Chapter 6:
Management of Non-Performing Assets: Remedial Measures

6.1 Measures Taken to Deal with NPA
6.2 General Remedial Measures
6.3 Legal Remedial Measures
6.4 NPA Management in Selected Banks
6.5 Initiatives Taken for Asset Quality by Selected Banks
Chapter 6

MANAGEMENT OF NON-PERFORMING ASSETS: REMEDIAL MEASURES

The issue of NPA management continues to be the biggest challenge before the banking sector. One of the major constraints of the competitive efficiency of banks is the tendency to accumulate the non-performing assets.\footnote{Shri G.P. Munniappan, Deputy Governor, Reserve Bank of India, at the NIBM Annual Day Celebrations January 6, 2003.}

It is a critical indicator for assessing banks credit risk assets quality and efficiency in allocation of resources to productive sectors reflecting the success of financial sector reforms, regulatory and supervisory process reforms, regulatory and supervisory process in particular selected public sector and private sector banks have made substantial progress in cleaning up the NPAs from their balance sheets.

A common perspective is that bank’s non-performing assets are influenced by structural nature of the economy. The structural nature of India’s financial market has undergone significant changes due to financial sector reforms.

6.1 Measures Taken to deal with NPAs

In India, whatever reduction of NPAs has been done so far is mostly by the banks themselves, according to the policy recommendations of different committees. The problem of NPAs was first brought into focus by the Narasimham Committee on financial system (1991), set up at the advent of the liberalization process. It was pointed out by the Committee that the genesis of the problem was in the laxity of the prudential norms relating to income recognition, asset classification and provisioning.\footnote{There was also a general perception that directed lending as a part of the policy of bank nationalization played a major role in creating large amounts of NPAs on the balance sheets of public sector banks since loans were extended irrespective of the credit-worthiness of the borrowers.} The Committee
Management of Non Performing Assets: Remedial Measures

placed emphasis on indentifying problem loans of banks and making provisions for such loans and so instituted a proper definition of NPAs. Apart from identification of bad assets, the Committee also suggested some ways to deal with them. In order to speed up the process of recovery of problem loans, it recommended the setting up of Debt Recovery Tribunals to adjudicate on bad debts of banks and also of an Asset Reconstruction Fund to take such loans off the bank’s balance Sheets. At the same time, to improve the financial health of banks, several other measures relating to freeing of interest rates on deposits and advances, reduction of cash reserve ratio (CRR) and statutory liquidity ratio (SLR) and deregulation of entry of new private sector banks etc. were taken by the RBI. The Narasimham Committee on Banking Sector Reform (1998) suggested the second-generation reforms. For improving the financial health of banks, the Committee mainly stressed improved capital adequacy along with asset classification norms and resolution of NPA Related problems. Subsequently, the Verma committee (1999), Formed in order to formulate appropriate policies to deal with weak PSBs, emphasized that "NPAs have been the single most vexing problem faced by the public sector banks. Banks that have been identified as weak are mainly so because of the loss of their income, high carrying costs of NPAs both in terms of their funding as well as provisioning and the general stagnation of operations caused by the NPAs in their books."[3]

In line with the recommendations of these Committees, a number of steps have been taken to resolve the problem of NPAs in our country. Various measures introduced by RBI since 1993 to assets and contain the growth of NPAs are described below.

Dismantling of controls and deregulation of working of commercial banks, permitting entry of new private sector banks and permission for foreign banks to open more branches are steps that were carried out under

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banking sector reforms. There steps had the effect of opening Indian banking to global standards by making them to function efficiently in a competitive environment. This is the initial step to create a structural frame- work for the public sector banks to enable them to adjust to the new environment and turn into dynamic and self reliant operating units. The process of deregulation frees the banks from the control of the finance ministry and RBI. The RBI, here after acts as regulator. In the year 1994 RBI further fine-tuned the process by constituting a separated a board of financial supervision (BFS) with the object viceroy role from the regulatory functions of RBI. Banks now operate independently in a competitive financial market, but have to comply with prudential norms and safe guards essential for their well being. RBI in the year 1993 introduced prudential norms as conveyed by Basel Accord of 1998 applicable to Indian Banks. These included standard relating to capital adequacy, Income recognition, Asset classification and provisioning for non-performing assets. This had the effect of providing a much-needed transparency with regard to the state of affairs of each bank and enabled instant corrective measures to be executed. Banks were permitted to seek infusion of fresh equity from the public retaining government share of equity capital at 51 percent. A number of PSBs entered the market and raised Tier I and Tier II capital accordingly. This has created a new class of stake-holder (albeit share holder) vitally interested in the well being of the banks and qualified empowered to question the board of directors at the appropriate forum.

Under chairmanship of Dr. A. S. Gangly and bring out appropriate set of standards, to make recommendations towards more effective functioning of bank boards. The group was to review the supervisory role of boards of banks and financial institutions and to obtain feedback on the functioning of the board vis-a-vis compliance, transparency, disclosures, audit committees etc. and submit recommendations for making the role of boards of directors more effective with a view to minimizing risk and over exposure.
6.2 General Remedial Measures

There are two approaches to reduce NPA. There are preventive and curative. Preventive measures stop the slippage of performing assets to become non-performing asset. It would be better to tackle the problem at the initial state. Curative measures help in bringing back the non-performing assets to performing one. These measures designed to maximize recoveries so that bank’s funds locked up in NPAs are released for recycling.

Pre-sanction Appraisal:- While recommending the credit proposal for sanction by senior officers, the field functionaries in bank by should make discreet queries about the promoters and approve only those conditions which are acceptable to borrowers and the bank. Timely sanction of credit is essential. The Security in only loan account should be examined taking into account their life durability selling position, reliability, demand, etc. All the important terms and conditions which the borrower is to comply with should be conveyed.

Post-sanction follow up:- A regular vision and a regular follow of information from the borrowers to the bank relating to the progress of enterprise and the end use of banks funds, should be ensured. Periodical inspection of the business or project should be made and at that time it becomes more imperative to have a dialogue with the borrower on the projected figure and actual received potential and borderline NPA account require quick diagnosis and remedial measures.

The Ripple effect:- This is a phenomenon that traces the deterioration of performing asset from its earliest state of incipient sickness to its logical end. The ripple effect also identifies the two components of NPAs. The first one is the 'Visible NPA' which duly gets reflected in the balance sheet and the other is 'Invisible NPA' that does not find a place in the balance sheet as such. The invisible NPA is the commencement stage where the interest component also
remains unpaid, though it booked as income recoverable. It is a fact that cost of dealing with 'invisible NPA' would always be very much less than that of initiating salvage operations with an NPA. hence, in accounts where one quarter of interest always remains unpaid, the reasons for the same has to be ascertained and proper remedial action has to be taken to see that the borrower shifts to position 'A' rather than position 'B' as details in the flow chart given below:

**FLOW CHART**

<table>
<thead>
<tr>
<th>Interest-1</th>
<th>One Quarter interest to be paid</th>
<th>Two Quarter Interest- 1 Installment remains to be paid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Installment paid on time without arrears</td>
<td>Invisible to NPA, though Performing</td>
<td>Visible NPA</td>
</tr>
</tbody>
</table>

Thus, a realistic and timely action or check would help the banks and the borrowers to maintain good financial relationship despite difference of option.

**Reminder System:** The cheapest mode of recovery is by sending reminders to the borrower the loan installment falls due. But efforts need to be strengthened in banks in sending reminder on timely basis.

**Visit to borrower's business premises or residence:** visits are needed to be properly planned. Involvement of staff at all level in the bank branch is called for frequent visits for hard core borrowers.

**Recovery Campus:** In respect of agricultural advances recovery campus, in properly planned way, should be organized during the harvest season. It is also to take the help of outsiders, particularly, revenue officers in the state government, local panchayat officials, regional managers in the
bank, etc. It also calls for professional approach to give a wide publicity to the recovery campus organized in the local area in respect of both the agricultural as well as industrial advances. Mobilize as many borrowers as possible and motivate the staff to get involved in the recovery drive.

**Rehabilitation of sick Units:** Rehabilitation, from banker’s angle is a process of patiently waiting for the unit to turnaround. Sick units should be identified on, timely basis. If sick units are found potentially viable, rehabilitation package has to be prepared without loss of time, keeping in mind the board parameters suggested by the RBI.

The package should be implemented at the realist by the bank and the borrower:- Close monitoring of the progress of implementation is called for. For successful rehabilitation, it is essential to create a sense of urgency on the part of both banks and borrowers. Efforts on the part of the Government in terms of concessions, relief etc. Should be made on timely basis.

**Re-phasing unpaid loan installments:** In respect of science and hardworking borrowers, bankers need to be sympathetic. If such borrowers fail to pay loan installments due to natural calamities or for some other convincing reasons, unpaid loan installments may be rephrased or rescheduled. Banker's efforts are needed to be strengthened in this regard.

**Mergers and Takeovers:** It is a process under which a sick unit is merged with a healthy unit or sometimes, a healthy unit acquires a sick unit. In case of a merger, the NPA will get immediately converted into a performing asset because it will acquire the status of the healthy unit.

**Sale of pledged and hypothecated goods or property:** In case of hypothecation, the possession is not with the bank whereas in pledge, in case of default by the borrowers, that bank can easily dispose of the goods charged
in its favour. But before sale, the bank should give reasonable notice to the borrowers to repay the loan falling which goods held by the bank may be sold. The new ordinance issued in June 2002, allows secured lenders to sell or lease assets which are charged with them by a defaulting borrower without a protracted legal tussle.

**Loan Compromise:**- A compromise may be called a negotiated settlement in which the borrower agrees to pay a certain amount to the banker after getting certain concessions. This should be voluntary. Professional approach should be adopted in preparing the compromise proposal for which bank is expected to introduce a scheme, it’s own 'One Time Settlement' Scheme. Committee approach should be adopted to decide on the loan compromise. Delay in taking decisions should be avoided.

**Other Measures:**- Seminars and regular training programmes on credit and NPA Management for all levels of executive should be concluded by banks. Existing system of Staff incentives may be offered to lawyers who can manage to get a decree in a record time.

### 6.3 Legal Remedial Measures

#### Recovery through Courts

Once an advance is identified as non-recoverable the branch/bank should resort to civil litigation without loss of time. Experience reveals that recovery through legal procedure is quite time-consuming and long drawn out affair. Yet, filing of civil suits has almost become a routine practice in the banking industry. It is therefore, necessary for people entrusted with the responsibility of handling such civil litigations to understand the legal procedures and the jargon there under, especially at the branch level. Such an understanding shall help the branch in taking necessary precautions while drafting a plaint, filing a civil suit and help in maintaining effective follow up with advocates to ensure timely obtention of the decree and its execution.
Pre-Filing Stage

Branch should ensure that documents are properly stamped (Pro-Note or Bill of Exchange not stamped or inadequately stamped are inadmissible in evidence while other documents are admissible on payment of duty and penalty), there are no blanks in the documents executed; corrections are authenticated, that the documents required to be registered with the Registrar of Assurances are duly registered and enforceable, i.e. not time-barred (normal period of limitation for a suit for recovery of a demand advance is three years from the date of advancement and in case of advances repayable by installments is three years from date of payment of each such installment), before delivering them to the advocate for filing in the court. Before filing plaint, branch has to ensure appropriation of credit balances of deposit accounts against loan outstanding as also of proceeds from sale of goods pledged, if any. Branch should also ascertain from the advocate, the court in which the suit is to be filed. Usually, the place of cause of action, residence of parties, and location of immovable property offered as security, etc. decides the jurisdiction. In mortgage suits, location of mortgaged property determines the jurisdiction.

All the persons, who are necessary parties to the suit, should be joined therein. In certain cases, there is a possibility of having different guarantors for different loan accounts of the same borrower. In such cases, filing a single suit against the borrower and all the guarantors may amount to misjoinder of parties. Such situations need to be discussed with advocate/legal department thoroughly beforehand. It is necessary to serve recall notice before initiating litigation. Branch has to give a reasonable time limit to the borrowers/guarantors to comply with the notice. In hurried situations, the branch may serve a recall notice at least by telegram. For a suit against State/Central Government, two month’s prior notice is mandatory under Sec.80 CPC. However, in case of urgency, the suit can be filed with a request to dispense notice and with leave of the court.
Management of Non Performing Assets: Remedial Measures

Branch should share full details of the circumstances leading to filing of the suit with the advocate. They should pass on the documents to the advocates under acknowledgement while retaining a set of Xerox copies in the branch. Branch has to calculate uncharged interest at contractual/applicable rate till the date of filing of suit and advise the advocate to incorporate it in the plaint along with the ledger outstanding and pray for decree for the total amount. Branch should verify the facts and figures relating to the account mentioned in the plaint and get it approved at the appropriate level before directing the advocate to file it in court. Branch has also to verify the court fee on plaint and pass on the requisite amount to the advocate against acknowledgement. Approved plaint and certified account statements may be delivered to advocate with instructions to file the suit.

Filing Stage

Branch should be careful in deciding the type of suit to be filed, based on the nature of securities and pleadings to be made. Wherever loans are secured by mortgages, it is to be ensured that the authority signing the plaint has express powers to sign plaint under a power of attorney granted under a Board resolution, or else, its maintenance may pose a problem at a later date. Branch should ensure timely filing of suit and call for suit particulars, viz. suit number, date of filing, amount of suit, date of next hearing, etc from the advocate.

Post-Filing Stage

While filing a suit, an application for appointment of receiver, in case of suit against companies, has to be filed. On Appointment of such receiver and his taking possession of hypothecated goods, the branch should provide him the necessary funds to preserve the goods, pay salaries of watchman, municipal taxes, insurance charges, etc. All these expenses are later to be claimed under the decree. Wherever appointment of receiver is not possible
and the bank thinks that the borrower should be restrained from alienating. The securities, etc., to protect itself; an application for attachment/injunction may be filed in consultation with the advocate. Secondly, in some situations the bank may feel that usage of the machinery by the defendant, while the suit is in progress, may result in wear and tear leading to poor market value and this being detrimental to its interest, the bank may file an application for injunction restraining the company from using the machinery or in lieu deposit appropriate amount in court. Wherever hypothecate goods are likely to deteriorate fast. The advocate may be asked to file application under Order 39 Rule 6 of CPC for interim sale of such moveable goods. Wherever borrowers/guarantors are observed to have assets that are disposable but are not charged to the bank and the charged assets are not likely to yield sufficient amount to satisfy the suit and the bank apprehends that the defendants are likely to alienate/dispose of such properties, the advocate may be asked to file an application praying for an attachment order against the said properties or for the court to direct the defendants to provide additional security, pending disposal of the suit.

Once the suit is filed, the branch has to be in constant touch with the advocate and ascertain the developments in the suit from time to time. The branch has to go through the judgment copy and ensure that the suit is decreed, as prayed for. Wherever preliminary decree is obtained, branch has to ensure timely filing of application for final decree. Wherever the decree passed by the court is not to the bank’s satisfaction and there is defendable cause for appeal, alternatives are to be evaluated in consultation with the legal department and appeals are to be preferred at the respective courts within the limitation period. Execution petition has to be filed for execution within decree-limitation period of 12 years to be computed from the date of money decree in recovery suits and from the date of final decree in case of title suits. Vigorous follow-up with the advocate is a must for quick initiation of sale
proceedings. Upon filing application by decree holder, court may order execution by delivery of any property specifically decreed; attachment and sale or by sale without attachment; arrest and detention in prison of the judgment debtor; and appointing a receiver. Executing court will order the attached/mortgaged property to be sold by auction and cause a proclamation of the intended sale. Sales proclamation must be published in the manner directed by the court, viz. distribution of pamphlets, newspaper publication, etc. A sale shall be stopped if the debt and costs are tendered to the officer conducting the sale or paid in the court. Decree holder can also bid for the sale with permission of the court. A sale may be set aside if: (1) judgment debtor deposits the decreed amount and other costs, etc., (2) there has been irregularity/fraud in publishing or conducting sale, and (3) judgment debtor has no saleable interest. Sale proceeds shall be applied towards (a) defraying the sale expenses, (b) discharging the amount under decree; and (c) other encumbrances, if any.

Banks may take recourse to criminal proceedings along with civil suits where misleading information has been furnished by the borrower. In addition, in case of valueless guarantee and diversion of funds, banks should initiate criminal proceedings. In case where the revival/rehabilitation is to be considered, the lenders should retain the right to exercise control over ownership/management. This can be done by pledge of promoter shareholding to the lenders, with the right to change ownership, if certain covenants/stipulation are not met. While many steps have been taken in the recent past in bringing changes to the legal environment to facilitate defective management of NP As, a lot is still desired. Practical issues and legal hurdles in implementation of several right conferred by law to the lenders have reduced the efficacy of these laws. Hence, these legal hurdles must be removed on a priority basis.
In the case of winding up of an insolvent company, same rules as prevailing under the law of insolvency with regard to persons adjudged insolvent are applicable. Nominally, bank, as a secured creditor, “stands outside” the winding-up or insolvency proceedings, relies on its security, and proceeds to realize the security and recover its debts in due course. Leave of court is required to continue a suit filed prior to the company being ordered to be wound up. Similarly, after commencement of winding up, no attachment can be levied against the property of the company, nor any sale of any of the properties or assets of the company can be made without leave of court. Whether the company is in liquidation or not, when the bank either itself appoints a receiver or has a receiver appointed by the court, particulars of such appointment should be filed by the bank with the Registrar of Companies within 30 days thereof.

The ideal course is to stop operations in the account after receiving a notice of winding-up petition and insist upon the company to make an application to the court for an order permitting certain payments. Debtors may voluntarily file bankruptcy, seeking relief from debts, or creditors may file an involuntary petition against a debtor, requesting a settlement. Once a bankruptcy petition is filed, an automatic stay takes effect. This stay restricts the use of virtually all legal remedies that creditors have against a debtor. In particular, a creditor cannot (1) pursue any lawsuit against the debtor that commenced before the bankruptcy,(2) enforce a judgment obtained before bankruptcy, (3) seize possession or exercise control on debtor property regarding a judgment obtained before bankruptcy, (4) take any act to establish, protect, or enforce a lien against the debtor, (5) take any act to collect a claim against a debtor that arose before bankruptcy, or (6) set off any debt owed to a debtor, such as funds on deposit at a bank.
Debt Recovery Tribunal (DRT)

The banks and the financial institutions can file a petition with DRTs. To hasten the recovery process, DRTs were established by Government of India to wide 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 and Debt Recovery Appellate Tribunal. These tribunals have been notified to entertain litigations where the amount of debt due to any bank or financial institutions or their consortium is not less than ₹10 lacs. In all such cases, a bank can file an application in the prescribed format accompanied by prescribed documents and ad-valor filing fee with the tribunal under whose jurisdiction.

- The defendant or any of the defendants at the time of making application, actually and voluntarily resides or carries on business or personally works for gain or
- The cause of action or in part arises.

Upon filing of a petition, the tribunal:

- Shall issue summons requiring the defendants to show cause within 30 days of the service of summons as to why the relief prayed for, should not be granted.
- After giving an opportunity to the parties of being heard, may pass such orders as it thinks fit to meet the ends of justice and shall send a copy of every order passed to the applicant and the defendants.
- May make any interim order by way of injunction or stay against the defendant debarring him for transferring, alienating or otherwise dealing or disposing of any property and assets belonging to him without prior permission of the tribunal.
- Shall issue a certificate under his signature on the basis of the order of the tribunal, to the Recovery Officer for recovery of the amount of debt specified in the certificate.
The Recover Certificate is conclusive and parties cannot dispute or make objection. The Recovery Officer, thereafter, proceeds to recover the amount by way of an attachment and sale of movable or immovable property. He may appoint a Receiver for the management of movable/immovable properties of the defendants. The Recovery Officer is authorized to recover the amount of debt due by 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 due amount.

Any person aggrieved by orders of such tribunal may appeal to the appellate tribunal within 45 days from the date on which the copy of the order is received (Section 20). No appeal, preferred by the debtors, shall be entertained, unless 75 percent of the amount of the debt due from him as determined by the tribunal is deposited in the Appellate Tribunal (Section 21). This condition has been withdrawn w.e.f 18th April 2004. (Supreme Court judgment in M/S Mardia Chemicals Ltd. Etc.) An important power conferred on the tribunal is that of making an interim order against the defendant to debar him from transferring, alienating or otherwise dealing with or disposing of any property or assets belonging to him, without prior permission of the tribunal.

The Government set up a working group (Chairman: Shri S.N. Aggarwal) to review the existing provisions of the above Act and the rules framed there under in the light of suggestions received from various quarters such as banks, FIs, DRTs and individuals as also to examine the adequacy of the infrastructure available to DRTs. The working group suggested certain amendments to the Act and rules framed there under. The Government, acting upon the recommendations, has substantially amended the DRT Act, 2003 to facilitate better administration of the Act including better remedies for the banks.
As on March 31st, 2003, there were 22 DRTs and five Debt Recovery Appellate Tribunals (DRATs). DRTs over a period of time, registered a substantial improvement in the recovery of debts due to banks and financial institutions. The poor recovery through DRTs can be attributed to various issues:

- Lack of infrastructure, manpower etc.
- Lack of banking knowledge
- Challenge to the verdicts of the appellate tribunals in the high court.

**Table 6.1**

NPA Recovery by DRT

(₹ In crores)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of case referred (i)</td>
<td>4028</td>
<td>3728</td>
<td>2004</td>
<td>6019</td>
<td>12872</td>
</tr>
<tr>
<td>Amount involved (ii)</td>
<td>9156</td>
<td>5819</td>
<td>4130</td>
<td>9797</td>
<td>14092</td>
</tr>
<tr>
<td>Amount Recovered (iii)</td>
<td>3463</td>
<td>3020</td>
<td>3348</td>
<td>3133</td>
<td>3930</td>
</tr>
<tr>
<td>(iii) as % of (ii)</td>
<td>37.8</td>
<td>51.9</td>
<td>81.1</td>
<td>32</td>
<td>27.89</td>
</tr>
</tbody>
</table>

Source: Trend & Progress of Banking in India, Various Issues.

**Credit Information Bureau India Ltd. (CIBIL)**

In pursuance to the Central Government Budget proposals, 2000-01, Credit Information Bureau (India) Ltd., (CIBIL) was set up in January 2001 by State Bank of India in collaboration with HDFC Ltd. CIBIL has been set up with an authorized capital of ₹ 50 crore and a paid up capital of ₹ 25 crore, with equity participation of 40 per cent each by SBI and HDFC and two foreign technology partners viz; Mis Dun and Bradstreet Information Services (India) Pvt. Ltd. And Trans Union International Inc., U.S.A. sharing the remaining 20 per cent (Trend and progress in Banking, 2001-2002, PP. 16, 26). The CIBIL was to be technology driven to ensure speedy processing, periodic updating and availability of error-free data at all times in the system. CIBIL’s technical partners have commenced the preliminary work relating to customization of software on the basis of the information furnished by some banks.
Based on the recommendations of the lyer’s Working Group, banks and FIs have been directed under Section 35A of the Banking Regulation Act, 1949 that they should submit the list of suit filed accounts of ₹ 1 crore and above as on March 31, 2002 and quarterly updates thereof till December 2002 and suit filed accounts of willful defaulters of ₹ 25 lacs and above as at end March, June, September and December 2002 to the RBI as well as to CIBIL for a period of one year till March 31, 2003. Thereafter, the aforesaid information should be submitted to CIBIL only and not to the RBI.

Banks and notified FIs would, however, continue to submit the data relating to non suit filed accounts of ₹ 1 crore and above, classified as doubtful and loss, as on March 31 and September 30 and also quarterly list of willful defaulters (₹ 25 lacs and above) where suits have not been filed only to RBI as hitherto. Thus, the statement of non suit filed accounts need not be sent by banks/FIs to CIBIL. There are approximately 98 banks, 22 non banking finance companies in India, as well as large number of co-operative banks and other regional credit grantors all of whom are potential users of CIBIL in the long term. All sectors of the financial industry in India recognize the need for a credit bureau. RBI had issued instruction to banks/FIs to obtain the consent of all the borrowers for dissemination of credit information to enable CIBIL to compile and disseminate credit information. The RBI accords highest priority to the development of an efficient CIBIL and would be closely monitoring the progress in this regard.

**Lok Adalat**

These are voluntary agencies created by the state government to assist in matters of loan compromise. Lok Adalats meet at different places for the convenience of banks and borrowers on a given date where both the bankers and the borrowers should be present. After looking into the evidence and listening to both parties, the Lok Adalat works out an acceptable compromise.
Thereafter, Lok Adalat issues a recovery certificate, which will enable the bank in obtaining decree from the concerned court. This arrangement shortens the period in obtaining decree from the concerned court, which would otherwise, normally, be awarded after a much longer period. In view of this unique advantage, the government is thinking of strengthening them and raising the monetary limit set for referred cases. Along with this, efforts should be made to give wide publicity to the scheme. Besides educating both banks and borrowers on Lok Adalats. Lok Adalat has proved an effective institution for settlement of dues in respect of smaller loans and the following guidelines were issued to banks and FIs:

- Ceiling of amount for coverage under Lok Adalats would be ₹ 10 lacs and above.
- The scheme may include both suit filed and non-suit filed accounts in the doubtful and loss category.
- The settlement formula must be flexible.

### Table 6.2

NPA Recovery by Lok Adalat

(₹ In crores)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of case referred (i)</td>
<td>160363</td>
<td>186535</td>
<td>548308</td>
<td>778833</td>
<td>616018</td>
</tr>
<tr>
<td>Amount involved (ii)</td>
<td>758</td>
<td>2142</td>
<td>4023</td>
<td>7235</td>
<td>5254</td>
</tr>
<tr>
<td>Amount Recovered (iii)</td>
<td>106</td>
<td>176</td>
<td>96</td>
<td>112</td>
<td>151</td>
</tr>
<tr>
<td>(iii) as % of (ii)</td>
<td>14</td>
<td>8.2</td>
<td>2.4</td>
<td>1.55</td>
<td>2.89</td>
</tr>
</tbody>
</table>

Source: Trend & Progress of Banking in India, Various Issues.
Corporate Debt Restructuring (CDR)

Despite their best efforts and intentions, sometimes corporate find themselves in financial difficulty because of factors, both internal and external, beyond their control. For the revival of the corporate as well as for the safety of the money lent by the banks and FIs, timely support through restructuring, in genuine cases, is called for. However, delay in agreement amongst different lending institutions often comes in the way of such endeavors.

Based on the experience in the other countries like the U.K, Thailand, Korea, etc., a Corporate Debt Restructuring System has been evolved (Reserve Bank of India, Trend and progress in Banking 2001-2002, P.7). A three tier CDR system was introduced on August 25, 2001 with the objective of ensuring timely and transparent mechanism for restructuring of the corporate debts of viable entities facing problems, outside the purview of BIFR, DRT and other legal proceedings, for the benefits of all concerned. In particular, the framework will aim at preserving viable corporate that are affected by certain internal and external factors and minimize the losses to the creditors and other stakeholders through an orderly and coordinated restructuring programme. This is applicable to only multiple banking/syndicate/consortium accounts, in the standard and sub-standard categories, with an outstanding exposure of ₹ 20 crore and above with banks and FIs. FIs should disclose the accounts restructured under this system, the standard, and sub-standard categories as also in aggregate, separately in the annual reports under “notes to accounts.” CDR system in the country will have a three-tier structure viz. CDR Standing Forum, CDR Empowered Group, CDR Cell.
CDR Standing Forum

The CDR Standing Forum would be the representative general body of all financial institutions and banks that participate in CDR system. CDR standing forum will be a self empowered body which will lay down policies and guidelines, guide and monitor the progress of corporate debt restructuring. The forum will also provide an official platform for both the creditors and borrowers (by consultation) to amicably and collectively evolve policies and guidelines for working out debt restructuring plans. The CDR standing forum shall meet at least once every six months and would review and monitor the progress of corporate debt restructuring system. The forum would also lay down the policies and guidelines to be followed by the CDR Empowered Group and CDR Cell for debt restructuring and would ensure their smooth functioning and adherence to the prescribed time schedules for debt restructuring. It can also review any individual decisions of the CDR Empowered Group and CDR Cell. The CDR standing forum, the CDR empowered group and CDR cell (described in following paragraphs) shall be housed in IDBI. All financial institutions and banks shall share the administrative and other costs on a sharing pattern, as determined by the standing forum.

CDR Empowered Group

The individual cases of corporate debt restructuring shall be decided by the CDR Empowered group, consisting of ED level representatives of IDBI, ICICI Limited and SBI as standing members, in addition to ED level representatives of financial institutions and banks who have an exposure to the concerned company. The empowered group will consider the preliminary report of all cases of request of restructuring, submitted to it by the CDR Cell and decide that restructuring of the company is prima-facie feasible and the enterprise is potentially viable in terms of the policies and guidelines evolved by standing forum. The CDR empowered group would be mandated to look
into each case of debt restructuring, examine the viability and rehabilitation potential of the company and approve the restructuring package within a specified time frame of 90 days, or at best 180 days of reference to the empowered group. The decisions of the CDR empowered group is final and action reference point. If restructuring of debts was found viable, feasible, and accepted by the empowered group, the company would be put on the restructuring mode. If, however, restructuring were not found viable, the creditors would then be free to take necessary steps for immediate recovery of dues and/or liquidation or winding up of the company, collectively or individually.

CDR Cell

The CDR standing forum and the CDR empowered group is to be assisted by a CDR cell in all their functions. The CDR cell will make the initial scrutiny of the proposals received from borrowers/lenders, by calling for proposed rehabilitation plan and other information and put up the matter before the CDR empowered group, within one month to decide whether rehabilitation is prima facie feasible. Once the CDR empowered cell agrees that restructuring is prima facie feasible the CDR cell proceeds to prepare detailed rehabilitation plan with the help of lenders and if necessary, outside experts. All references for corporate debt restructuring by lenders or borrowers are to be made to the CDR cell. It is the responsibility of the lead institution/major stakeholder to the corporate, to work out a preliminary restructuring plan in consultation with other stakeholders and submit to the CDR cell within one month. The CDR cell prepares the restructuring plan in terms of the general policies and guidelines approved by the CDR standing forum and place for the consideration of the empowered group within 30 days for decision. The empowered group can approve or suggest modifications but a final decision must be taken within a total period of 90 days, which, for sufficient reasons, can be extended, maximum up to 180 days from the date from the date of reference.
Other Features

- CDR is a non-statutory mechanism.
- CDR mechanism is a voluntary system based on debtors-creditors agreement and inter-creditor agreement.
- The scheme is not to be applied to the accounts involving only one financial institutions or one bank. The CDR mechanism cover only multiple banking accounts/syndication/consortium accounts with outstanding exposure of ₹ 20 crore and above by banks and institutions.
- The CDR system is applicable to standard, sub-standard, and doubtful accounts.

However, as an interim measures, permission for corporate debt restructuring can be made available by RBI on the basis of specific recommendation of CDR “Core Group”, if a minimum of 75 per cent (by value) of the lenders constituting banks and FIs consent for CDR, irrespective of differences in asset classification status in banks/financial institutions. There is no requirement of the account/company being sick, NPA, or being in default for a specified period before reference to the CDR Group. However, potentially viable cases of NPAs will get priority. This approach provides the necessary flexibility and facilitates timely intervention for debt restructuring. Prescribing any milestone(s) is not necessary, since the debt restructuring exercise is being triggered by banking and financial institutions or with their consent. In no case, the requests of any corporate indulging in willful default or misfeasance will be considered for restructuring under CDR.

- Reference to Corporate Debt Restructuring System could be triggered by (i) any or more of the secured creditor who have minimum 20 per cent share in either working capital or term finance, or (ii) by the concerned corporate, if supported by a bank of financial institution having stake as in (i) above.
The Debtor-Creditor Agreement (DCA) and the Inter-creditor Agreement (ICA) provide the legal basis to the CDR mechanism. The debtors have to accede to the DCA, either at the time of original loan documentation (for future cases) or at the time of reference to Corporate Debt Restructuring Cell. Similarly, all participants in the CDR mechanism, through their membership of the Standing Forum, have to enter into a legally binding agreement, with necessary enforcement and penal clauses, to operate the system through laid down policies and guidelines. One of the most important elements of DCA is the standstill agreement binding for 90 days, or 180 days by both sides. Under this clause, both the debtor and creditors agrees to a legally including stand still whereby both the parties commit themselves not to taking resources to any other legal action during the “stand-still” period. This is necessary for enabling the CDR System to undertake the necessary debt restructuring exercise without any outside intervention, judicial or otherwise. The ICA is a legally binding agreement amongst the secured creditors, with necessary enforcement and penal clauses, wherein the creditors commit to abide by the various elements of CDR system. Further, the creditors agree that if 75 per cent of secured creditors by value, agree to a debt restructuring package, the same would be binding on the remaining secured creditors.

The CDR mechanism is being stabilized. Certain revisions are envisaged with respect to the eligibility criteria (amount of borrowings) and time frame for restructuring. The foreign banks are not members of CDR forum, though they attend meetings and it is expected that they would be signing the agreement shortly. The first ARC to be operational in India- Asset Reconstruction Company of India (ARCIL) 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, the RBI guidelines recommend involvement of independent consultants, banks are so far restore to their internal teams for restructuring programs.
Company Mergers

Under The Companies Act, 1956, mergers are permitted in 1977, section 72-A was inserted in the Income Tax Act to offer tax incentives to healthy companies, which take over the sick companies and prepare revival plans. Response to this scheme has been limited because of delays in completing formalities laid down by the High Court and the Income Tax Department. Tax incentives are found to be inadequate to motivate healthy companies to come forward and take advantage of the scheme. Recovery of bank dues on company-mergers is not assured since hardly 7-8 percent of sick companies are successfully revived. Encouraged by the success achieved in company mergers in developed countries, a review of the scheme under section 72A of the Income Tax Act is called for.

In view of the global phenomenon of consolidation and convergence, the report of the committee on the banking sector reforms had suggested mergers among strong banks, both in public and private sector and even of banks with financial institutions and NBFCs. The phenomenon of mergers in banking sectors is relatively recent one in India. There was one merger in early nineties i.e. New Bank of India with Punjab National Bank. However, there has been a spate of mergers in recent past, viz. 20th Century finance with Centurion Bank, Times Bank with HDFC Bank, Bank of Madura with ICICI Bank, Bareilly Corporation Bank with Bank of Baroda and Sikkim Bank with Union Bank of India and most recently Global Trust Bank with Oriental Bank of Commerce.

National Company Law Tribunal (NCLT)

As per the announcement made in the Budget 2001-02, Sick Industrial Companies Act (SICA) will be repealed and Board for Industrial Finance and Reconstruction (BIFR) will be wound-up. As an alternative arrangement, it is proposed to set up NCLT by amending the Companies Act, 1956. NCLT is expected to consolidate the powers of BIFR, High Court and Company Law
Board to avoid multiplicity of forums. In matters of rehabilitation of sick units, all concerned parties are supposed to abide, by the order of NCLT. There shall be 10 benches, which will deal with rehabilitation, reconstruction, and winding up of companies. It is estimated to complete the entire process during a period of 2-3 years as against 10-12 years taken presently. The tribunal will have addition powers of contempt of court.

A rehabilitation and revival fund will be constituted to make interim payment of dues to workers of a company declared sick or under liquidation, for protection of assets of sick company and to rehabilitate sick companies. While NCLT will be acting on the lines of BIFR in the matter of rehabilitation, viability of the projects will be assessed on ‘cash test’ and not the present ‘net worth’ test. Another important change will be in respect of time limit for completing each formality relating to rehabilitation and Winding up. Though the bill is well drafted to ensure NCLT to become, time wise, more effective than BIFR in respect of rehabilitation, and winding up, doubts are raised about the implementation of the bill taking into account the present political set-up.


Only recourse available with banks and financial institutions (FIs) to recover their non-performing assets, before the enactment of this Act, was by way of filing cases against the borrower in the DRTs or civil courts. Banks followed up their cases hoping that the DRT/Civil courts rules in their favour delivering the locked up dues to them. Unfortunately, the judicial process is often a lengthy one, with the result that the DRTs/courts have not been able to match the high expectations of the banking sector to recover their huge burden of NPA. All the 29 DRTs in the country combined have been able to recover, in the 7 years of their existence, only about 10 percent of the total dues. The SARFAESI Act (Annexure1) empowers banks and financial
institutions (FIs) to directly enforce the security interest, pledged to them at the time of sanctioning the loan without having to go through the judicial process. Further, the option of approaching the DRT always remain open to the Banks/ FIs, which they can exercise at any time. In addition, the pending cases will continue with the DRTs and will be disposed only after the bank informs the DRT that it has recovered the NPA on its own. In this way the banks/FIs have double recourse for recovering their NPAs.

The process of enforcement of the securities can be done either by the banks/FIs themselves, or through Securitisation Companies or Asset Reconstruction Companies, specialized agencies that will be created and registered under the provisions of this Act. The bank now has the right to directly sell the financial assets (that it is holding as security against defaulting loan accounts classified as NPA), to these newly formed companies. These companies will pay the bank’s dues usually in the form of bonds or debentures. After acquisition from the bank, it is up to the Securitization Company or Asset Reconstruction Company to recover the asset from the borrower and then either further sell off/auction off the assets; or in case of the asset being a business, try to revive it, i.e., reconstruct the asset.

Table 6.3
NPA Recovery by SARFAESI

(₹ In crores)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of case referred (i)</td>
<td>60178</td>
<td>83942</td>
<td>61670</td>
<td>78366</td>
<td>118642</td>
</tr>
<tr>
<td>Amount involved (ii)</td>
<td>9058</td>
<td>7263</td>
<td>12067</td>
<td>14249</td>
<td>30604</td>
</tr>
<tr>
<td>Amount Recovered (iii)</td>
<td>3749</td>
<td>4429</td>
<td>3982</td>
<td>4269</td>
<td>11561</td>
</tr>
<tr>
<td>(iii) as % of (ii)</td>
<td>41.4</td>
<td>61</td>
<td>33</td>
<td>30</td>
<td>37.78</td>
</tr>
</tbody>
</table>

Source: Trend & Progress of Banking in India, Various Issues.
This Act may be quite useful for the banks/FIs. The banks/FIs have initiated the process of recovery of their dues under this Act soon after the commencement of the same, which shows their anxiety to recover their NPAs. The Act has recognised the urgency of framing legislation empowering the banks/FIs whose hands had been tied until now, to unlock their NPAs on their own. There are hopes that this empowerment will go a long way in bringing back into circulation the massive amount of locked up funds in the form of NPAs. It also opens up a completely new area of private enterprise in the form of the Securitisation Companies or Asset Reconstruction Companies. The Act will lead to the reconstruction of hitherto decaying financial Assets a large number of which are sick industrial units, which will give a great boost to the overall health of the economy. In spite of many good objects and merits, the Act has some of concern, which needs to be addressed by the government.

Circumvention of the Judicial Process

Any legislation that empowers one party to a dispute (in this case, the creditor) to take action without due judicial process against the other Party (in this case, the borrower) has an inbuilt potential for misuse. In their eagerness to recover their NPAs, the banks/FIs or Securitisation Companies/Asset Reconstruction Companies may violate the inalienable fundamental rights of the borrowers, which may lead to unnecessary litigation. Though the borrowers have the right to approach the DRTs in case of grievances, (but the same will not cause delay in actual recovery of Dues), since the Act allows the banks and Securitisation companies/asset reconstruction Company to initiate action, it amounts to post corrective action.

Double-Protection to the Creditor

Empowerment to the banks to act on their own to recover their dues out of court and simultaneously through the judicial process, amounts to ‘Double-protection’ of the creditor and leaves the borrower with almost no
remedy except to challenge the action in court, which seems to be unreasonable. Moreover, during the pendency of the claim in DRT, the enforcement of security under this Act appears to be an act of double enforcement against a single claim. In case of enforcement of claim of banks/FIs through DRT/Civil court, against the charged/Mortgaged Properties, the DRT/civil court first examines and decides the legality and validity of the charge/mortgage. DRTs, then passes an order for the recovery of dues, whereas, in case of enforcement of their claim by the banks/FIs under this Act, the validity/legality of the charge/mortgage is not examined nor they are empowered to do so, meaning thereby, in the rare case of defective charge or mortgage too, the recovery shall take place.

The Act provides in case of any dispute between the creditor and the securitisation company/reconstruction company the matter shall be resolved by way of arbitration, under the provisions of Indian Arbitration Act, which is again a time consuming process and as such the recovery of dues will be unduly delayed. The recovery through Securitisation company /Asset-reconstruction company involves extra expenditure, which the Acts stipulates to be an additional burden on the borrower, whereas, by way of recovery through DRTs/civil courts, this expenditure can be saved. Moreover, in case of recovery through DRT/civil court the amount of expenses, other than the claim amount, is decided by the DRT/civil court as cost of the suit, whereas in case of recovery under this Act, the cost shall be decided by banks/FIs/securitization company/reconstruction company themselves, which may be on the higher side/unreasonable. In case of enforcement of claim in consortium advances, the creditors can enforce only with the consent of the other creditors having minimum 75 percent share in the loan whereas, enforcement of claim through DRT/civil Court can be intitated by a single creditor by impleading the other creditors as respondents in the case. The act also provides that the Securitisation company may acquire financial assets of
Management of Non Performing Assets: Remedial Measures

Banks/FIs by issuing a debenture or bond, thus the actual recovery of dues will not take effect immediately.

Impractical Stipulations

Lastly even if all the Provisions of the Act are accepted as the need of the hour (and as having enough checks on misuse in the form of the DRTs and DRATs), the stipulation to take help from the district administrative machinery i.e. the Chief metropolitan Magistrate or the District Magistrate for enforcement of security interest is to be questioned for its practicality, considering that our district administrative machinery is unable to provide assistance even to the existing DRTs for their recovery work. CRISIL, which has analyzed the provisions of the new act in detail, estimate their impact on the banking system. They observed that the effectiveness of the new Act in tackling the banking system’s NPA problem is marred by some significant exclusion. (IBA Bulletin, August 2003, PP 16-18) There are:

- Only secured assets brought within the ambit, so it shall be of no assistance to unsecured lenders. According to the (RBI) statistics for scheduled commercial banks, about 13.5 percent of the total advances in the banking system in the years 2002 was unsecured. In such cases, banks would have to resort to the conventional recovery process through the judicial system and debt recovery tribunals (DRT).
- For advances secured by agricultural land (collateral) cannot be enforced. About 11 percent of the total NPAs in the banking system have agricultural land as collateral. Banks have also not been allowed to enforce aircrafts or shipping vessels. However, these form an insignificant proportion of the NPAs and hence, shall only have a marginal impact on the banks’ ability to recover their loans.
- Loans below ₹ 1,00,000 have also been kept outside purview. The study indicates that about 18 percent of NPAs are below ₹ 1,00,000. Hence, these NPAs will not come within the ambit of the Act (and
DRT) and banks will have to resort to traditional measures of recovery in such cases.

The above exclusions imply that over 42 percent of the bad debts shall remain outside the ambit of the foreclosure laws, though there could be some overlap between these segments. In particular, loans below ₹ 100,000 may fall in both agricultural and unsecured loans segments. This would partly be offset, by the fact that there is certain other exclusion the analysis such as cases in which the amount due is less than 20 percent of the principal and interest thereon. Assuming that one third of loans below RS, 100,000 overlap with these segments, it is estimated that about 36.4 percent of the NPAs shall remain outside the jurisdiction of the Act.

**Asset Reconstruction Company (ARC)**

An Asset Reconstruction Company (ARC) specializes in recovery and liquidation of assets. The NPAs can be assigned to ARC by banks at a discounted price. The ARC has the objective of floating bonds and making the recovery from the borrowers directly. This engenders a one-time clearing of the balance sheets of the banks of sticky loans. ARCs can have several alternate structures. They can either be publicly or privately owned or a combination of both, and can be either separately capitalized units or wholly owned subsidiaries. In several countries, including Czech Republic (1995), Sweden (1992) and Thailand (1998), the troubled bank was split into a ‘good’ bank and a ‘bad’ bank (RBI Annual Report 2001-2002, P 165). This approach is probably best when only one or a few banks are in serious difficulty. In Hungary, bad banks issued bonds guaranteed by the government, which were not established as separate entities but many banks were required to establish a special organizational section for the management of impaired loans. However, when such an approach is followed, it is important that the ‘bad’ banks do not end up with the ‘bad’ assets. The alternate approach used in the
Unites States (1989) during the savings and loan crisis and more recently in Korea (1997) and Malaysia (1998), has been to establish a single asset management corporation to purchase NPLs from a number of banks, forming one large ‘bad’ bank for the whole banking industry. In case a large number of banks are in difficulty and the assets acquired have a certain degree of homogeneity, a single entity may reap economies of scale and make best use of scarce managerial talent.

Other countries have tried variants of both types of approaches. Japan, for instance, established a type of private sector AMC, the Japanese Cooperative Credit Purchasing Company, to which the NPLs of banks were sold, while providing the banks with some tax benefits. In view of its limited success, the Japanese government launched a new scheme in November 1998 under which a troubled bank would be taken under government control after a report from the inspection agency. The NPLs of these, ‘bridge banks’ are to be transferred to the Resolution and Collection Organisation, funded by the Deposit Insurance Corporation.

In the Indian context, the Committee on the Financial System (Chairman: Shri M. Narasimham) (1991) had recommended the setting up of an Asset Reconstruction Fund (ARF). A number of concerns were expressed. First, it was felt that a centralized all-India fund would be severely handicapped in its recovery efforts by lack of widespread geographical reach which individual banks possess. Secondly, there could be a moral hazard problem, and banks could become complacent about recovery and even the health accounts could become sick, in course of time. Thirdly, given the large fiscal deficits, there would be a problem of financing the ARF. Subsequently, the Committee on Banking Sector Reforms (Chairman: Shri M. Narasimham) in 1998 recommended transfer of sticky assets of banks to an ARC. Thereafter, the Committee on Restructuring Weak Public Sector Banks
Management of Non Performing Assets: Remedial Measures (Chairman: Shri M.S. Verma) also viewed the separation of NP As and its transfer thereof to an ARF as an important element in a comprehensive restructuring strategy for the weak banks. In recognition of the same, the Union Budget, 2003-03, proposed setting up of a pilot ARC. In a recent country report on India, the International Monetary Fund laid out a series of recommendations on how an effective ARC could be set up in the country.

- The laws need to be in place: ARCs must have sufficient legal powers to recover assets and dispose of them without going through the courts. To put pressure on borrowers to co-operate with the ARC, the sick Industrial Companies Act and the Board for Industrial and Financial Restructuring Act have to be repealed. The ARC will not be effective without these legal reforms.

- There is conflict of interest of banks and financial institutions own the ARC as bank and institutions will be the ARC’s shareholders and customers. As shareholders, they have an interest in its financial performance. As sellers of bad loans, on the other hand, they would want the highest price, which would affect the ARC’s profitability. The ARC should have operational independence.

- Banks should recognize hidden losses: The bad loans are worth a lot less than what banks have recognized on their balance sheet. Thus, if banks transfer their bad debts at market prices, they will have to take further losses. The government should try and quantify these losses and work out a plan to recapitalize banks.

- Resolving the problems of bad loans has to include a strategy for restructuring companies. The success in restructuring of companies depends on a range of other issues viz. bankruptcy law, labour laws and competition policies, among others. Therefore, it requires a range of reforms in other areas.
While the setting up of the ARC is useful, it would be naïve to expect that it will completely solve India’s bad loans problem. ARCs with statutory and regulatory powers are likely to emerge as nodal resolution agencies coexisting with CDR mechanism. In absence of direct funding support by the Government, ARCs would be self-help mechanism for the banking system. The onus now is with the banks FIs and ARCs to clean up the NPAs. The banks FIs have to be proactive in making realistic provisions based on assessment of realization from NP As towards their dues. These practices will also enable banks FIs to move to internationally acceptable norms. ARCs can add value by cutting short the time of resolution as well as maximizing recoveries, possible through debt aggregation and focused approach to resolution.

Though a lot more needs to be done, the initial response to ARCIL has been encouraging. ARCIL has raised capital of ₹100 crore from the banking system by acquiring large as well as small accounts on portfolio basis. In one year of its existence, ARCIL has acquired 189 assets with total dues of ₹9600 crore from 16 banks. Of these, 121 accounts are small cases and 68 accounts are medium to large cases. ARCIL has commenced implementation of resolution strategy in respect of these accounts.

6.4 NPA Management Policy in Selected Banks

In terms of RBI guidelines each bank should have a loan Recovery Policy, setting down the manners of recovery to reduce the NPA level of the bank as per target. It is very important for a Bank’s profitability that all loan assets of the bank be brought up to standard assets as far as possible, in order to have a quantitative up gradation of credit portfolio. Thus, non performing assets are brought down to the maximum possible by recovering over-dues expeditiously. With this object, the selected banks have also declared their Loan Recovery Policy.
Accordingly, each bank evolves recovery policy for non-performing assets setting out the thrust areas and broad parameters with targeted levels of reductions which changes from year to year while the basic framework remains same.

**Basic Framework**

The basic framework of loan recovery is more or less similar in all the selected banks. This is as follows:

**Compromise settlement** It should ensure to recover its dues to the maximum possible at minimum expense. All compromise proposals to the next higher authority of post facto scrutiny. In settlement cases, it is important that the bank could promptly recycle the funds with advantage, instead of resorting to expensive recovery proceedings spread over a longer period of time.

**Identification of Defaulter** Proper distinction needs to be made between willful defaulters and non willful defaulters i.e. defaulting due to circumstances beyond their control.

**Realizable value of security** Where security is available for assessing the realizable value, proper weight age has to be given to the location, condition and marketable title and possession thereof.

**Staff Accountability** Where staff accountability has not been examined, it should be ensured that the same is completed expeditiously within a time frame.

**Recovery at Different Levels** Special Cells to be set up at all regional/zonal levels. Recovery officers be appointed at branches having sizeable NPAs and their recovery progress monitored on monthly basis.
Adequate Attention should be paid to upgrade Sub-Standard Assets

It is to be ensured by the top management that there is no significant deviation from the general principles of compromise or write-offs.

The basic framework is similar, the approach with respect to NPA management policy is same in all the selected banks. Reduction in NPAs can be achieved by equally important measures given as below.

Up gradation of Asset: To upgrade an asset, need based replacement of reschedulement and rehabilitation of eligible account should be done expeditiously. Interest and installment are to be recovered on due date. All standard assets should be constantly reviewed and follow up. Quick remedial measures be taken wherever required to prevent accounts becoming NPA. Constant touch with borrower and regular stock inspection should be done.

Write-off loss Assets, where full provision is to be made and prospects of recovery are zero, should be written off. Advances under schematic lending having no recovery prospects in near future of security are either very meager or realization from it in near future are not for seen and initiation of legal action has started. Partial sprite off is permitted in respect of doubtful asset accounts for financial years 2001-02 and 2002-03.

Compromise settlements and other: All compromise proposals clearly spell out the basis on which the negotiated amount of settlement has been arrived at and comparative advantages of having the compromise including the present value of funds to be received.
6.5 Initiatives Taken for Asset Quality by Selected Banks

State Bank of India (SBI)

- Bank has started the Dynamic Credit rating review of borrowal accounts to capture deterioration in credit quality promptly and to initiate corrective action and facilitate correct pricing of risk.

- An Early Warning Control System (EWCS) is being put in place to put in place a system driven, parameterized, quantified, trigger based monitoring system of credit exposures.

- Your bank has developed behavior model for monitoring and scoring the retail borrower performance. The coverage of behavior model is gradually being expanded to cover entire retail related baskets of products.

- Coverage of Loan Originating System/Loan Lifecycle Management system (LOS/LLMS) is being steadily augmented to cover the entire credit portfolio.

- In order to focus on capital conservation and maximisation of return on capital, SBI bank has introduced Risk Based Budgeting (RBB). As a measure to quantify the reduction in risk we will be introducing levers to assess improvement periodically, based on Credit Risk Weighted Assets (CRWAs). Achievement of the budgeted advances levels will be subject to achievements under the specified levers.

- Credit Risk Management Department studies 37 industries covering sectors, such as Telecom, Power, Coal, Aviation, NBFC, Textile, Iron and Steel covering approximately 85% of the Banks’ credit exposures. The detailed study covers market factors, potential and Portfolio Quality Index (PQI) based on which Industry-wise limits are set for taking bank-wide exposures.

- The Bank is implementing the Risk Adjusted Return on Capital (RAROC) framework in FY 2015-16.
Models for estimation of Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD) have been developed internally. The Bank has procured Credit Risk Management System (CRMS) for computation of IRB capital.

Punjab National Bank (PNB)

The accumulation of stressed assets remained the concern for the Bank. The Bank initiated various measures to arrest the incremental deliquencies and fresh slippages to improve the quality of assets. In all NPAs, account-specific resolution strategies were implemented and progress was monitored regularly.

A new system driven Preventive Monitoring System (Early Warning) was operationalised in the Bank w.e.f. July 2014 for better monitoring of borrowers’ financial health and taking timely action for reduction/containment of NPAs.

Daily progress of recovery in NPAs (outstanding ₹ 10 lacs and above) was monitored and placed before Top Management. Further, compromise/negotiated settlements through one to one meeting with borrowers was adopted as another vital strategy to tackle NPAs. The Bank also had 17 Asset Recovery Management Branches (ARMBs) and 20 Special Asset Recovery Cells (SARCs) which function exclusively for resolving NPAs.

The Debt Recovery Tribunal Cases Monitoring System Version 1.1 was one such endeavor that was ahead of its times and a pro-active step towards resolution of NPAs. In order to monitor progress of the cases that were filed in DRT, and made branches and counsel/advocates proactive for follow-up of such cases, an easy and hassle free Online Portal was introduced. The very purpose of the Portal was to take legal processes to their logical end and to make
available up-to-date information about each and every case that has been filed in DRT.

- Another pro-active initiative of Punjab National Bank, was streamlining the entire process of various steps followed in undertaking SARFAESI Action. Details of all the NPA Accounts eligible for initiating SARFAESI Action were entered in the Portal by the branches which can be accessed by the Circle Offices, FGM Offices and Head Office for monitoring purposes. Branches could also generate reports of accounts where a particular action was pending. All the details relating to progress of SARFAESI Action, particular account is just a click away like 13 (2) Notice Issue, 13 (4) Notice Issue, Possession of IPs, Reserve Price Fixation and conduct of E-Auction. Circles and FGMOs could follow-up with the branches in case of delays.

- During FY’15, in 5539 Rin Mukti Shivirs, cash recovery of ₹ 269 crore was made in 64393 accounts and 27355 accounts were upgraded with balance outstanding of ₹ 388 crore. Thus, NPAs aggregating ₹ 656 crore were resolved in these shivirs.

- One Time Settlement (OTS) was marketed as a product for faster resolution of NPAs and OTS cases in 55,320 accounts were approved.

- Due to the above highlighted initiatives, the Bank recovered ₹ 3143 crore in freshly slipped accounts.

- Accounts with aggregate outstanding of ₹ 999.62 crore were upgraded to standard category. Total cash recoveries in NPA accounts amounted to ₹ 2925 crore. Through well defined recovery policy ₹ 655 crore were recovered in approved OTS cases through negotiated settlements. During FY’15, the Bank recovered ₹ 1017 crore in the accounts written off earlier.
HDFC Bank

The asset quality of the Indian banking industry came under pressure from broader macroeconomic factors as well as issues specific to certain sectors in the economy.

- To manage credit risk, the Bank has a comprehensive centralized risk management function, independent from the operations and business units of the Bank. Distinct policies, processes and systems are in place for the retail and wholesale businesses. In the retail loan businesses, the credit cycle is managed through appropriate front-end credit, operational and collection processes. For wholesale credit exposures, management of credit risk is done through target market definition, appropriate credit approval processes, ongoing post-disbursement monitoring and remedial management procedures. Overall portfolio diversification, prudential ceilings, security structures and periodic as well as proactive reviews facilitate risk mitigation and management.

- The banking industry on an overall basis saw an increase in debt restructuring and non-performing assets, besides corrective actions under RBI’s Framework for Revitalising Distressed Assets in the Economy, which became fully effective from 1st April 2014. HDFC Bank, in these challenging times, has been able to maintain asset quality of a high standard and contain the level of delinquencies. Bank believes in highest standards of governance in recognition and reporting of delinquent and restructured accounts.

- The Bank has comprehensive credit risk management architecture. The Board of Directors of the Bank endorses the credit risk strategy and approves the credit risk policies of the Bank. This is done taking into consideration the Bank’s risk appetite, derived from perceived risks in the business, balanced by the targeted profitability level for the risks taken up. The Board oversees the credit risk management functions of the Bank.
• The Risk Policy & Monitoring Committee (‘RPMC’), which is a committee of the Board, guides the development of policies, procedures and systems for managing credit risk, towards implementing the credit risk strategy of the Bank. The RPMC ensures that these are adequate and appropriate to changing business conditions, the structure and needs of the Bank and the risk appetite of the Bank. The RPMC periodically reviews the Bank’s portfolio composition and the status of impaired assets.

ICICI Bank

The ICICI Bank’s risk management framework is based on a clear understanding of various risks, disciplined risk assessment and measurement procedures and continuous monitoring. The policies and procedures established for this purpose are continuously benchmarked with international best practices. The Board of Directors has oversight on all the risks assumed by the Bank. Specific Committees have been constituted to facilitate focused oversight of various risks as follows:

• The Risk Committee of the Board reviews risk management policies of the Bank pertaining to credit, market, liquidity, operational, outsourcing and reputation risks and business continuity management.

• The Committee also reviews the Risk Appetite & Enterprise Risk Management frameworks, Internal Capital Adequacy Assessment Process (ICAAP) and stress testing. The stress testing framework includes a wide range of Bank-specific and market (systemic) scenarios. The ICAAP exercise covers the domestic and overseas operations of the Bank, banking subsidiaries and material nonbanking subsidiaries.

• The Committee reviews migration to the advanced approaches under Basel II and implementation of Basel III, risk return profile of the Bank, compliance with RBI guidelines pertaining to credit, market and
• The Committee reviews the level and direction of major risks pertaining to credit, market, liquidity, operational, compliance, group, management and capital at risk as part of risk profile templates. In addition, the Committee has oversight on risks of subsidiaries covered under the Group Risk Management Framework. The Risk Committee also reviews the Liquidity Contingency Plan for the Bank and the threshold limits.

• The Credit Committee of the Board, apart from sanctioning credit proposals based on the Bank’s credit authorisation framework, reviews developments in key industrial sectors and the Bank’s exposure to these sectors as well as to large borrower accounts and borrower groups. The Credit Committee also reviews the major credit portfolios, non-performing loans, accounts under watch, over dues and incremental sanctions.