CHAPTER VI

RECOVERY OF BANK'S LOAN

Introduction

Since the nationalisation of commercial banks, public sector banks have been rendering Yeoman's service to the nation by lending to the various sectors of the national economy. The shift from class banking to mass banking has changed the facet of the banking industry. The public sector banks have shouldered the additional responsibility entrusted to them by lending of borrowers, both small and big, coming under the various preferred sectors of the national economy. One of the main factors which seriously affects the profitability of the banks is the problem of recovery of advances. Needless to say, once the borrower has availed of loans and advances, a number of extraneous factors with all the cumulative effects will start influencing the use of the loans and conduct of the loan account.

Recovery is a recurring worry for banks. Recycling of advances is important, without which the bank's liquidity is in jeopardy. Besides that the community does not get benefits unless new advances and new borrowers are encouraged. Banking industry has witnessed a phenomenal growth in the last decades. There is always a constant and consistent need to maintain 'Growth rate' from year to year in advances besides maintaining 'share' with other banks. Impact of advances is not created without this growth and recycling. Recycling is affected by poor recovery of advances, which is once again the result of variety of reasons like:
(a) Inadequate project appraisal
(b) Financing through intermediaries
(c) Improper borrower selection
(d) Political interference and pressures
(e) Failure to finance at the right time and at right quantum
(f) Inadequate manpower

Bank Manager's position is really precarious as he has to manage with hundred and thousands of borrowal accounts. Dealing with a large number of accounts requires altogether a different type of strategy. All these may destroy the very enthusiasm and initiative of the bank manager.

Advances are repayable on demand (in case of overdrafts) or repayable after a specified period or by instalments (in case of loans) or on maturity (in respect of bills). Irregularity in payment of instalment or interest is deemed to be default. Before tackling the default, the nature of default may be considered. Defaults occur on account of:

1. **Ignorance** : This has to be tackled by constant and frequent reminders and counselling the borrowers as friend, philosopher and guide.

2. **Genuine Difficulties** : These are due to external factors which are beyond the scope and powers of borrowers.

3. **Mismanagement** : Internal factors like extravagance, financial indiscipline, overspending and living habits beyond one's means etc.

4. **Intentional** : Deliberate actions to defraud the bank. This constitutes a threat to bank.
Perhaps no other concept has become more familiar and significant in to-day's banking scenario as increasing overdues in banks due to non-recovery or poor recovery of advances. The volume of overdues is inversely related to bank's profitability. So strategies should be chalked out to reduce the quantities of outstanding in overdues by way of good recovery. The parameters of a branch manager's performance has at once been shifted from mere mobilisation of deposits or giving credit to the other important area of recovery. Recovery management has rightly assumed cardinal importance in to-days's banking due to the following reasons:

Banks can deploy only 56.5% of the freshly mobilised deposit in loans and advances as they are required to provide for statutory requirements like SLR (Statutory Liquidity Ratio) and CRR (Cash Reserve Ratio). As against this bank can lend out cent per cent of the amount recovered from borrowers. This advantage of recovered fund over fresh fund further consolidates if the priority sector lending commitment of 40% is taken into account.

Recommendations of the Narashimham Committee

Reserve Bank of India appointed the Committee on Financial System constituted under the chairmanship of Sri M. Narashimham. The committee made several recommendations pertaining to financial system. One of the recommendations of the committee on the system is the introduction of a proper system of recognition of income, classification of assets and provisioning for bad debts on prudential basis. It has been decided by Reserve Bank of India to implement the recommendations in a phased manner over a three year period commenced
from the accounting year beginning 1st April, 1992. The recommendations of the committee on Financial system, on which Reserve Bank of India has made certain amendments are enumerated below:

Income of the credit institution should be taken into account on actual receipt basis and not on accrual basis including cases where the units have been placed under nursing or where the reschedulement of debt has been made and the account is being conducted accordingly. In the case of non-performing assets identified as on 31.03.1994, no further interest will be charged. Any amount subsequently realised will be notionally adjusted against the past irregularity. In other words, if interest as on 31st March, 1995 remains unpaid (past due) for any two quarters, in that event no interest will be charged in the account and taken to income account unless it becomes a performing asset.

Non-performing assets

Non-performing assets (NPA) has been defined as advances made in respect of which interest has remained unpaid for a period of four quarters as on 31.03.1993, three quarters as on 31.03.1994 and two quarters for the year ending as on 31st March, 1995 and onwards. Banks are advised not to charge interest on advances which is termed as non-performing assets. Non-recovery of advances/loans have affected the profitability of banks, as a result of which banks are facing a lot of serious problems. This may be well understood from the following discussion.

A term loan will be treated as NPA if interest remains past due for a period of two quarters. However, where interest is being recovered but instalments of principal amount are overdue for a period of two
quarters, such a term loan are to be classified as NPA (non-performing assets).

A cash credit or overdraft account will be treated as NPA if the account remains out of order for a period of two quarters. An account should be treated as out of order if the outstanding balance remains continuously in excess of limit/drawing power. In cases where the outstanding balance in the principal operating account is less than their sanctioned limit/drawing power, but there are no credits continuously for six months as on the date of balance sheet or credits are not enough to cover the interest debited during the period, these accounts should be treated as out of order.

Bills purchased/discounted account should be treated as NPA if the bills remain unpaid and overdue for two quarters. Overdue interest should not be charged and taken into income account in respect of overdue bills unless it is realised. Any other credit facility should be treated as NPA if any amount to be received in respect of the facility remains past due for a period of two quarters of the financial year. An amount is to be termed as 'Past Due' when it remains outstanding for 30 days beyond due date. Thus while interest may become due on say, 31st March, it becomes past due only on 30th April.

Classification of Assets

The advances of the bank are to be classified into four broad groups as under:

(1) **Standard Assets**: Standard assets is one which does not disclose any problem, and which does not carry more than normal risk attached to the business. Such asset is not a non-performing asset (NPA).
However, Government guaranteed advances, although categorised as NPA for the purpose of income recognition, are to be treated as standard assets.

(ii) **Sub-standard Assets**: Substandard Asset is one which has been classified as NPA for a period not exceeding two years. In case of term loans, where instalments of principal and interest have remained past due for a period of two quarters at the ending of the financial year and onwards, then the loan account has to be treated as sub-standard. An asset where the terms of the loan agreement regarding interest and principal have been re-negotiated or re-scheduled after commencement of production, should be classified as sub-standard and should remain in such category at least for two years of satisfactory performance under the re-negotiated or rescheduled terms.

(iii) **Doubtful Assets**: A doubtful asset is one which has remained NPA for a period exceeding two years. In the case of term loans, those accounts where instalments of principal amount have remained overdue for a period exceeding two years should be treated as doubtful. Here too, as in the case of sub-standard asset, rescheduling does not entitle the bank to upgrade the quality of an advance automatically.

(iv) **Loss Assets**: Loss asset is one where loss has been identified by the bank's internal or external auditors or the Reserve Bank of India inspection, but the account has not been written off wholly or partly.
Table 6.1
Classification of loan assets of Public Sector Banks

<table>
<thead>
<tr>
<th>Classification of Assets</th>
<th>As on 31st March</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Standard Assets</td>
<td>130087</td>
</tr>
<tr>
<td></td>
<td>(76.8)</td>
</tr>
<tr>
<td>2. Sub-standard Assets</td>
<td>12552</td>
</tr>
<tr>
<td></td>
<td>(7.4)</td>
</tr>
<tr>
<td>3. Doubtful Assets</td>
<td>20106</td>
</tr>
<tr>
<td></td>
<td>(11.9)</td>
</tr>
<tr>
<td>4. Loss Assets</td>
<td>3930</td>
</tr>
<tr>
<td></td>
<td>(2.3)</td>
</tr>
<tr>
<td>5. Advances with</td>
<td>2665</td>
</tr>
<tr>
<td>balances less than Rs. 25000/-</td>
<td>(1.6)</td>
</tr>
<tr>
<td>included in NPA</td>
<td></td>
</tr>
<tr>
<td>6. Total advances</td>
<td>169340</td>
</tr>
<tr>
<td></td>
<td>(100)</td>
</tr>
</tbody>
</table>

Note: Figures in bracket indicate per cent share in total advances.

Sources: Report on Trend and Progress of Banking in India, 1997–98
It is seen from the table 6.1 that in absolute terms, standard assets out of total advances has increased from Rs. 130087 crore in March, 1993 to Rs. 239318 crore in March, 1998. The total advances during the period March, 1993 and March, 1998 were Rs. 169340 crore and Rs. 284971 crore respectively. In percentage term, it increased from 76.8 per cent as on March, 1993 to 84.0 per cent as on March, 1998.

It has been clarified that in respect of advances granted for agricultural purposes where interest payment is on half yearly basis synchronising with harvest, branches (bank's) should adopt the agricultural season as the basis. In other words, if interest has not been paid during the last two seasons of harvest (covering two half-years) after it has become past due, then such an advance should be treated as NPA. It has also been clarified by the Reserve Bank of India that availability of security or net worth of borrower/guarantor should not be taken into account for the purpose of treating an advance as NPA or otherwise, as income recognition is based on recovery. Credit facilities backed by Govt. guarantees though past due should not be treated as NPA. These advances will be treated as standard assets for the purpose of asset classification and provisioning norms only and not for the purpose of recognition of income. In other words, if Govt. guaranteed advances become past due and thereby NPA, the interest on such advances need not be taken to income account unless the interest has been realised. While considering an account for the purpose of classification, all the facilities granted to a borrower will have to be taken into view as one and treated as NPA and not the particular facility or part thereof which has become irregular. It may be recalled
that when a claim is made to DICGC (Deposit Insurance and Credit Guarantee Corporation of India), banks are required to make consolidated claim in respect of the entire dues from a borrower and not in respect of dues under a facility. Presently, banks are not permitted to upgrade the classification of any advance in respect of which the terms have been renegotiated unless the package of renegotiated terms has worked satisfactorily for a period of two years. As per the norms whenever additional credit facilities are sanctioned such facilities would entail provisioning according to the classification of original advance as sub-standard or doubtful. It has been decided by Reserve Bank of India that provisions would continue to be made in respect of the dues to a bank for existing credit facilities sanctioned to a unit under rehabilitation as per their classification as sub-standard or doubtful. If any advance becomes NPA in any year interest accrued and credited to income account of the bank in the corresponding previous year should be reversed or provided for, if the same is not realised. This will apply to Govt. guaranteed accounts also.

It has been decided by Reserve Bank of India that advances against Term Deposits, National Savings Certificate (NSC), Indira Vikash Patra, Kishan Vikash Patras and Life Insurance Corporation of India's policies will be exempted from provisioning requirements. Advances against such securities should not be treated as NPA although interest thereon has not been paid for two quarters as on 31st March of a year. Interest on such advances may be taken into income account on dates provided adequate margin is available in the accounts. However, in respect of such advances below Rs. 25,000/- a general provision of 7.5% are to be made on the total outstanding as in the case of all other
advances below Rs. 25000/-.

While making provisions to the extent of 7.5% on total advances, amount guaranteed by ECGC/DICGC should not be deducted from the amount of advances. The recoveries on NPA accounts, later on received, needs to be first of all appropriated towards irregularity as on 1st April of a year and then interest for the financial year and then irregularity as on 1st April of the next year and so on.

Problems in recovering the advances by the banks has overburdened them (banks), for making provisions of non-performing assets (Advances for which there is no recovery) out of their income, which adversely affects the profitability of the banks.

Mode of provisioning

1. Loss Assets: 100% of the outstanding

2. Doubtful Assets:

   (a) 100% of the extent to which the advance is not covered by the realisable value of security to which the bank has a valid recourse, and the realisable value is estimated on a realistic basis.

   (b) Over and above item (a) above, depending upon the period for which the asset has remained doubtful, 20% - 50% of the secured portion (i.e. estimated realisable value of the outstanding) on the following basis.

<table>
<thead>
<tr>
<th>Period for which the advance has been considered doubtful</th>
<th>% of provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Upto one year</td>
<td>20%</td>
</tr>
<tr>
<td>One year to three years</td>
<td>30%</td>
</tr>
<tr>
<td>More than three years</td>
<td>50%</td>
</tr>
</tbody>
</table>

3. Sub-standard Assets: A general provision of 10% on total outstanding.
In respect of advances covered by the guarantee of ECGC/DICGC, the risk weight of 50% should be limited to the amount guaranteed and not the entire outstanding balance in the accounts. Thus it is seen that when an account is declared NPA, 10% to 100% of its outstanding, depending on its relative position in asset classification schedule, is to be provided against the bank's operating profit. Recovery of NPA set free the amount so provided giving new lease to bank's advance portfolio. More the recovery of NPA, more is the asset turnover ratio and more is the profitability. Recovery eases Bank's liquidity strain, particularly when the pace of fresh fund mobilisation is slow.

Steps for improving recoveries

For improving recoveries, the Reserve Bank of India has advised banks that they may obtain the services of utilisation Reporters-cum-Recovery Facilitators on a contract basis. The facilitors could be paid suitable commission for reporting maintenance of assets. Similarly, they could also be paid as commission a suitable percentage of recovery effected through them. Such utilisation Reporter/Recovery Facilitator could cover a few villages and Panchayats. Wherever required, adequate gestation period may be allowed in such a way that the commencement of recovery coincides with accrual of incremental income from the project. In the case of projects in which accrual of income is low in the beginning but goes up over a period of time, size of the loan instalments in the initial period may be suitably reduced. Further with a view to enabling the borrower to utilise a higher percentage of incremental income for his own consumption, wherever possible, longer repayment period may be allowed subject to the economic life of the asset.
Reducing of non-performing assets (NPA) has been one of the main tasks of the Banks during the last couple of years. The NPA constitute 4.5% of the total assets. The new norms on income recognition and on performing assets, have led many banks to operate losses from the year 1993 onwards. Further strict provisioning requirements has made the problems of credit institution more serious. According to one report three nationalised banks were required to make provisions for the year 1993–94 over Rs. 200 crore each, three other banks over Rs. 300 crore and one bank had to do so for over Rs. 600 crore. Consequently, the profits of the banks in general are substantially affected.

Memorandum of Understanding (MOUs) with Banks

Against this background, Reserve Bank of India has made banks to agree for a commitment for improving performance in the field of recovery, through a Memorandum of Understanding (MOU). Reserve Bank of India has further decided to impose penalties on Banks for non-compliance of MOUs. One of the important areas covered under MOU is recovery management. This should be so because the percentage of overdues to demand is 60%.

The recovery measures available to a bank may be discussed as under:

Recovery measures; filing a suit

Filing a suit against the borrower and getting a decree from the court is a long drawn process, it is the experience in the banking circles that it normally takes at least 10 years before a decree could be obtained. Getting a decree executed would involve further time. It is felt that there are very few cases where banking institution having
successfully disposed off properties mortgaged to them and realise their dues within a period of decade. Even the first hearing of the case is taken up after 2-3 years. By the time the bank gets a decree, the borrower would have expired or disposed off the property or would have disappeared from the area. The number of suit filed accounts of the public sector banks as at the end of March, 1993 was 10,24,620 and the amounts involved was over Rs. 4071 crore. Today Banks are holding innumerable decrees which are not executable even after spending nearly 50% of the claim amount by way of legal fees, stamps and other charges.

Because of the above legal constraints, banks are placing increasing reliance on non-legal measures of recovery. These are — compromise proposal. Compromise relates to

(i) Waiver of penal interest
(ii) Reduction in interest rate
(iii) Write off the account or a part of the amount of interest debited to the account of the borrower.

Compromise proposal can aptly be called the "Music of the time", when the volume of the NPA is ever-swelling and legal measure is none-too-effective, it is only left for us to strike a deal with the defaulting borrowers, albeit at some revenue loss, either actual or future. This tool is best effective in a situation where borrower's ability to repay and bank's ability to recover the debt by other recovery means are limited. Finally, compromise proposal is settled when a balance is arrived in between the bank's and the borrower's bargaining capacities. However as gathered from practical experiences, compromise settlements have an implied demonstrative effect. Even capable

1. IBA Bulletin, October, 1994
borrower's, after knowing bank's uneviable position in legal battles try to wrestle out settlement schemes grossly unremunerative to the bank. Sometimes, they go for paper compromise in order to delay the suit or execution proceedings. Such cases are to be dealt with grif and determination. In short, bank's approach to a settlement offer should be rational multidimensional, adaptive and probabilistic. To decide over acceptability of a particular settlement scheme, SWOT (strength, weakness, opportunity and stake of the negotiating sides) analysis is very appropriate.

We should analyse any settlement proposal in a realistic perspective comprising of various parameters like actual and notional loss, mode of payment, recovery sacrifice ratio, risk and uncertainty implication, cost of capital, existing tangible securities and the overall position of the account. An analysis may be done in the following way — 'A' borrowed money from Bank 'B' which now swelled to Rs. 10 lacs, due to non-payment interest and instalments. There was innate scarcity of security and bank agreed in principle to consider a proposal for compromise from the borrower's end. However, three modes of payment have been evolved during negotiation.

(i) Accept Rs. 8.00 lacs instantaneously in full and final settlement of the account

(ii) Pay Rs. 10.00 lacs in 10 equal quarterly instalments

(iii) Pay Rs. 8 lacs in quarterly instalments of Rs. 1 lac each along with interest @ 12% p.a. Primafacie it seems that as we are getting the full outstanding balance in terms of the second option, as above, it is the best choice. Again, as option no. 3 ensures realisation of interest, it is better than option number one. Thus our order
of acceptance comes to 2>3>1. Is it really so? It reveals from further
analysis that the first option involves a straight write-off amounting
to Rs. 2 lacs. But an amount of Rs. 8 lacs is instantaneously available
which generates about Rs. 1.27 lacs of interest each year @ 15% p.a., if
recycled. Thus, the impact of write off is offset in about 18 months
only.

In case of second option, if Rs. 10 lacs is paid in 10 quarterly
instalments there is no direct sacrifice. However, if we take into
account the prevalent cost of capital (equivalent to the floor rate of
lending, 15%), the present value of all the instalments in aggregate,
discounted at the cost of capital will be,

\[ \frac{R}{(1+k)^t}, \text{ which at constant } \]
\[ t=1 \]

R reduced to

\[ R \left\{ \frac{(1+k)^{n-1}}{k} \right\} (1+k)^n \]

where, R = amount of instalment per quarter, t = any period in between 1
to nth quarter while n = 8, k = rate of interest = 15/400 per quarter.

The above formula yields a present value of Rs. 8.24 lacs. This
indicates that Rs. 10 lacs payable in 10 equal quarterly instalment is
equivalent to Rs. 8.24 lacs payable initially.

The third option involves payment of interest @ 12% p.a. which
produces an instalment amount of Rs. 1.14 lacs on equated term. Total
repayment thus will be Rs. 1.14 lacs x 8 = Rs. 9.12 lacs over a repayment
period of two years. However, the present value of this amount,
discounted at the cost of capital will be Rs. 7.76 lacs as per the above
formula.
Thus if we consider at this juncture, the order of acceptability of the options 2>1>3, as present values of the options are 8.24>8.00>7.76 respectively. However, even at this stage there is ample scope for reappraisal. As all of us know, money received immediately is of greater value than received at some future date, due to re-investment opportunity, elements of uncertainty risk, inflation etc. we have so far considered the fund reinvestment aspect only, but did not consider the risk and uncertainty implications of the options. As a rule, the more prolonged a repayment schedule, the more risks involved in it. The variability of returns and the risk associated with a repayment scheme increases with the passage of time. Where instalments have been guaranteed contractually, the standard deviation and therefore the risk may be constant over time. We have so far resorted to a riskless analysis of returns which conforms to a zero coefficient of variation.

\[
\text{Co-efficient of variation (C.V.)} = \frac{\sigma}{E} \text{ (standard deviation)}
\]

However, when the country's economic condition is under depression, uncertainty is reigning in the business environment, a risk-adjusted discount rate tends to give a more rational analysis. Thus, a moderate co-efficient of variation squeezes the present value of option no.2 below Rs. 8 lacs. The only viable option then remains the immediate payment of Rs. 8 lacs (option no.1) which previously seemed unfavourable.

**Debt discounting and Debt swapping**

These recovery measures are relatively unknown in Indian context, but situation may emerge in future when banks will start discounting the debts to ensure early recovery from the borrowers, or
different banks may arrange swapping of loans between themselves to facilitate monitoring of repayment etc.

Publication of name

A very recent development, it was announced by our Hon'ble Union Minister of Finance during the budget session of 1994 that the names of defaulting borrowers will henceforth be circulated by RBI among all banks, financial institutions and others. This is to ensure that such borrowers are debarred from availing credit facilities with other banks and therefore they are compelled to repay their existing debts. The Reserve Bank of India has since devised a return regarding the defaulting borrowers and banks are required to send the information periodically in a floppy disk.

Recovery Melas

The idea of recovery melas has not been popularised as required because it involves repayment of the loans taken, as the repayment culture among the borrowers of any rank leaves much to be desired. It is human nature that there is always a reluctance to repay when once the funds are in the hands of the borrowers received through bank loans. Hence there was urgency to aggressively use the strategy of recovery melas at all the bank branches in the country, particularly when the non-performing assets have put many banks in the alarming position during 1992, 1993 and 1994.

Suggestion on Recovery mela

The Recovery mela should starts with those who have paid the loans promptly and in the first monthly meeting, such borrowers should
be honoured by the branch managers by giving them some token gifts in the presence of the customers of the branch and other members of the public. The manager should praise those who have been regular in their repayments and must emphasise that only such repayments help the banks in recycling the funds to lend to others for gainful employment. This type of recovery mela meeting will send right signals to the defaulters to repay their dues promptly so that they can comfortably attend the next meeting after they settle their dues. The continuous holding of monthly recovery melas will increase the premium on the integrity of the borrowers and develop a sense of discipline to repay on the due dates. Some of the recovery melas may be attended by the higher authorities by prior appointment and they can honour the borrowers who are regular in repayment which will boost up their morale and it will also transform the minds of wilful defaulters to take a decision to repay and who may in turn advise other defaulters to repay the bank loans without default. This is a chain reaction to produce the desired result to reduce the level of non-performing assets. In some of the meetings, the local prominent leaders may participate or preside.

In each 'Recovery Mela' function which should preferably be held in the bank premises, the speeches made should create an awareness amongst the public that the loans taken from the banks should be promptly repaid. The customers should be informed about the progress in recovery figures and their co-operation sought whenever there is a problem in difficult cases. This type of involvement of the customers in the task of recovery for the bank will create a sense of belongings in the minds of the customers, that the bank is their and they must do something in improving its recovery performance. The occasion may also be
utilised by the manager to project the image of the branch by highlighting its performance in other areas. Every year banks can issue credit rating cards to the borrowers who are regular in their repayments. Such cards can be distributed in Recovery Melas.

**Awards to managers showing good recovery performance; suggestions**

Managers who show good performance in recovery of overdues should be also publicly honoured by higher authorities in branch functions. Best performers at the district level, state level and national level in recoveries may be identified every year and may be honoured by issuing certificates and medals in functions or conferences of managers. Best recovery managers may also be selected from rural, semi-urban, urban and metropolitan branches separately. The outstanding recovery effort of every staff should also be taken into consideration and due weightage should be given in the performance appraisal form for giving special benefits or promotions at the time of interviews. The recovery melas should concentrate on aggressive recovery of non-performing assets in a big way. Normal repayments coming in the ordinary course as per stipulations are not recoveries from NPA. Atleast interest overdues from NPAs should be recovered as part of the effort in recovery melas.

Forcible recovery should be made only from wilful defaulters and not from genuine defaulters. The image of the bank may suffer from forcible recovery from genuine defaulters. Only money lenders can afford to this task and not the banks who have a responsibility to help the genuine defaulters to turn the corner by giving rehabilitation assistance to earn and repay with a time bound programme. To get the full benefit of recovery melas, they should be organised at the grass
root level every quarter with a continuous follow up to persuade the wilful defaulters for a change of heart and mind to repay. In the functions, the field officers have a key role to play as they have to be in constant touch with all types of borrowers to maintain a high percentage of recovery position. There are some branches where recovery percentage was as high as 90 to 95% and such branches can be classified as high rated performers. There is a distinction between recovery and repayment. The long term effect and impact of recovery melas should be a smooth flow of repayment on due dates without the banker reminding the borrowers to repay on due dates. If this stage can be achieved and reached by the bankers, the guidelines of the Reserve Bank of India to reduce NPAS would no longer become necessary. Hence the years to come, the borrowers should co-operate to repay on due dates and bankers should be borrower friendly, so that the NPAS should only reflect outstandings of genuine defaulters in the bank's balance sheets. One of the main effects of recovery camps is that in view of recent guidelines on asset classification and provisioning, many non-performing assets turns into performing assets which has got a direct impact on profitability of the bank.

The problems of recovery of bank loans has somewhat increased with the declaration of Debt Relief Scheme. This scheme has adversely affected recovery management, as the scheme helped only defaulters and the regular repayers were deprived of the benefit. It is to the extent that all those borrowers who were repaying upto 1990, have intentionally ceased from repaying and preferred to be declared as defaulter with a hope that such relief would come again. The banking scenario has tremendously changed in the last few years. The edifice built over two
decades is crumbling and emphasis is more on viability of the system instead of feeling pride solely in meeting social obligations.  

Table 6.2  
NPA recoveries and slippages in Public Sector Banks  
(Amount in Rs. crore )

<table>
<thead>
<tr>
<th>Year</th>
<th>Recoveries</th>
<th>Slippage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994-95</td>
<td>7892</td>
<td>5236</td>
</tr>
<tr>
<td>1995-96</td>
<td>7752</td>
<td>11028</td>
</tr>
<tr>
<td>1996-97</td>
<td>9207</td>
<td>11123</td>
</tr>
</tbody>
</table>


From the above table, it is clear that although the recoveries reported during 1994-97 were significant, the level of slippage i.e. fresh accretion of NPAs were significantly more. Consequently the level of NPAs show a rise, eroding whatever NPA reduction was made.

The focus in 2000 and beyond will be on the quality on business instead of its volume and through this on profits. With the rise in competition from within the system by entry of private sector banks and foreign banks, stricter income recognition and provisioning norms, increase in surplus staff with the closer of unviable branches and large scale computerisation, lower spread due to likely interest deregulation and with ever increasing establishment expenses, profitability of banks is likely to come under heavy strain. Unless some specific measures are taken to improve the profit and profitability of the banks, the viability of banks will be at stake. Recovery of advances is taking long time due to outside interference and unduly lengthy legal procedures.
This can be overcome to a great extent through setting up of tribunal at all important centres.

**Recovery Tribunals**

Following recommendations of several high level committees including Narasimham panel on financial sector reforms and assurance of the Finance Minister on the floor of parliament to be set up tribunals to hear and decide the claim of banks, the bankers have been anxiously looking forward to the new set up of recovery. The new Act called, "The Recovery of Debts Due to Banks and Financial Institutions Act, 1993" has come into force from 24.6.93. Under the Act, Tribunals are to be set up in Bombay, Calcutta, Delhi and Madras. The tribunals are also expected to be set up in Guwahati, Bhopal, Bangalore, Jaipur, Ahmedabad and Patna. An Appellate Tribunal is to be established in Bombay. The tribunals shall become functional on the issue of notification by the Central Government.

The pecuniary jurisdiction of the tribunals is for the adjudication of claims of Rs. 10 lacs and above. However, the Central Government is empowered to extend the jurisdiction to cover cases above Rs. 1 lakh. The Act is passed primarily for establishment of tribunals and for expeditious adjudication and recovery of debts due to banks and financial institutions. The Tribunals have jurisdiction, power and authority to entertain and decide application from banks for recovery of dues and on all related matters. Only banks and financial institutions can avail the benefit of speedy process of recovery laid down in the Act. Further the debt to be recovered by a bank should arise during the course of business activity undertaken by it. The procedure for filing a
claim by the bank before a tribunal is simple in form. Unlike drafting of plaint by an advocate following the procedure for filing of a suit in the civil court, the claim is to be presented by making an application to the tribunal. On receipt of notice from a tribunal the defendants (defaulting borrowers) are required to file with the tribunal within one month in four sets the reply of the application and endorse a copy of reply to the bank. The tribunal shall thereafter notify the parties the date and place of hearing of the application and after hearing the parties, it shall pass necessary orders to meet the ends of justice. The Act provides that tribunals shall deal with the application expediously and shall try by dispose of the application finally within six months. This is in contrast to the trial of a suit by the court where no time limit is prescribed for disposal. However, where the appeal is filed by the borrower of the bank disputing the amount determined by the tribunal, then such an appeal shall not be entertained by the appellate tribunal unless the borrower has deposited with it 75% of amount of debt due from him. However, in case of sufficient cause the Appellate Tribunal is empowered to waive or reduce the amount of deposit. After disposal of application, the tribunal shall issue a certificate to the recovery officer appointed under the Act, for making recovery of debt. The setting up of tribunals for recovery of bank's debts has already made lot of defaulters running scared and forced them to come to terms with the banks.

Delhi High Court on Recovery Tribunals

A division bench of the Delhi High Court comprising of justice D.P. Wadha and Justice M.K. Sharma, on 10th March, 1995, quashed the Central Government notification dated July 5, 1994 issued under the
recovery of debts due to banks and Financial Act, 1993 constituting debts Recovery Tribunal within the jurisdiction of Delhi. It has been held that the recovery of debts Act is unconstitutional as it erodes the independence of judiciary and is irrational, discriminatory unreasonable arbitrary and is hit by Article 14 of the constitution. On July 25, 1994, the court had stayed the operation of the Act and its applicability in Delhi because the court was prima facie of view that the Act was unconstitutional. Having held the Act to be unconstitutional, the court found it necessary to issue consequential directions that the applications pending before the tribunal would be transferred to the original side of the High Court. The decision to set up Debt Recovery Tribunals had been taken in the light of the fact that as on September 30, 1990, over 15 lakh cases for recovery of over Rs. 6,000 crores (Rs. 5,622 crores due to public sector banks and Rs. 391 crores due to financial institutions) had been pending before various courts.

Steps for recovery

It is important to create a climate which promotes prompt repayment of loans. For this, it is necessary that loans are not written off. Support from the Government is essential in recovery of loans. In this context, although most of the states have passed legislation on the lines of the Talwar Committee recommendations for recovery of overdues, the implementation of these recommendations by the State Governments are to be improved. Adequate care has to be taken at the time of formulation of the schemes to ensure that realistic assumptions are made. Availability of infrastructural support like marketing, veterinary services etc. must also be ensured for the success of the schemes. Some
provision for unforeseen calamities like droughts should be built into the repayment programme. The availability of crop insurance takes care of this to some extent. However, in the case of dairy loans, such safeguards are not available and during periods of drought, particularly, borrowers have to buy fodder at exhorbitant prices to feed their animals.

In case of Industrial loans, Technical feasibility, economic and financial viability and managerial competence of the applicant should be carefully examined. District Industries Centre (DIC) may be requested to sponsor only such proposals which are economically viable and technically feasible. The managers of the DIC should be personally contacted and proposals forwarded by them may be discussed at length wherever necessary. Financing of vehicles to small scale industry units wherever needed should be considered on merit for enhancing the operative efficiency of the assisted units. Inventory of stocks should be regularly and physically checked on monthly basis and stock statement report should be received as stipulated in sanction letter. Nursing/rehabilitation programme should be initiated in time in case of potentially viable units.

Transport Loan Recovery

In case of transport and other loans, instalments should be fixed on the higher side in the beginning as the chances of breakdown/repair expenses in the respect of vehicles are nil or minimum during the initial years. Concerned transport authority should be pursuaded to issue permit to the transport operators only after getting 'No objection certificate' from the financing bank. If the RTO does not co-operate,
the matter should be taken up in the District Consultative Committee (DCC)/State Level Banker Committee (SLBC) meetings. Seasonality of operation should be kept in mind for scheduling the recovery of bank loans.

"Repayment of loans has to come out of surplus generated and not out of capital employed". The source of repayment of loan has to be determined. Main source is the surplus generated. Sometimes, a life policy taken as security may clear off the liabilities from the claim proceeds. Sometimes, a deposit or a Government security taken as security may clear off the advance at the time of maturity. Disposal of assets in part or full may clear off the advances. But in running business, the repayment has to come out of the surplus only. When the borrower is making losses and is not in a position to meet the instalment repayment, any recovery either towards principal or interest results in withdrawing the capital itself. This does not mean that bank should not recall the advance or take necessary steps to safeguard the advance, when the advance is irregular. If necessary, they may recover the loan at the cost of borrower. But when the difficulties that the borrower is facing are not genuine and if it is necessary, they may recover the loan at the cost of borrower. But when the difficulties that the borrower is facing are genuine and if it is temporary, the bank has to consider rescheduling the repayment. For this, the borrower should be honest enough to reveal the position to the banker from time to time. The banker should have an open mind and open heart to find out the correct position at each stage to give practical and positive help. But many a times, the problem is in identifying the problem itself. As a

2. Srinivasan, H.V., Banker's Handbook of Credit Management, 1986
healthy norm, the repayment of term loans comes from the monthly or periodical surplus generated and working capital advances are regularised from sale proceeds. Working capital advances are perpetual in nature. When sale proceeds which include profit element are smooth, regular and adequate, the working capital advances are safe and regular.

Instalment repayment depends on income. Mere income (i.e. gross) should not be taken into account, but it is the net income of the borrowers on which the instalment of the repayment of loans are fixed. Gross income may be Rs. 3000 p.m. but the net may be less than Rs. 300. New units take some time to generate real profits even after production. A reasonable repayment holiday is given for advances.

Repayment is ensured when the borrower has liquid assets. When the business is running in difficulties from time to time, from one hope to another and bank has the hope of success and survival, the bank may consider temporary assistance by way of bridge loan to such units which are expecting assistance from other term lending or government institutions against commitment. Bridge loans are cleared out of the proceeds of such commitments.

There are certain aspects to consider in case of units solely run by single man, as to what happens to business after his retirement or death. Linking the advance with salary, gratuity, life policy etc. are the ways to safeguard the advance against future probabilities.