which had recently been introduced for the senior citizens and for those who had attained the age of 55 years and taken VRS.

2. While furnishing the action taken notes, the Ministry of Finance replied as follows:

> "Inflation hurts everyday particularly the poor whose incomes are not indexed to prices. High inflation puts a pressure on interest rates leading to a rise in project costs and investment. It also reduces real interest rates affecting adversely savings rates. Therefore, containment of inflation remains high on the agenda of the government. Anti-inflationary policies of the government include strict fiscal and monetary discipline, rationalisation of excise and import duties of essential commodities so that there is no undue burden on the poor, effective supply-demand management of essential items through liberal tariff and trade policies, and strengthening the public distribution system.
>
> On the 18th August 2004 government reduced customs and excise duties on selected petroleum products to keep their domestic retail prices in check in the face of the global oil price surge to a record high. Customs duty on petrol, diesel, LPG and kerosene were reduced by 5 per cent each, while excise duty was reduced by 3 per cent each for petrol and diesel and 4 per cent for kerosene.

Duty Concessions

(In per cent)

	Customs		Excise	
	New	Old	New	Old
Petrol	15	20	23	26
Diesel	15	20	8	11
Kerosene	5	10	12	16
LPG	5	10	8	8

- On the 20th August 2004 government reduced customs duties on non-alloy steel and ships for breaking to 5 per cent from 10 and 15 per cent respectively in order to check high inflation in metals and metal products. Melting scrap of iron and steel was fully exempted from customs duty.

Customs Duty

Product category	New	Old
Non alloy steel	5	10
Ships for breaking	5	15
Iron and Steel scrap	Nil	5

- To check the liquidity overhang in the system. On September 11, 2004 the Reserve Bank of India has hiked the cash reserve ratio (CRR) to be maintained by banks, by 50 basis points to 5 per cent of their demand and time liabilities. The CRR will be raised in two stages by 25 basis points each: First, from the fortnight beginning September 18 and then from October 2. The move is expected to take out around $s 8,000 crore worth of liquidity from the system. The money supply has been hovering at 16.6 per cent as compared to 14 per cent last year.

- In a bid to control on the prices of edible oils and make its availability easily, the Government on September 16, 2004 cut tariff values on many vegetable oils by around $ 50 per tonne. The tariff value on crude palm oil was cut to $454 a ton from $504/ton; RBD palm oil to $489/ton from $543/ton from $532/ton; RBD palmolein to $497/ton from $552/ton; palmolein to $488/ton form $542/ton and crude soybean oil to $565/ton form $628/ton."

3. The Committee are constrained to note that the reply of the Government is silent on the issue pertaining to reintroduction of saving schemes for senior citizens and persons who have attained the age of 55 years and availed VRS. Taking note of the fact that inflation had affected the senior citizens the most and after realizing their financial plight the Committee had desired the Government to introduce some attractive savings schemes and tax free bonds for senior citizens after the withdrawal of Tax Free Bonds Schemes. The Committee reiterate their earlier recommendation and desire the Government to consider the reintroduction of tax free bonds and formulate attractive savings schemes for senior citizens expeditiously.

Non-Life Insurance—Fall in market share of Public Sector Insurance Companies

Recommendation (No. 5, Para No. 56)

4. The Committee were distressed to note that the management expenses of General Insurance Companies continued to be in excess of stipulated amount. Only New India Insurance Company had managed to limit these expenses within the permissible limit during the years 2001-02 and 2002-03. But thereafter it had increased tremendously. It was particularly regrettable to note that the insurance companies continued to incur excessive expenditure on management and IRDA had failed to effectively regulate this despite Committee's earlier recommendation to this effect. The Committee, therefore, recommended that this issue should be taken by IRDA on priority basis. The Government should hasten the process of modernisation/ computerisation of the general insurance companies so that such expenses were reduced and their services were improved Besides, they (insurance companies) should introduce new products to attract the masses and approach the untapped areas in a big way.

5. In their action taken reply, the Ministry of Finance (Department of Economic Affairs and Expenditure) have stated as under:

"The public sector insurance companies have already initiated the process of computerisation and networking of their offices. It is expected that implementation and use of IT in the public sector general insurance companies would help in controlling management expenses. Further, with an effort to cut down the wage bill, which forms a substantial portion of management expenses, the companies have implemented Special Voluntary Retirement Scheme to right size their employees strength. All these measures are expected to reduce the management expenses in the long run. Apart from the cost cutting measures, the companies have also initiated steps for increasing their business through corporate tie ups, opening of extension counters in rural areas and introduction in innovative products. With the control of expenses and increase in business, it is expected that management expenses ratio will be brought down to the permissible limit."

6. The Committee are constrained to find that their repeated recommendations for cutting the management expenses have not been taken by Government/IRDA seriously. They take note of the Government reply that the public sector general insurance companies have initiated computerisation/modernisation drive in order to cut the management expenses. They are of the view that this will not be sufficient unless time-bound target is fixed for completing the work of computerisation/modernisation. They desire the Government to fix the time frame within which the public sector general insurance companies should complete this work and would like to be apprised of the progress on a half yearly basis.

Subsidy

Recommendation (No. 7, Para Nos. 74, 75, 76)

7. The Committee noted that subsidies were an important fiscal instrument for correcting or modifying market determined outcomes to achieve specified objectives. The trend of providing subsidy had started since 1951-52 in the form of food subsidy. The subsidies had successively grown over the years and had been budgeted at Rs. 43,516 crore in 2004-05 (BE). The major portion of subsidy was accounted for by food subsidy. Its share in total subsidy in the current year had been kept at Rs. 25,800 crore.

8. The Committee were informed that a number of Committees had examined the issue of reforming subsidies and had suggested measures in this regard. Consequent upon this several measures had been taken *viz*. targeted approach to food subsidy (BPL families and Antyodaya Anna Yojana) under Public Distribution System, allowing Food Corporation of India to access market loans carrying lower interest rates, encouraging private trade in food grains, liquidating excess food grains stocks, modifying the Retention Price Scheme based subsidy on fertilisers as per the recommendations of the Expenditure Reforms Commission, and proposed phasing out of subsidies on PDS kerosene and LPG. They were given to understand that recently the National Institute of Public Finance and Policy (NIPFP) had been asked to prepare a blue print to ensure better targeting of subsidies.

9. The Committee expressed their deep concern over the fact that despite provision of huge sums by way of subsidies, objectives had not been fulfilled due to serious shortcomings in the delivery mechanism. Therefore, the Committee recommended that the Government should formulate a strategy to reduce pilferages and ensure benefits of subsidy to the really needy people. The study being conducted by NIPFP was to be expedited and the Committee should

be apprised of the recommendations and action taken by the Government at the earliest.

10. The Ministry in their written reply have submitted the following:

"In order to facilitate better targeting of subsidies, the Ministry of Finance has instituted a study in mid July 2004 to be undertaken by National Institute of Public Finance and Policy (NIPFP), with the following terms of reference:

(i) Examination of implicit and explicit subsidies under different budget heads and classifying them in to merit and non-merit categories.

(ii) Examining the design of major non-merit subsidies with a view to better target them to intended groups.

(iii) Analyzing the food subsidies in greater detail to improve the functioning of Food Corporation of India.

(iv) Quantifying the subsidy amount incurred on schemes for the poor, like small and marginal farmers, farm labour and the urban poor.

(v) Presenting a design to target, subsidies at the poor, like small and marginal farmers, or labour, urban poor, etc.

The National Institute of Public Finance & Policy (NIPFP) has submitted an Interim Report to the Ministry and the Report is under examination."

11. Expressing concern over the growing subsidy bill and poor delivery mechanism, the Committee had recommended to the Government to take effective measures so as to ensure better targeting of subsidies. They are given to understand that the National Institute of Public Finance and Policy (NIPFP) which was entrusted the job has since submitted an interim report. They would like to know the contents of the report and action taken by the Government thereon. Besides, they desire that the final report of the NIPFP should be expedited and the Committee be apprised of the developments from time-to-time.

Fall of Global Trust Bank (GTB) and role of RBI as regulator

Recommendation (No. 8, Para Nos. 84, 85, 86)

12. The Committee took note of the fact that while undertaking a review of the Global Trust Bank's performance by way of annual inspections for the years ending 31st March 2001 and 2003, the RBI had noted wide variance in the key indicators which had been wrongly certified by the Statutory Auditors, however, no action seemed to have

been initiated against them, since the Statutory Auditors came under the strict vigil of the Institute of Chartered Accountants of India, which failed to take action against them. The Committee found that this was a very serious and anomalous situation under which the RBI which was mainly responsible for monitoring the working of the banks had no control to take action against the erring auditors at the same time RBI as a strict regulator could not be absolved of their responsibility.

13. Besides, amalgamating the unhealthy banks with those which were performing well was not a healthy practice by any means, as this practice on the contrary encourages the unscrupulous entities to score their own vested interests by playing with the public money in a reckless and surreptitious manner.

14. In order to ensure that such happenings were not repeated in the future, sufficient safeguards, both legislative as well as administrative had to be built into the system. At the same time those who were responsible for such a failure should not be spared and suitable action including criminal action ought to be taken against them without further loss of time, so that such actions provide deterrence to other as well. The Committee desired to be apprised of the action in this regard at the earliest.

15. In their written submission the Ministry furnished *inter-alia* following reply:

"(i) The continuance of Shri Gelli as CEO was not considered prudent or desirable and on RBI's advice, Shri Gelli stepped down from the position of the CMD with effect from April 12, 2001 and subsequently resigned from the Board as a Director on June 16, 2001.

In February 2004, when Shri Gelli re-entered the Board of GTB, RBI expressed serious discomfort and the same was communicated to the Board/Government. Shri Gelli resigned from the Board of Directors of the bank in its meeting held on March 12, 2004.

RBI's action of asking Shri Gelli to step down from the chairmanship and directorship was expected to send strong signals to the shareholders and the market forces should have disciplined the errant behaviour. However, despite the regulator's actions, the market did not respond and continued to repose its faith in the bank as reflected in its market valuation.

(ii) Other actions taken in this regard include:—

(a) In terms of the scheme of amalgamation, all the employees of erstwhile GTB continue in service and are deemed to have been appointed in OBC. As such, irregularities if any, committed by the staff of the erstwhile GTB would have to be looked into by OBC for fixing staff accountability and initiating appropriate disciplinary and other proceedings. We have advised OBC in this regard.

(b) RBI complained against M/s. Lovelock and Lewes and M/s Pricewaterhouse, who were the statutory auditors for GTB for the years 2001-02 and 2002-03 respectively for making wrong classification of NPAs.

(c) RBI is examining the feasibility of initiating criminal action against the promoters/directors of the erstwhile GTB for misrepresenting/misreporting the financial statements for the period ended March 31, 2002 and 2003.

(iii) The important measures taken to strengthen the banking sector and prevent such recurrences in future are briefly, the following:

(a) As reported earlier, the following prudential/supervisory actions were taken:

- Introduction of capital adequacy standards on the lines of the Basel norms.
- Prudential norms on asset classification, income recognition and provisioning.
- Introduction of valuation norms and capital for market risk for investments.
- Enhancing transparency and disclosure requirements for published accounts.
- Aligning exposure/capital market exposure norms, single borrower and group-borrower ceiling with international best practices.
- Introduction of off-site monitoring system and strengthening of the supervisory framework/introduction of Risk Based Supervision for banks.
- The accounting treatment for impaired assets has been made closer to the international best practices and the final accounts of banks are transparent and more amenable to meaningful interpretation of their performance.
- Introduction of a framework for prompt corrective action.

(b) Further, RBI has taken measures to improve corporate governance in banks. RBI has put in place a system to ensure the 'fit and proper' status of CEOs of banks through a due diligence process. To ensure the continuing 'fit and proper' status of the Board of

Directors, RBI issued a directive to banks on June 25, 2004, in terms of which the Boards of the banks should constitute Nomination Committees to scrutinize the declarations relating to qualifications, expertise, track record, integrity, and other 'fit and proper' criteria of directors periodically.

(c) In the draft guidelines on ownership and governance issued on July 2, 2004 RBI has reiterated 'fit and proper' criteria for appointment of directors and CEO, so that the suitability of persons for appointments/continuation as directors/CEO is ensured.

(d) The draft guidelines on ownership and governance also envisage that the capital requirement of existing private sector banks should be on par with the entry level capital requirement for new private sector banks prescribed in RBI guidelines of January 3, 2001, which is initially Rs. 200 crore, with a commitment to increase to Rs. 300 crore within three years so that they have sufficient minimum size for financial stability. In order to meet this requirement, all banks in private sector should have a net worth of Rs. 300 crore at all times and those falling below the level will be required to submit to RBI for approval, a time bound programme for capital augmentation.

(iv) As regards legislative measures, the status is as follows:

(a) Section 30 of the Banking Regulation Act relates to audit of a banking company. Presently, there is no obligation on the auditors of a banking company to report any violation of the provisions of B.R. Act and regulations or directions issued thereunder while auditing books of the banks. Under the core principles of international accounting standards, the auditors are obliged to report to the supervisor the matters of significance, which are likely to have an adverse effect on the working of the banking company. Section 45MA of the RBI Act already casts an obligation on the auditors of the non-banking financial companies to report to the Reserve Bank any violation of any provision of RBI Act or direction issued thereunder.

In the Banking Regulation (Amendment) Miscellaneous Provisions Bill, 2003, which was tabled in the Parliament in August, 2003 but lapsed due to dissolution of Parliament, it was proposed to amend Section 30 of B.R. Act to provide that the RBI may direct the auditor in the matter relating to balance sheet, profit and loss account, disclosure of liabilities in the books of account or any other matter relating thereto. It was also proposed to provide that it would be the duty of the auditor to enquire and state in the report whether or not the banking company has complied with the provisions of this Act or any direction or notification or order issued thereunder. The Auditors should also enquire whether the information or statements called for by the RBI have been furnished to it or not and in case the bank has not complied with this requirement, the auditor would make a report to the RBI. The Bill is now being re-examined/reviewed."

16. The Committee find that after the fall of Global Trust Bank the RBI has taken several measures against the erring parties viz. Chairman and Managing Director, Statutory Auditors, Promoters and Directors of the erstwhile Global Trust Bank (GTB). Besides, the RBI also took various prudential and supervisory actions and measures to improve corporate governance in the Banks, so that such incidents do not take place in future. However, the Committee are surprised to find that Section 30 of the Banking Regulation (BR) Act which relates to audit of a banking company, does not cast any obligation on the auditors of a banking company to report any violation of the provisions of BR Act and regulations or directions issued thereunder while auditing books of the banks. They are given to understand that the Banking Regulation (Amendment) and Miscellaneous Provisions Bill, 2003, which was introduced in Lok Sabha in August 2003 but lapsed due to dissolution of Lok Sabha, proposed to amend Section 30 of BR Act to empower the RBI to direct auditors of banking companies in the matter relating to balance sheet, profit and loss account, disclosure of liabilities in the books of account or any other matter relating thereto. Under the above mentioned Bill, the Auditors were also required to enquire whether the information or statements called for by the RBI have been furnished to it or not and in case the bank concerned had not complied with this requirement, the auditor would make a report to the RBI. They take note of the fact that such a provision is already available in the relevant chapters of the Reserve Bank of India Act, 1934 which deals with non banking financial companies but the absence thereof in the Banking Regulation Act is conspicuous.

17. The Committee note that though a new Bill, viz., the Banking Regulation (Amendment) Bill, 2005 has been introduced recently and referred to them for examination and report, unlike the earlier Bill of 2003 that lapsed, it does not seek to amend Section 30 for

empowering RBI in connection with audit of Banking companies. In this regard, they have been informed that only such of the amendments that were felt to be of critical importance in the Bill proposed earlier were finally incorporated in the Banking Regulation (Amendment) Bill, 2005. The Committee are unable to understand as to why this important provision aimed at empowering RBI in the matter of audit of banking companies has not been considered to be of priority. The Committee, therefore, desire that provisions for enabling RBI to regulate auditors by amending Section 30 should be incorporated in the Banking Regulation (Amendment) Bill, 2005.

Disinvestment Policy Document

Recommendation (Sl. No. 11, Para Nos. 124, 125 and 126)

18. The Committee had expressed their serious concern over the fact that despite their repeated recommendations in their earlier reports on Demands for Grants in 2001-2002, 2002-2003 and 2003-2004, urging the Government to bring out a comprehensive disinvestment policy document which should be laid before the Parliament for its approval, the Government had neither complied with the recommendations nor did they submit convincing reasons as to why the recommendations of the Committee were not implemented. The Committee had also regretted to recall that in their reply in September, 2002 *vide* OM No. 45011/3/2000-Parl (Vol. II) dated 6.9.2002, the Government had made a request to the Committee to allow some more time to prepare and bring out a policy document which had not been materialised till date. The Committee were deeply concerned that in the absence of a uniform Comprehensive Policy, disinvestment of PSUs was being done on case-to-case basis thus subjecting disinvestment programme volunerable to public comments and apprehensions. The Committee strongly urge the Government to shun its case-to-case basis approach and adopt a cohesive and uniform approach so that the policy might gain more transparency and credibility.

19. The Committee had been informed that the policy as stated in the NCMP was the policy of the Government towards disinvestment. The Committee were not able to understand as to why the Government was wary of bringing forward a Comprehensive Policy Document which might address all the aspects such as valuation, employees welfare, etc. and which would deal with all types of PSUs. In the absence of a clear cut policy, the Government had to evolve a new methodology every time to deal with a particular situation. They were not convinced by the Government's reply that adequate publicity had

been given to the policy as stated in NCMP in the Budget Speech, interviews of the Finance Minister on TV and print media. They could see no reason why the Government could not bring the policy document before Parliament in deference to the wishes of the Committee.

20. The Committee therefore reiterated their earlier recommendations urging the Government to bring out a comprehensive document on disinvestment policy to be placed before the Parliament for its approval without further delay.

21. In their reply the Ministry have stated as under:

"The policy of the Government with respect to the public sector has been laid down in the National Common Minimum Programme and the Government is following these principles while implementing disinvestment on a case-by-case basis. A paper outlining the implementation strategy for disinvestment is under consideration."

22. On being asked about the factual position on the preparation of disinvestment policy document, the Ministry of Finance, Department of Disinvestment—replied as below:

"The undersigned is directed to refer to OM No. 11/1/13/2004-FC dated 23.2.005 of the Lok Sabha Secretariat on the above subject and to say that preparation of white paper on Disinvestment has already been identified by the Government as one of the thrust areas for implementation by the Department of Disinvestment and the work is under progress."

23. The Committee are not satisfied with the casual reply of the Government that the policy as stated in NCMP constitutes the disinvestment policy of the Government. They take note of the fact that Government are preparing a White Paper on the subject. They are of the view that neither the principles laid down in NCMP nor the White Paper can be a substitute for a comprehensive disinvestment policy covering all aspects such as valuation and employees welfare etc. The Committee cannot help noting that the Government chose to give a stereotyped reply on the subject. Hence, they reiterate their earlier recommendation that the Government should come out with a comprehensive disinvestment policy document without further delay and desire that the preparation of the White Paper be expedited.

CHAPTER II

RECOMMENDATIONS/OBSERVATIONS WHICH HAVE BEEN ACCEPTED BY THE GOVERNMENT

Recommendation (Sl. No. 1, Para Nos. 21, 22, 23, 24, 25 & 26)

It could be seen that inflation rate (based on WPI) had a noticeable increase in the year 2002-03. Thereafter it had reduced to 4.6 per cent in 2002-04. It remained below 5 per cent till the middle of May 2004. Subsequently this rate has increased and reached the level of 7.61 per cent during the week ending July 31, 2004. Retail price inflation, as measured by the Consumer Price Index for Industrial Workers (CPI-IW) stood at 3.5 per cent in March 2004. The annual rate of inflation based on CPI-IW was 3.0 per cent during June 2004.

The Committee further noticed that computation of CPI-IW and WPI differ substantially in terms of base year, weightage given to different items etc. It is further seen that CPI-IW is more sensitive to changes in food prices while changes in petroleum product prices are better reflected in WPI. They find that work on constructing a separate price index for services has been started.

The basic reasons furnished for rise in inflation are increase in the prices of potatoes by 40.6%, tea by 24%, minerals by 153%, coal by 15.9%, petroleum products by 14.2 per cent, sugar, gur and khandsari by 11.9%, basic metals and metal products by 29.2% and iron and steel by 45%.

The Committee are unable to comprehend the lower growth in inflation rate based on CPI-IW, which was 3.0% in June 2004 as compared to WPI which was 5.8% in the same period, when much of the price rise is in respect of food and minerals. In case of petroleum products it is only 14.2%. The Committee desire that this should be further explained.

They are also of the opinion that the base year for computing CPI-IW should be updated to make it truly representative of retail price. The work of preparing a service price index should be expedited.

They apprehend that growing inflation will frustrate the achievement made by decade old reforms process. The Government should tackle this menace tactfully by employing its resources to the full extent. They expect that the Government would come out with adequate fiscal and monetary measures to handle this situation. The reasons causing present inflation need to be identified and dealt with effectively. The Committee, therefore, recommend that in order to maintain the tempo of growth the Government must tackle the situation without delay.

Reply of the Government

The WPI and CPI (IW) series differ significantly in terms of their weighting diagram. While food articles have a weight of 57 percent in the CPI (IW) series, food articles in the primary group and food products in the manufactured products group in the WPI series together have a weight of only 27 percent. The CPI (IW) series is therefore, more sensitive to changes in food prices. The fuel group on the other hand gets a much higher weight in the WPI series (14.23) than in the CPI (IW) series (6.28). International price movements of crude oil would, therefore, have a greater bearing on the WPI series than on the CPI (IW) series in terms of their direct impact.

Weighting diagram of Major groups of WPI

Item	WPI
1	2
All commodities	100.00
Primary articles	22.03
Fuel, power, light & lubricants	14.23
Manufactured products	63.74
Primary articles (22.03)	
Food articles	15.40
Food-grains	5.01
Rice	2.45
Wheat	1.38
Fruits & vegetables	2.92
Non-food articles	6.14

1	2
Fuel, power light & lubricants (14.23)	
Coal Mining	1.75
Minerals Oils	6.99
Liquefied petroleum gas	1.84
Kerosene	0.69
Petrol	0.89
High speed diesel oil	2.02
Electricity	5.48
Manufactured products (63.74)	
Food products	11.54
Sugar	3.62
Edible oils	2.76

Weighting diagram of Major groups of CPI (IW)

CPI (IW) General	100.00
Food	57.00
Pan, supari, tobacco and intoxicants	3.15
Fuel & light	6.28
Housing	8.67
Clothing, bedding and footwear	8.54
Miscellaneous group	16.36

Items responsible for high inflation

The current high inflation in terms of WPI is partly statistical due to the fact the WPI base was low at this time last year. In fact, WPI for all commodities remained in the narrow band of 173.7 to 174.1 for 19 weeks during 26 April to 30 August 2003 and the annual WPI inflation declined from 6.7% to 3.9% during this period. On contrast, in the current year the WPI increased from 181.2 on 24 April, 2004 to 187.2 on 7 August, 2004 driven by sharp increases in the prices of petroleum products and some manufactured products, and annual inflation has increased from 4.3% to 8% during this period.

In addition to statistical reasons mentioned above, high rate of inflation in the current year is due to substantial price rise (more than 10%) in nine items/groups *viz*. **potatoes (46.9%), tea (26.1%), minerals (15.3%), coal (15.9%), petroleum products (17.4%), sugar-gur-khandsari (11.2%), coconut oil (24.3%), iron and steel (46.2%), and other basic metals and products (17.6%). These items/groups have total weights of only 21.8% in the WPI, but contributed 69% to the current annual inflation** compared to their contribution of only 34.6% last year. Though the prices of food articles remained moderate, the other group of WPI like Fuel and Manufactured products have substantially contributed in the high inflation rate which are not reflected at the same rate in CPI.

In fact, Iron & steel, with weights of only 3.6%, contributed 20.2% to the inflation. If we add minerals, coal, POL and other metals, composite weights of these five groups become 17.6%, and their contribution amounts to 62.7% of the overall inflation.

Consumer Price Index

In the opinion of some economists, WPI inflation is not an appropriate measure to determine the impact of price rise on the cost of living of the common man. Rather, the Consumer Price Index for Industrial Workers (CPI), which includes selected services and is measured on the basis of retail prices and also used to determine the dearness allowance (DA) of industrial workers in both the public and private sectors, would be an appropriate indicator of general inflation. In sharp contrast to the WPI, the CPI inflation had been stable and moderate. This is because food and primary products constitute higher weights in CPI than in WPI and in general the price increases of these items have been moderate in the current year.

Annual point-to-point inflation in terms of the CPI-IW declined significantly from 5.1 per cent in April 2003-04 to 3.5 per cent in March 2003-04 and further to 2.2 per cent in April 2004. Although the inflation rate increased to 2.8 per cent in May 2004, 3 per cent in June 2004 and further 3.2 per cent in July 2004, it is still lower than 4.2 per cent recorded in July 2003 and lower than the average WPI inflation at 7.0% in July 2004.

The current series of CPI (IW) are estimated with 1982 as the base year. An expert group constituted by the Government to revise the CPI-IW base is at a very advanced stage of submitting their report.

Anti-inflationary measures

Inflation hurts everybody particularly the poor whose incomes are not indexed to prices. High inflation puts a pressure on interest rates leading to a rise in project costs and investment. It also reduces real interest rates affecting adversely savings rates. Therefore, containment of inflation remains high on the agenda of the government. Anti-inflationary policies of the government include strict fiscal and monetary discipline, rationalisation of excise and import duties of essential commodities so that there is no undue burden on the poor, effective supply-demand management of essential items through liberal tariff and trade policies, and strengthening the public distribution system.

- On the 18th August 2004 government reduced customs and excise duties on selected petroleum products to keep their domestic retail prices in check in the face of the global oil price surge to a record high. Customs duty on petrol, diesel, LPG and kerosene were reduced by 5% each, while excise duty was reduced by 3% each for petrol and diesel and 4% for kerosene.

DUTY CONCESSIONS

(In per cent)

	Customs		Excise	
	New	Old	New	Old
Petrol	15	20	23	26
Diesel	15	20	8	11
Kerosene	5	10	12	16
LPG	5	10	8	8

- On the 20th August 2004 government reduced customs duties on non-alloy steel and ships for breaking to 5 per cent from 10 and 15 per cent respectively in order to check high inflation in metals and metal products. Melting scrap of iron and steel was fully exempted from customs duty.

Custom Duty

Product category	New	Old
Non-alloy steel	5	10
Ships for breaking	5	15
Iron and steel Scrap	Nil	5

- To check the liquidity overhang in the system. On September 11, 2004 the Reserve Bank of India has hiked the cash reserve ratio (CRR) to be maintained by banks, by 50 basis points to 5 per cent of their demand and time liabilities. The CRR will be raised in two stages by 25 basis points each: First, from the fortnight beginning September 18 and then from October 2. The move is expected to take out around Rs. 8,000 crore worth of liquidity from the system. The money supply has been hovering at 16.6 per cent as compared to 14 per cent last year.
- In a bid to control on the prices of edible oils and made its availability easily, the Government on September 16, 2004 cut tariff values on many vegetable oils by around $50 per ton. The tariff value on crude palm oil was cut to $454 a ton from $504/ton; RBD palm oil to $489/ton from $543/ton; Palm oil to $471/ton from $523/ton; crude palmolein to $479/ton from $532/ton; RBD palmolein to $497/ton from $552/ton; palmolein to $488/ton from $542/ton and crude soyabean oil to $565/ton from $628/ton.

Recommendation (Sl. No. 2, Para No. 35)

It is observed that different cesses have been imposed from time to time on various items and products, such as coal and coke, jute, tea, coffee, tobacco, rubber, sugar etc. The proceeds from these cesses are deposited in Consolidated Fund of India. The Committee are given to understand that the proceeds of these cesses are exclusively used for the development of the industry/cause for which they have been imposed. They note that the recently imposed induction cess aims to collect Rs. 5000 crore (Rs. 2400 crores from cess of percent on aggregate duties on customs, excise and service tax and Rs. 2510 crore from cess on corporate and income taxes) which is to be spent on elementary education.

Reply of the Government

Committee's observations noted as statement of facts.

[Ministry of Finance's OM No. 9 (5)-W&M/2004
dated the September 29, 2004]

Recommendation (Sl. No. 2, Para No. 36)

The Committee apprehend that the huge amount of cess money may remain unutilized and could be diverted to other areas. The Committee, therefore, desire that there should be a non lapsable dedicated fund where the proceeds should be deposited. They do not agree with the contention of the Ministry that institution of such a fund makes sense only when there is surplus budget. Even now, there are some existing funds like Central Road Fund wherein the proceeds of cess are kept. Therefore, in view of the Committee such a fund of perpetual nature should be established for education as early as possible, so that the proceeds are utilized for development of this sector alone.

Reply of the Government

Government has established a fund titled as **'Prathmik Shiksha Kosh'** which will be maintained by the Ministry of Human Resource Development, Department of Elementary Education and Literacy on a proforma basis. The money for it would flow from the education cess. The receipts will be utilized solely and exclusively for elementary education, including Sarva Shiksha Abhiyan and Nutritional Support to Primary Education (Mid-day Meal Scheme). The fund will be non-lapsable in nature and balances remaining un-utilised in a year will be available on a rollover basis for the said purposes.

[Ministry of Finance OM No. 9 (5)-W&M/2004
dated the September 29, 2004]

Recommendation (Sl.No. 6, Para No. 61)

The Committee find that there has been constant shortfall in the actual utilization of funds under this head. The major savings in this regard have been made by CPWD. The Committee are unable to comprehend the reasons for huge savings made by CPWD. If the requirements were lower why provisions at BE stage were always kept at higher side. The Committee take serious view of such budgetary allocations and recommend that the Government should take utmost care while making provisions based on actual requirements. They would further like to be apprised of details of expenditure made by CPWD during the last five years.

Reply of the Government

As per the norms of Govt. of India all Major Works of Civil/ Electrical nature are required to be done through CPWD. After the approval of Competent Authority for any Civil/Electrical Work estimate is taken from CPWD and based on the estimate and the availability of funds in the budget the authorization issued through the Pay & Accounts Office to CPWD. No authorization can be issued unless the budget provision of equivalent amount exist in the budget in case where the CPWD fails to complete the job before the end of the financial year the CPWD is not entitled for drawing the funds even though it is authorized to them by the PAO and so the funds remains unutilized to that extent. Since CPWD has its own procedures of awarding the budget to sub-contractors etc. and there is no control of CNP over the procedures of CPWD. Therefore, actual expenditure depends on authorization of budget amount to CPWD and at times it becomes difficult to avoid savings. However, the authorization made has reduced in subsequent years. The committee's recommendations is noted for future compliance. The details of expenditure made by CPWD during the last five years is as follows:—

(Figures are in thousand)

Year	Authorization made	Utilization of fund by CPWD
1999-2000	*	*
2000-01	17700	5024
2001-02	12284	5432
2002-03	11000	8160
2003-04	4826	2391

*There is no saving in expenditure under Major Works during the year 1999-2000.

Recommendation (Sl.No. 8, Para No. 83)

The Committee note with serious concern the recent developments that have taken place in the Global Trust Bank ultimately resulting in placing it under an Order of Moratorium for about three months *w.e.f.* July 24, 2004 by the Reserve Bank of India. This step has reportedly been taken to protect the interest of the depositors as well as the banking system. In order to further mitigate the problem of the investors, the Reserve Bank of India has prepared a scheme of amalgamation of the bank with Oriental Bank of Commerce.

Reply of the Government

(i) On an application of RBI, the Central Government issued an Order of Moratorium in respect of Global Trust Bank Ltd. effective from the close of business on July 24, 2004 upto and inclusive of October 23, 2004.

(ii) A proposal was received from Oriental Bank of Commerce (OBC) for merger of Global Trust Bank Ltd. (GTB) with it. Taking into account the interests of depositors of GTB, as well as its strengths and weaknesses, RBI prepared a draft scheme of amalgamation of GTB with OBC and the draft scheme of amalgamation was forwarded to both the banks on July 26, 2004. The banks were given time up to August 7, 2004 to consider the draft Scheme. The draft Scheme was placed on the website of RBI and notices were also published inviting objections/suggestions from depositors, shareholders and others by August 7, 2004.

(iii) The suggestions and objections to the draft scheme of amalgamation received from the Transferor bank, Transferee bank, depositors, shareholders of the Transferor bank and others were examined by RBI and the same were forwarded to Government of India along with a copy of the final draft Scheme of Amalgamation of the GTB with OBC and recommended for sanction without further modification or with such modifications as Government may consider necessary, in terms of Sub-Section (7) of Section 45 of the Banking Regulation Act, 1949.

(iv) The Government of India sanctioned the Scheme of Amalgamation of GTB with OBC on August 13, 2004. The Scheme has come into force in August 14, 2004.

(v) Customers, including depositors of the GTB were able to operate their accounts as customers of OBC with effect from August 14, 2004.

(vi) In accordance with the Scheme of Amalgamation, if any surplus remains after meeting all the liabilities out of the realisation of assets of the GTB, the shareholders may receive *pro-rata* payment.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl. No. 8, Para No. 84)

The Committee take note of the fact that while undertaking a review of the bank's performance by way of annual inspections for the years ending 31st March 2001 and 2003, the RBI had noted wide variance in the key indicators which had been wrongly certified by the statutory auditors, however, no actions seems to have been initiated against them, since the Statutory Auditors come under the strict vigil of the Institute of Chartered Accountants for India, which failed to take action against them. The Committee find that this is a very serious and anomalous situation under which the RBI, which is mainly responsible for monitoring the working of the banks, has no control to take action against the erring auditors at the same time RBI as a strict regulator cannot be absolved of their responsibility.

Reply of the Government

(i) RBI's inspection with reference to the bank's position as on March 31, 2002, conducted from July to October 2002, revealed significant variation between the assets classified as non-performing by the bank and those classified as NPA by the Inspecting Officers. There was also considerable shortfall in provisioning. After considering the provisions required to be made by the bank, the IO assessed the net worth to be negative at (-) Rs. 416.70 crore. In view of the very large variance in the assessment of the bank's financial position as reported by the auditors and as assessed by the RBI inspectors, the RBI engaged a firm of Chartered Accountants to undertake an independent assessment and reconcile the position. The Chartered Accountants' report dated February 24, 2003 confirmed RBI's assessment, except for minor differences. A complaint was filed with ICAI against the statutory auditors for 2001-02 for wrong classification in respect of NPAs in the accounts for 2001-02. The bank was put on a monthly monitoring schedule and the bank was advised to change the statutory auditors for the year ended March 31, 2003.

(ii) The RBI inspection that was conducted from October 2003 to January 2004 found that the divergence between the reported accounts and the assessment of the Inspecting Officers of the NPAs and of the required level of provisioning continued to be very large; against the marginally positive net worth reported by the bank for March 2003 at Rs. 2.42 crore, erosion in the net worth was in fact Rs. 740 crore. In view of the large divergence between the NPA figures reported by the bank duly certified by the statutory auditors and those assessed by the RBI Inspectors, the explanation of the auditors was called for. As the explanation provided was not satisfactory, the matter was reported to the Institute of Chartered Accountants of India (ICAI), for initiating action.

(iii) Apart from debarring the firms that had audited the bank's books for 2001-02 and 2002-03 from statutory audit, banks and financial institutions have been advised by RBI not to use the services of the two firms of Chartered Accountants for any audit related work. CAG has also been advised about the action taken by RBI for similar action by CAG.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl.No. 8, Para No. 85)

Besides, amalgamating the unhealthy banks with those which are performing well is not a healthy practice by any means, as this practice on the contrary encourages the unscrupulous entities to score their own vested interests by playing with the public money in a reckless and surreptitious manner.

Reply of the Government

(i) The amalgamation was done after having given sufficient time and opportunity to the bank to infuse capital while simultaneously ensuring through directions issued to it, that it did not increase its risk-weighted assets.

Since the bank failed to either infuse capital or to offer any viable solution, the option of compulsory merger was resorted to. This option is exercised only as a last resort in public interest and in the interest of the depositors. OBC's proposal to takeover GTB was examined from the perspective of the strength of the bank and synergies available. OBC's financial parameters showed that it had sufficient financial strength to absorb GTB. So far as the synergies were concerned, the two banks complemented each other, OBC being north based and GTB having its branches mainly in the south. They had a common technology platform (FINACLE). GTB's strength in non-interest income portfolio benefited OBC. In view of the strategic advantages available in the amalgamation of GTB with OBC, this was considered the optimal solution.

(ii) In this regard, it is useful to note the various remedies and options available to RBI for dealing with weak banks.

One option is to allow the weak bank to function as a narrow bank, which *inter alia* means restricting the growth of risk-weighed assets. This is unlikely to help a weak bank in the long run since it would result in (a) absence of growth and loss of customers (b) mismatch in pricing of assets and liabilities (c) staff attrition/loss of morale (d) lack of solvency and tight liquidity making the bank highly vulnerable to large withdrawals.

Second option is to restructure and recapitalised the bank by further infusion of capital and other corrective measures. Although infusion of capital is the preferable option for resolution of problem banks, one of the important concerns in this regard is the source of funds. As regulators, it is necessary for RBI to ensure that the contributions/ investments are made from genuine and *bona-fide* sources in a transparent manner and do not attract domestic and international legal prohibitions against money laundering and related offences as applicable. RBI has also to ensure that prudential standards are not compromised.

Third option would be to merge the weak bank with another bank under the provisions of the Banking Regulation Act, 1949.

(a) Voluntary merger under Section 44A of the Banking Regulation Act, 1949.

> "Section 44A sets out of the procedure to be followed in case of voluntary merger/amalgamation between two banking companies. Voluntary mergers are the least cost option and take into account the interests of both depositors and shareholders."

(b) Reconstitution/Amalgamation under Section 45 of the Banking Regulation Act, 1949.

"Section 45 of the Act empowers RBI to apply to the Central Government for suspension of business by a banking company and prepare a scheme of reconstitution or amalgamation. The merger under Section 45 of the Act, *ibid* is done to protect the interests of the depositors and in the interest of the banking system.

Lastly, when all attempts to restructure a weak bank fail, it may be placed under liquidation. In such a case, the claims of insured depositor may have to be borne by Deposit Insurance and Credit Guarantee Corporation (DICGC). This option has certain disadvantages; (a) the pay off by DICGC would be a direct cost to the exchequer (b) the depositors would lose confidence in the banking system (c) the investors' confidence will be shaken (d) liquidation of a bank may also lead to 'domino effect' and would cause systemic problems.

It may be stated that amongst the various options discussed above, compulsory merger under Section 45 has been resorted to as a viable option for resolution of many problem banks, in the interest of the depositors based on past experiences of RBI.

(iii) In order to prevent unscrupulous persons from acquiring control of the banks, RBI is currently insisting on 'fit and proper' status of directors both at the time of induction and for their continuance. RBI has also put in place a mechanism by which it ensures that shareholders, whose aggregate holdings are above the specified thresholds, meet the fitness and propriety tests before grants of acknowledgment of transfer of shares. In determining whether the applicant (including all entities connected with the applicant) is fit and proper to hold the position of a shareholder at the lowest threshold of 5% and above, RBI takes into account all relevant criteria, including the applicant's integrity, reputation and track record in financial matters and compliance with tax laws which are necessary to protect the interests of the depositors and the integrity of the financial system.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl. No. 8, Para No. 87)

The Chartered Accountants Act, 1949, which is a very old and toothless legislation, should be amended forthwith.

Reply of the Government

This matter has to be taken up with Department of Company Affairs for amendment for the Chartered Accountants Act, 1949. A reference has been made to them.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl.No. 9, Para No. 99)

The Committee note with serious concern the rising trend of public debt, which is 43.37% of GDP as per the budgetary estimates for the year 2004-05. The share of internal debt in the total outstanding domestic debt of the Central Government was 66.4 per cent at the end of March, 2003. They further find that the large and persistent fiscal deficit is primarily responsible for increasing internal debt. Further taking advantage of lower interest rates and large build up of foreign exchange, the Government prepaid external debt of US$ 2.9 billion and US$ 3.8 billion in the years 2002-03 and 2003-04 respectively by borrowing from market. Thus the external debt has been reduced while internal debt has continued to swell.

Reply of the Government

Committee's observations are accepted as statement of facts.

Recommendation (Sl. No. 9, Para No. 100)

It is further seen that the debt-GDP ratio for the Centre and State Governments together increased from 70.7% in 2001-02 to 74.7% in 2003-04. The alarming increase in debt-GDP ratio has been on account of burgeoning fiscal deficit which impacts of inflation and interest rates adversely. The Committee apprehend that continually increasing ratio of debt to GDP runs the risk that debt will get on unsustainable path which can lead to national insolvency.

Reply of the Government

The Committee's observations are noted. The Fiscal Responsibility and Budget Management (FRBM) Act, 2003 seeks to address the concerns raised by the Committee.

Recommendation (Sl. No. 13, Para No. 138)

The Committee are not inclined to accept the reasons stated by the Government for the variations between BE, RE and Actuals. The

Government's reply that the projections were revised on the assessment of activities to be undertaken by the Department is not convincing. The Committee are not able to understand why such variations as above have occurred for four years. In the opinion of the Committee, the Government could have projected realistic estimates in the following years based on past experience. The Committee feel that the Government have not taken due care while making budgetary allocations over the years. The Government should adhere to fiscal prudence and avoid violent budgetary variations and make budgetary projection/allocations more realistic and accurate in future.

Reply of the Government

While submitting the Budget Estimates for the ensuing year, the estimates of office expenditure are projected on the basis of the anticipated activities during the year for which the estimates are submitted. While every effort is made to make realistic estimates, the actual expenditure depends on the volume of work that is actually undertaken in the Department during that particular year. The major factor which governs the patterns and volume of the expenditure in this Department is the volume of disinvestment cases pursued by the Department during any particular year. There is increased requirement of use of office machines and equipments, telephones, staff cars and stationery, etc., throughout the process and diminishes with the completion of the transaction.

The activities of the Department being new and without comparable precedent in the Government, the estimates of the office expenditure could not be related to any past precedent. The requirements for office expenditure is reviewed at the time of Revised Estimates keeping in view the activities in hand and anticipated during the rest of the relevant Financial year. The actual expenditure over the years, has gradually come closer to the Revised Estimates. The Government would in keeping with the spirit of the recommendations of the august Committee, make additional efforts to ensure that the budgetary projections are as realistic, actual and accurate as possible.

[Ministry of Finance (Department of Disinvestment) O.M. No. 35 (1) 13/2004-Parl. Vol-II dated 19.10.2004]

CHAPTER III

RECOMMENDATIONS/OBSERVATIONS WHICH THE COMMITTEE DO NOT DESIRE TO PURSUE IN VIEW OF THE GOVERNMENT'S REPLIES

Recommendation (Sl. No. 3, Para Nos. 40 & 41)

The Committee take note of the fact that from the year 2001-2002 onwards there has been constant savings in expenditure under this head. They find that in the year 2001-02 funds, as allocated could not be spent because of cancellation of scheduled tour programmes of officials and austerity in expenditure. In the subsequent year *i.e.* 2002-03 again higher budgetary allocations were made in anticipation of official tours, however they could not materialize due to some unexplained factor. Again the budgetary estimates were kept at even higher side in the following year (2003-04). However the actual expenditure incurred has always been abysmally low compared to the estimated amount.

It is seen that no austerity has been exercised while making allocations at budgetary stage. Even while revising allocations, little consideration has been paid to the actual expenditure incurred in the past. This shows that budgetary and revised estimates have always been made without taking into account the actual requirements as experienced in the previous years. The Committee would therefore recommend that projection of required funds should be made on a more realistic basis so that resources are not unnecessarily kept unused and are allocated more judiciously.

Reply of the Government

It pertains to domestic travel expenses for Central Stamp Depot (CSD), Nasik Road.

Surrender under Domestic Travel Expenses (DTE) for these years against BE/RE is mainly due to the reasons that tour programmes of various officials did not materialize and also because of austerity observed in expenditure. More provision was made in BE for the year 2003-04 mainly due to increase in air/railway fare. The officials of Central Stamp Depot (CSD) were to make extensive tours to recover the huge dues outstanding in various States. However, majority of the tours did not materialize. The figure for domestic travel expenses for CSD was reduced in RE 2003-04.

The actual expenditure in the year 2003-04 under domestic travel expenses for CSD was Rs. 0.58 lakhs only.

The Committee's recommendation is noted for future compliance.

Recommendation (Sl. No. 4, Para No. 45 & 46)

It is seen that throughout the period 2001-02 to 2003-04 the budgetary allocations for giving Grants-in-Aid to various financial institutions were revised upwards at RE stage owing to additional requirements for obligatory transfer of foreign assistance. The actual expenditure, however, varied depending on actual claims for reimbursement received from financial institutions. Thus, the budgetary allocations have always been less than the requirements and had to be subsequently revised upwards to make up for the shortfall.

The Committee are unable to comprehend the reasons for keeping lower outlays when the actual requirement is far higher. This shortsightedness on the part of the Government may result in undue diversion of resources. Therefore, the Committee recommend that every effort should be taken to make realistic estimations of allocations keeping in view all the anticipated demands.

Reply of the Government

In this regard, Banking Division have conveyed the observations of the Standing Committee on Finance to the concerned Financial Institutions and requested them to provide realistic estimates at both the stages of BE and RE in future. A copy of their letter No. 15(5) 2004-IF.I. dated 6th September, 2004, is enclosed.

In so far as grant assistance to UTI is concerned, the Capital Market Division has informed that the Non-Plan assistance as mentioned in para 42 of the Report have been provided to UTI pursuant to the decision of Cabinet Committee on Economic Affairs that the Government will honour the redemption guarantee for the US-64 unit holders and will also meet any shortfall in the Assured Return Schemes (ARSs) of the erstwhile UTI. With a view to ring-fence the liability of the Government of India, the decision to foreclose ARSs have been taken from time to time after taking into account the economic scenario and the trends in the interest rates. The exact amount of assistance required to foreclose ARSs also depends on the net asset value (NAV) of the scheme as on the date of foreclosure. Although, every effort have been made to provide a fair estimate of the assistance at the budgetary stage itself, because of the reasons mentioned above, the figures had to be revised at RE stage for the period under reference.

During the financial year 2004-05, a provision of Rs. 1200 crore have been made for assistance to UTI. So far, a total assistance of Rs. 724 crore (50% as cash and 50% as Bonds) have been provided to UTI for the foreclosure of two ARSs. It also proposed to foreclose the balance three ARSs by March, 2005. Although the exact shortfall would be based on the NAV of the schemes of the date of foreclosure, it is expected that the requirement would be met out of the budgetary provisions made during the year.

[MoF/DEA/F. No. 5/15/2004-IFA, dated 23rd Sept. 2004]

F.No. 15(5)/2004-IF-1
Government of India
Ministry of Finance
(Banking Division)

JEEVAN DEEP BUILDING, 3RD FLOOR,
PARLIAMENT STREET, NEW DELHI
Dated 6th September, 2004

To

CMD IDBI, Mumbai
CMD, SIDBI, Lucknow
CMD, NABARD, Mumbai
CMD, IIBI, Kolkata
CMD, Exim Bank, Mumbai
CMD, IFCI Ltd., New Delhi
MD & CEO, ICICI Bank, Mumbai
Chief Operating Officer, IDFC, Mumbai

Subject: Examination of Demands for Grants (2004-05) of M/o Finance

Sir,

I am directed to refer to the above mentioned subject and to convey the observation of Standing Committee on Finance (Lok Sabha) on Demands for Grants (2004-05) to various financial institutions that projected outlays in Budget Estimates are lower than the actual requirement in the Revised Estimates. The Committee has adversely commented that this shortsightedness may result in undue diversion of resources. The Committee has recommended that every effort should be taken to make realistic estimations of allocations keeping in view all the anticipated demands. You are therefore requested to provide a realistic estimate at both the BE and RE stages to avoid such adverse comments from Standing Committee on Finance in future.

Yours faithfully,

Sd/-
(Margaret)
Under Secretary to the Govt. of India.

Recommendation (Sl. No. 5, Para No. 55)

The Committee take serious note of the fact that the market share of non-life public insurance companies has gone down by 4.75 per cent in the last year. This is due to competitive pressure from private players, lesser use of technology and inadequate utilization of the distribution channels. They are constrained to express their anguish that if such trend is not arrested the day is not too far when the entire business will be grabbed by private players. They are of the view that competition *per se* is not bad as it compels the competitors to improve the quality of the product/service. The public sector non-life insurance companies will have to upgrade the quality of the service in order to be able to face the competition from the private operators.

Reply of the Government

The public sector non-life insurance companies have initiated a series of measures for improvement in the quality of services to face the competition from private players effectively. These include upgradation of information technology through implementation of "Genesis Enterprise" programme and networking of Branch Offices, Division Offices and Regional Offices with their Head Office. Implementation of IT plan would facilitate on-line issue of policies/documents, quicker settlement of claims leading to greater degree of customers' satisfaction. Apart from this, the public sector companies have entered into tie-up arrangements with corporate clients to ensure cashless claim settlement at the point of servicing of claims. It is expected that with the improvement in the quality of services, the public sector general insurance companies will be able to face competition from the private players more effectively.

[Ministry of Finance OM. No. 64 (77)/2004-OS) (Ins.)
dated 29th September, 2004]

Recommendation (Sl. No. 10, Para No. 109)

The Committee are deeply concerned to note that the major burden of fiscal adjustment has been borne by capital expenditure and its share of percentage of GDP was merely 2.5 per cent in 2002-03. The Committee take note of the fact that in the Budget 2004-05, the share of plan expenditure has been raised by 20% which is the biggest increase so far. The non-plan expenditure consists of mainly four items *viz*. Interest payment, expenditure on defence (both revenue and capital), expenditure on subsidies and transfer to the States. These four components comprise about 85 per cent of the total non-plan budget of the Central Government.

Reply of the Government

The level of capital expenditure in the Central Budget has been around 2.5 per cent of GDP for past several years. Since a substantial part of fiscal deficit is used up in financing revenue deficit, the availability of resources for capital expenditure has been limited. In fact, time bound elimination of revenue deficit to create fiscal space for more capital expenditure is one of the prime objectives leading to the enactment of the Fiscal Responsibility and Budget Management Act, 2003. However, growth in capital expenditure has kept pace with the GDP growth. There are two developments having a bearing in this matter which need to be noted. Firstly, Plan Grants to States have been increasing year after year and since the assets created from such financing support belong to the State Government, there is capital expenditure but in the books of the State Government.

Another factor leading to an apparent stagnation in the capital expenditure of Central Government to GDP ratio is that the Central Public Sector Undertakings (CPSUs) are being permitted to avail of external aid directly rather than through Central Budget. If the external aid to CPSUs were to be routed through the Budget, the capital expenditure of the Central Government would have been higher by way of equity and loans investment.

Therefore, while the capital expenditure in Central Budget appears to be low or stagnating as per cent of GDP, it is important to simultaneously note that through its policy of disintermediation of external aid to CPSUs and a steady rise in the level of grants to States, the Central Government has been facilitating the incurrence of capital expenditure.

Other observations of the Committee have been noted.

Recommendation (Sl. No 10, Para No. 110)

They further find that the Government is intending to reduce non-plan expenditure by reducing interest expenditure, better targetting of subsidies, lesser expenditure on general administration and by following FRBM Rules, 2004 strictly. It is further found that in the plan expenditure itself, the share of expenditure on creating capital assets is merely 30 per cent.

Reply of the Government

As explained at reply to para 109 above, Plan grants to States are revenue expenditure of the Central Government, but these are intended to finance the capital expenditure and social sector developmental expenditure of the States. Therefore, low share of the capital expenditure in Plan is not necessarily indicative of any lack of productivity or capital efficiency of the overall Plan Expenditure of the Centre.

Recommendation (Sl. No. 10, Para No. 111)

In the view of the Committee, the Government should immediately formulate strategy to reduce non-plan expenditure and also strictly adhere to the rules framed under FRBM Act.

Reply of the Government

The Committee's observations have been noted.

[OSD (FRBM), dated 30th September, 2004]

Recommendation (Sl. No. 12, Para No. 135)

From the reply of the Government, the Committee find that the proposal for creation of Disinvestment Fund has not found favour with the Government despite the clear commitment made by the Minister of Disinvestment in 2002 in this regard. The Committee are constrained to point out that the Committee's repeated recommendations for creation of disinvestment proceeds fund have not been heeded with seriousness by the Government. The Committee are of the opinion that unless a concrete system is put in place to manage the revenues collected from disinvestment of PSUs the disinvestment policy will never be able to acquire the desired impetus. They are given to understand that Finance Minister has announced in the Budget (2004-2005) that though the disinvestment proceeds are credited into Consolidated Fund of India but in 2005-06 Budget he will be informing about the deployment of this amount to specified social sector schemes. They are of the view that when the Government could inform about the deployment of the amounts received from disinvestment proceeds, there is no reason why it can not create a separate disinvestment fund which will lend more transparency to the utilization of the proceeds. The Committee, therefore, reiterate their earlier recommendation and urge upon the Government to keep the objectives of disinvestment clearly in mind and create a non-lapsable, dedicated Disinvestment Fund without further delay. The Committee want to be apprised of consistent decision of the Government in this regard.

Reply of the Government

Proposals for creation of a fund to manage disinvestment proceeds are under consideration. As laid down in the National Common Minimum Programme, Government believes that there must be a direct link between privatization and social needs, like for example the use of privatization revenues for designated social sector schemes. Accordingly, as assured by the Finance Minister in his Budget Speech—2004-05, the revenue generated through disinvestment will be utilized for specific social sector schemes and utilization would be reported at the time of presenting the Budget for the succeeding year.

[Ministry of Finance (Department of Disinvestment) O.M. No. 35(1)/3/2004-Parl. Vol-II dated 25th January, 2005]

Government decided on 27th January, 2005 to constitute a Fund into which the realisation from sale of minority shareholding of the Government in profitable PSEs would be channelised. The Fund would be maintained outside the Consolidated Fund of India and would be professionally managed by selected Public Sector Financial entities, which have the requisite experience, to provide sustainable returns to the Government without affecting the corpus. This Fund would be called "National Investment Fund" to denote the permanent nature of the corpus and the objectives to which its income is to be applied. A detailed plan for the constitution of the Fund and the specific schemes to be financed from its income would be prepared separately. The broad investment objectives will be—

(i) Investment in social sector projects which promote education, health care and employment;

(ii) Capital investment in selected profitable and revivable Public Sector Enterprises that yield adequate returns, in order to enlarge their capital base to finance expansion/diversification.

[Ministry of Finance (Department of Disinvestment) O.M. No. 3/18/2004-DD-II, dated 8 February, 2005]

CHAPTER IV

RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH REPLIES OF THE GOVERNMENT HAVE NOT BEEN ACCEPTED BY THE COMMITTEE

Recommendation (Sl. No. 1, Para No. 27)

The Committee are also of the view that inflation hits the senior citizens the most and therefore, the Government have to ensure that there are attractive saving schemes for them. Tax free RBI bonds, offering annual interest of 6.5% was one such instrument which enabled people to park their savings, however, the same has since been withdrawn. It has resulted in causing much distress, particularly to the senior citizens many of whom were availing this facility. The Committee, therefore, desire that Government should consider reintroducing these tax free bonds, apart from the scheme which has recently been introduced for the senior citizens and for those who have attained the age of 55 years and taken VRS.

Reply of the Government

Reply of the Government was silent pertaining to the issue contained in the Committee's recommendations at Sl. No. 1 Para No. 27.

Recommendation (Sl. No. 5, Para No. 56)

The Committee is distressed to note that the management expenses of General Insurance Companies continue to be in excess of stipulated amount. Only New India Insurance Company managed to limit these expenses within the permissible limit during the years 2001-02 and 2002-03. But thereafter it has increased tremendously. It is particularly regrettable to note that the insurance companies continue to incur excessive expenditure on management and IRDA have failed to effectively regulate this despite Committee's earlier recommendation to this effect. The Committee, therefore, recommends that this issue should be taken by IRDA on priority basis. The Government should hasten the process of modernisation/computerisation of the general insurance companies so that such expenses are reduced and their services are improved. Besides, they (insurance companies) should introduce new products to attract the masses and approach the untapped areas in a big way.

Reply of the Government

The public sector insurance companies have already initiated the process of computerisation and networking of their offices. It is expected that implementation and use of IT in the public sector general insurance companies would help in controlling management expenses. Further, with an effort to cut down the wage bill, which forms a substantial portion of management expenses, the companies have implemented Special Voluntary Retirement Scheme to right size their employees strength. All these measures are expected to reduce the management expenses in the long run. Apart from the cost cutting measures, the companies have also initiated steps for increasing their business through corporate tie-ups, opening of extension counters in rural areas and introduction in innovative products. With the control of expenses and increase in business, it is expected that management expenses ratio will be brought down to the permissible limit.

[Ministry of Finance O.M. No. 64 (77)/2004-OSD (Ins.),
dated 29th Sept. 2004]

Recommendation (Sl. No. 7, Para Nos. 74, 75, 76)

The Committee note that subsidies are an important fiscal instrument for correcting or modifying market determined outcomes to achieve specified objectives. The trend of providing subsidy started since 1951-52 in the form of food subsidy. The subsidies have successively grown over the years and has been budgeted at Rs. 43,516 crore in 2004-05 (BE). The major portion of subsidy is accounted for by food subsidy. Its share in total subsidy in the current year has been kept at Rs. 25,800 crore.

It is further seen that a number of Committees have examined the issue of reforming subsidies and have suggested measures in this regard. Consequent upon this several measures have been *viz*. Targeted approach to food subsidy (BPL families and Antyodaya Anna Yojana) under Public Distribution System, allowing Food Corporation of India to access market loans carrying lower interest rates, encouraging private trade in food grains, liquidating excess foodgrains stocks, modifying the Retention Price Scheme based subsidy on fertilisers as per the recommendations of the Expenditure Reforms Commission, and proposed phasing out of subsidies on PDS kerosene and LPG. They are given to understand that recently the National Institute of Public Finance and Policy (NIPFPO) has been asked to prepare a blue print to ensure better targetting of subsidies.

The Committee note with deep concern that despite provision of huge sums by way of subsidies, objectives had not been fulfilled due to serious shortcomings in the delivery mechanism. Therefore, the Committee recommend that the Government should formulate a strategy to reduce pilferages and ensure benefits of subsidy to the really needy people. The study being conducted by NIPFPO be expedited and the Committee be apprised of the recommendations and action taken by the Government at the earliest.

Reply of the Government

In order to facilitate better targetting of subsidies, the Ministry of Finance has instituted a study in mid-July 2004 to be undertaken by National Institute of Public Finance and Policy (NIPFP), with the following terms of reference:

(i) Examination of implicit and explicit subsidies under different budget heads and classifying them in to merit and non-merit categories.

(ii) Examining the design of major non-merit subsidies with a view to better target them to intended groups.

(iii) Analyzing the food subsidies in greater detail to improve the functioning of Food Corporation of India.

(iv) Quantifying the subsidy amount incurred on schemes for the poor, like small and marginal farmers, farm labour and the urban poor.

(v) Presenting a design to target, subsidies at the poor, like small and marginal farmers, or labour, urban poor, etc.

The National Institute of Public Finance & Policy (NIPFP) has submitted and Interim Report to the Ministry and the Report is under examination.

Recommendation (Sl. No. 8, Para No. 84)

The Committee take note of the fact that while undertaking a review of the bank's performance by way of annual inspections for the years ending 31st March 2001 and 2003, the RBI had noted wide variance in the key indicators which had been wrongly certified by the statutory auditors, however, no action seems to have been initiated against them, since the Statutory Auditors come under the strict vigil of the Institute of Chartered Accountants for India, which failed to take action against them. The Committee find that this is a very serious and anomalous situation under which the RBI which was mainly responsible for monitoring the working of the banks, has no control to take action against the erring auditors at the same time RBI as a strict regulator cannot be absolved of their responsibility.

Reply of the Government

(i) RBI's inspection with reference to the bank's position as on March 31, 2002, conducted from July to October 2002, revealed significant variation between the assets classified as non-performing by the bank and those classified as NPA by the Inspecting Officers. There was also considerable shortfall in provisioning. After considering the provisions required to be made by the bank, the IO assessed the net worth to be negative at (-) Rs. 416.70 crore. In view of the very large variance in the assessment of the bank's financial position as reported by the auditors and as assessed by the RBI inspectors, the RBI engaged a firm of Chartered Accountants to undertake an independent assessment and reconcile the position. The Chartered Accountants' report dated February 24, 2003 confirmed RBI's assessment, except for minor differences. A complaint was filed with ICAI against the statutory auditors for 2001-02 for wrong classification in respect of NPAs in the accounts for 2001-02. The bank was put on a monthly monitoring schedule and the bank was advised to change the statutory auditors for the year ended March 31, 2003.

(ii) The RBI inspection that was conducted from October 2003 to January 2004 found that the divergence between the reported accounts and the assessment of the Inspecting Officers of the NPAs and of the required level of provisioning continued to be very large; against the marginally positive net worth reported by the bank for March 2003 at Rs. 2.42 crore, erosion in the net worth was in fact Rs. 740 crore. In view of the large divergence between the NPA figures reported by the bank duly certified by the statutory auditors and those assessed by the RBI Inspectors, the explanation of the auditors was called for. As the explanation provided was not satisfactory, the matter was reported to the Institute of Chartered Accountants of India (ICAI), for initiating action.

(iii) Apart from debarring the firms that had audited the bank's books for 2001-02 and 2002-03 from statutory audit, banks and financial institutions have been advised by RBI not to use the services of the two firms of Chartered Accountants for any audit related work. CAG has also been advised about the action taken by RBI for similar action by CAG.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl. No. 8, Para No. 85)

Besides, amalgamating the unhealthy banks with those which are performing well is not a healthy practice by any means, as this practice on the contrary encourages the unscrupulous entities to score their own vested interests by playing with the public money in a reckless and surreptitious manner.

Reply of the Government

(i) The amalgamation was done after having given sufficient time and opportunity to the bank to infuse capital while simultaneously ensuring through directions issued to it, that it did not increase its risk-weighted assets.

Since the bank failed to either infuse capital or to offer any viable solution, the option of compulsory merger was resorted to. This option is exercised only as a last resort in public interest and in the interest of the depositors. OBC's proposal to takeover GTB was examined from the perspective of the strength of the bank and synergies available. OBC's financial parameters showed that it had sufficient financial strength to absorb GTB. So far as the synergies were concerned, the two banks complemented each other, OBC being north based and GTB having its branches mainly in the south. They had a common technology platform (FINACLE). GTB's strength in non-interest income portfolio benefited OBC. In view of the strategic advantages available in the amalgamation of GTB with OBC, this was considered the optimal solution.

(ii) In this regard, it is useful to note the various remedies and options available to RBI for dealing with weak banks.

One option is to allow the weak bank to function as a narrow bank, which *inter alia* means restricting the growth of risk-weighed assets. This is unlikely to help a weak bank in the long run since it would result in (a) absence of growth and loss of customers (b) mismatch in pricing of assets and liabilities (c) staff attrition/loss of morale (d) lack of solvency and tight liquidity making the bank highly vulnerable to large withdrawals.

Second option is to restructure and recapitalised the bank by further infusion of capital and other corrective measures. Although infusion of capital is the preferable option for resolution of problem banks, one of the important concerns in this regard is the source of funds. As regulators, it is necessary for RBI to ensure that the contributions/investments are made from genuine and bonafide sources in a transparent manner and do not attract domestic and international legal prohibitions against money laundering and related offences as applicable. RBI has also to ensure that prudential standards are not compromised.

Third option would be to merge the weak bank with another bank under the provisions of the Banking Regulation Act, 1949.

(a) Voluntary merger under Section 44A of the Banking Regulation Act, 1949.

"Section 44A sets out of the procedure to be followed in case of voluntary merger/amalgamation between two banking companies. Voluntary mergers are the least cost option and take into account the interests of both depositors and shareholders."

(b) Reconstitution/Amalgamation under Section 45 of the Banking Regulation Act, 1949.

"Section 45 of the Act empowers RBI to apply to the Central Government for suspension of business by a banking company and prepare a scheme of reconstitution or amalgamation. The merger under Section 45 of the Act, *ibid* is done to protect the interests of the depositors and in the interest of the banking system.

Lastly, when all attempts to restructure a weak bank fail, it may be placed under liquidation. In such a case, the claims of insured depositor may have to be borne by Deposit Insurance and Credit Guarantee Corporation (DICGC). This option has certain disadvantages; (a) the pay off by DICGC would be a direct cost to the exchequer (b) the depositors would lose confidence in the banking system (c) the investors' confidence will be shaken (d) liquidation of a bank may also lead to 'domino effect' and would cause systemic problems.

It may be stated that amongst the various options discussed above, compulsory merger under Section 45 has been resorted to as a viable option for resolution of many problem banks, in the interest of the depositors based on past experiences of RBI.

(iii) In order to prevent unscrupulous persons from acquiring control of the banks, RBI is currently insisting on 'fit and proper' status of directors both at the time of induction and for their continuance. RBI has also put in place a mechanism by which it ensures that shareholders, whose aggregate holdings are above the specified thresholds, meet the fitness and propriety tests before grant of acknowledgement of transfer of shares. In determining whether the applicant (including all entities connected with the applicant) is fit and proper to hold the position of a shareholder at the lowest threshold of 5% and above, RBI takes into account all relevant criteria, including the applicant's integrity, reputation and track record in financial matters and compliance with tax laws which are necessary to protect the interests of the depositors and the integrity of the financial system.

[Ministry of Finance OM No. 11/19/2004-BOA]

Recommendation (Sl. No. 8, Para No. 86)

In order to ensure that such happenings are not repeated in the future, sufficient safeguards, both legislative as well as administrative have to be built into the system. At the same time those who are responsible for such a failure should not be spared and suitable action including criminal action ought to be taken against them without further loss of time, so that such actions provide deterrence to others as well. The Committee would like to be apprised of the action in this regard at the earliest.

Reply of the Government

(i) The continuance of Shri Gelli as CEO was not considered prudent or desirable and on RBI's advice, Shri Gelli stepped down from the position of the CMD with effect from April 12, 2001 and subsequently resigned from the Board as a Director on June 16, 2001.

In February 2004, when Shri Gelli re-entered the Board of GTB, RBI expressed serious discomfort and the same was communicated to the Board/Government. Shri Gelli resigned from the Board of Directors of the bank in its meeting held on March 12, 2004.

RBI's action of asking Shri Gelli to step down from the chairmanship and directorship was expected to send strong signals to the shareholders and the market forces should have disciplined the errant behaviour. However, despite the regulator's actions, the market did not respond and continued to repose its faith in the bank as reflected in its market valuation.

(ii) Other actions taken in this regard include:—

(a) In terms of the scheme of amalgamation, all the employees of erstwhile GTB continue in service and are deemed to have been appointed in OBC. As such, irregularities if any, committed by the staff of the erstwhile GTB would have to be looked into by OBC for fixing staff accountability and initiating appropriate disciplinary and other proceedings. We have advised OBC in this regard.

(b) RBI complained against M/s. Lovelock and Lewes and M/s Pricewaterhouse, who were the statutory auditors for GTB for the years 2001-02 and 2002-03 respectively for making wrong classification of NPAs.

(c) RBI is examining the feasibility of initiating criminal action against the promoters/directors of the erstwhile GTB for misrepresenting/misreporting the financial statements for the period ended March 31, 2002 and 2003.

(iii) The important measures taken to strengthen the banking sector and prevent such recurrences in future are briefly, the following:

(a) As reported earlier, the following prudential/supervisory actions were taken:

- Introduction of capital adequacy standards on the lines of the Basel norms.
- Prudential norms on asset classification, income recognition and provisioning.
- Introduction of valuation norms and capital for market risk for investments.
- Enhancing transparency and disclosure requirements for published accounts.
- Aligning exposure/capital market exposure norms, single borrower and group-borrower ceiling with international best practices.
- Introduction of off-site monitoring system and strengthening of the supervisory framework/introduction of Risk Based Supervision for banks.
- The accounting treatment for impaired assets has been made closer to the international best practices and the final

accounts of banks are transparent and more amenable to meaningful interpretation of their performance.

- Introduction of a framework for prompt corrective action.

(b) Further, RBI has taken measures to improve corporate governance in banks. RBI has put in place a system to ensure the 'fit and proper' status of CEOs of banks through a due diligence process. To ensure the continuing 'fit and proper' status of the Board of Directors, RBI issued a directive to banks on June 25, 2004, in terms of which the Boards of the banks should constitute Nomination Committees to scrutinize the declarations relating to qualifications, expertise, track record, integrity, and other 'fit and proper' criteria of directors periodically.

(c) In the draft guidelines on ownership and governance issued on July 2, 2004 RBI has reiterated 'fit and proper' criteria for appointment of directors and CEO, so that the suitability of persons for appointments/continuation as directors/CEO is ensured.

(d) The draft guidelines on ownership and governance also envisage that the capital requirement of existing private sector banks should be on par with the entry level capital requirement for new private sector banks prescribed in RBI guidelines of January 3, 2001, which is initially Rs. 200 crore, with a commitment to increase to Rs. 300 crore within three years so that they have sufficient minimum size for financial stability. In order to meet this requirement, all banks in private sector should have a net worth of Rs. 300 crore at all times and those falling below the level will be required to submit to RBI for approval, a time-bound programme for capital augmentation.

(iv) As regards legislative measures, the status is as follows:

(a) Section 30 of the Banking Regulation Act relates to audit of a banking company. Presently, there is no obligation on the auditors of a banking company to report any violation of the provisions of B.R. Act and regulations or directions issued thereunder while auditing books of the banks. Under the core principles of international accounting standards, the auditors are obliged to report to the supervisor the matters of significance, which are likely to have an adverse effect on the working of the banking company. Section 45MA of the RBI Act already casts an obligation on the auditors of the non-banking financial companies to report to the Reserve Bank any violation of any provision of RBI Act or direction issued thereunder.

(b) In the Banking Regulation (Amendment) Miscellaneous Provisions Bill, 2003, which was tabled in the Parliament in August, 2003 but lapsed due to dissolution of Parliament, it was proposed to amend Section 30 of B.R. Act to provide that the RBI may direct the auditor in the matter relating to balance sheet, profit and loss account, disclosure of liabilities in the books of account or any other matter relating thereto. It was also proposed to provide that it would be the duty of the auditor to enquire and state in the report whether or not the banking company has complied with the provisions of this Act or any direction or notification or order issued thereunder. The Auditors should also enquire whether the information or statements called for by the RBI have been furnished to it or not and in case the bank has not complied with this requirement, the auditor would make a report to the RBI. The Bill is now being re-examined/reviewed.

[Ministry of Finance, O.M. No. 11/19-2004-BOA]

Recommendation (Sl. No. 11, Para No. 124)

The Committee are seriously concerned that despite their repeated recommendations in their earlier reports on Demands for Grants in 2001-2002, 2002-2003 and 2003-2004, urging the Government to bring out a comprehensive disinvestment policy document which should be laid before the Parliament for its approval, the Government neither complied with their recommendations nor did the Government give convincing reasons why the recommendations of the Committee were not implemented. The Committee regret to recall that in their reply in September, 2002 *vide* OM No. 45011/3/2000-Parl (Vol. II) dated 6.9.2002, the Government had made a request to the Committee to allow some more time to prepare and bring out a policy document which has not materialized till date. The Committee are deeply concerned that in the absence of a uniform Comprehensive Policy, disinvestment of PSUs is being done on case-to-case basis thus subjecting disinvestment programme vulnerable to public comments and apprehensions. The Committee strongly urged the Government to shun its case-to-case basis approach and adopt a cohesive and uniform approach so that the policy may gain more transparency and credibility.

The Committee have been informed that the policy as stated in the NCMP is the policy of the Government towards disinvestment. The Committee are not able to understand as to why the Government is wary of bringing forward a Comprehensive Policy Document which may address all the aspects such as valuation, employees welfare, etc. and which will deal with all types of PSUs. In the absence of a clear cut policy, the Government has to evolve a new methodology every time to deal with a particular situation. They are not convinced by the Government's reply that adequate publicity has been given to the policy as stated in NCMP in the Budget Speech, interviews of the Finance Minister on TV and print media. They see no reason why the Government cannot bring the policy document before Parliament in difference to the wishes of the Committee.

The Committee, therefore, reiterate their earlier recommendations urging the Government to bring out a comprehensive documents on disinvestment policy to be placed before the Parliament for its approval without further delay.

Reply of the Government (i)

The policy of the Government with respect to the public sector has been laid down in the National Common Minimum Programme and the Government is following these principles while implementing disinvestment on a case-by-case basis. A paper outlining the implementation strategy for disinvestment is under consideration.

[Ministry of Finance (Department of Disinvestment) O.M. No. 35(1)/3/2004-Parl. Vol-II dated 25th January, 2005]

Reply of the Government (ii)

Preparation of White Paper on Disinvestment has already been identified by the Government as one of the thrust areas for implementation by the Department of Disinvestment and the work is under progress.

[Ministry of Finance (Department of Disinvestment) O.M. No. 35(1)/3/2004-Parl. dated 3rd March, 2005]

CHAPTER V

RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH FINAL REPLY OF THE GOVERNMENT IS STILL AWAITED

—NIL—

New Delhi;	MAJ. GEN. (RETD.) B.C. KHANDURI,
25 *August*, 2005	*Chairman,*
03 *Bhadra*, 1927 *(Saka)*	*Standing Committee on Finance.*

MINUTES OF THE THIRD SITTING OF STANDING COMMITTEE ON FINANCE

The Committee sat on Monday, 22nd August, 2005 from 1500 to 1630 hrs.

PRESENT

Maj. Gen. (Retd.) B.C. Khanduri—*Chairman*

MEMBERS

Lok Sabha

2. Shri Gurudas Dasgupta
3. Shri A. Krishnaswamy
4. Shri Rupchand Pal
5. Shri Shriniwas D. Patil
6. Shri K.S. Rao
7. Shri Lakshman Seth
8. Shri G.M. Siddeshwara
9. Shri Magunta Sreenivasulu Reddy

Rajya Sabha

10. Shri Chittabrata Majumdar
11. Shri C. Ramachandraiah

SECRETARIAT

1. Dr. (Smt.) P.K. Sandhu — *Additional Secretary*
2. Shri R.K. Jain — *Deputy Secretary*

2. ** ** ** ** **

3. ** ** ** ** **

4. ** ** ** ** **

5. ** ** ** ** **

6. Thereafter, the Committee considered and adopted the draft reports on (i) Action taken by the Government on the recommendations contained in the First Report of the Committee on Demands for Grants (2004-05) of the Ministry of Finance (Departments of Economic Affairs, Expenditure and Disinvestment) and (ii) The Actuaries Bill, 2005 without any modification/amendment.

7. The Committee authorised the Chairman to finalise the Reports and to make verbal and other consequential changes arising out of the factual verification and present the same to both the Houses of Parliament.

The Committee then adjourned.

APPENDIX

(*Vide* Para 3 of the Introduction)

ANALYSIS OF THE ACTION TAKEN BY GOVERNMENT ON THE RECOMMENDATIONS CONTAINED IN THE FIRST REPORT OF THE STANDING COMMITTEE ON FINANCE (FORTEENTH LOK SABHA) ON DEMANDS FOR GRANTS (2004-05) OF THE MINISTRY OF FINANCE (DEPARTMENT OF ECONOMIC AFFAIRS, EXPENDITURE AND DISINVESTMENT)

		Total	% of Total
(i)	Total number of recommendations	13	
(ii)	Recommendations/observations which have been accepted by the Government (*Vide* Recommendations at Sl. Nos. 1, 2, 6, 8, 9, 13)	6	46.12
(iii)	Recommendations/observations which the Committee do not desire to pursue in view of the Government's replies (*Vide* Recommendations at Sl. Nos. 3, 4, 5, 9, 10, 12)	6	46.12
(iv)	Recommendations/observations in respect of which replies of the Government have not been accepted by the Committee (*Vide* Recommendations at Sl. Nos. 1, 5, 7, 8, 11)	5	38.4
(v)	Recommendation/observation in respect of which final reply of the Government is still awaited (Nil)	Nil	00.00