

SUMMARY NOTE ON RIA PROJECT IN FINANCIAL SECTOR

CUTS has conducted Regulatory Impact Assessment (RIA) exercise on select legislations in banking (focusing on debt recovery laws in India). Key findings are highlighted below:

1. Baseline Scenario

DRT Act

- Insufficient number of Recovery Tribunals (RTs) - 39 Debt Recovery Tribunals (DRTs) and 5 Debt Recovery Appellate Tribunals (DRATs)
- Inadequate composition – One Preceding Officer (PO) per DRT and One Chairperson per DRAT
- Inadequate qualification of PO and Chairperson and sub-optimal composition, i.e., absence of technical member
- Absence of incentive - disincentive system for PO and Chairperson
- Absence of mandatory time limits for disposal of matters (existence of recommendatory timeline)
- Sub-optimal process of filing vacancies
- Multiple adjournments (despite having statutory provision)
- Exercise of jurisdiction by other courts/authorities
- Absence of clarity on priority of creditors' claims

SARFAESI Act

- Absence of time period for Chief Metropolitan Magistrate (CMM)/ District Magistrate (DM) to take possession of secured assets
- No accountability if application is not disposed of by DRTs/DRATs within prescribed period
- Exercise of jurisdiction by other judicial *foras*
- Taking over management by secured creditors for limited period
- Lack of clarity on process of taking over of possession, when actual possession is with third party
- No guidance on determination of correct valuation of security
- Requirement for consent of borrower for sale of movable property
- No priority to claims of secured creditors

2. Estimation of costs (key findings)

- Total opportunity cost due to delay in debt recovery (of up to four years) has been estimated up to Rs. 35,000 cr. on a consolidated basis (DRT Act and SARFAESI Act)
- Low debt recovery has resulted in credit risk premium of around 300 basis points, resulting in high cost of funds (*Raghuram Rajan address*)
- Opportunity cost of litigation for fiscal 2013-14 has been estimated around Rs. 2,000 cr.
- Social cost of the amount of loans written off by commercial banks in last five years (i.e., Rs.1,61,018 cr., equivalent to 1.27 per cent of GDP) would have allowed 1.5 million of the poorest children to get a full university degree from top private universities of the country (*Raghuram Rajan address*)

3. Recommendations (based on the cost-benefit analysis)

DRT Act

- Increase in number of DRTs to 63 from existing 39 (*estimated additional cost – Rs. 63 crore in addition to infrastructure cost*)
- Technical members should be inducted in the DRTs and DRATs (*estimated additional cost – Rs. 6.60 crore per annum*)
- Constitution of independent advisory body to recommend candidates for appointments (*estimated additional cost – Rs. 20.40 lakhs per annum*)
- Increasing cost of adjournments to litigants through increased adjournment fee (*estimated additional cost to litigants for first additional amendments – Rs. 37.50 crore*)

SARFAESI Act

- Specific time period to be provided for CMM/DM to take possession (*Increase in administration and management costs of Magistrate*)
- Statutory provision of additional management fee for the secured creditor (*Increase in cost to borrower in terms of greater fund outflow and delayed repossession of secured asset*)
- Statutory penalties in case of unjustifiable challenge before RTs (*estimated additional salary cost – Rs. 2.64 crore per annum*)

Common Issues

- Provision for mandatory time limit with reimbursement of application fee on non-compliance (*Estimated reimbursement cost to RTs/ government - Rs. 24 crore per annum*)



- Penalising the party approaching other courts/ judicial authorities (*additional litigation cost to parties approaching other judicial authorities*)

4. Findings in relation to law making process

- The DRT Act and SARFAESI Act (legislations under review) and their subsequent amendments, were passed through the ordinance route.
- While developing policies/ regulations, limited thought seem to be given to implementation bottlenecks, capacity of regulatory institutions and regulated entities, resulting in good provisions remaining ineffective. As a result, government end up bearing significant costs of regulation, and also faces the flak of the non-attainment of objectives.

Note: These are initial findings and the project reports are under finalisation.
