

REZORCE RESEARCH FOUNDATION

[REGISTERED UNDER THE INDIAN TRUSTS ACT, 1882]

Thursday, 10 October, 2013

The Chairman

Committee of Petitions – Rajya Sabha

Attention: Deputy Director – Rajya Sabha Secretariat – Shri. Rajendra Tiwari

Parliament House Annexe New Delhi 110001

Respected Sirs,

Sub: **Bill Number 12 – Rajya Sabha Committee of Petitions**

- Petition praying to take immediate steps to control the increasing Non-Performing Assets (NPAs) in the Banking Sector

Ref: Your advertisement in The Hindu, Bangalore

Rezorce Research Foundation is the R & D Wing of Rezorce Managed Solutions Pvt. Ltd., Bangalore [www.rezorce.com].

Rezorce is a business intelligence company. Identification of absconding clients [delinquent clients] is one of Rezorce key competencies. Absconding clients are those bank and financial institution customers who have disappeared after taking loans. We have **four patents** pending in the area. We have a successful track record working with institutions both the private and public sector around India.

The response to this petition is based on our experience dealing with NPA clients.

Our response is limited to Section 1.1 (i) – Government should take immediate steps to correct the increasing NPAs.

Our Suggestions - Key Elements

The key elements of this response are:

1. Mandatory Listing of all loans given to private and public sector companies in the Ministry of Company Affairs, GOI database
2. Mandatory recording of all land mortgages with the state land record authority
3. Framework for industry – wide listing of defaulters – Company as well as Directors – covering all banks and financial institutions – going beyond credit reports
4. Mandatory validation of basic KYC documents shared by borrowers at the time of giving loans
5. Withholding funding for new projects when projects promoted by same promoters are NPA.

Detailed Submissions

1. Mandatory Listing in MCA, GOI Records

We notice NPA companies closing down and Directors absconding. Most times the loans are given on land and machinery hypothecation and personal pledge of Directors. In cases where land and machinery are given as hypothecation, Ministry of Company Affairs provides for registration of such hypothecation with the Government. Banks insist on borrowers to pay for the stamp duty and registration charges.

Some managers insist on borrowers to go through with the hypothecation process with MCA. Others are not so insistent. We find many cases where loans given to companies are not registered at all. Companies legally close down, even when they are NPA with banks and institutions.

The advantages of such registration include:

1. All lenders can access government records and verify the extent of loan and the details of hypothecation
2. Companies cannot close their operations and move on, since MCA insists on banks' written concurrence to close the operations
3. Customers and vendors can also gauge the extent of exposure the company has to banks and facilities availed thereof.

Governmental Intervention

1. Government insists on mandatory compliance of document filing with MCA of all loans taken by any private or public limited companies whenever a credit facility is availed, irrespective of the size of the loan.
2. The documents must be filed, irrespective of whether any fixed asset is shared as security or not
3. Mandatory internal and departmental audits to ensure compliance of such document filing for new loans given and any credit enhancement
4. The compliance should include banks, financial institutions and NBFC
5. In order to reduce compliance charges, the stamp duty value and filing fee may be reduced

2. Mandatory Recording of all Land Mortgages

When land and / or buildings are hypothecated, it is necessary to register the encumbrance with the relevant Sub – Registrar of the State Revenue Department.

Banks insist on borrowers to independently go through the process and share such proof with the banks. This is done since banks do not have the physical manpower to do the process themselves.

It is not the duty of the borrower to run around for registration of the encumbrance. Such registration does not help the borrower in any manner. If due to work pressure, carelessness or connivance such registration does not happen, then the borrower is at liberty to sell the hypothecated property to someone else with duplicate papers.

The loophole must be plugged by fixing responsibility of such hypothecation on banks or financial institutions instead of borrowers.

Governmental Intervention

1. Government insists on mandatory compliance of hypothecation of all property documents with the concerned sub – registrar
2. Banks / financial institutions must arrange for a special officer to be a part of such registration and not leave it to borrowers to complete the compliance process
3. Mandatory internal and departmental audits to ensure compliance of such document filing
4. Jurisdictional Sub Registrars to be held accountable under criminal sections if such hypothecated property is allowed to be sold by the borrower.

2. Nation – wide, Industry Framework of NPA Holders

Credit Bureau reports are considered for decision making today. In today's situation, Companies and Directors are considered as independent entities for purpose of credit rating. The situation encourages serial defaulters to open and operate new companies and approach different banks or branches in different states to take new loans.

The process of linking companies and directors as single entities for assessing credit worthiness may be sticky and difficult to implement.

The government must initiate a new industry – wide, national framework of NPA holders that can link companies and directors. Banks and financial institutions [including micro finance companies] can contribute to list their existing NPA on an online portal that can be managed by the industry itself. The framework can link the company with promoters. Any corporate loans availed by promoters that have been become NPA anywhere in India can be tracked. In addition to the credit bureau reports, bankers will mine for defaulter information in this framework

This framework shall be an effective safeguard against serial promoters – both in the large scale and MSME sectors - who avail institutional credit and mis-utilize credit before moving to a new location and starting the same process all over again. It helps that their personal credit history is extremely clean and only their companies bleed.

Governmental Intervention

1. Providing a legal framework for establishment of such a nation – wide, industry – wide, online framework where banks manage information for mutual benefit

4. Mandatory Document Validation

We live in a technology era where any photo identity document can be created or morphed using color photo – copying machines and software like Photoshop. In addition to fraudulent creation of records, it is common for people to share dated information to obtain loans. Old Voter ID, Ration Card or DL with dated address information is used as KYC proof at the time of taking loans.]

Bankers are totally ill – equipped to handle frauds that frequently happen in these cases. Validating documents can reduce willful defaults by a large percentage. Willful defaulters generally plan and execute their schemes well. Providing untraceable information is a part of the game.

E-Governance investments across the country provide an opportunity for prevention of such frauds and NPA due to willful defaults. It but takes a couple of rupees and a few minutes of time for a trained person to check identity, address and land record information online.

Governmental Intervention

1. Make mandatory KYC document validation for both banks and financial institutions.
2. Mandatory internal and departmental audits to ensure compliance of such document verification

5. Withholding New Facilities for Existing NPA Groups

Promoters have a responsibility to ensure that their projects succeed, especially when it is funded with public money. Promoters, who have NPA in one company, must not be given additional facilities for any other group company till the NPA are cleared.

For taxation purposes, many large industrial groups have one or more companies on NPA, even while they enjoy all banking facilities for other group companies. Banks also generally treat company on merit and a performing company is not denied banking facility, since the company may move to a competitor.

Government should mandate banks against extending any new facility and withdrawing existing facilities for all group companies if even one company promoted by the same promoter is NPA.

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Governmental Intervention

1. Advise RBI to introduce process to recall credit / advance facility to all group companies / companies by same promoters if any one company becomes NPA
2. Introduce a process to take existing bank NOC to open a fresh account with another bank, if any group company has NPA.

We are prepared to appear before the committee if airfare is reimbursed.

Thanks and regards

Yours sincerely

For Rezorce Research Foundation



Narendra KV

Director and Managing Trustee

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