Classification of Assets

While new private banks are careful about their asset quality and consequently have low non-performing assets (NPAs), public sector banks have large NPAs due to wrong lending policies followed earlier and also due to government regulations that require them to lend to sectors where potential of default is high. Allaying the fears that bulk of the Non-Performing Assets (NPA) was from priority sector, NPA from priority sector constituted was lower at 46 percent than that of the corporate sector at 48 per cent. Loans and advances account for around 40 per cent of the assets of SCBs. However, delay/default in payment of interest and/or repayment of principal has rendered a significant proportion of the loan assets non-performing. As per RBI's prudential norms, a Non-Performing Asset (NPA) is a credit facility in respect of which interest/installment has remained unpaid for more than two quarters after it has become past due. “Past due” denotes grace period of one month after it has become due for payment by the borrower.
Regulations for asset classification

Assets are classified into four classes - Standard, Sub-standard, Doubtful, and Loss assets. NPA consist of assets under three categories: sub-standard, doubtful and loss. RBI for these classes of assets should evolve clear, uniform, and consistent definitions. The banks should classify their assets based on weaknesses and dependency on collateral securities into four categories:

i. **Standard Assets:** It carries not more than the normal risk attached to the business and is not an NPA. Standard assets are the ones in which the bank is receiving interest as well as the principal amount of the loan regularly from the customer. Here it is also very important that in this case the arrears of interest and the principal amount of loan do not exceed 90 days at the end of financial year. If asset fails to be in category of standard asset that is amount due more than 90days then it is NPA and NPAs are further need to classify in sub categories.

ii. **Sub-standard Asset:** A sub-standard asset is one which has remained NPA for a period less than or equal to 12months from 31.3.2005. In such case the current net worth of the borrower/guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the banks in full. In other words, such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.
iii. **Doubtful Assets:** With effect from 31.3.2005, an asset is to be classified as doubtful, if it has remained NPA for a period exceeding 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristics that the weaknesses make collection or liquidation in full, - on the basis of currently known facts, conditions and values- highly questionable and improbable. Under this category there are three stages: D-I Doubtful up to one year D-II Doubtful for further two years D-III Doubtful beyond three years.

iv. **Loss Assets:** An asset identified by the bank or internal/ external auditors or RBI inspection as loss asset, but the amount has not yet been written off wholly or partly. The banking industry has significant market inefficiencies caused by the large amounts of Non Performing Assets (NPA)in bank portfolios, accumulated over several years. Discussions on non-performing assets have been going on for several years now. One of the earliest writings on NPA defined them as "assets which cannot be recycled or disposed off immediately, and which do not yield returns to the bank, examples of which are: Overdue and stagnant accounts, suit filed accounts, suspense accounts and miscellaneous assets, cash and bank balances with other banks, and amounts locked up in frauds".
Guidelines for the classification of assets

Classification of assets into above categories should be done taking into account the degree of well defined credit weaknesses and the extent of dependencies on collateral security for the realization of dues.

Banks should establish appropriate internal systems to eliminate the tendency to delay or postpone the identification of NPAs especially in respect of high value of accounts.

Account with temporary Deficiencies:

The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies, which are temporary in nature as such as non availability of adequate drawing power based on latest stock.

Asset classification to be borrower–wise and not facility-wise:

It is difficult to envisage a situation when only one facility to a borrower becomes a problem credit and not others. Therefore, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility or a part there of, which has become irregular.
Advances under consortium arrangements:

Asset classified of accounts under consortium should be based on the record of recovery of the individual member banks and other aspects having bearing on the recoverability of the advances. Accounts where there is erosion in the value of security can be reckoned as significant when the realizable value of the security is less than 50 percent of the value assessed by the bank or accepted by RBI at the time of last inspection, as the case may be. Such NPAs may be straightway classified under doubtful category and provisioning should be made as applicable to doubtful assets.

Agricultural Advances

In respect of advances granted for agricultural purpose where interest and / or installment of principal remains unpaid after it has become past due for two harvest seasons but for a period not exceeding two half years , such an advance should be treated as NPA.

Where the natural calamities impair the repaying capacity of agricultural borrowers, banks may decide on their own as a relief measure-conversion of the short – term production loan into a term or re-schedulement of the repayment period.

In such cases of conversation or re-schedulement, the term loan as well as fresh short-term loan may be treated as current dues and need not be classified as NPA.
Restructuring /rescheduling of loans:

A standard asset where the terms of the loan arrangement regarding interest and principal have been renegotiated or rescheduled after the commencement of production should be as sub-standard and should remain in such category for at least one year of satisfactory performance under the renegotiated or restructured terms. In case of substandard and doubtful assets also, rescheduling does not entitle a bank to upgrade the quality of advances automatically unless there is satisfactory performance under the rescheduled–renegotiated terms.

Exceptions: As trading involves only buying and selling of commodities and the problems associated with manufacturing units such as bottleneck in commercial production, time and cost escalation etc. are not applicable to them.

NPA Norms

Provisional Norms:

Banks will be required to make provisions for bad and doubtful debts on a uniform and consistent basis so that the balance sheets reflect a true picture of the financial status of the bank. The Narsimham Committee has recommended the following provisioning norms

(i) 100 per cent of loss assets or 100 per cent of out-standings for loss assets;

(ii) 100 per cent of security shortfall for doubtful assets and 20 percent to 50 per cent of the secured portion; and
(iii) 10 per cent of the total outstanding for substandard assets.

A provision of 1% on standard assets is required as suggested by Narsimham Committee II, 1998. Banks need to have better credit appraisal systems so as to prevent NPA from occurring. The most important relaxation is that the banks have been allowed to make provisions for only 30 per cent of the "provisioning requirements" as calculated using the Narsimham Committee recommendations on provisioning. The encouraging profits recently declared by several banks have to be seen in the light of provisions made by them. To the extent that provisions have not been made, the profits would be fictitious.

**Disclosure Norms:**

Banks should disclose in balance sheets maturity pattern of advances, deposits, investments and borrowings. Apart from this, banks are also required to give details of their exposure to foreign currency assets and liabilities and movement of bad loans. These disclosures were to be made for the year ending March 2000. In fact, the banks must be forced to make public the nature of NPA being written off. This should be done to ensure that the taxpayer’s money given to the banks, as capital is not used to write off private loans without adequate efforts and punishment of defaulters.
MEASURES TO RECOVER NPAs

Over the last few years Indian banking in its attempt to integrate itself with the global banking has been facing lots of hurdles in its way due to its inherent weaknesses, despite its high sounding claims and lofty achievements. One of the major hurdles, the Indian banking is facing today, is its ever-growing size of non-performing assets over which the top management of almost each bank is baffled. On account of the intricacies involved in handling the NPA the ticklish task of assets management of the bank has become a tight rope walk affair for the controlling heads, because a little wavering „this or that side‟ may land the concern bank in trouble. The growing NPA is a potent source of worry for the finance minister as well, because in a developing country like ours, banking is seen as an important instrument of development, while with the backbreaking NPA banks have become helpless burden on the economy.

NPA with outstanding up to 5 crore:

In case of doubtful and loss assets, through the modified schemes, the banks have been directed to follow up a settlement formula under which the minimum amount to be recovered, amounts to be entire outstanding running ledger balances as on the date the account was identified as NPA i.e. the date from which
the interest was not charged to the running ledger, an analysis of the given formula shows that RBI has been very much generous in granting huge relaxation to the borrowers who were not coming forward for setting their overdue loans due to one or other reason. The scheme is of high practical value as it protects the borrowers who were having genuine problems in clearing their dues because the interest component constituted a multiplied amount of principal outstanding. On the other hand, the concerned banks were also finding in difficult to sacrifice the entire interest component, but outstanding in the dummy ledger. Now as per the provision to the scheme, they will be ready to grant such relaxation in favour of the borrowers. These guidelines have come as a windfall for borrowers who after a lot of negotiations were almost ready to repay back their principal as well as part of the interest component to settle their accounts, as under the modified scheme, they would be able to save the interest component. To that extent the concerned bank stands to lose. In the case of sub standard assets, the settlement formula as given in the modified scheme states that the minimum sum to be recovered must contain the entire running ledge outstanding balance as on the date of the account was identified as NPA i.e. the date from which interest was not charged to the running ledger plus interest at the existing prime lending rate of the bank. As per the modified scheme, the terms suggested for the payment of settlement amount NPA are simple and pragmatic. As per the terms of the scheme, the settlement amount should be paid in lump sum by the borrower. However in case of the borrower is unable to repay back in a lump sum, the scheme allows sufficient
breathing period to enable him to arrange the funds and clear at least 25 percent of the settlement amount to be paid upfront and the remaining amount to be recovered in installments spread over a period of one year along with interest at the existing PLR from the date of settlement up to the date of final payment.

**NPA with outstanding over Rs. 5 crores:**

For recovery of NPA over Rs. 5 crore, RBI has left the matter to the concerned banks and advised that the concerned banks may formulate policy guidelines regarding their settlement and recovery. The freedom, in such cases, is given to the banks, because the attending circumstances in each case may vary from the other. Therefore it was in the right direction that adopting a generalized approach was not thought appropriate. In cases, where the amount involved is above Rs.5 crore, RBI expects CMD of each bank to supervise the NPA personally. The CMDs of the concerned banks are advised to review all such cases within a given timeframe and decide the course of action in terms of rehabilitation/restructuring. RBI also desires the submission of a quarterly report of all NPA above Rs. 5 crore from PSU banks. Thus by putting up the cut-off dates for the implementing of the scheme, RBI desires the banks to realize the seriousness of the issue and gear up to sweep away the NPA in one go. For commercial banks, it is a golden opportunity to clear the mess, consolidate and come out on a track leading the path of global banking. The time given for weeding out the disastrous NPA is neither too long nor too short and the banks,
with proper planning and follow up can drastically reduce their NPAs, if they firmly resolve to do so. RBI expects the commercial banks to follow the guidelines in letter and spirit without any discrimination or discretion as a slight dilution may jeopardize their interest. A proper monitoring system is also desired to be evolved for monitoring the progress of the scheme. As this is a rare opportunity given to the defaulting borrowers, they can avail the chance given for the settlement of their loans. Without adequate publicity of the scheme the response from the defaulting borrowers may not be there to the expected level.

**Legal and Regulatory Regime**

**A. Debt Recovery Tribunals (DRTs)**

DRTs were set up under the Recovery of Debts due to Banks and Financial Institutions Act, 1993. Under the Act, two types of Tribunals were set up i.e. Debt Recovery Tribunal (DRT) and Debt Recovery Appellate Tribunal (DRAT). The DRTs are vested with competence to entertain cases referred to them, by the banks and FIs for recovery of debts due to the same. The order passed by a DRT is appeal able to the Appellate Tribunal but no appeal shall be entertained by the DRAT unless the applicant deposits 75% of the amount due from him as determined by it. However, the Appellate Tribunal may, for reasons to be received in writing, waive or reduce the amount of such deposit. Advances of Rs. 1 million and above can be settled through DRT process. An important power conferred on the Tribunal is that of making an interim order(whether by way of injunction or
stay) against the defendant to debar him from transferring, alienating or otherwise dealing with or disposing of any property and the assets belonging to him within prior permission of the Tribunal. This order can be passed even while the claim is pending. DRTs are criticized in respect of recovery made considering the size of NPAs in the Country. In general, it is observed that the defendants approach the High Court challenging the verdict of the Appellate Tribunal which leads to further delays in recovery. Validity of the Act is often challenged in the court, which hinders the progress of the DRTs. Lastly, many needs to be done for making the DRTs stronger in terms of infrastructure.

B. Lokadalats

The institution of Lokadalat constituted under the Legal Services Authorities Act, 1987 helps in resolving disputes between the parties by conciliation, mediation, compromise or amicable settlement. It is known for effecting mediation and counseling between the parties and to reduce burden on the court, especially for small loans. Cases involving suit claims up to Rs. L million can be brought before the Lokadalat and every award of the Lokadalat shall be deemed to be a decree of a Civil Court and no appeal can lie to any court against the award made by the Lokadalat. Several people of particular localities/ various social organizations are approaching Lokadalats which are generally presided over by two or three senior persons including retired senior civil servants, defense personnel and judicial officers. They take up cases which are suitable for
settlement of debt for certain consideration. Parties are heard and they explain their legal position. They are advised to reach to some settlement due to social pressure of senior bureaucrats or judicial officers or social workers. If the compromise is arrived at, the parties to the litigation sign a statement in presence of Lokadalats which is expected to be filed in court to obtain a consent decree. Normally, if such settlement contains a clause that if the compromise is not adhered to by the parties, the suits pending in the court will proceed in accordance with the law and parties will have a right to get the decree from the court. In general, it is observed that banks do not get the full advantage of the Lokadalats. It is difficult to collect the concerned borrowers willing to go in for compromise on the day when the Lokadalat meets. In any case, we should continue our efforts to seek the help of the Lokadalat.

C. Enactment of SRFAESI Act

The "The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act" (SRFAESI) provides the formal legal basis and regulatory framework for setting up Asset Reconstruction Companies (ARCs) in India. In addition to asset reconstruction and ARCs, the Act deals with the following largely aspects,

- Securitization and Securitization Companies
- Enforcement of Security Interest
- Creation of a central registry in which all securitization and asset reconstruction transactions as well as any creation of security interests has to be filed.

The Reserve Bank of India (RBI), the designated regulatory authority for ARCS has issued Directions, Guidance Notes, Application Form and Guidelines to Banks in April 2003 for regulating functioning of the proposed ARCS and these Directions/ Guidance Notes cover various aspects relating to registration, operations and funding of ARCS and resolution of NPAs by ARCS. The RBI has also issued guidelines to banks and financial institutions on issues relating to transfer of assets to ARCS, consideration for the same and valuation of instruments issued by the ARCS. Additionally, the Central Government has issued the security enforcement rules ("Enforcement Rules"), which lays down the procedure to be followed by a secured creditor while enforcing its security interest pursuant to the Act. The Act permits the secured creditors (if 75% of the secured creditors agree) to enforce their security interest in relation to the underlying security without reference to the Court after giving a 60 day notice to the defaulting borrower upon classification of the corresponding financial assistance as a non-performing asset. The Act permits the secured creditors to take any of the following measures:
• Take over possession of the secured assets of the borrower including right to transfer by way of lease, assignment or sale;

• Take over the management of the secured assets including the right to transfer by way of lease, assignment or sale;

• Appoint any person as a manager of the secured asset (such person could be the ARC if they do not accept any pecuniary liability); and

• Recover receivables of the borrower in respect of any secured asset which has been transferred. After taking over possession of the secured assets, the secured creditors are required to obtain valuation of the assets. These secured assets may be sold by using any of the following routes to obtain maximum value.

• By obtaining quotations from persons dealing in such assets or otherwise interested in buying the assets;

• By inviting tenders from the public;

• By holding public auctions; or

• By private treaty.

Lenders have seized collateral in some cases and while it has not yet been possible to recover value from most such seizures due to certain legal hurdles, lenders are now clearly in a much better bargaining position vis-à-vis defaulting borrowers than they were before the enactment of SRFAESI Act. When the legal hurdles are removed, the bargaining power of lenders is likely to improve further.
and one would expect to see a large number of NPAs being resolved in quick time, either through security enforcement or through settlements. Under the SRFAESI Act ARCS can be set up under the Companies Act, 1956. The Act designates any person holding not less than 10% of the paid-up equity capital of the ARC as a sponsor and prohibits any sponsor from holding a controlling interest in, being the holding company of or being in control of the ARC. The SRFAESI and SRFAESI Rules/ Guidelines require ARCS to have a minimum net-owned fund of not less than Rs. 20,000,000. Further, the Directions require that an ARC should maintain, on an ongoing basis, a minimum capital adequacy ratio of 15% of its risk weighted assets. ARCS have been granted a maximum realization time frame of five years from the date of acquisition of the assets. The Act stipulates several measures that can be undertaken by ARCs for asset reconstruction. These include:

- Enforcement of security interest;
- Taking over or changing the management of the business of the borrower;
- The sale or lease of the business of the borrower;
- Settlement of the borrowers' dues; and
- Restructuring or rescheduling of debt.

ARCS are also permitted to act as a manager of collateral assets taken over by the lenders under security enforcement rights available to them or as a recovery agent for any bank or financial institution and to receive a fee for the discharge of
these functions. They can also be appointed to act as a receiver, if appointed by any Court or DRT.

D. Institution of CDR Mechanism

The RBI has instituted the Corporate Debt Restructuring (CDR) mechanism for resolution of NPAs of viable entities facing financial difficulties. The CDR mechanism instituted in India is broadly along the lines of similar systems in the UK, Thailand, Korea and Malaysia. The objective of the CDR mechanism has been to ensure timely and transparent restructuring of corporate debt outside the purview of the Board for Industrial and Financial Reconstruction (BIFR), DRTs or other legal proceedings. The framework is intended to preserve viable corporate affected by certain internal/external factors and minimize losses to creditors/other stakeholders through an orderly and coordinated restructuring programme. RBI has issued revised guidelines in February 2003 with respect to the CDR mechanism. Corporate borrowers with borrowings from the banking system of Rs. 20 crores and above under multiple banking arrangement are eligible under the CDR mechanism. Accounts falling under standard, sub-standard or doubtful categories can be considered for restructuring. CDR is a non-statutory mechanism based on debtor-creditor agreement and inter-creditor agreement. Restructuring helps in aligning repayment obligations for bankers with the cash flow projections as reassessed at the time of restructuring. Therefore it is critical to prepare a restructuring plan on the lines of the expected business plan along with projected
cash flows. The CDR process is being stabilized. Certain revisions are envisaged with respect to the eligibility criteria (amount of borrowings) and time frame for restructuring. Foreign banks are not members of the CDR forum, and it is expected that they would be signing the agreements shortly. However they attend meetings. The first ARC to be operational in India- Asset Reconstruction Company of India (ARGIL) is a member of the CDR forum. Lenders in India prefer to resort to CDR mechanism to avoid unnecessary delays in multiple lender arrangements and to increase transparency in the process. While in the RBI guidelines it has been recommended to involve independent consultants, banks are so far resorting to their internal teams for recommending restructuring programs.

E. Compromise Settlement Schemes

One Time Settlement Schemes

NPAs in all sectors, which have become doubtful or loss as on 31st March 2000. The scheme also covers NPAs classified as sub-standard as on 31st March 2000, which have subsequently become doubtful or loss. All cases on which the banks have initiated action under the SRFAESI Act and also cases pending before Courts/DRTs/BIFR, subject to consent decree being obtained from the Courts/DRTs/BIFR are covered. However cases of willful default, fraud and malfeasance are not covered. As per the OTS scheme, for NPAs up to Rs. 10crores, the minimum amount that should be recovered should be 100% of the outstanding balance in the account.
Negotiated Settlement Schemes

The RBI/Government has been encouraging banks to design and implement policies for negotiated settlements, particularly for old and unresolved NPAs. The broad framework for such settlements was put in place in July 1995. Specific guidelines were issued in May 1999 to public sector banks for one-time settlements of NPAs of small scale sector. This scheme was valid until September 2000 and enabled banks to recover Rs 6.7 billion from various accounts. Revised guidelines were issued in July 2000 for recovery of NPAs of Rs. 50 million and less. These guidelines were effective until June 2001 and helped banks recover Rs. 26 billion.
Annexure 3

RBI GUIDELINES FOR CLASSIFYING ADVANCES

AS PER HEALTH CODE SYSTEM

Code 1: Satisfactory

This category covers all borrowers where:

(a) Conduct of the account is satisfactory;

(b) All terms and conditions (like punctual submission of stock statements, monthly statements of select operational data wherever applicable, quarterly operating statements wherever applicable, half–yearly operating and funds flow statements wherever applicable, balance sheets for annual review, etc., execution of annual acknowledgement of debt and security, etc.) are complied with;

(c) All accounts of the borrowers are in order;

(d) The safety of the advances is not in doubt.

Code 2: Irregular

This category of borrowers covers those accounts where the safety of the advances is not suspected though there may have been occasional irregularities which may be considered as a short–term phenomenon, e.g.: 
(i) The accounts are overdrawn beyond the drawing power (based on the value of security less margin) or the sanctioned limit for a temporary period. It should however, be noted that frequent overdrawing in accounts are not to be constructed as short-term Phenomenon.

(ii) Installments in respect of term loans overdue for less than six months or import bills under LIC, installments under deferred payment guarantee, if overdue for less than three months.

(iii) Some of the bills (not exceeding 10 percent – 15 percent of the total outstanding in the bills purchased / discounted account of the borrower) are overdue for payment by less than three moths and/or refund in respect of unpaid bills in not forthcoming immediately.

**Code 3: Sick-Viable / Under Nursing:**

Units in respect of which nursing/ revival programmes are taken up should be included under this category.

**Code 4: Sick –Non-viable/ Sticky:**

Accounts of borrowers under this category are those where the irregularities mentioned above persist, say for a period of six months and over and there are no immediate prospects of regularisation. Alternatively or in addition, the accounts could throw up some of the usual signs of incipient sickness, such as:
(i) Apparent stagnation in the business as reflected by slow/ negligible turnover in the account;

(ii) Frequent requires for overdrawing or issue cheques without ensuring availability of funds in the account;

(iii) Bills purchased / discounted drawn by the borrower remaining overdue for three months and more or the recovery of such bills from the borrower poses difficulties;

(iv) In the case of term loans, six or more monthly installments, two or more quarterly installments./ one or more half-yearly installments are overdue;

(v) Unexplained delays in submission of stock statements/ quarterly/ half yearly operating statements / balance a sheets and other information required by the bank;

(vi) Slow movement/ stagnation of stocks observed during inspections;

(vii) Low/ negligible level of activity observed during inspections or suspension/ closure of the business;

(viii) Persistent delay in compliance or non-compliance with vital requirements like exemption of documents, producing additional security when required, etc

(ix) Diversion of funds to sister concerns / acquiring capital assets not relevant to the business / large personal withdrawals;
(x) Pressure on the liquidity leading to non-payment of wages to workers/
    statutory dues / rents of office and factory premises;
(xii) Current liabilities exceeding current assets;
(xii) Any grave feature observed by the auditors of the bank which remain to
    be rectified;
(xiii) Basic weaknesses revealed by the financial statements of the unit such
    as continued cash loss beyond one year.

It should be noted that the above indications are not exhaustive and not all
of them may simultaneously be observed. Each bank has essentially to rely on its
own judgment on the above illustrative alarms signals while classifying the
borrower.

Sick units, which are considered potentially viable and keep under a
nursing programme by the bank should not come under this category, but should
be included under Health Code-3.

**Code 5: Advance Recalled:**

This category consists of those accounts where the repayments is highly
doubtful and nursing is not considered worthwhile. If a decision has been taken
(or likely to be taken) to recall the advances, such borrowers will be classified
under this code.
Code 6: Suit-field Accounts:

This category consists of accounts where legal action or recovery proceedings under the Public Debt Recovery Act wherever applicable have been initiated. These accounts may further be classified as under:

(a) Amount of advances where suits are pending for more than five years;
(b) Advances where suits are pending for more than two and upto five years;
(c) Advances where suits are pending for two years or less.

Code 7: Decreed Debts:

The advances where suits have been field and decree obtained will come under this category. This may be further classified into following:

(i) Amount of debts where decrees are pending execution for more than five years;
(ii) Amount of advances where decrees are pending execution for more than two and upto five years;
(iii) Amount of advances where decrees are pending for one to two years; and
(iv) Amount of advances where decrees are pending for less than one year.

Code 8: Debts Classified by the Bank as Bad/ Doubtful: All advances appearing under the Health Code numbers 3 to 7 and where recoverability of the bank’s dues has become doubtful on account of shortfalls in value of security,
difficulty in enforcing and realizing the securities, or inability/unwillingness of the borrowers or repay to bank’s dues partly or wholly, would come under this code. Such advances which are classified under Health Code No.8 should be excluded from the categories under health code numbers 3 to 7.

Note: RBI has given freedom to banks to continue or discontinue with the “Health Code” system.

Efficacy of the Health Code System:

A system of recognition of income based on the Health Code classification was thereafter introduced in the year 1989, where in the banks were advised to recognise income only on realisation basis, initially in respect of accounts under Health-codes No.6 and above and subsequently for those under Health Code No.5 also. While the Health Code classification was serving as a useful monitoring and Management Information Mechanism, absence of a transparent, objective and uniform yardstick for measurement of problem (sticky) advances was the major drawback of this system. Further, it was not useful as an enforcement tool due to absence of a benchmark in respect of the time to be taken by banks. For recalling the loan once it becomes problematic, deciding to file/filing of suit thereafter execution of the decrees obtained,

This was modified subsequently, for the accounting year 1990-91, banks should not charge and take into account interest on advances classified as 5 under HC system for advances under HC-4 application of interest was left to the
discretion of banks based on availability of adequate security. In sum a system of transparency.

The principals for income recognition, asset classification and provisioning enunciated through the Health Code System are discussed. Several “irregularities” included under the Health Code are similar to those considered in the definition of “non-performing assets” under the new package of prudential norms.

The feature of “Out of Order” cash credit/over draft accounts i.e. accounts overdrawn beyond drawing power/sanctioned limit, accounts with slow/negligible turnover or frequent over drawing included under clause (i) of Health Code 2 and clauses (i) and (ii) of Health Code 4 are also one of the adverse feature in determining NPAs.

A NPA has been defined as a credit facility in respect of which an amount remains unpaid for two quarters. Clauses (i) and (ii) of Health Code 4 are taken to this definition. (iii) bills purchased / discounted drawn by the borrower remaining overdrawn for 3 months and more ……. “ (iv) In case of term loan six or more monthly installments/two or more quarterly installment/one or more half-yearly installments are overdue.

In view of the above, it can be said that concept of NPA was evolved ten years ago although the term, as such as not in vogue. The basic difference between the Health Code System and the new package of prudential norms is that provisioning under the former is required to be made only with respect to the
portion of the advance not covered by realisable security whereas under the new package, in addition to consideration of availability of security track record of payment (or non-payment) by the borrowers, is also to be considered.

The Health Code System was required to be monitored by the Board of Directors through half-yearly returns and the same also submitted to Reserve Bank of India. The latter, through Circular DOS No.B.4/16.14.001/93-94 dated March 19th, 1994, considering the introduction of the new norms, the burden on the banks due to twin track classification and the new norms, the burden on the banks due to twin track classification and the conflict between the two system, decided that with effect from April 1st, 1994, “The Health Code classification shall cease to be subject of supervisory interest and reporting” (to the Reserve Banks of India and the Board of Directors). However, banks if they so desire, may continue to use the Health Code as Management Information System.

It may be appropriate to mention Sukhamoy Chakravorthy Committee (1985) report on Monetary System which has worded out recommendations on interest rate structure and other details of facilitate planned economic growth with the public sector investment driving growth and government trying to reduce dependence of foreign aid. Foreign banks rarely cropped up in this report but for the Narasimham Committee the logic is different. The Narasimham committee suggestions aim at financial engineering to keep pace with the current global consciousness. It can work provided the Government puts on par foreign and India banks which is not so.
Annexure – 4

NPA MANAGEMENT & SUGGESTIONS FOR CONTAINING NPAs

Measures for NPA management

The following are some general measures suggested for reduction of NPAs.

Preventive Measures:

1. Proper selection of the borrower / activity
2. Financing only viable schemes
3. Extending need based finance.
4. Ensuring proper end-use.
5. Proper post sanction followup.
6. Regular contacts with borrowers.
7. Regular monitoring of the accounts.
8. Avoiding over drawing and
9. Holding of recovery camps.

Corrective Measures:

1. Recovery
2. Rephasement
3. Rehabilitation
Drastic Measures:

1. Enforcement of primary securities charged to the Bank
2. Filing of suit.

Though qualitative lending correct execution of loaning documents and proper charging of securities binds the borrower to repay bank's dues and helps in recovery, the recovery can be accelerated at a much faster pace through effective.

1. Supervision and
2. Follow-up

Supervision:

Supervision of advances by bank officials includes:

(a) Ensuring proper end use of funds and creation of assets out of loan / credit / margin / subsidy within the anticipated period and compliance of all terms and conditions stipulated in the sanction letter.

(b) Timely and periodical inspection of the securities charged to the bank.

(c) Proper watch on the conduct of the borrower and operations in the account in various segments such as Ledger/Bills/Godowns.

(d) Proper maintenance of requisite records for Limitation, Insurance due date, mutation/noting of bank's lien, inspection, field visit village wise locality wise and irregularity-wise master charts etc. so that follow-up of supervised advances is cost effective and efficient.
(e) Timely receipt, proper scrutiny and interpretation of data to ascertain shortcomings in hypothecation stock statements/ Monthly Select operation Data/Quarterly Information System Returns (as per Chore Committee) submitted by the borrowers at the prescribed intervals.

(f) Constant touch with persons trading with the borrower to obtain market report in regard to his trade dealings, solvency etc.

Follow-Up:

In the case of deficiencies/irregularities observed, the borrower concerned/departments/forums should be vigorously followed up for rectification of these irregularities.

1) Issue of reminders/notices for deposit of installments, overdue interest, overdrawing and for realisation of overdue bills etc. to the borrowers at the appropriate time.

2) Personal contacts with the borrowers at periodical intervals.

3) If both steps (a) and (b) do not give desired results, local pressure tactic, if possible, may be applied and guarantor if any may be pursued to get the amount deposited by the borrower.

4) In case of defaulter in rural areas, letter may be written with full particulars of the borrower to the manager of bank branch and secretary of Primary Agriculture Credit Society in whose service area the borrower resides/operates the activity, with copies to the:
I. Controlling officer of the addressee bank/society

II. Lead Bank Officer of the district

III. Bank’s own district co-coordinator.

As per RBI guidelines, since bankers cannot finance the defaulters of other banks, the addressee bank will not make fresh loan to the borrower. The borrower can be pressurised by making him aware of this aspect.

(5) In case of Government sponsored programmes, particularly Integrated Rural Development Programme, list of defaulters along with complete details should be sent to Block Development Office (BDO) for Placement before the Block Level consultative Committee (BLCC).

The issue may be followed up by ensuring monthly meeting and by getting the discussions/decisions recorded in the minutes of the meeting. One copy of the minutes should be sent each to Lead Bank officer and Bank’s Own District Coordinator in case no fruitful results turn up for onward discussions. The Bank’s bottom line improvement largely depends on reduction in NPAs and preventing fresh NPAs would also help to improve the profitability of Banks. However good the credit dispensation process may be, total elimination of NPAs is not possible in banking business owning to externalities but their incidence can be minimized.
The following steps may be taken to reduce NPAs.

1) Massive recovery campaigns are launched.
2) Specific branch were recovery targets are allocated and budget for recovery may also be precrinal.
3) Recovery agents may be appointed.
4) Infrastructure/adequate machinery is provided to branch to render a helping hand.
5) Branch managers are exhorted to exercise extraordinary care in the selection of fresh borrowers so that new borrowal accounts does not enter in NPA list.
6) Lot of understanding needed among bank staff and customers to address them self to the problem of recovery.
7) Prompt control/follow-up/ monitoring measures help to prove borrowal accounts becoming irregular.

Alternate Methods for NPA Management

An effective resolution of the problem of NPA is hampered on account of inadequate legal provisions, the existing bottlenecks in the debt recovery process, absence of alternate avenue for wiping out the chronic NPAs from the banks' balance sheets and lack of credit information exchange facilities among the banks. At the policy level, there is need for legislation, which will make recovery processes smoother and legal action quicker. In consultation with the Government,
the Reserve Bank of India has initiated some measures on the above aspects for providing alternate methods to the banks for resolving their NPA problem. Some of the impending methods, which are under active consideration of the Reserve Bank of India / Government, are briefly discussed below.

1. Corporate Debt Restructuring (CDR):

Another method suggested for the reduction of NPAs is Corporate Debt Restructuring. The process is mainly restructuring the debt portfolio of the borrowers among its creditors to assist the borrowers in the revival of the projects and continue operations through reduction in existing debt burden and establishment of credit lines with implied assumption that the lender would prefer reduction in risk to optimization of returns. The objective of CDR is to ensure a timely and transparent mechanism for restructuring of the debts of viable corporate entities affected by internal and external factors, outside the purview of BIFR, DRT or other legal proceedings, for the benefit of all concerned. The major features of the CDR mechanism are:

1) It would be a voluntary system based on debtor-creditor agreement and inter-creditor agreement,

2) The scheme will not apply to accounts involving only one financial institution or one bank; instead, it will cover multiple banking accounts/syndication/consortium accounts with outstanding exposure of Rs.20 Crore and above by banks and institutions,
3) It would be only applicable to standard and substandard account, with potential cases of NPAs getting a priority.

2. Credit Information Bureau (CIB):

A Credit Information Bureau has been established with a paid-up capital of Rs.25 crore, in order to coordinate sharing of information on the borrowers of credit institutions. The CIB will perform the role of collecting and disseminating information on the list of suit-filed accounts and the list of defaulters including willful defaulters, which is presently handled by the RBI.

3. Defaulters' List:

For providing information regarding the defaulter borrowers to the banks and financial institution, the RBI introduced annual publication of the list of defaulters (suit-filed cases) to banks and financial institutions of Rs. 1 crore and above in 1995. The coverage of the scheme was widened by bi-annual circulation of the names of defaulters of Rs.1 crore and above in the doubtful or loss category. A scheme for collection and dissemination of information on willful defaulters with outstanding balance of Rs.25 lakh and above, on quarterly basis, was also introduced in February 1999. Pending appropriate amendments in the banking laws, the RBI has also advised banks to incorporate a condition in the loan agreement for obtaining consent of the borrowers to disclose their names in the event of their becoming defaulters. RBI has advised the banks to complete the process of obtaining consent of the borrowers by September 30th, 2001.
4. Debt Recovery Tribunals (DRTs):

The need for DRTs was felt in the light of difficulties faced in recovery of loans in the normal course due to legal proceedings involved in the recovery of suit filled loans as also the high cost of litigation. On the basis of recommendations of the Nanisimham Committee (1991) the Government of India promulgated an ordinance called Recovery of Debts Due to Banks and Financial Institutions on 24th June, 1993. The same ordinance was replaced by an Act on 27th August, 1993. The Act envisages the establishment of Recovery Tribunals for expeditious adjudication of recovery of debts due to banks and financial institutions. The Act provided for two-tier structure of DRTs and an Appellate Tribunal. This Act is extended to the whole of the country except Jammu and Kashmir. These provisions apply when debts due to any bank or financial institution or to a consortium of banks/ institutions exceed Rs. 10 lakhs. However, the Central Government can reduce this limit up to Rs. 1 lakh by issuing the notification. The debt, which is to be recovered with the help of DRTs has to be result of business activities. Tribunals are to be headed by a person of the rank of High Court Judge to be called as Proceeding Officer. Along with the Proceeding Officer, a Recovery Officer and other officers are employed by the Central Government. The rules for the conduct of the Tribunals have been framed under the Act. The tribunals have to decide the claim within six months and after that the presiding officer issues a certificate under his signature as order of the Tribunal to the recovery officer for the recovery of the debt specified in the certificate. The
recovery certificate is conclusive and parties cannot dispute or make objections. The recovery officer, thereafter, proceeds to recover the amount by way of an attachment and sale of movable or immovable property. Officer may appoint a receiver for management of movable and immovable properties of the defendants. The recovery officer is authorized to recover the amount of debt due and sale of the property in the manner laid down in the Income Tax Act. The recovery officer, has been vested with the powers as exercised by the income tax officer for the purpose of recovery of the due amount. The DRTs have got more power including directing the defendant to submit the amount committed by him to the bank within a month. If the defendant fails to do so, then the DRTs are empowered to issue certificates enabling the banks to recover the committed amounts. Such new amendment will help banks in recovering their dues quickly. There are 29 DRTs and 5 DRATs at Allahabad, New Delhi, Mumbai, Chennai and Kolkata. The Finance Ministry is monitoring progress of DRTs on the continuous basis.

At the initial stages, DRTs had some problems. Now almost all the DRTs have space, infrastructure etc. Banks rendered adequate support in setting up of the new DRTs and smooth functioning of the old DRTs. However, some DRTs have reported the shortage of staff in the cadre of stenographers. Coordinating committees are constituted for ensuring better coordination between banks and DRTs / DRATs. Other problems faced by DRTs are: (a) further improvement in
infrastructure facilities available to DRTs is very much required, (b) it has been observed that appointments on DRTs are made either of persons on deputation for short period or who are on the verge of retirement, (c) inadequate staff to handle administrative tasks at DRTs. In order to solve these problems and other problems faced by the DRTs, many suggestions were made and the same are being considered.

5. One-Time Settlement/Compromise Scheme:

The RBI in consultation with the Government of India issued guidelines for recovery of loan dues owned to commercial banks up to Rs.10 lakh. The time limit for processing of applications received under the revised guidelines for compromise settlement of chronic NPAs of public sector banks, was extended up to December 31st, 2003. Based on the requests received for further extension of the time limit for operation of the guidelines and in consultation with Government of India, the time limit for receiving applications was further extended up to July 31st, 2004 by the government.

For improving flow of credit to Small and Medium Enterprises (SME), the Union Finance Minister issued detailed guidelines on debt restructuring mechanism for units in the SME sector. These guidelines were issued in September 2005, to all Scheduled Commercial Banks to ensure that they restructure debt of all eligible SMEs. The one-time settlement scheme for recovery of NPAs below Rs.10 crore provides for a simplified, non-discretionary
and non-discriminatory mechanism for onetime settlement of chronic NPAs in the SME sector. The scheme covers all NPAs in the SME sector, which have become doubtful or loss as on March 31st, 2004 with outstanding balance of Rs. 10 crore and below on the date on which the account was classified as doubtful. The last date for receipt of applications from borrowers was March 31st, 2006. The processing under the revised guidelines was required to be completed by June 30th, 2006.

6. Lok Adalats:

Lok Adalats were granted judicious status with the enactment of the Legal Service Authority Act of 1987. It is a convenient method for settlement of disputes between banks and small borrowers. Consequently, RBI issued necessary guidelines to banks and other financial institutions advising them to resort mechanism of Lok Adalats for the recovery of debts. The Government revised the monetary ceiling of cases to be referred to Lok Adalats organized by Civil Courts from Rs.5 lakh to Rs.20 lakh.

7. Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI): The Act provides, *inter alia* for enforcement of security interest for realization of dues without the intervention of Courts or Tribunals. The Security Interest (Enforcement) Rules, 2002 has, also been notified by Government to enable secured creditors to authorize their officials to enforce the securities and recover the dues from the borrowers. The
Supreme Court in its judgment on April, 2004 in M/s. Mardia Chemicals has upheld the constitutional validity of the Act and its provisions except that a subsection 2 of Section 17 by the secured creditor, in case the borrower wants to appeal against the secured creditor's notice under Section 13 (4) of the Act. It has declared Section 17 (2) as unconstitutional and violative of Article 14 of the Constitution of India. In the wake of this judgment, many banks have pointed out practical difficulties, which are likely to arise in speeding up the recovery of NPAs. The suggestion of banks, IBA and other organizations in this regard are being examined to carry out necessary amendments in the Act. In the Union Budget 2004-05, the Government proposed to amend the relevant provisions of the Act to address appropriately the Supreme Court's concerns over a fair deal to borrowers while, at the same time, ensuring that the recovery process is not delayed or diluted.

8. Asset Reconstruction Companies (ARCs):

To address the problem of accumulated NPAs, the first Narasimham Committee, suggested the setting up of an Asset Reconstruction Fund, but this suggestion could not be implemented. Reiterating this arrangement, the second Narasimham Committee and Varma Committee suggested the setting up of an Asset Reconstruction Company (ARC). The ARC, which would take over all loan assets in the doubtful and loss categories, would issue to the banks NPA Swap
Bonds representing the realizable value of the assets transferred, provided the stamp duties are not excessive.

Securitization and Reconstruction of Financial Assets and Enforcement of Security. Interest Act, 2002 was enacted to pave the way for setting up of Asset Reconstruction Companies (ARCs) in India. To solve the problem of bad loans, several institutions have initiated steps towards establishment of ARCs, which takeover non-performing loans of banks and Financial Institutions at a discounted rate, and manage and dispose such assets. Under the Act, it is envisaged that ARCs shall be registered with RBI and RBI would issue necessary guidelines to ARCs for conducting business. RBI issued the guidelines on April 2003. However the Act was, challenged by a group of companies led by M/s. Mardia Chemicals and Industries Ltd.

The first ARC was granted registration in August 2003. The Reserve Bank has so far granted certificate of registration (CoR) to four Asset Reconstruction Companies out of which Asset Reconstruction Company (India) Limited (ARCIL) has already started its operations.

Supply of Information on Defaulters by Credit Information Bureau deregulation of interest rates, freedom to charge lending rates, prudential norms in line with international standards etc, were the other measures initiated by Reserve Bank of India to reduce NPAs in banks.
Suggestions for Containing / Reducing NPAs

The following preventive and corrective elaborate measures can be suggested for reducing NPAs in Indian banking sector:

1) Banks should examine the viability of the project before providing financial assistance. It is necessary to ensure that the project will generate sufficient return on the resources invested in it. The viability of the project depends upon technical feasibility, marketability of the products at a profitable price, availability of financial resources in time and proper management of the unit.

2) Sanction of financial assistance after proper appraisal alone is not sufficient for recovery of advances. Disbursement of funds according to the requirements of the project, effective supervision and timely follow-up, involvement of all the staff members for better recovery and update knowledge of NPA accounts are also equally essential. If proper care is taken for appraisal, supervision and follow-up of the advances, future NPAs can be avoided.

3) The services of professionals should be used in credit appraisal. Towards implementing such professionalism, professional such as Chartered Accountants, Engineers, Lawyers etc. should be recruited and associated at all levels of credit appraisals (and of course at other stages too). However, good the credit dispensation process may be, total elimination of NPAs is not possible in banking business owing to the externalities, but their incidence can
be minimized by taking necessary precautions. Special care should be taken for those advances which are showing irregularities and likely to become NPAs.

4) While assessing the business risks, assessing of the mental shape of the borrowers is very important. This psychological evaluation could be done only through the interaction/ personal touch maintained with the borrowers. This understanding will go a long way in sanctioning loans and in recovering the same. In a situation wherein the banks are already saddled with large quantum of NPAs, launching a strategic initiative for reducing their quantum by taking recovery monitoring as a broad based movement through technological aid can bring about substantial improvement in its functioning. As the PSBs undertake lending to different sectors of the economy and have geographical spread through its branch network, the viability will depend upon the profit generating capacities of its operations. Effective NPAs reduction policies of the PSBs must encompass the objectives of sound risk management, credit administration and staff motivation. Therefore, NPA reduction as an organization goal is important for the PSBs to survive global competition.

5) There should be operational restructuring covering aspects like revamping management, staff and branch rationalization. Simultaneous steps should be taken to prevent reemergence of NPAs by stricter application of prudential norms. By the use of ‘Critical Amount Concept’ and other strategies like Lok Adalat, CDR scheme and ARCs etc., NPAs in future can be reduced to a great extent.
6) To make the functioning of DRTs more effective, it will be matter of economic sense to provide basic infrastructure to them. As against significant opportunity cost of funds locked in cases filed with DRTs, only a fraction of such cost can facilitate the DRTs to function in an efficient manner. The DRTs with access to data base across the country can function more efficiently as less adjournments and less uncertainty can be expected.

7) Since awarding interest under Section 34 and Order 34 Rule 11 of the Code of Civil Procedure is within the discretion of the Courts, Courts often interfere in the rate of interest and in some cases without giving reasons. The Hon'ble Supreme Court in SBI vs. Y.V. Rao's case has held that court should not normally interfere in the rate of interest agreed to between the parties even where mortgage is taken and that Section 21-A of the Banking Regulation Act, 1949 debarring Courts from re-opening transactions on the question of interest is valid. However, to make things more clear and certain, appropriate amendments should be brought under Section 34 and Order 34 Rule 11 of CPC making it obligatory on the part of the Courts to award contractual rate of interests from the date of suit till realization.

8) The existing number of courts and their infrastructure in the country is not enough to cope up with the present workload besides the huge backlog of cases. Therefore, Banks and Financial Institutions should take up the matter with the Union Government for establishing more courts at all levels and in particular for disposing of the cases of the Banks and the Financial Institutions.
Till more courts are established, the prudent option would be to use the existing legal set up to the best advantage of the banks. To that end, the banks and financial institutions may lead a higher level of delegation to the Chief Justice of the High Court in each state to allocate a separate court for trying their cases. If such exclusive courts were allocated, it would be convenient for the Banks and financial institutions to follow up the cases before such courts with the advocates concerned. Further, banks and Financial Institutions could send their own Law Officers (who are all advocates by profession) to such exclusive courts for conducting and following up cases. If the Law Officers conduct cases before such courts, then in course of time they would acquire highly specialized professional skills in conducting banks cases, thereby, paving the way for effective and speedier disposal of cases at relatively lesser expenses. The same methodology may be adopted in conducting cases before DRTs also.

9) In order to expedite the pace of recovery, the State Government should consider the following suggestions:

1) All priority sector advances upto Rs.2 lakh should be declared as State Sponsored Scheme and covered under the ‘Public Money (Recovery of Dues) Act’.

2) Recovery Certificate to be computerized at the district level and proper monitoring may be undertaken.
3) A separate ‘Recovery Cell’ at each district headquarters may be set up under the control and supervision of the District Collector. The Lead District Manager along with the representatives of commercial banks and revenue authorities should conduct periodical meetings to review the performance.

4) Recovery Certificates with the revenue authorities remain pending for years together. There are instances where pendency is about five years. Therefore, there is a need to fix a time frame for execution.

5) In many cases, Recovery Certificates are returned with remarks ‘Borrower is not available’. “No moveable / immovable assets are available”. In such cases, the revenue authority should arrange a joint inspection with the banks authorities so that interest of the banks could be safeguarded.

6) Name of the defaulters should be published in the local newspapers. This will have good impact on image conscious defaulters.

7) Recovery proceeds should be remitted to banks immediately.

8) Revenue authorities and bankers should take up regular reconciliation of Recovery Certificates. Wherever, Recovery Certificates are not available, duplicate should be filed.

9) Revenue authorities face problems in recovery of dues from women beneficiaries. Hence, Women Collection Mains should be appointed for recovery of such dues.
10) Majority of the banks has a demand that the scope of the directed credit under priority sector should be reduced gradually from 40 per cent to 10 per cent as recommended by Narasimham Committee. But in a country like ours, we cannot move away from the stark reality of poverty and hence, the necessity of continuing credit to the priority sector cannot be disputed. In other words, reforms will not come in the way of priority sector lending as the Government has not accepted the recommendations of Narasimham Committee on the aspect of reduction of priority sector lending from 40 per cent to 10 per cent under the redefined category. Therefore, much improvement can be achieved by enabling the banks to select the beneficiaries themselves rather than depending on Government agencies.

11) In credit policy announced in October 1998, a general provision @0.25 per cent on standard loans has been allowed. However, it is a wise step in the right direction, but it should be at least 1.00 per cent as demanded by majority of the respondents. Likewise, starting from 1999-2000, banks will be exempted from tax to the extent of 5.00 per cent of doubtful and loss assets for 5 years to clean up their balance sheet, but it should be at least 10 per cent as the quantum of NPAs is comparatively high in banking sector and the period of 5 years should be extended further.

The quality and performance of advances have a direct bearing on the profitability and viability of banks. Despite an efficient credit appraisal and disbursement mechanism, problem can still arise due to various factors. The
essential component of a sound NPA management system is quick identification of non-performing advances, their containment at minimum levels and ensuring that their impingement on the financials in minimum. Management of NPAs continues to be the foremost challenge of the Indian banking system. In the recent past, there has been a conscious and persistent effort through the prescription of strict objective norms for the identification and classification of NPAs. This was also supplemented by the sustained efforts both by the the Government and the RBI for setting up the requisite infrastructure as also systems/ procedures for effecting recoveries/ reduction of NPAs. However, realizing the rigidities in the legal system, the government enacted the securitization bill that would ensure that legal inadequacies do not thwart the resolve to reduce the NPAs of banks. In addition banks have been advised to strengthen their credit administration machinery and put in place effective credit risk management systems to reduce the fresh incidence of NPAs. The sum up, the biggest ever challenge that the industry now faces is the phenomenon of NPAs. Therefore, banking industry and financial institutions should act in concert with unity of motive, chalk out strategy to reduce the existing and future NPAs. If that is done, the banking industry could add one more feather to its cap for having successfully tackle this perilous phenomenon of NPA. The road ahead of us in the new century is going to be different from the tract traversed hitherto. The competition will be growing as never before, challenges will be more while banking for profits and the solution lies in converting these challenges into opportunities through proactive strategies and better credit administration.
1. Definition of financial asset and property under Section 2 of The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interests (SARFAESI) Act, the following assets can be charged to the bank and bank can realize them under Act.

Book debts:
Under Section 2(1) (i) (1) (IV) (V) and F(IV) and if they are charged to the bank then in case of default, bank can issue notice under Section (13) (d) of SARFAESI Act to debtors.

Intangible assets:
Under Section 2(T)(V) of Act as assets being know-how, patent, copy right, trademarks, licence, franchise or any other business or commercial rights of similar nature.

2. "Section 14 of SARFAESI Act assigns a duty on Chief Metropolitan Magistrate or District Magistrate as an Administrative Head of the District to assist secured creditor in taking physical possession of secured asset."
3. It is the debts recovery tribunal DRT/DRAT who are empowered to hear the objections of anybody including mortgagor/borrower against the decision of the bank to take the possession of secured assets. Further Section 14(3)(1) protects Chief Metropolitan Magistrate and District Magistrate that if they act in pursuance of this Section, they cannot be called in question in any Court or before any authority. As such in my view the District Magistrate or Chief Metropolitan Magistrate is liable for offence under Section 29 of the Act if he does not act on the request of the secured creditor or delay the efforts in taking possession of secured assets by providing an opportunity to hear the objections of anybody including mortgagor/borrower and try to adjudicate on merits of the bank's decision.

4. By the effect of Section 34, and 35 of this Act, no Civil Court has any jurisdiction to entertain any suit or Proceedings in respect of the secured assets. Once a notice has been issued by the bank as secured creditor to mortgagor under Section 13(2) or (4) of this Act, the only DRT and DART are empowered to determine the disputes by or under this Act in respect of secured assets. If the suit or proceedings are existing before any assets. If the suit or proceedings are existing before any Civil Court prior to issuing of notice under this Act by secured creditor, they can also be got stayed or dropped if they are inconsistent to the rights of a secured creditor under this Act. In such a case the bank can request Civil Court itself or proceed to DRT for this purpose.
5. It is mandatory to classify the account as non-performing asset in book of account of the bank in accordance with directions and guidelines issued by the Reserve Bank of India (RBI) before taking any step under this Act. Therefore, the procedural management of a classified NPA account should be an such a manner which may not give any room for DRT to apprehend any violation of backward districts initiative (BDI) guidelines and treat the account as upgraded or performing one. Once the account is classified as NPA to hold on operations and debit of any kind should be allowed to appear as recovery. If bank decides to allow hold on operations in order to give some more time to borrower, enabling him to come up from crisis and upgrade the account, it should be allowed through a separate current account. Similarly as in NPA account the interest is not to be changed on accrual basis and can be charged on recovery basis, any credit if adjusted towards interest should be routed through a replica account. This system will facilitate in processing of OTS/OCS proposals also while calculating of notional dues and minimum acceptable amount as per the policy laid down by the bank or RBI.

6. The bank cannot take possession under Section 13(4) of SARFAESI Act if the mortgaged property has been leased our prior to mortgage and if leased out after mortgage in accordance with provisions of Section 65 A of Transfer of Property Act. It can take possession of the property which is leased out after mortgage in contravention of provisions of Section 65 A of Transfer of Property Act.
PRO_FORMA OF THE QUESTIONNAIRE USED

A. PERSONAL INFORMATION

Name : 
Designation : 
Name of the Bank : 
Cadre : 1. Senior Management
        2. Middle Management
        3. Junior Management
Work Experience : 1. Less than 10 years
                 2. 10 – 20 years
                     3. More than 20 years

B. OPINION ON REASONS FOR NPAs

1. Please tick the reason which you consider important for NPAs from the most popularly accepted reasons listed below:
   a. Political Interference
   b. Willful default
   c. Diversion of funds
   d. Lack of legal support
   e. Deficiency in the credit appraisal standards
   f. Lack of supervision and follow-up
   g. Higher rate of interest

C. OPINION ON NPAs

Please indicate with (√) mark whether you agree or disagree with the following statements.

1. There is a feeling that banks are not able to bring down the rate of interest to borrowers on account of NPAs.
   Agree ( ) Disagree ( )
2. There is no system in the bank to fix the rate of interest to the borrower on the basis of repaying capacity. 
   Agree ( ) Disagree ( )

3. Overall cost to the borrower in terms of interest rate, processing charges, legal charges, supervision and follow-up etc charges, is very high and it results in NPAs. 
   Agree ( ) Disagree ( )

4. The rate of interest charged to the borrower is much in excess of the declared PLR (PLR +6% and above) for most of the borrowers. 
   Agree ( ) Disagree ( )

5. Present Capital Adequacy norms can reduce / minimize the risk of NPAs for banks. 
   Agree ( ) Disagree ( )

6. Bank raise subordinate debt at high cost supplements the tier II Capital and Capital Adequacy. 
   Agree ( ) Disagree ( )

7. It is generally felt that banks do not pay adequate attention to borrower customers as they do in the case of deposit customers. 
   Agree ( ) Disagree ( )

8. There is no system of exchange of information among banks about their experience with borrowing customers. 
   Agree ( ) Disagree ( )

9. There is a general feeling that banks do not have an effective market intelligence system to know more about the borrowers and act accordingly. 
   Agree ( ) Disagree ( )

10. Availability of staff to manage loan portfolio is generally inadequate. 
    Agree ( ) Disagree ( )

11. Because of growing NPAs, there is a tendency among banks to switch over to investments in Government Securities. 
    Agree ( ) Disagree ( )

12. Of late, there is a general aversion to lending among banks because of NPAs. 
    Agree ( ) Disagree ( )

13. Only banks and other stake holders other than defaulting borrowers get affected because of NPAs. 
    Agree ( ) Disagree ( )
14. Representative bodies like FICCI, Chambers of Commerce & Industry, Confederation of Indian Industry, Federation of India Exporters Association etc, do not support banking industry in recovering the banks’ dues from their members.

Agree (  ) Disagree (  )

D. OPINION ON IMPACT OF NPAs

Pl tick on one – which you consider is the most important

A. Erosion of Profit (  )
B. Increasing spread (  )
C. Increasing intermediation cost (  )
D. Increasing Provisions (  )
E. Declining reserves and surpluses (  )
F. Increasing market borrowings (  )

E. SUGGESTIONS

Please indicate your view by placing a (√) at all statements you agree with.

1. The problems of NPA can be contained to a great extent by maintaining a continuous rapport / relationship with borrower customers. (  )

2. Borrowers have to be made more accountable / responsible to contain the NPA problem. (  )

3. Involvement of Auditors, Accountants, Regulators, Representatives bodies etc, would help to recover the banks dues in an effective manner. (  )

4. Corporate Governance in Corporate bodies can help to improve the conduct of accounts with banks and bring down the level of NPAs. (  )

F. GENERAL COMMENTS / SUGGESTIONS ABOUT NPAs

Please offer your comments / suggestions relating to NPAs