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Why And How Bankers Conceal Non Performing Assets (NPAs)

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Identifying potential NPAs in banking sector is a challenging job and requires a lot of skillfulness on the part of the lender. Skill can be acquired through formal training as well as through experience in loans department. Identification of potential NPAs can be undertaken through different direct or indirect signals of an asset which have been discussed in the previous chapter. If signals are identified and action is taken in time, occurrence of NPAs can be avoided. In present chapter, monitoring of NPAs has been discussed in detail along with other issues of hiding of NPAs and credit information sharing. Data has been included in few selected points which could be collected from various branches of the public sector banks.

REVIEW OF LITERATURE

Kalra (2012) has observed that provisioning norms which are set by Reserve Bank of India gave imagining results relating to nonperforming assets. High level of NPAs in banking industry has attracted public as well as foreign researchers to analyse its reasons.

Kamra (2013) has analysed the nonperforming assets (NPAs)of three selected nationalised banks namely State Bank Of India (SBI), Punjab National Bank (PNB), and Central Bank Of India (CBI). He concluded that banks are judged these days neither by no. of branches nor by the volume of deposits they attract in the market rather by the quality of assets which their balance-sheet possess.

Sikdar and Makkad (2013) concluded that non- performing assets are a standard criterion for assessing the credit risk of the commercial banks. They studied annual reports of the banks to know about the steps taken by banks to reduce existing NPAs.

Dr. Ganesan and Santhana (2013) in their paper titled "Non Performing Assets: A study of State Bank of India" have done elaborated study for State Bank's sources and deployment of funds and for gross and net NPAs, their impact on the profitability of SBI.

Shalini (2013) pointed out the significant role that credit management plays and includes planning, organizing, controlling, directing and coordinating the credit policies in order to eliminate the NPAs from banker's balance sheet and make them more profitable.

Mahajan (2014) in his article named "Trends of NPAs in Indian Banking Sector" has examined the dimensional approach of NPAs in the banking system with special focus on concept of NPAs in Indian banking sector in comparison to global companies. He made a study of NPAs of five different countries namely Brazil, Russia, India, China and South Africa (BRICKS).

Pawar (2015) in his research paper, "Management of Selected Commercial Cooperative Banks in Gujarat" has discussed about management of NPAs by selected Commercial Cooperative Banks

OBJECTIVE OF THE STUDY

To analyse why and how bankers conceal Non Performing Assets (NPAs)

It is not only the bankers who need to focus on the asset quality, but also the regulators. Concealing NPAs is a normal practice in Indian banking. Now, not only the RBI is issuing guidelines to monitor stressed assets but the Finance Ministry is also taking up the issue seriously. The Reserve Bank has directed all Public Sector Bank branches (PSBs) to manage these assets in such a way so as to be more transparent in their reporting. But, bankers follow their own style of working. Various practices are reportedly being adopted by the commercial banks to window dress the NPA advances so as to somehow defer declaration of such accounts as NPA accounts.

It is undoubtedly an illegal practice. Hence, no leads on such accounts are directly available in the banks. No clues to this can be found in the balance sheet as well as other records of the bank. Such information could be known only by way of informal discussions with the customers and the bank officials who provided information hesitantly and on condition of strict anonymity. Therefore, evidences provided in this section have limited reliability. However going by the objectives of the study, we have tried to analyze this aspect also though concrete evidences in this regard could not be generated. Hence with these limitations we produce below the practices being generally adopted by the banks to conceal or defer the declaration of NPAs.

1) In cash credit accounts, main/ primary security with the bank is stock of raw material, finished and semi finished goods lying with the borrower. The borrower has to submit stock statement in respect of the stock being held by him. The periodicity of such statement may vary from one limit to another from one month to a year. On the basis of such stock statement a drawing power in cash credit limit to the borrower is allocated. With the introduction of core banking solution(CBS) system in the bank, on the cut off date the computer system marks the drawing power of the borrower limit as Nil in case figure of total stocks as per stock statement submitted by the borrower is not fed into it. Accordingly, debit operations in the account are not allowed. Non submission of the stock statement continuously for six months automatically converts the account in NPA advance. Now, during our study, it was observed that stock statement in the case of a number of clients of the bank were not being received at regular intervals, and at the stipulated time. However, in the computer system, the figure of the stock was being fed into by the branch official on their own. Accordingly, drawing power (DP) was being allowed in such accounts in clear violation of the guidelines of the bank in this regard. In some of the accounts, stock statement for the last six to nine months were not received; but still such borrowers continued to enjoy the facility afforded by the bank.
2) Cash credit limit is required to be renewed once in a year. At the time of renewal, borrower has to submit financial papers to the bank and on the basis of these financial papers, fresh appraisal of the limit sanctioned to the borrower is conducted. It is only after the appraisal, the limit of the borrower is renewed and drawing power is allowed. If a particular limit remains overdue for renewal for a period of 180 days, the same falls into the NPA category on technical grounds. During our visits to various branches, it was noticed that in spite of repeated reminders by the banks, the concerned borrower did not submit the financial papers. However, the branch official was reportedly marking date of renewal into the system on their own. It was further noticed that the credit summations in some of these accounts was on a very lower side in proportion to the limit sanctioned, hence showing sticky signs.
3) In the case of certain accounts, branch officials in order to defer/ postpone the declaration of NPA initiated certain transaction to the credit of the sticky accounts. The said credit entries were being made by debiting some other account with the branch, though with the consent of the said account holder. This practice again is quite risky and tantamount to breach of basic principles of lending. In a particular case, the borrower was unable to repay the amount so arranged by the bankers from the other amount, thus ultimately causing financial loss to some other persons. The account of this particular borrower was declared as NPA advances after a gap of three months.

4) Restructuring of loan is another tool in the hands of the bankers which is, of course legal. While restructuring, the bank officials extend the term of the loan with a certain period so as to provide leverage to the borrower to regularize the account. It was also noticed during visits to branches that certain accounts were being restructured without proper appraisal of the facts and circumstances of the particular case.

5) Bankers who are on the verge of transfer or retirement sometimes resort to such practices so as to defer the slippage of certain accounts. In one such incident, one of the branch managers who was due to get transferred allowed certain adhoc facility to the borrower so as to postpone the slippage of account into NPA category. Eventually after the transfer of the concerned branch manager the account was categorized as NPA and the bank branch suffered a loss of amount Rs. 30.00 crore in the said case.(Reference: G.H. Agro in PNB)

WHY BANK BRANCHES CONCEAL NPAs?

In banking sector, CEO’s salary is in no way related to occurrence of bad loans. So bank branches high level officials care least about NPAs occurrence, and its timely reporting as well as controlling at the right end.

RBI’s former governor, Mr. RaghuramRajan while delivering the Dr. VerghereKurien Memorial Lecture at Institute of Rural Management, Anand (IRMA) stressed for keeping the sanctity of the debt contract not only by the small borrowers but also by the large borrowers as many of large borrowers regard it as their divine right to get discounts from the banks. Mr. Rajan also emphasized that the major issue these days is to identify the problem loans in time so as to deal with these quickly. Hiding the problem and pushing it for future is not a way to deal with issue and is totally a bad idea. Keeping NPAs in branches balance sheets makes their financial picture as not transmitting or reflecting ones. Same way, bad image goes to all investor analysts (The Times of India, 2014).This may be the reason for hiding of NPAs by the banks. Following are some of the reasons that may prevent bank branches to disclose NPAs at right time.

1. For fear of their jobs, career promotions (bank employees).
2. To maintain goodwill in the market for attracting more deposits.
3. Bank branches lack autonomy in their functions. They play according to the directions given to them from the top.
4. Disguised NPAs are operated in banking books till the time they are promoted and shifted to some other branch. Till that time, reframing of the account goes on.
5. Bank officials are making promises to big ticket accounts for not classifying their accounts as NPAs till the last moment, i.e. till branch power permits.
6. NPAs are disclosed only once in every quarter in the accounts of the bank branch. So, in order to oblige the customers, bank branches keep bad loans away from their accounts and sound financial results are disclosed by putting those accounts under restructure schemes and showing them as “restructured assets” in the books.
7. Lure of bank branches to keep their old customers with them puts them under pressure to hide actual position of accounts. For that purpose, many a times bad practices are followed by bank branches (Field Study and The Times of India, July 12, 2014).

How Bank Branches Conceal NPAs?

1. By making adjustment entry from someone’s other accounts in the branch for only one/two days. (So that account is not transferred to NPAs category).
2. Depositing cash from Bank’s own cash-in-hand for one day.
3. In case NPA occurs due to non-submission of stock statement, then bank branches sometimes enter the amount of stock in the system and allow the drawing power to the borrower, thus regularizing the sticky account.

4. Non-Submission of financial papers by the borrowers is shown as having been received by the bank branch.
5. Accounts are rephrased /restructured without their proper appraisal, i.e. whether there is a need to restructure is not properly visualized and the borrower is unduly accommodated.

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