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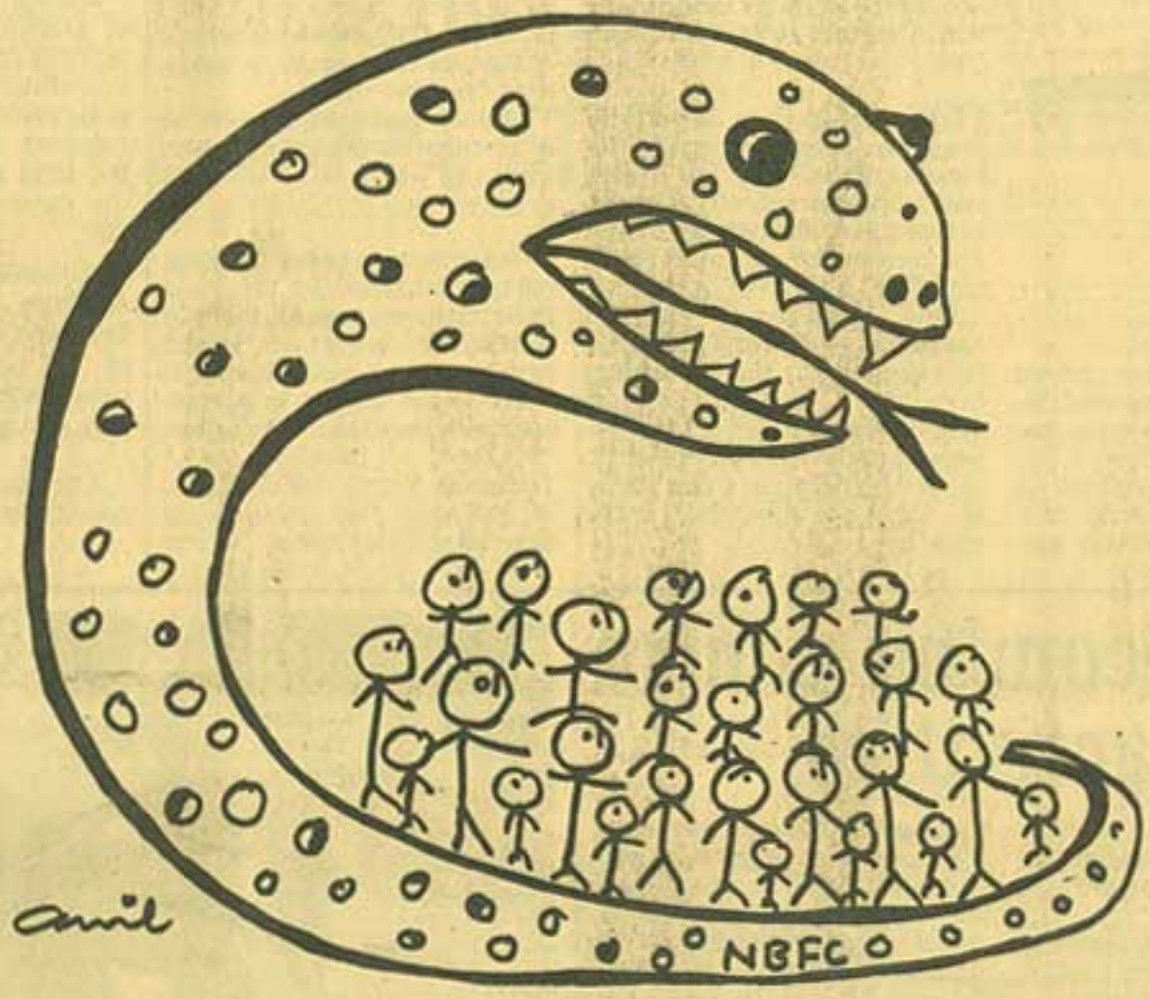
Loot under the regulators' nose

There is essentially a lack of commitment to protect public money and will to punish the guilty, says **Uttam Gupta**



FIVE years after the securities scam, the investors have been gripped by yet another scandal. The scam involving CRB capital and other group companies runs into several hundred crores. With the liabilities of the group exceeding its assets by a whopping about Rs 800 crore, the investors have suffered that much loss. Small investors alone — about 100 thousand of them — have lost about Rs 233 crore in fixed deposits.

The so-called guardians of the investors have swung into action. The RBI wants compulsory registration of all NBFCs by July 8, 1997; those who do not get this done by the deadline, will be debarred from doing business. The ministry of finance (MoF) would like to have nominee directors of the government on the boards of NBFCs. The Prime Minister would wish to see all fixed deposits with NBFCs covered by comprehensive insurance and has directed MoF to come up with a scheme. Political parties want a probe by the JPC. There is even talk of regulating and monitoring the rating institutions.

All this, however, fails to enthuse the beleaguered investors as their prime concern is to get back their life-time's savings, whereas what the authorities are contemplating purportedly aims at preventing recurrence of such a scam but virtually no relief in the present case. For the future also, few would take the regulators' action plan seriously.

In the aftermath of the securities scam, the government promised a great deal, but the result was nil. Even as the offenders got away scot-free, the banks/FIs and PSUs were saddled with huge losses. The irony is that the latter are involved in legal battles — remember the infamous NHB vs Grindlays' Bank case — spending crores even as the former lives in safe heaven.

How serious the guardians are towards the plight of the investors may be gauged from what they are doing in the *la affair* CRB. On this, all that one can see is a trigger mechanism customary to any company that is declared bankrupt and comes under liquidation, i e appointment of an official liquidator, freezing of bank accounts of all companies with which Mr Bhansali and his associates are connected, including those with remote connection, e g Daewoo securities, and stopping of trading orders in the shares belonging to the group etc.

The known/identified assets of the group are only a fraction of what it owes the creditors. So, in the normal course, this is all that can be recovered. Even recovery of this limited amount — estimated at about Rs 67.5 crore, is going to be a long-drawn process. Moreover, as and when this is realised, it will be cornered by the most powerful claimants, i e banks. This is abundantly clear from the stand taken by the banks in an affidavit to the Bombay High Court which is hearing a petition moved by the Investors Grievances Forum, on behalf of the small investors pleading first preference for them in distribution of recovered proceeds.

Even as the regulatory authorities have done little to protest investors' interests, they are quick to exhort them to exercise due diligence while deciding to invest. What precautions should the investors take? They can proceed only on the basis of information made available through the prospectus of other sources, e g media reports. They cannot check its authenticity which is the job of regulatory bodies/watchdogs.

What has been their role in preventing, or shall we say making of the scam? A careful scrutiny of various developments in the CRB case will bring us unprecedented lapses on their part. In some instances, the nature of lapses would point towards the possibility of complicity of the regulators in the fraud perpetrated by the promoters.

Consider for instance, the infamous Mutual Fund (MF) issue, i e Arihant Manghal for a whopping Rs 229 crore in August 1994. The enquiries conducted by Sebi in November 1994 confirmed the irregularities, including diversion of the funds collected from the issue to other group companies in a clandestine manner. And yet, all that the watchdog did was to put a ban on new issue up to June 30, 1996. This is like exonerating a person for the robbery already committed and telling him to refrain from repeating it for a short while.

The group got, in principle, approval of the RBI to set up a bank in July 1996. By this time, the apex bank should have known about the loot in the Arihant Mangal. It did not matter whether Sebi on its own informed RBI or not. The information must be collected from all possible sources, including Sebi which claims that it does send a report. The RBI glossed over it and instead went ahead, giving its nod on the basis of the so-called favourable reports received from the banks dealing with the group. On what basis the banks gave positive recommendation is a mystery. By the time the RBI revoked group's licence in April 1997, the Bhubaneshwar branch of the bank had already robbed Rs 50 crore from the public.

Any NBFC having a net worth of more than Rs 50 lakh is mandatorily required to register itself with the RBI. On this criterion, the registration should have been done way back in 1991. It was not done, and RBI did not bother. CRB capital got itself registered in October 1996 when it became clear that without this, it could not take advantage of the deregulation of interest rates announced earlier in July 1996.

CRB capital had an excellent rating from CARE; majority equity in the latter is held by IDBI whose CMD is also its chairman. This was maintained up to January 1997 despite its cash flows from operations and investment during 1995-96 being substantially in the negative of about Rs 210 crore. In its affidavit filed in Bombay High Court, CARE has stated that information/analysis provided by it should not be treated as fully accurate/complete. Not to talk of the degree of accuracy. It is a clear-cut case of sleeping over badly managed/mismanaged affairs.

The country's largest bank, i e SBI allowed itself to be looted to the extent of a huge Rs 58 crore under an extra-ordinary facility that permitted encashment of warrants for interest and principal repayment against pre-funded deposits. The bank went on encashing forged warrants without receiving advance deposits from CRB and list of dividend warrants required under the agreement. A close scrutiny reveals that fraud came to notice on March 8, 1997 when the amount was only Rs 1 crore. The balance of Rs 57 crore was swindled between March 8 and March 19, 1997.

The problem is not due to lack of an effective legislation or rules/regulations to deal with the NBFC. Even if there is some loophole/lacuna in the existing law, what prevents the government from filling that void? It is essentially one of lack of commitment to protect and safeguard public money and absence of the will to punish the guilty and get the money back.