

November 30, 2007

All Scheduled Commercial Banks
(Excluding RRBs)

Dear Sir,

**Mid-Term Review of the Annual Policy for the year 2007- 08:
Recovery Agents engaged by banks – Draft guidelines**

Please refer to the paragraphs 172 and 173 of the mid-term review of the Annual Policy for the year 2007-08, a copy of which is furnished in Annex 1. In view of the rise in the number of litigations against banks in the recent past for engaging recovery agents, it is felt that the adverse publicity might result in serious reputation risk not only for the bank concerned but also for the banking sector as a whole. An urgent need has, therefore, arisen to review the policy, practice and procedure involved in engagement of recovery agents by banks in India. In this backdrop, the Reserve Bank proposes to issue operational guidelines for adoption by all commercial banks, which are furnished in the Annex 2. The issue of extending similar guidelines to NBFCs, as appropriate, is being considered separately.

2. You may please furnish your views and comments on the proposed guidelines within a period of one month from the date of this letter. Views and comments in this regard may please be addressed to the undersigned at the under-mentioned address or may be sent by email:

12th Floor, Central Office Building,
Reserve Bank of India
Shahid Bhagat Singh Road, Fort,
Mumbai – 400 001
Fax : 022 - 22705691

Yours faithfully

(Prashant Saran)
Chief General Manager-in-Charge

Extracts of Paragraphs 172 and 173 of the Mid-term review of the Annual Policy for the year 2007-08

(f) Recovery Agents Engaged by Banks

172. In view of the rise in the number of litigations against banks for engaging recovery agents in the recent past, it is felt that the adverse publicity could result in serious reputational risk for the banking sector as a whole. An urgent need has, therefore, arisen to review the policy, practice, procedure involved in the engagement of recovery agents by banks in India. Accordingly, banks are urged to follow prescribed specific considerations while engaging recovery agents.

173. Complaints received by the Reserve Bank regarding abusive practices followed by a bank's recovery agents would invite serious supervisory disapproval. The Reserve Bank would consider imposing a temporary ban (or even a permanent ban in case of persistent abusive practices) for engaging recovery agents on those banks where strictures have been passed/ penalties have been imposed by a High Court/Supreme Court or against its Directors/Officers with regard to the abusive practices followed by their recovery agents. An operational circular in this regard would be issued by November 15, 2007.

**Mid-Term Review of the Annual Policy for the year 2007- 08:
Recovery Agents engaged by banks – Draft guidelines**

There has been a rise in the number of litigations against banks and adverse publicity in the recent past for engaging recovery agents. The consequent likely implications for reputation risk not only for the bank concerned but also for the banking sector as a whole has necessitated a review of the policy, practice and procedure involved in engagement of recovery agents by banks in India. In this backdrop, the Reserve Bank proposes to issue the following operational guidelines for adoption by all commercial banks. A reference to 'agent' in these guidelines would include agencies engaged by the bank and their agents / employees, as well as the bank's own employees.

Engagement of Recovery Agents

2. Banks are advised to take into account the following specific aspects while engaging recovery agents:

- (i) Banks should have a due diligence process in place for engagement of recovery agents, which should be so structured to cover, among others, individuals involved in the recovery process.
- (ii) To ensure due notice and appropriate authorization by the banks, they should inform the borrower the details of recovery agents engaged for the purpose, while forwarding default cases to the recovery agents. The details should include their telephone numbers etc. The recovery agents should call the borrowers only from telephone numbers notified to the borrower.
- (iii) Each bank should have a mechanism whereby the borrowers' grievances with regard to the recovery process can be addressed. The details of the mechanism should also be furnished to the borrower while advising the details of the recovery agent as at item (ii) above.

Methods followed by Recovery Agents

(iv) It is understood that some banks set very stiff recovery targets or offer high incentives to recovery agents. These have, in turn, induced the recovery agents to use intimidatory and questionable methods for recovery of dues. Banks are, therefore, advised to ensure that the contracts with the recovery agents do not induce adoption of uncivilized, unlawful and questionable behaviour or recovery process.

(v) A reference is invited to para 2 (v) (c) of Circular DBOD.Leg.No.BC.104/09.07.007 /2002-03 dated May 5, 2003 regarding Guidelines on Fair Practices Code for Lenders and para 6.3 of the Master Circular DBOD.FSD.BC.17/ 24.01.11/2007-08 dated July 2, 2007 on Credit Card Operations. In terms of these guidelines, banks were advised that in the matter of recovery of loans, (a) the lenders should not resort to undue harassment viz. persistently bothering the borrowers at odd hours, use of muscle power for recovery of loans, etc. (b) the banks should ensure that agents engaged by them for debt collection refrain from action/s that could damage the integrity and reputation of the bank (c) their agents should not resort to intimidation or harassment of any kind, either verbal or physical, against any person in their debt collection efforts, including acts intended to humiliate publicly or intrude into the privacy of the borrowers'/ credit card holders' family members, referees and friends, making threatening and anonymous calls or making false and misleading representations.

(vi) A reference is also invited to paragraph 6 of the "Code of Bank's Commitment to Customers" (BCSBI Code) whereby banks are required to strictly abide by the codes pertaining to collection of dues.

Training for Recovery Agents

(vii) In terms of Para 5.7.1 of our Circular DBOD.NO.BP. 40/ 21.04.158/ 2006-07 dated November 3, 2006, on guidelines on managing risks and code of conduct in outsourcing of financial services by banks, banks were advised that they should ensure that, among others, the recovery agents are properly trained to handle with care and sensitivity, their responsibilities, in particular aspects like hours of calling, privacy of customer information etc.

(viii) Reserve Bank has requested the Indian Banks' Association to formulate, in consultation with Indian Institute of Banking and Finance (IIBF), a certificate course for Direct Sales Agents / Direct Marketing Agents / Recovery Agents with minimum 100 hours of training. Once the above course is introduced by IIBF, banks should ensure that over a period of one year all their Recovery Agents undergo the above training and obtain the certificate from the above institute. Further, the service providers engaged by banks should also employ only such personnel who have undergone the above training and obtained the certificate from the IIBF.

Taking possession of property mortgaged / hypothecated to banks

(ix) In a recent case which came up before the Honourable Supreme Court, the Honourable Court observed that we are governed by rule of law in the country and the recovery of loans or seizure of vehicles could be done only through legal means. In this connection it may be mentioned that the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) and the Security Interest (Enforcement) Rules, 2002 framed thereunder have laid down well defined procedures not only for enforcing security interest but also for auctioning the movable and immovable property after enforcing the security interest. It is, therefore, desirable that banks rely only on legal remedies available under the relevant statutes which allow the banks to enforce the security interest without intervention of the Courts.

(x) Where banks have incorporated a re-possession clause in the contract with the borrower and rely on such re-possession clause for enforcing their rights, they should ensure that such repossession clause is legally valid, is clearly brought to the notice of the borrower at the time of execution of the contract, and the contract contains terms and conditions regarding (a) notice period to be given to the customers before taking possession (b) the procedure which the bank would follow for taking possession of the property and (c) the procedure which the bank would follow for sale / auction of property. This is expected to ensure that there is adequate upfront transparency and the bank is effectively addressing its legal and reputation risks.

Use of forum of Lok Adalats

(xi) The Honourable Supreme Court also observed that loans, personal loans, credit card loans and housing loans with less than Rs.10 lakh can be referred to Lok Adalats. In this connection, banks' attention is invited to Circular DBOD.No.Leg.BC.21/09.06.002/2004-05 dated August 3, 2004 wherein they were advised to use the forum of Lok Adalats organized by Civil Courts for recovery of loans. Banks are advised that they should preferably use the forum of Lok Adalats for recovery of personal loans, credit card loans or housing loans with less than Rs.10 lakh as suggested by the Honourable Supreme Court.

3. Banks, as principals, are responsible for the actions of their agents. Hence, they should ensure that their agents engaged for recovery of their dues should strictly adhere to the above guidelines and instructions, including the BCSBI Code, while engaged in the process of recovery of dues.

4. Complaints received by Reserve Bank regarding violation of the above guidelines and adoption of abusive practices followed by banks' recovery agents would be viewed seriously. Reserve Bank may consider imposing a ban on a bank from engaging recovery agents in a particular area, either jurisdictional or functional, for a limited period. In case of persistent breach of above guidelines, Reserve Bank may consider extending the period of ban or the area of ban. Similar supervisory action could be attracted when the High Courts or the Supreme Court pass strictures or impose penalties against any bank or its Directors/ Officers/ agents with regard to policy, practice and procedure related to the recovery process.