A study of management of Non-Performing Assets (NPAs) in Credit Cooperatives

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&

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Abstract

Cooperatives in India were shaped with a view to provide formal credit to agriculture and rural cottage and village industries which in 50’s were organised in the form of Cooperatives. Over the year, the cooperatives have lost the place of prominence which they once enjoyed and are now in the middle of massive transformation.

Agricultural loaning has been plagued with uncertainties. Many times natural calamities have forced bank to restructure and write of old loans. Writing of old loans have become a big political issue which many feel tends to encourage culture of wilful default. Large scale defaults of loans outstanding have the impact of eroding the financial soundness of the system, critically affecting the operational efficiency.

Recovery of credit is absolutely essential for recycling of credit. Timely recovery of advances keeps the business running and continues flow of funds helps retaining the customers and reducing Non-Performing Assets [NPAs].

The paper intends to examine the magnitude of NPAs in the Cooperative credit system, causes for the same, strategies adopted by different banks in reducing the Non-performing assets and the future road Map.

I. Background

Credit cooperatives play an important role in the rural areas, providing timely credit and other support for uplifting the economic conditions of farming community. Cooperative Banks have a portfolio of loans and advances that are highly tilted toward Agriculture and that too short term agriculture [crop loaning]. Both Government of India and State Governments (many) are giving interest subvention on crop loans issued through the cooperative sector, which make it the cheapest loan in the banking system. They also cater to services like loans, deposits, and other banking related activities like Universal banks but widely differ in their values and governance structures.
They have achieved many landmarks since their creation and have helped normal rural Indian to feel empowered and secure. For the past three decades, cooperative banking system has several outstanding achievements to its credit, in many parts of our country. The most striking is its extensive rural outreach. Cooperatives have been known to serve the last mile clients / farmer with their innovative Crop loan system, supported by their membership base. They have become an integral part of the success of Indian Financial Inclusion story, particularly covering the farming community. The story, however, has not been smooth and has its share of glitches and woes placed at various sources.

II. Cooperative Credit Structure in India

As per the data given in Reports on trends and Progress in banking 2015-16 by Reserve Bank Of India, as at end-March 2016, India’s co-operative banking sector comprised of 1,574 urban cooperative banks (UCBs) and 93,913 rural co-operative credit institutions, including short-term and long-term credit institutions (Chart).

Table I Cooperative Credit Structure in India [position as on 31.03.2016]

<table>
<thead>
<tr>
<th>Credit Cooperatives (95,487)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Urban Co-operatives (1,574)</td>
</tr>
<tr>
<td>Scheduled UCBs (52)</td>
</tr>
<tr>
<td>Multi State (31)</td>
</tr>
<tr>
<td>Single State (21)</td>
</tr>
<tr>
<td>Non-Scheduled UCBs (1,522)</td>
</tr>
<tr>
<td>Multi State (20)</td>
</tr>
<tr>
<td>Single State (1,502)</td>
</tr>
<tr>
<td>Rural Co-operatives (93,913)</td>
</tr>
<tr>
<td>Long Term (722)</td>
</tr>
<tr>
<td>SCARDBs (20)</td>
</tr>
<tr>
<td>PCARDBs (702)</td>
</tr>
<tr>
<td>Short Term (93,191)</td>
</tr>
<tr>
<td>StCBs (32)</td>
</tr>
<tr>
<td>DCCBs (370)</td>
</tr>
<tr>
<td>PACS (92,780)</td>
</tr>
</tbody>
</table>

StCBs: State Co-operative Banks; DCCBs: District Central Co-operative Banks; PACS: Primary Agricultural Credit Societies; SCARDBs: State Co-operative Agriculture and Rural Development Banks; PCARDBs: Primary Co-operative Agriculture and Rural Development Banks.

Notes:
1. Figures in parenthesis indicate the number of institutions at end-March 2016 for UCBs and at end-March 2015 for rural co-operatives.
2. For rural co-operatives, the number of co-operatives refers to reporting co-operatives.

Source: RBI

Introduction of Prudential Norms

In order to reflect Bank's actual financial health in its balance sheet, RBI had introduced prudential norms for Income Recognition, Asset Classification and
Provisioning norms for the advances and investment portfolio of all banks, including Cooperative Banks. The policy of income recognition is based on the record of recovery.

RBI has further advised that if the applicable Co-operative Societies Act and/or rules made there under or any other applicable statutory provisions are stringent than prescribed by RBI, they shall continue to be applicable.

**Status of StCBs/ DCCBs:**

Indian rural economy, which is based on agriculture faces vagaries of natural calamities such as cyclone, drought, earthquake, fire, flood, tsunami, hailstorm, landslide, avalanche, cloud burst, pest attack and cold wave/frost, etc. Periodical but frequent occurrence of natural calamity takes a heavy toll and cause wide spread damage to economic pursuits, particularly in the rural areas. As cooperative banks mostly deal in rural areas, they are impacted the most on account of it also.

As per data available in ENSURE, NABARD, the following were the status of the StCBs and DCCBs during the last 3 years, under a few important parameters:

<table>
<thead>
<tr>
<th>Sl. No</th>
<th>Particulars</th>
<th>Bank</th>
<th>2014-15</th>
<th>2015-16</th>
<th>2016-17</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Total No. of Banks</td>
<td>StCBs</td>
<td>32</td>
<td>33</td>
<td>30</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>371</td>
<td>371</td>
<td>368</td>
</tr>
<tr>
<td>2.</td>
<td>No. in Profit</td>
<td>StCBs</td>
<td>28</td>
<td>29</td>
<td>28</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>310</td>
<td>322</td>
<td>317</td>
</tr>
<tr>
<td>3.</td>
<td>No. in Current Loss</td>
<td>StCBs</td>
<td>4</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>61</td>
<td>49</td>
<td>51</td>
</tr>
<tr>
<td>4.</td>
<td>Amount of Current Loss [Rs Cr]</td>
<td>StCBs</td>
<td>24.94</td>
<td>98.77</td>
<td>18.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>1090.55</td>
<td>435.77</td>
<td>734.18</td>
</tr>
<tr>
<td>5.</td>
<td>No having Accumulated Losses</td>
<td>StCBs</td>
<td>7</td>
<td>8</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>114</td>
<td>104</td>
<td>110</td>
</tr>
<tr>
<td>6.</td>
<td>Amount of Accumulated Loss [Rs Cr]</td>
<td>StCBs</td>
<td>616.76</td>
<td>697.30</td>
<td>378.28</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>4651.58</td>
<td>4781.97</td>
<td>5196.23</td>
</tr>
<tr>
<td>7.</td>
<td>No. having CRAR less than mandated 9%</td>
<td>StCBs</td>
<td>11</td>
<td>5</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>141</td>
<td>110</td>
<td>27</td>
</tr>
<tr>
<td>8.</td>
<td>Total Gross NPAs of the bank/s [Amount – Rs Cr]</td>
<td>StCBs</td>
<td>5755.02</td>
<td>5564.12</td>
<td>4965.80</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>22167.16</td>
<td>22848.16</td>
<td>26096.05</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Total</td>
<td>27922.18</td>
<td>28412.28</td>
<td>31061.85</td>
</tr>
<tr>
<td>9.</td>
<td>Total Gross NPAs of the bank/s [% to loan O/S]</td>
<td>StCBs</td>
<td>5.0</td>
<td>4.5</td>
<td>3.9</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>9.9</td>
<td>9.4</td>
<td>10.4</td>
</tr>
<tr>
<td>10.</td>
<td>Total Net NPAs of the bank/s [Amount – Rs Cr]</td>
<td>StCBs</td>
<td>1854.97</td>
<td>1718.92</td>
<td>1285.32</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DCCBs</td>
<td>7782.82</td>
<td>7901.10</td>
<td>10214.25</td>
</tr>
</tbody>
</table>
As can be seen from above, the gross non-performing assets (NPA) of District cooperative banks (DCCBs) shot up to Rs.22848.16 crore and Rs.26096.05 crore for the fiscal 2015-16 and 2016-17 forming 9.4% and 10.4% of total loans outstanding.

At present co-operative banks are under considerable pressure causing decline in productivity and efficiency. Due to financial impairment, the co-operative credit structure is steadily losing its ability to meet the rapidly growing credit needs of agriculture. This, coupled with the widening gap between their level of skills and the increasing computerisation of banks, has caused considerable concern in the regulatory and supervisory space. Improvement in recoveries and reduction of NPAs is essential to speed up the growth and profitability of cooperative banks.

A look at the Gross & NPA levels of the Banks for the last 3 years as per the ensure data of NABARD reveals a picture which can suggest a very clear future road map.

Table II. Gross NPA position of DCCBs [2014-15 to 2016-17]
[Source: Ensure data NABARD]

As can be seen from the above table around 115 DCCBs have a gross NPA within the acceptable banking levels. Of these, 52 DCCBs, as on in March 2017 have a gross NPA of up to 3 %. These are very good Bank who have put in place effective strategies for managing the non-performing assets in the system.

Further the number of DCC banks having gross NPAs of more than 10% continued to be substantial at 166, 153, & 148, respectively, during the last 3 years, clearly indicating poor credit risk management. This makes Cooperative Banks vulnerable to...
further declines in the asset quality and higher provisioning needs in future. It also restricts their ability to draw refinance from higher financing bodies and increase their lending.

34 DCCBs have gross NPAs of over 50% as on 31st March 2017.

In such Banks, if the existing levels of NPA are converted into risk cost and factored in MCLR, these banks would probably be not able to lend because the base rate would be much above the existing market rates. Then in that case how these banks should approach farmers and what kind of products should they offer so as to get positive margins is a question which needs to be answered. These banks are only able to have curtailed fresh lending and as a result the farmer members of the PACS have shifted to other financial institutions along with their deposits.

As a further analysis of the NPA data, we have analysed the DCCB on the net NPA wise Position. This indicates that many banks have been able to make adequate provisions for the gross NPA to reflect 0 or near zero NNPA. The Banks with higher NNPAAs indicate a very weak financial position.

### Net NPA position of DCCBs [2014-15 to 2016-17]

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of DCCB in Net NPA Percent Band</th>
<th>0%</th>
<th>Upto 5%</th>
<th>5-10%</th>
<th>10-20%</th>
<th>20%-50%</th>
<th>Beyond 50%</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014-15</td>
<td></td>
<td>77</td>
<td>154</td>
<td>57</td>
<td>34</td>
<td>36</td>
<td>13</td>
<td>371</td>
</tr>
<tr>
<td>2015-16</td>
<td></td>
<td>83</td>
<td>160</td>
<td>56</td>
<td>32</td>
<td>26</td>
<td>14</td>
<td>371</td>
</tr>
<tr>
<td>2016-17</td>
<td></td>
<td>82</td>
<td>152</td>
<td>55</td>
<td>38</td>
<td>28</td>
<td>14</td>
<td>369</td>
</tr>
</tbody>
</table>

[Source: Ensure data NABARD]

What is worrisome in the 2 tables indicated above, is the fact that the banks are moving from left to right [from better to worse] instead of movement from right to left.

In the prevailing political climate and very weak financial strength, such Banks which constitute around 20% of total DCCBs would have to strategize for recovery of old overdues, retain the confidence of its clients, generate minimum viable business at the PACS level and also attract new deposit.

### Factors contributing for rise in NPAs:

There are many reasons as to why a loan goes bad. The situation has worsened due to banks aggressively pushing loans, even unsecured ones, to individuals/ members to prevent idle assets on their books.
Most customers of the cooperative banks are not financially educated and more often than not, banks offer them more and more loans, without checking their financial position.

The external factors such as ineffective recovery machinery, wilful defaults, natural calamities, change in Govt. policies, demonetisation and exclusion of cooperative banks for accepting the SBNs, Loans waivers etc. have all added to the problems of NPAs and have hurt the cooperative banks more than other banks.

Frequent Agricultural loan waivers have become a norm particularly in the recent years. Farm loan waivers impact public sector banks and cooperative banks the most due to their high exposure to agriculture and farmer loans. Though the government reimburses farm loan waiver, such schemes create second order impact in terms of impaired credit discipline and low further loan availability. Frequent occurrence of such populist actions leads to risks of impaired credit discipline and weak risk-reward for banks. Further frequent farm waivers create expectations of future waivers and can be a serious disincentive in loan repayments.

A day after UP government had announced a waiver, Governor of the Reserve Bank of India (RBI) Urjit Patel, had denounced it. “I think it undermines an honest credit culture. It impacts credit discipline. In other words, waivers are in general more of hazard,” he had said speaking to media. “Waivers are in general more of hazard. It also entails at the end of the day transfer from taxpayers to borrowers,” he added.

Similarly, Arundhati Bhattacharya chairman of State Bank of India has voiced concern over it. “Credit discipline breaks when you waive off farm loans. The money will come in today because the government will pay but when we will give loan in future, farmers will wait for next elections. Support to the farmers is necessary but not at the cost of credit discipline,” she said. Thus the banks in cooperative fold are having higher NPA’s because of the inherent nature of their loan portfolio.

More farm loan waivers on the cards as India approaches 2019 general elections, as indicated below:

<table>
<thead>
<tr>
<th>States which have already declared waiver or have elections scheduled</th>
<th>Total bank credit to agriculture* (May 2017) (Rs. billion)</th>
<th>Agri credit outstanding as % of GSDP</th>
<th>Debt waiver announced (Rs. billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gujarat</td>
<td>512.00</td>
<td>4.60</td>
<td>--</td>
</tr>
<tr>
<td>Himachal Pradesh</td>
<td>64.00</td>
<td>4.90</td>
<td>--</td>
</tr>
<tr>
<td>Karnataka</td>
<td>1,131.00</td>
<td>9.60</td>
<td>--</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>798.00</td>
<td>10.40</td>
<td>--</td>
</tr>
<tr>
<td>Chhattisgarh</td>
<td>150.00</td>
<td>5.20</td>
<td>--</td>
</tr>
<tr>
<td>States which have already declared waiver or have elections scheduled</td>
<td>Total bank credit to agriculture* (May 2017) (Rs. billion)</td>
<td>Agri credit outstanding as % of GSDP</td>
<td>Debt waiver announced (Rs. billion)</td>
</tr>
<tr>
<td>---------------------------------------------------------------</td>
<td>-----------------------------------------------------</td>
<td>----------------------------------</td>
<td>----------------------------------</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>645.00</td>
<td>10.10</td>
<td>--</td>
</tr>
<tr>
<td>All India (general elections)</td>
<td>12,686.00</td>
<td>8.30</td>
<td>--</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>968.00</td>
<td>4.30</td>
<td>305.00</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>1,438.00</td>
<td>11.10</td>
<td>364.00</td>
</tr>
<tr>
<td>Punjab</td>
<td>740.00</td>
<td>16.30</td>
<td>100.00</td>
</tr>
</tbody>
</table>

*estimated, includes credit by SCBs, rural banks and co-operative banks

**Source:** Rajya Sabha question, RBI Handbook of Statistics, CMIE and Mint calculations.

### Reserve Bank of India on NPA management in Banks

The thinking of RBI on NPA management in banks is clear from its circular on Prompt Corrective action [RBI/2016-17/276 DBS.CO.PPD. BC.No.8/11.01.005/2016-17 April 13, 2017]. Though the circular is issued for all Scheduled Commercial Banks, the direction of thinking clearly states that

A. Capital, asset quality and profitability continue to be the key areas for monitoring in the revised framework.

B. Indicators to be tracked for Capital, asset quality and profitability would be CRAR/ Common Equity Tier I [Ratio1], Net NPA [Ratio2] and Return on Assets [Ratio3] respectively.

The details of which are under:

<table>
<thead>
<tr>
<th>PCA matrix - Areas, indicators and risk thresholds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indicator</td>
</tr>
<tr>
<td>----------------</td>
</tr>
<tr>
<td><strong>Area</strong></td>
</tr>
<tr>
<td>Capital (Breach of either CRAR or CET 1 ratio to trigger PCA)</td>
</tr>
<tr>
<td>CRAR: Minimum regulatory prescription for capital to risk assets ratio + applicable capital conservation buffer(CCB)</td>
</tr>
<tr>
<td>current minimum RBI prescription of 10.25% (9% minimum total capital plus 1.25% of CCB as on March 31, 2017)</td>
</tr>
<tr>
<td>And/ Or: Regulatory pre-specified trigger of Common Equity Tier 1 (CET 1) and applicable capital conservation buffer(CCB)</td>
</tr>
<tr>
<td>current minimum RBI prescription of 5.5% (5.5% plus 1.25% of CCB as on March 31, 2017)</td>
</tr>
<tr>
<td><strong>Breach of either CRAR or CET 1 ratio to trigger PCA</strong></td>
</tr>
</tbody>
</table>

1. CET 1 ratio = the percentage of core equity capital, net of regulatory adjustments, to total risk weighted assets as defined in RBI Basel III guidelines.
2. NPA ratio = the percentage of net NPA to net advances.
3. ROA = the percentage of profit after tax to average total assets.
<table>
<thead>
<tr>
<th>Asset Quality</th>
<th>Net Non-performing advances (NNPA) ratio</th>
<th>&gt;=6.0% but &lt;9.0%</th>
<th>&gt;=9.0% but &lt;12.0%</th>
<th>&gt;=12.0%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profitability</td>
<td>Return on assets (ROA)</td>
<td>Negative ROA for two consecutive years</td>
<td>Negative ROA for three consecutive years</td>
<td>Negative ROA for four consecutive years</td>
</tr>
<tr>
<td>Leverage</td>
<td>Tier 1 Leverage ratio&lt;sup&gt;4&lt;/sup&gt;</td>
<td>&lt;=4.0% but &gt; 3.5% (leverage is over 25 times the Tier 1 capital)</td>
<td>&lt; 3.5% (leverage is over 28.6 times the Tier 1 capital)</td>
<td></td>
</tr>
</tbody>
</table>

<sup>4</sup>CGB would be 1.875% and 2.5% as on March 31, 2018 and March 31, 2019 respectively.

### Mandatory and discretionary actions

<table>
<thead>
<tr>
<th>Specifications</th>
<th>Mandatory actions</th>
<th>Discretionary actions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk Threshold 1</td>
<td>Restriction on dividend distribution/remittance of profits. Promoters/owners/parent in the case of foreign banks to bring in capital</td>
<td>Common menu</td>
</tr>
<tr>
<td>Risk Threshold 2</td>
<td>In addition to mandatory actions of Threshold 1, Restriction on branch expansion; domestic and/or overseas Higher provisions as part of the coverage regime</td>
<td>Special Supervisory Interactions Strategy related Governance related Capital related Credit risk related Market risk related HR related Profitability related Operations related Any other</td>
</tr>
<tr>
<td>Risk Threshold 3</td>
<td>In addition to mandatory actions of Threshold 1, Restriction on branch expansion; domestic and/or overseas Restriction on management compensation and directors’ fees, as applicable</td>
<td></td>
</tr>
</tbody>
</table>
Though PCA guidelines are not made applicable to Cooperative Banks today it very clearly indicates the actions which must be initiated in the bank for reach of Risk thrash holds.

As can be seen from the above-mentioned tables on gross NPA and Net NPA, many of the DCCBs have already breached or may be on the verge of breaching these thrash hold limits. Any future strategy for NPA management and bringing them down to manageable level must include regulators and supervisory actions on all such banks including time bound action plan.

RBI in its policy announcements have indicated that Banks must move from the stage of “Identification of NPAs” to “Resolution of NPA’s”. RBI’s call for resolution of NPAs talks about the following:

A. **Amendment in banking law to give RBI more powers**: The Banking Regulation Act is in the process of being amended to give RBI more powers to monitor bank accounts of big defaulters. The amendment in the banking law will enable setting up of a committee to oversee companies that have been the biggest defaulters of loans.

B. **Applicability to Cooperative Banks**:

1. The Supreme Court held that Cooperative banks can recover outstanding loans only through the mechanism provided in State cooperative laws and need not approach the Debts Recovery Tribunal.

2. The Bench pointed out that the reason for excluding cooperative banks from the purview of the RDB Act [Recovery of Debts Due to Banks and Financial Institutions Act] seemed to be that they had comprehensive, self-contained and less expensive remedies available under the State Co-operative Societies Acts, while commercial banks and financial institutions had to file suits in civil courts.

3. The RDB Act was, therefore, designed to deal with other banks and financial institutions, which had to have recourse to the time-consuming process of civil courts. The bench held that if cooperative disputes also went to the tribunals, they would be overburdened and the whole object of speedy recovery of debts due to banks and financial institutions would be defeated.

4. In conclusion, unless this decision of the bench is revised, the co-operative banks cannot recover their loans through the DRTs.

Thus in case of the Cooperative banks there would be very strong need to strengthen the mechanism provided in the State cooperative laws and put them to effective use.
C. **Stringent NPA recovery rules:** It is true that the NPA problem has to be tackled before the time borrower starts defaulting. This needs a risk assessment by the lenders and red-flagging the early signs of a possible default. RBI has introduced the concept of special mention accounts [SMA] which are standard assets but are showing signs of incipient sickness. [RBI/2013-14/503 DBOD.BP.BC.No.97/ 21.04.132 / 2013-14 February 26, 2014]. The SMA circular of RBI talks about the corrective action plan which would automatically trigger itself in case the loan account shows signs of sickness.

D. Loan restructuring schemes / one time settlement of those NPAs which have very slim possibility of recovery through legal or other means.

**Statement of the problem**

Recovery of credit is very important for ensuring smooth flow of recycling of credit. It had attracted substantial awareness and had been examined by several committees and research workers.

The management of Overdue is the most important task for the banker as it affects the profitability as well as corrosion of the working funds. The success of the banking also depends more on managing the overdues. The expansion of overdue will result in increasing of non-performing assets and will reduce the banks performance significantly. This area assumes more substance now, with the introduction of stringent Non-performing assets (NPA) norms.

Timely recovery of advances not only keeps the business running with continuous flow of funds but also reduces the bad debts and keeps the borrowers (both individual and cooperative societies) eligible for obtaining the credit in prospect. The incidence of overdues in the agricultural credit system has been increasing over the years and has been progressively eroding the financial soundness of the system. This continues to be the big issue.

Inspite of the fact that agricultural lending by its very nature is risky, many cooperative Banks have achieve gross NPA of less than 5% and net NPA of less than 2%.

The wide variation in the percentage of NPA position can be seen across the regions of our country, indicating the divergence of recovery management positions of the banks. As an example, the position of NPAs in the DCCBs of Northern Region, during the last 3 years, was as under: [data as per ENSURE, NABARD]

<table>
<thead>
<tr>
<th>Sl. No</th>
<th>State</th>
<th>As on</th>
<th>Gross NPA [ % wise % in figures]</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Highest</td>
</tr>
</tbody>
</table>

STCCS Seminar: Mishra & Udupa  Paper on NPA Management in STCCS 11  Page
<table>
<thead>
<tr>
<th>DCCB Name</th>
<th>%</th>
<th>DCCB Name</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chhattisgarh</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.03.15</td>
<td>Bilaspur DCCB</td>
<td>28.0</td>
<td>Ambikapur DCCB</td>
</tr>
<tr>
<td>31.03.16</td>
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<td>30.9</td>
<td>Rajnandgaon DCCB</td>
</tr>
<tr>
<td>31.03.17</td>
<td>Bilaspur DCCB</td>
<td>32.2</td>
<td>Rajnandgaon DCCB</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.03.15</td>
<td>Datia DCCB</td>
<td>74.8</td>
<td>Ujjain DCCB</td>
</tr>
<tr>
<td>31.03.16</td>
<td>Datia DCCB</td>
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<td>Ujjain DCCB</td>
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<tr>
<td>31.03.17</td>
<td>Datia DCCB</td>
<td>96.0</td>
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<tr>
<td>Uttarakhand</td>
<td></td>
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</tr>
<tr>
<td>31.03.15</td>
<td>Uttarkashi DCCB</td>
<td>21.6</td>
<td>Rudrapur DCCB</td>
</tr>
<tr>
<td>31.03.16</td>
<td>Uttarkashi DCCB</td>
<td>18.3</td>
<td>Rudrapur DCCB</td>
</tr>
<tr>
<td>31.03.17</td>
<td>Uttarkashi DCCB</td>
<td>18.1</td>
<td>Rudrapur DCCB</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.03.15</td>
<td>Deoria Kasia DCCB</td>
<td>99.9</td>
<td>Rampur DCCB</td>
</tr>
<tr>
<td>31.03.16</td>
<td>Deoria Kasia DCCB</td>
<td>99.9</td>
<td>Rampur DCCB</td>
</tr>
<tr>
<td>31.03.17</td>
<td>Rampur DCCB</td>
<td>98.7</td>
<td>Rampur DCCB</td>
</tr>
</tbody>
</table>

Northern Region Total

<table>
<thead>
<tr>
<th>DCCB Name</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>31.03.15</td>
<td>Deoria Kasia DCCB</td>
</tr>
<tr>
<td>31.03.16</td>
<td>Deoria Kasia DCCB</td>
</tr>
<tr>
<td>31.03.17</td>
<td>Jaunpur DCCB</td>
</tr>
</tbody>
</table>

It can be seen from above, the NPAs range from 99.9% [UP] to 0.4% [same UP state]. This also indicates that the management of NPAs is also based on the practices adopted by the bank towards effective Credit risk management.

**Best Practices**

In spite of the fact that agricultural lending by its very nature is more risky, large number of DCCBs are able to achieve gross NPA of less than 5% and net NPA of less than 2% [even 0% NNPA]. Strategy to achieve these is a tall order but it is also observed that some DCCBs like Sangli in Maharashtra have been able to reduce NPA from High levels of above 65% to the manageable level.

When the Banks in short term cooperative structure work in the same environment [Government policy announcements of loan waiver], same product [almost 100% agriculture financing with major share going for crop loans], same types of clients [predominantly farmers], same regulators [Registrar cooperatives and RBI], same set of policy guidelines [GoI scheme of int. subvention on crop loans], why should they differ in their operating parameters.

After study of banks across the country, we can safely conclude that good banks do same things more effectively. They give more responsibilities to their directors, improve the quality of management, achieve better coordination with the machinery and people involved in revenue recovery mechanism, have better outreach with their
clients, study their requirements and are able to tweak their products as per the requirements of their clients.

The paper attempts to examine the set of policy initiatives shaped in these banks and steps taken by them to achieve such low levels of NPAs. These have been showcased in the subsequent pages with a view to encourage other bankers to replicate them elsewhere.

These efforts can be classified in the following subheads:

1. Due diligence and internal processes of the Management
2. Precise planning for recovery.
3. Cultivating new clients and adding members at the ground-Self Help groups, JLGs & Farmers Club
4. Strengthening PACS-Addressing imbalance and incentivising the recovery efforts at the PACS level.
5. Customer relationship building efforts of the Bank
6. Taking advantage of the provisions of the Cooperative societies Act for recovery.

Best Due Diligence Practices

a. Management due diligence and internal processes.

a.1 No new NPA - Thanjavur DCCB

Thanjavur DCCBs mantra towards NPA is “NNN” i.e No New NPA and “Catch NPA before they become NPA”.

Accordingly they are not having any new NPA at present. This is achieved by close monitoring of overdue accounts so that they are contained well before it has move to a NPA. They also ensure that “a borrower shall always remain a borrower and not become a defaulter”. Their strategies for curbing of NPAs are

- Correct Selection of borrower,
- Stringent procedures for sanction of loan,
- Monitoring of loan accounts and
- Continuous recovery process.

The bank is following the strategy as indicated below:

**A. Selection of the best borrower:** All efforts, from the PACS level to the DCCB level are taken to ensure proper selection of the borrower.
B. **Loan Policy**: Zero Percent tolerance in deviation from following the loan policy and procedures with regard to sanction and disbursement of loans. Deviation if any found is rectified then and there, the observations are also reviewed regularly in audit committee and risk management committee.

C. **Monitoring of old and new accounts borrower account**: Since, the bank has implemented CBS, all the loan accounts are monitored on a daily basis. Special reports are generated for monitoring of the borrower accounts and also to identify “**Early Warning Signals**”.

D. **Continuous recovery process**: The bank after analysing ground level situations has come to an conclusion that exclusive recovery teams at **HO** level is the need of the hour. Accordingly, the bank has constituted 3 recovery teams for recovery of loans, monitoring of loan accounts and giving loan repayment counselling for the borrowers.

E. **“Targeting the defaulters in the NPA account assets”** so that such assets become performing assets and bank dues are recovered.

### a.2 Belagavi District Central Cooperative Bank † Focus on Documentation, & Checklist

Strategy followed by the bank was as under:

A. **Strong controls before sanction of loan**: Strong focus on correct documentation as per the bank’s Check list is ensured. The Bank takes recourse to legal opinion also relating to legal title of the property, taken as security.

B. Loan are sanctioned under specific terms and conditions, which are followed by the branches concerned.

C. Further they to follow up with the customer for loan recovery on a regular basis and ensure that it does not become overdue / NPA. The bank has also formed recovery teams for every taluka level, for monitoring and recovery of loans

D. If the NPA loans are not recovered after all the procedure, they file the **ABN** case against the Borrowers.

E. The movement of NPA’s in last **18 years [ from 1999 to 2016]** was as under:

<table>
<thead>
<tr>
<th>Year</th>
<th>NPA %</th>
<th>Year</th>
<th>NPA %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999</td>
<td>16.48</td>
<td>2008</td>
<td>18.85</td>
</tr>
<tr>
<td>2001</td>
<td>19.46</td>
<td>2010</td>
<td>10.35</td>
</tr>
<tr>
<td>2002</td>
<td>21.13</td>
<td>2011</td>
<td>8.97</td>
</tr>
<tr>
<td>2003</td>
<td>31.47</td>
<td>2012</td>
<td>6.66</td>
</tr>
<tr>
<td>2004</td>
<td>31.99</td>
<td>2013</td>
<td>5.68</td>
</tr>
<tr>
<td>2005</td>
<td>41.65</td>
<td>2014</td>
<td>3.12</td>
</tr>
</tbody>
</table>
a.3 Internal Mechanism for prevention of NPAs  †  Process followed by Rajkot DCCB

Before sanction and disbursement of loan to the borrower, the bank follows the following aspect.

A. Identify the financial needs of the borrowers
B. Ensuring to providing geographical based activity specific credit product.
C. Loans issued based on “Income generation capacity” of the borrower /project
D. Loans issued based on Repayment capacity of the borrowers
E. Bank follows the 'MAST' principles of good security for loans † i.e. Marketability of asset, Ascertainty of value, Stability of value and Transferability of title.
F. Ensuring proper compilation of credit and security documentation, which will help for smooth disposal of the securities.
G. In case of Agriculture advance, repayment is synchronized with the harvesting season.
H. Provision of assistance from Board of Directors for recovery. They do not interfere either in making any recommendations or in loan appraisal process.

b. Precise planning of Recovery

As was observed in 3 States of Gujarat [ in Rajkot DCCB], Maharashtra [in Satara DCCB] and West Bengal [in Hooghly DCCB], the banks have adopted precise action plan for recovery of loans. In Rajkot and Satara which have gross NPA of less than 0.50% and in Hooghly which has recovery of over 95%, the Banks have perfected the task of precise recovery plan.

The recovery plan adopted by the banks consists of the following strategies:

A. The end use of loans sanctioned to prevent fund diversion is ensured by asset verification by bank officials.
B. Primary importance is given to the economics of the Scheme and the quality of asset created.
C. Each Borrower is personally contacted by concerned PACS Secretary, Branch manager and recovery officer, when the loan becomes overdue.
D. A well laid out plan of action is followed, in case of default. Starting from informal contact by the PACS Secretary, Board of PACS, issue of first notice

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</thead>
<tbody>
<tr>
<td>2006</td>
<td>22.19</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td>1.95</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>15.64</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td></td>
<td>2.99</td>
<td></td>
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</tbody>
</table>
by the PACS Secretary, followed by action under the provisions of Cooperative Societies Act.

E. Monthly meetings are arranged at Taluka level with Branch managers and PACS Secretaries for review of PACS wise targets and achievements, with regard to both loans issue and recovery.

F. The Banks encourage PACS to achieve 100% recovery. The PACS Secretary were incentivised for 100% recovery at the ground level and also for increasing the Business of the PACS.

G. Officers/inspectors are specially deputed to look after recovery process of large societies which have huge amount of demand and where committee members are not active.

H. Those who pay before time are assured of fresh loans. All the banks were also strong enough financially to meet the credit requirement of all its members.

I. In case of chronic defaults, recovery is made through public auction and attachment.

c. Cultivating new clients and adding members at the ground through Self Help groups, JLGs & Farmers Club

Hooghly DCCB as on 31st March 2017 had 26487 SHGs with total of 177701 members. These SHGs have a very healthy repayment rate of 98.47% [as on 31 March 2017]. The bank also has 385 Farmers club. The bank encourages these farmers club in helping Bank with the collection of overdue & NPA loans.

Similarly BIDAR DCCB has a client base of 16313 SHGs, of which 7967 SHGs are promoted by the PACS. 2337748 women are members of these 16313 SHGs. They are viable clients to the Bank. These SHGs have mobilised internal savings of over 50 crore for bank and repayment record is over 99%. Engaging with SHGs and JLGs is a sure way of reducing NPAs.

![Table](Table.png)

[Source: Web site of BIDAR DCCB]
Engaging with SHGs and JLGs also helps the bank in 2 more ways

i) **Increasing the membership of the ground level organisations [PACS]** and thereby the share capital of these institutions.

ii) Strengthening the mechanism of social collateral i.e., using the social influence of women SHG groups and farmers clubs in NPA recovery.

d. **Customer relationship Building**

Almost all banks having very low NPAs insist on maintaining a very strong relationship with its client’s. This is manifest in following ways:

A. Almost in all such Banks, the good client which pay their earlier loans are assured of fresh loans.

B. **Special Schemes of the bank for prompt paying Borrower:** Satara DCCB, in addition to that, offers interest rebates to farmers for timely repayment. Because of introduction of Debt waiver schemes for farmers members, the repayment culture / mentality of farmer members was getting impacted. To ensure that the borrowers do not getting influenced by such schemes, the bank had introduced many borrower benefit schemes, as under:

- The bank has a group insurance for 2.5 lakh borrowers, which offers Mediclaim to the borrower couple (borrower & spouse) as an **additional benefit** for prompt repayment.

- **Zero percent interest** is offered on Education Loans and Society godown / Building Construction Loan for prompt repaying borrowers. Bank has made provision of Rs. 117.00 lakhs for the year 2016-17 from its own profit.

- **Zero percent interest** on ST(SAO) loan upto Rs. 3.00 lakh on prompt repayment (the bank bears the 2% subvention for loans between Rs. 1.00 lakh and Rs. 3.00 lakh, which remains after GoI and State Govt, subvention).

- **Interest rebate for MT/LT loans:** Bank has introduced Interest rebate to the farmers on the interest for the current year instalment since last 3 years on the term loan for capital formation, as under:

<table>
<thead>
<tr>
<th>Sr No</th>
<th>Year</th>
<th>Actual Interest Rate charge</th>
<th>Percentage of Interest rebate offered on current year installment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2014-15</td>
<td>13%</td>
<td>10%</td>
</tr>
<tr>
<td>2</td>
<td>2015-16</td>
<td>13%</td>
<td>4%</td>
</tr>
<tr>
<td>3</td>
<td>2016-17</td>
<td>13%</td>
<td>2%</td>
</tr>
</tbody>
</table>

Agriculture Expert Advice:

- Rajkot DCC Bank has developed healthy relationship with farmers by providing expert agriculture advice at field level on plant nutrition, plant protection and marketing of agriculture produce by Agriculture officers of the banks.
- Bank is regularly organizing Crop Information Meeting ("Pak Shibir") at village level in association with State Co-Op. Bank, IFFCO, and KRIBHCO.
- Bank officials attend the AGM (Annual General Meeting) of PACS and guide for recovery and its benefits like crop insurance, lower interest rate, accidental insurance cover, medical help etc.

JLG finance to the landless farmers: Srikakulam DCCB has introduced JLG finance to the landless farmers and business people. Under this product the Bank made area based scheme on dairy with the help of DDM NABARD. Weaver card is also one of the important products for artisans. This has helped the bank in ensuring good recovery.

e. Strengthening PACS - Addressing imbalance and incentivising the recovery efforts at the PACS level.

Due to tier system of lending's and since the ultimate lender in case of STCCS is the primary society [PACS], there are frequent imbalance in the amount of principal and interest outstanding at the PACS level and borrowings O/S (principal and interest) by PACS at the DCCB level. Imbalances were one of the cause for overdues and NPAs at the DCCB level. Two Banks - Satara in Maharashtra and Sriganganagar in Rajasthan have taken preventive steps to address this major cause of NPAs – imbalances.

Imbalance Reduction Scheme in Satara DCCB:

The following were the major reason for imbalance, in the system:

a. Delay in Passing on of Recoveries: The loan amount recovered [principle and interest] at the PACS level is remitted to DCCBs with substantial delay by PACS. The DCCB while adjusting the remitted amount to the PACS dues adjusts it partly under interest and partly under principle. Due to the delayed passing on the recoveries by the PACS, the amount of interest payable by the PACS increases than the amount collected by PACS from its members. This results in imbalance of principal and interest outstandings. As these “Accounting entries” gets compounded over the years, in subsequent years, while DCCB shows O/S under Principal, there is no O/S under Principle at the PACS level, leading to imbalance in figures.

b. Use by PACS for Administrative Purposes: The recovered loan amount from the members, instead of passing on the same to its lender [DCCB] is utilised by
PACS for salary and other administrative expenses. Due to this, the PACS do not either pass on the recoveries or pass on only part of the recoveries to the DCCB. As a result, in subsequent years while DCCB shows O/S under Principle, there is no O/S principle at the PACS level leading to imbalance. [Accounting problems compounded over the years]

c. Fraud and embezzlement: Imbalance also occurs on account of fraud and embezzlement of cash at PACS level, resulting in non passing on of recoveries by PACS to DCCBs. [Same impact as in “B” above].

Recognising the fact that these “Imbalances” were impacting the flow of funds [to the farmer members of their area of operation] and regular recoveries, the bank adopted an innovative method for recovering and reducing these imbalance, by adopting **two fold strategy**, as under:

**A. Blocking of Imbalance Amount for Recovery:**

i) Imbalance amount as of 30.09.1997 of all the affected societies were identified and segregated separately under the head "Imbalance Amount Receivable". These were recovered from the PACS in 10 annual and equal instalments.

ii) Interest upto 30.09.1997, on the imbalance loan amount was also calculated. The bank segregated this interest amount into separate loan and recovered this in 10 annual equal instalments, separately.

iii) As a relief measure, charging of further interest on this blocked amount was waived off from that day and the amount paid by the PACS were credited to the respective accounts only.

iv) While recovering these instalments, care was taken to ensure that there would be no further imbalance at the PACS level.

v) To ensure such PACS do not slip further into imbalance on account of payment of these dues, the following strategies were adopted:

   a. PACS were encouraged to do higher loan business with higher interest rates to enable them to earn more income.

   b. Expenditure control was imposed on such PACS, with an instruction to incur expenditure only with the permission of bank/ Asst. Registrar. Unnecessary expenditure were thus controlled.

   c. Specific recovery plans were prepared for such PACS, under guidance and monitoring of the bank/AR/DDR to ensure full recovery of their current dues.

   d. Permission was given to obtain higher Share capital linkage from members, to increase their own funds.

   e. Incentives were given to the all those PACS which have complied to the above norms, to ensure cascading effect.
vi) The bank was thus able to recover the full imbalance amount from these PACS in 10 years’ time, from 1997.

**B. Introduction of Mirror accounting system in PACS:** To ensure that no further Imbalance is created at the PACS level and to minimise the occurrence of Frauds and embezzlement, the bank introduced a concept called Mirror accounting system. The bank took two specific steps for the same, to ensure that the PACS do not deal in cash, as under:

a) Each PACS was linked to nearby specified bank branch. This could be done as the bank had its own branch within 50 – 500 mt of every PACS.

b) Every cash transaction of the PACS member was linked to the specified branch. This was done through a mechanism of **three leaves receipt;** one for the customer, second one for the society and third for the Bank. Every borrower member when he repays the loan amount would pay it thru the branch only and not at PACS.

c) Due to the 3 leaves receipt system, the repayment made by the borrower gets accounted properly at both PACS [society copy] and DCCB [bank copy] level, thus effectively nullifying the chance of creation of imbalance.

This effective means that though loans and advances remain in the books of PACS, the actual cash transaction would take place in the branches.

Thus, while ensuring the full passing on of recoveries in the same proportion of the members’ payment, the bank had effective also eliminated the risk of frauds at the level of PACS and also got greater control over their operations.

The bank was able to effectively reduce imbalance by these methods, and ensure that further Imbalance does not recur in the future.

In case of Sriganganagar DCCB, the bank keeps a close watch on the PACS with imbalances. The position of Imbalance at the PACS level is as under:

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Year</th>
<th>PACS Total number</th>
<th>PACS having imbalance</th>
<th>% of PACS having imbalance</th>
<th>Imbalance amt. [Rs. in Crore]</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2014-15</td>
<td>320</td>
<td>19</td>
<td>5.9</td>
<td>10.78</td>
</tr>
<tr>
<td>2</td>
<td>2015-16</td>
<td>320</td>
<td>23</td>
<td>7.2</td>
<td>8.44</td>
</tr>
<tr>
<td>3</td>
<td>2016-17</td>
<td>323</td>
<td>49</td>
<td>15.2</td>
<td>12.50</td>
</tr>
</tbody>
</table>

The bank recognises that **not** containing imbalance at the PACS level would lead to **slackening** of bank’s effort in NPA management. Accordingly bank has taken following steps.

i) All such societies are subject to detailed annual inspection by Banks staff.
ii) Audit of the society is taken up by CA / Auditor from Cooperation department, Government of Rajasthan. The departmental auditor is asked to give detailed report on the reasons of imbalance.

iii) The Secretary of such PACS are being regularly trained and intensely monitored to increase the business of the Society.

iv) Bank Has put in place **e-recovery** – PACS Loan [OD] recovery management system to keep track of recovery action initiated under provision 99 & 100 of Rajasthan State Cooperative Societies Act, 2001. The system enables updated knowledge on notice/decree/kurki warrant on day to day basis.

The bank had indicated that due to these efforts, it was able to contain the imbalances to a large extent, which otherwise would have increased substantially, given the present recovery climate.

f. **Incentivising the recovery efforts at PACS level**

To ensure full recovery of its dues and with a view to pave way for competition amongst the PACS and to reward the better performing PACS, 3 DCCBs of our country, **[Satara, Sriganganagar and Rajkot]**, have adopted an incentive mechanism for the secretary and the Board of PACS, which are showing higher recoveries and increased business of the societies, as indicated below:

A. **Satara and Sriganganagar DCCBs:** The banks had adopted a “**Reward mechanism**”, by way of **Cash incentives** to the PACS / its Secretaries, which have achieved 100% recovery during the year. This paves the way for competition amongst the PACS and motivates the secretaries for taking up the task of recoveries, seriously.

B. **Rajkot Bank**: The incentive mechanism adopted by the bank was as under:

- The bank had introduced a scheme to give a **motor bike** to encourage the PACS for best performance in recovery, loan, administrative cost, social responsibility etc.
- PACS are divided in 4 groups as per their loan outstanding, from each group 3 PACS are selected.
- Every year 12 PACS are encouraged with a motor bike for recovery purpose.

**Role of the Board of Directors in NPA Management**

Since STCCS is a member driven institutions, Board of Directors play an important role in the overall functioning of the cooperative banks. Awareness and clarity of their **role**, helps in performing their expected **role**.
Being institutions functioning since long, many Boards of the DCCBs have understood their importance and have taken initiatives for the betterment of their banks.

A. In Satara DCCB, the following steps were taken:

1. To ensure that all loans are sanctioned to only the needy and correct members, sanction of all loans & advances (except Gold Loan and Loans against FD) are done by the Executive Committee/ BoD, based on the recommendations made by the officials headed by the CEO.
2. No sanctioning powers to given CEO/Departmental Heads/ Officers of any other sub-committees of the BoD.
3. Further the Board ensures that the Directors does not influence the bank in appraisal, adherence to policy and procedure, documentation, etc.
4. At the PACS level, if a defaulter is fugitive or those who have overdues for more than 5 years or if a defaulter has deceased, then such accounts are taken on agenda for coercive measures for recovery.
5. A separate action plan for recovery of such dues is prepared & implemented while joint recovery tour of Head office level & block level recovery officers. A meeting of BOD of PACS is arranged on the day of recovery tour.
6. Such chronic defaulters are called before the BOD members & asked to repay the overdue amount. The conversation in this regard are also noted in the proceedings of BOD meeting of PACS.

B. In Sriganganaagr DCCB the board of PACS pass a resolution for issue of notice under provisions of Rajasthan State Cooperative Societies Act.

Recovery through Tie up arrangements

As indicated earlier, there are many other cooperative institutions in the rural areas which function alongside the Cooperative banks in providing necessary assistance to the rural population. Having a strong tie up with each other would be a win win situation for all such institutions.

Recognising this fact, Satara DCC Bank has developed very strong linkages with the sugar mills working in the district, as indicated below:

1. Sugar mill members are provided with Crop loans by the DCCB to ensure availability of adequate sugar cane to the mill.
2. The sugar mills are also financed by the bank, strictly based on norms, after taking adequate security.
3. The sugar mill would also ensure to deduct the bank dues from its members sugar cane dues payable and pass on the same to the DCCB.
4. Since this is a regular arrangement, the bank had structured this arrangement properly, to ensure the recoveries are passed on to the bank in time, as under:

- The list of members loans outstanding including overdue amount & interest is prepared and submitted to sugar factories to tap due recovery.
- All the sugar factories extends best co-operation for making recovery out of Sugarcane crushing and proceed the recovery amount for credit to members loan outstanding.
- Sometimes some members provide sugarcane in respect of other names to avoid recovery. However the sugar factories takes action at the time of scrutiny and find out such borrowers.

5. In addition, PACs also submit the recovery memorandum to Milk Societies and Agriculture Produce Marketing Committee [APMC] to recover the due amount out of agricultural products.

6. All banks can work on this method for effective loan recovery. If needed, the State Governments should facilitate adjustment of outstanding /overdue loan amounts from the sale proceeds of the farmers produce.

g. Working within the provisions of the State Cooperative Societies Act for recovery of Dues

Normal measures to be adopted by bank officials for recovery of dues

1. Whenever, a borrower commits defaults on repayment of the loans [principal and interest], as per the dates specified in the Agreement, the Loan Account becomes 'Overdue'. Once the Loan A/c is an overdue A/c, then the Banker has necessarily to adopt measures which will result into recovery of overdue amounts.

2. The mechanism to be adopted by Co-op. Banks for effecting recovery of overdue amounts is indicated in the respective States Co-operative Societies Act and is more or less as indicated below:

   A. Whenever the borrower commits default in repayment of loan amount, immediately the bank should serve 'Preliminary Notices' to the principal borrower and the sureties advising them to repay the amount of overdues with interest etc. It must also be communicated that the bank shall proceed to take further action against the principal borrower and sureties in case of failure to repay the amount of loan/over dues, immediately.

   B. It has been often said “A stitch in time saves nine”. Thus, the banker must be vigilant, right from the disbursment of loan amount till the recovery of the
entire loan amount. There should be effective supervision over the amount of loan sanctioned.

C. After issue of such preliminary notices, there may be a positive response from the principal borrower and he may repay the amount of defaulted loan instalment, or the principal borrower and the surety may approach the authorities of the bank and may explain their genuine difficulties regarding repayment of loan amount or there may offer to repay the dues partially. There may be cases where there is no response from the borrower / sureties.

D. With this background, the bank should proceed further to devise such steps which will result in recovery of dues.

3. Recovery through salary / wages:

A. Under various State Cooperative Acts (e.g. Section 49 of M.C.S. Act 1960) it has been provided that if a member of a society. /Bank authorises his Employer to make deduction from his salary/wages, in order to satisfy the claims of the society/Bank, then on receipt of requisition letter from the concerned Bank, the Employer shall proceed to make deduction from the salary/wages from the concerned employee/member to meet the claims of the Bank. The Employer must remit the amount so deducted immediately to the Bank concerned.

B. Non-compliance of these provisions under the State Cooperative Act shall be constructed as 'offence' and further Civil and Criminal action can be instituted against such Erring Employer.

C. In addition to the above, there are provisions under the Indian Payment of Wages Act 1936 (vide Section 7(2) and Section 7(2)(j) which stipulates that the Employer shall make deduction from the salary/wages of an Employee to satisfy the claims of the Cooperative Society / Banks.

4. Settlement of Disputes under Revenue Recovery Act in States

- Based on the noting of the Management, the Board of Directors may pass a Resolution authorizing the Manager/or such other officer to file "Dispute Application" in the Co-op. Court against the defaulting principal borrower and his sureties [the opponents].
- As indicated in Section 91 of the MCS Act, the co-operative courts are empowers to decide on such ‘Disputes’. Section 95 further empowers the court to direct attachment of property.
• Section 96 of the MCS Act, provides that the Co-operative courts after giving reasonable opportunity to the parties to the dispute may make an award on the dispute.

• After hearing both sides, the court shall deliver a judgment in the open court. On the basis of the judgment, a final award / decree shall be passed.

• Under Section 97 of the MCS Act, an appeal against the decision under Section 96 or order under Section 95 can be made by the aggrieved party to the Co-operative Appellate Court within 2 months from the date of the decision or order.

5. **Power of the Registrar to issue Recovery Certificate:**
   A. Under the provisions of Section 101 of M.C.S. Act 1960, the **Registrar of Co-op. Societies** is competent to make an enquiry on the merits of the application made to him by a Co-op. Bank for grant of 'Recovery Certificate' against the borrowers and sureties.
   B. The Registrar shall apply 'The Principles of summery procedure' for disposal of such cases/applications.
   C. After hearing both parties, the Registrar, shall grant a Certificate that the opponents are in arrears and are responsible to pay the amount to the society with interest, cost of recovery etc.
   D. Once, 'The Certificate of Recovery' is issued it becomes 'Final'. The word 'Final' denotes that it is not appealable in any Court of Law.
   E. Thus, in short, the application under Section 101 is similar to that of 'dispute application'. We are required to enclose all the papers relevant to documents etc., alongwith the application under Section 101.
   F. The Co-op. Banks, after obtaining awards are required to execute the same so as to recover the decreed amount from the opponents.

6. **Award execution methods**
   A. There are following broad methods / measures by which an award can be executed.
      • By issue of Demand Notice to opponents directing them to repay the entire amount as mentioned in the award.
      • By attachment and sale of movable property.
      • By attachment and sale of immovable property.
      • Without attachment, in case of Mortgage Decree, immovable property can be sold out.
   B. The Registrar of Co-op. Societies in Maharashtra State, has also empowered the officials, not below the rank of Branch Manager of Co-op. Banks, to

The banks with low NPA are able to make effective use of the provisions of the Cooperative Societies Act of their respective states and the recovery machinery of the Registrar of Cooperative societies. This is clearly visible in Hooghly, Satara, Rajkot and Sriganganagar DCCBs.

Many Banks in the same states are not able to effectively utilise the statutory provisions for effecting bank recovery, thus increasing their overdues and NPAs resulting in increasing losses.

Use of Debt Recovery Tribunals [DRTs] and SARFAESI Act

1. Debt Recovery Tribunals [DRT] :
   A. The Debts Recovery Tribunals were established by the Government of India under an Act of Parliament (Act 51 of 1993) for expeditious adjudication and recovery of debts due to banks and financial institutions. Accordingly the DRTs were set up in different parts of the country as per the Recovery of Debts due to banks and Financial Institutions Act, 1993 and Debts Recovery Tribunal (Procedure) Rules, 1993.
   B. As per the provisions (Section 19) of the DRT Act, banks and financial Institutions could apply to the Tribunal for recovery of debts of Rs.10 Lakh or more by making an application called Original application to it.
   C. The Tribunal has powers to pass an interim order preventing the borrower from selling/ disposing off / tampering with the property and can pass orders for attaching the properties of the borrower in case it is satisfied that the latter may sell/ dispose off whole or part of the property.
   D. Further the Tribunal has powers to appoint a receiver for taking care of the property.
   E. Issue of Decree under section 19(20) of the Act: The Tribunal, after giving opportunities to both the parties, issues an order directing the borrower to pay a specific amount to the bank.
   F. Based on the order, the Tribunal then issues a certificate of recovery to the Recovery Officer (RO).
   G. The RO can then proceed to recover the amount by attachment & sale of property or by appointment of receiver for management of the property in terms of section 25 of the Act. As per Section 20 of the Act, the aggrieved party can file an appeal against the order of the DRT before the Appellate Tribunal within 45 days.
A. **SARFAESI Act, 2002**: The major 3 objectives of the Act is to regulate:

- Securitization and
- Reconstruction of financial assets and
- Enforcement of security interest.

B. From the point of view of the Cooperative Banks, the ‘Enforcement of security interest’ is of particular importance and use for recovery of their bad loans.

C. This is one of the most important provisions contained in the Act. The provisions are penal and gives a right to the lender to divest the property from a defaulting borrower, sell and recover the amount due.

D. To be successful under the Act, the lender has to strictly adhere to the various provisions and rules made under the Act.

E. The specialty of the Act is that the security interest can be enforced without intervention of the courts subject to procedures being followed as per provisions of the Act and the related Rules. Any slightest deviation in the procedure can lead to the whole exercise being a nullity in the eyes of law.

F. Procedure to be followed are as under:

- Under Section 13(2) of the Act, a 60 days’ notice has to be served by the bank on the borrower with a request to discharge the loan liability
- The notice must contain details of amount payable by the borrower and the security interest intended to be enforced.
- On receipt of notice, if the borrower makes a representation or raises an objection, the secured creditor must consider such representation or objection.
- If the secured creditor comes to the conclusion that the said representation or objection is not acceptable or tenable, he must communicate the reasons for non-acceptance of representation or objection within one week of receipt of the above.

G. **Modes Of Recovery Available** (S.13(4)) : If borrower fails to discharge the liability, secured creditor has the following options

- Take possession of secured asset
- Take over the management of the business of the borrower including the right to transfer by way of lease, sale, assignment, etc.
- The said rights must be exercised only where substantial part of business of borrower is held as security for the debt.
- Appoint a manager to manage the security asset taken over.
- Issue notice to persons who acquired the secured asset from the borrower or from whom money is due.
The CMM (chief metropolitan magistrate) or DM (district magistrate) is empowered even to use force necessary for taking steps towards securing compliance.

H. Non-application under the Act- Section 31: The exemptions under this Act i.e. properties which cannot be attached have been detailed in the schedule to the Act. Some of the important ones relevant for the Cooperative Banks are:

- Any security interest securing repayment of any financial assistance not exceeding Rs.1 lakh.
- Security interest not registered under this Act.
- Any security interest created in agricultural land.
- A lien on any goods, money or security given under the Indian Contract Act, 1872
- A pledge of movables u/s 172 of the Indian Contract Act
- Any conditional sale or hire-purchase or lease or any other contract in which no security interest has been created.
- Properties not liable to attachment under s.60 of CPC 1908 excluding properties specifically charged for raising the loan.
- The amount due is less than 20 per cent of the principal and interest

I. Miscellaneous aspects: No civil court has any jurisdiction under this Act. The Indian Limitation Act, 1963 is applicable to this Act.

The SARFAESI Rules specify as to who should be the AO of a bank, the place of serving of the Demand Notice, the mode of its delivery, measures to be taken if the amount mentioned in the notice is not paid- the manner of takeover of possession of property, steps to be taken thereafter, custody of property, manner in which the property could be sold, the manner of valuation of assets, serving of notice before sale & the contents of the sale notice, sale of assets & issuance of certificate of sale, appointment of Manager, procedure for recovery of shortfall of amount due to the bank.

A judicious utility of the available measures will greatly facilitate recovery of loans in banks.

**Conclusion † Future Road map**

Banks are highly levered entities compared to that of other business entities due to their nature of business. Besides bank’s assets are mainly financial assets value of which can go down sharply during the difficult times.
Cooperative banks are no exception to this rule. So all banks have to be operated within regulatory guidelines which stipulate several norms and procedures to contain risk. Imposition of prudential norms by the regulator, was more with an intention of ensuring that the banks do business in a prudent manner and not to restrict banks from issuing loans.

The best practices adopted by various banks have given positive results to them resulting in not only their sustainable viability, but also enabling them to serve their members better.

RBI, the regulator of banks, in the near future, is expected to adopt uniform standards for all types of banks for issuing/ extending license, which could be harsher for cooperative banks, than those that are imposed now. Further, the STCCS would be facing lot of competition from the new age banks such as Small finance banks and payment banks in addition to the RRBs, in the coming days.

Hence there is an urgent felt need for other banks of STCCS to adopt suitable NPA management practices, to attain current and sustainable viability. Banks have to design strategy in such a way that mistakes made earlier are not repeated in the future.

In view of the above, the following suggestions are made for the cooperative banks, towards achieving better NPA management.

1. **Loan Policy of the bank**: Every bank **must have** a Board approved Loan policy. The loan policy plays a vital role in creating awareness amongst its employees about their role in issue and recovery of loans. As indicated in Satara DCCBs policy, the banks management should ensure that the employees follow the policy in letter and spirit. The loan policy should clearly indicate the following:
   - The process to be followed while sanctioning the loan including the application formats and sanctioning powers.
   - The inspection process to be followed before processing the application process and the method of assessment of loans.
   - The security [both primary and collateral] and documentation types to be followed for different types of loans,
   - Disbursement norms including the drawing power calculation for CC /OD loans, along with margin requirement (**Ex**: Inventory ‡ 25%, receivable ‡ between 25% to 40% & Pledge ‡ 20%, Hypothecation ‡ 25 – 40%) and deviation powers, if any, of the top management.
• Post disbursement issue with regard to compliance to various sanction terms and conditions, including asset creation.

• The review and monitoring mechanism with detailed processes in each stage, including the frequency of inspection for a regular account and for a stressed account, needs to be specified. The review and monitoring mechanism should be separately specified for Short term loans, CC loans and Term loans.

• NPA management policy including tolerance level at the branches and strategy for managing them within acceptable benchmark.

• It should also mention the NPA handling issues and the reporting format of NPA.

• In short, the loan policy should clearly mention the complete procedures to be followed by the banks staff, under each type of loans.

Further, all the staff should be trained in the components of loan policy, for better adherence. The internal auditor and statutory auditor should also be requested to check the actual lending and its adherence to the set loan management policy.

2. Exposure norms: Given the divergent lending opportunities available to banks these days, all banks should have their own exposure norms, so as to ensure that all eggs are not put in one basket. These exposure norms needs be segregated into two categories. One, RBI/ NABARD imposed exposure norms, as indicated in CMA norms. The other should be Banks own internal exposure norms to be fixed taking into account the geographic specific activity that can be undertaken in their area of operation.

3. Principles of good lending: Principles of good lending means, the fundamental practices of lending, so that the loan portfolio would remain healthy. The starting point of good lending practices is the selection of the borrower. The borrower’s intention and his capability understood through borrowers study and banker’s opinion about the borrower are the important aspect of good lending. If these two things are observed accurately, the chances of NPA would come down substantially.

The other principles of lending include, understanding the requirement of fund, purpose of the loan, the stipulation of proper security for the lending, etc. Cooperative Banks need to incorporate this as a culture amongst its staff and Board members, including at the PACS level. This will go a long way in alleviating the problems of overdues and NPAs.

4. Customer Profiles: By default, most of the customers/ borrowers of STCCS are rural poor. Since the category of borrower is riskier, banks resort to under financing/ lower issue of loans. However this method is fraught with practical difficulties. This aspect of lending results in the rural poor availing further loans
from other sources at higher interest rates, resulting in multiple financing. When they not be able to generate the desired return required to repay the loan, they would first default to the banks, resulting in unrest for large number of people. In a democratic set up, this would led to government intervention and would eventually result in bad loan. Hence cooperative banks have to be careful and ensure that Scale of finance and Unit cost for all types of rural loans are fixed adequately and adequate loans are issued in time. Satara DCCB is found to have followed this principle successfully.

5. **Strengthening PACS:** Given the fact that the PACS are the final lending tier in the STCCS, without they being strong and financially viable, the structure cannot be viable for long. Hence measures taken by many DCCBs including Satara DCCB for strengthening the PACS, including suitable training and regular inspection, should be a inbuilt policy of all DCCBs/ StCBs. This should also include the mechanism for checking “Imbalances” and supporting the PACS both for appraising & recovery of loans and starting new business by them.

6. **Incentivising the recovery efforts at the PACS level:** Since majority of the loans are lent through PACS in the STCCS, recovery also should be initiated at their level. However, PACS get a very small margin in the loans recovered. Hence a few DCCBs have adopted an incentive mechanism for motivating the PACS to take proper steps for recovery. As done by Satara DCCB, banks can include this as a Reward mechanism, as part of their Recovery strategy.

7. **Customer relationship efforts:** Some DCCBs such as Satara, Rajkot, etc. have incorporated a specific policy in their plan of action to build up their relationship with their borrower members. Satara DCCB proudly calls itself a ‘Farmers bank” and have taken many steps for incentivising the prompt paying borrower members. Further, the borrowers are assured of fresh loans based on adequate Scale of finance/ Unit Cost. Such initiatives could also help the banks in ensuring better recovery, in these days of vitiating credit culture.

8. **Proper identification and classification of NPAs:** As RBI repeatedly emphasises, there is a strong need for system being able to give a feedback about the incipient signs of sickness in accounts much before they become NPA. RBI has devised a Category of Special Mention Accounts for non-agricultural loans within a window of 90 days [from default date to loan becoming NPA]. In agricultural advance, this window is 2 crop seasons. Banks must take advantage of this higher period for ensuring that loan accounts do not become NPA. SMA accounts should also trigger time bound action plan and banks should ensure adherence to the same.

9. **Recovery of Loans through the provisions of the State Acts:** Cooperative banks can recover outstanding loans through the mechanism provided in State...
Cooperative laws. Most of the States had comprehensive, self-contained and less expensive remedies available under the State Co-operative Societies Acts. They can be effectively put to use, provided the banks have put in place a proper mechanism. As this is an important aspect of NPA management, banks need to give more importance to this aspect. Banks may like to follow the good practices followed by banks such as Satara and Rajkot in this regard.

10. **Strategy for Prompt corrective action**: Whenever bank cross the risk thresholds in terms of CRAR, Gross and Net NPA and Return on assets, the bank’s Board or the RCS should initiate a prompt corrective action, to prevent further sliding of the parameter and to take steps to solve the related issues. The cooperative banks Board need to fix such threshold individually based on the geographical location and other factors and taken suitable action, as required.

11. **Movement from NPA identification to NPA resolution**: While NPA identification is also an important factor, NPA resolutions are more important in resolving the pertinent issues. Hence banks need to adopt suitable area specific NPA resolution mechanisms, for containing NPAs. The StCBs/ Cooperative federation can assist the banks in this regard. It should also involve a subset of activities like creating linkages with APMC, milk societies, sugar mill etc.

12. **Risk Mitigation Measures**: Banks by nature cannot avoid risks. Actually not taking risk is the biggest risk. However excess risks taking would lead to the collapse of the organisation. So proper approach to risk of its business would be to manage the risk. Proper identification of Market risk, Credit risk, Operational risk and liquidity risk and management of the same assumes prime importance. Banks should take suitable area specific steps, in this regard. The StCBs/ Cooperative federation can assist the banks in this regard.

13. **Implementation of OTS**: Under One Time Settlement (OTS) the borrower / guarantor presents a proposal to the lender for settlement of all the dues of the lender. Upon sanction by the lender, it becomes an agreement between the borrower and lender whereby the borrower/guarantor, make payments. Upon entire payments, the lender discharges the borrower of the debt and releases all the securities. OTS is a situation in which both the borrower and lender feel happy to have come out of the situation. Before envisaging strict action on chronic and wilful defaulters, banks may consider OTS scheme also, on case by case basis. Banks may formulate suitable internal policies in this regard, to be made known to the top and middle level management officials. OTS may be required for very old NPAs which are almost impossible to recover.

14. **Regulatory and supervisory policies of the State Government**: As cooperatives comes under the State list, State Governments also have a major role in the functioning of the banks. However, since RBI is the regulator of all
banks including the cooperative banks, the regulatory and supervisory policies of the RCS/ State Govt Cooperation department should be synchronised with the line of thinking of RBI and NABARD.

15. Mergers and Consolidation: There are DCCBs which may not be able to survive because of very high NPAs. Even though these are very few in numbers, their failure would result in very strong negative repercussions for all banks in Cooperative sector. The state government should seriously think about mergers and consolidation to avoid such situation.

16. Computerisation of STCCS: While most of the StCBs/ DCCBs have moved to the CBS platform, most of the PACS are still working in manual system. PACS of Kerala state have shown the way with regard to the benefits that can accrue on account of computerisation of banking system. Steps needs to be taken in this regard, by all concerned, for betterment of the cooperative system.

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