Responsible Banking
Working Paper 3

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Promoting Human Rights in Business

Disclosure can stop cronyism:

How irresponsible lending can be stopped through transparent public disclosure[1]

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Abstract

This working paper explores how lending behavior and practices of banks have created a NonPerforming Asset crisis in India, where loans to capitalists continue to be written off but, surprisingly, small loans given to small businessmen and farmers are chased through recovery agents. Are bank lending practices determined by a kind of cronyism? Are there ways of making the system more transparent and accountable? This paper touches on these questions and offers some ways forward.

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Vijay Mallya, well-known industrialist and Chairman of United Breweries Group, who founded the now defunct Kingfisher Airlines, is charged with up to 22 cases in various courts because of loan default of Rs 9,091.40 crore as on November 30, 2015. He left the country on March 2, 2016 and the Public Sector Banks to whom he owed this huge amount filed a case against him in the Debt Recovery Tribunal. In August 2014, the State Bank of India sent a notice to the borrower wherein it alleged Kingfisher Airlines of fund diversion to other United Breweries Group companies and held the parent company, United Breweries Group, responsible for 'deliberately avoiding payment to lenders'[2]. K C Chakravarty, former deputy governor of the Reserve Bank of India stated, "The Kingfisher case is an example of collective failure of the system. The banks should have declared it a NPA much earlier. Why did the RBI even clear the restructuring of Kingfisher?"[3]

Yet Vijay Mallya is only the tip of the iceberg. Together all the willful defaulters owe stateowned banks at least Rs 64,335 crore.[45]

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[1] This is a revised version of the chapter that appeared in the Status of CSR Report, Corporate Responsibility Watch, 2016

[2] http://indianexpress.com/article/explained/what-is-vijay-mallya-accused-of/

[3] http://indianexpress.com/article/india/india-news-india/sunday-story-once-upon-a-time-there-was-a-kingvijaymallya/

[4] At the end of September 2015, State Bank of India had the most willful defaulters — 1,160 — who owed it Rs

[5] ,700 crore. Punjab National Bank had 904 willful defaulters, who owed it Rs 10,869 crore at the end of December 2015. Source; http://indianexpress.com/article/explained/what-is-vijay-mallya-accused-of/

While this is one set of narratives, another set of discourses highlights that in the year 2014 alone, 5650 farmers and 6750 agricultural labourers committed suicide[6]. Activist Kishore Tiwari is of the view that debts are the core reasons for the farmers' suicides. There are also various examples of cases where one can say that the decision to pursue these farmers – but give Vijay Mallya free rein for so long – can be seen as prejudiced. The system looks very rigid to the farmers who are committing suicides, but looks very flexible to some corporates. Why?

The incidental achievement of the notorious case of Vijay Mallya-Kingfisher story is that it has brought the problem of Non-Performing Assets[7] to public attention. Going by insightful media reports, as on March 2014, the NPAs of 40 listed banks were 2.42 trillion, up from 1.8 trillion in March 2013 or a 33% rise. And these are just the NPAs. Restructured assets at all banks are an additional 3.66 trillion (7.8% of advances)[8]. To be precise, the total Gross Non Performing Assets (GNPAs) of banks stood at Rs 5,94,929 crores as at end March 2016. Between financial years 2012-13 and 2014-15, 29 public sector banks wrote off a total of Rs 1,14,182 crore. An amount of Rs 52542 crore was written off in the year 2014-15 alone.

The crisis resulting from NPAs and wilful defaulters has created furore and anticipation in both the financial sector as well as in India's civil society and raised questions of the transparency and ethical business conduct of banks. Clearly, banks have significant responsibilities as custodians of public money and as powerful sources of finance for activities that impact people, the environment and the wider economy.

Kingfisher's is not an isolated case; there are many such examples that require a closer look. One such example is the Winsome Group, which is into diamond trading and which has accumulated loans of Rs.6581 Crores from a consortium of 15 PSBs.[9] Another example is Reliance Gas Transportation Infrastructure (RGTIL), which owns and operates a 1,386 km gas pipeline connecting the Andhra coast with Gujarat, and has received a sanction from publicsector banks to repay its principal loan by 2030-31, as against the current repayment schedule of doing so over the next four years. The company, well known for its linkages with political parties, had a total debt of Rs 16,010 crore as of 2014-15.[10] In November 2014, the agreement for a loan between SBI and Adani Group, set to be the largest given by a domestic bank for an overseas project, was signed off, disregarding serious doubts over Adani Group's ability to service the debt[11].

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[6] National Crime Records Bureau Report, 2014

[7] The banks classify an account as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter. In the light of the NPA crisis affecting the PSBs, there was a delay in reflecting the overdue amounts borrowed by the companies as NPAs. In the case of Vijay Mallya and several corporate entities like Winsome group, they are categorized as willful defaulters. RBI classifies willful defaulters as those borrowers who have the assets/capacity to relay the loans but are unwilling to pay back.

[8] http://cag.gov.in/sites/default/files/cag_pdf/4jan2016/psu_audit-bank.html

[9] http://www.thehindu.com/news/national/winsome-groups-rs-7000cr-default-acriminalconspiracy/article8742334.ece

[10] http://www.business-standard.com/article/companies/ambani-company-gets-loanrestructuringpackage-115061200040_1.html

[11] The SBI Chairperson announced the agreement in Australia during a bilateral visit, but then in December 2015, denied having loaned any amount to the Adani group and said that only an MoU was signed, on the basis of which they could do a due diligence process.
http://www.dnaindia.com/money/report-state-bank-of-india-denies-funding-adani-s-australiancoalproject-2153562

Additionally, there is an example of the Rampal based Coal Power Plant, a joint project of India and Bangladesh, in which the Export-Import Bank of India has committed to pay the debts. In 2012, the plant was proposed to be built in Rampal, but the development since then has been held back by delays. The area is surrounded by world's largest mangrove forest, the Sundarbans, a living and effective natural fence protecting the coastal belt areas of Bangladesh, and a UNESCO World Heritage Site. The proposed 1320 MW power plant project (made of two generating units of 660MW), is alleged to threaten irreparable damage to the livelihoods of two million inhabitants dependent in this area[12]; there is also a threat of massive environmental impact. The Indian Exim Bank is proposed to be the financial partner for paying the debt despite huge financial risks involved in the project. Though currently under scrutiny from UNESCO, the project looks to be going ahead, despite the apparent environmental and social costs. From a financial perspective, this is just another example of the stalling of a project funded by the Indian banks: stalling which has resulted in accumulation of NPAs.

All this has happened in a context in which banks, especially the Government owned banks, have evolved systems of due diligence. A senior bank representative [13] stated, "The government banks, over the period, have been successful in erecting a very strong foolproof system. It cannot be easily broken unless there is connivance. It is true, in many cases, that one can easily link to a nexus, although this cannot be proved." Talking about the regulatory reforms he said, "there are RBI representatives on every bank's board, all big loans are passed with their knowledge." So, we may infer, this system could be penetrated only through cronyism.

A challenge that the Public Sector Banking system faces may be how to become independent of 'informal' pressure from politicians and bureaucrats who hold positions of power in the Government system. Often huge loans get disbursed without adequate risk assessment or with persuasion and pressure. In these cases, there have been reports of possible violations of principles of transparency, risks of damage to the environment and even infringements of consumer rights.

Recognising the Need for a Citizen's Watch over Banks: Towards greater accountability

There is no dearth of monthly, fortnightly and weekly statements that different Banks make to regulatory organisations. Banks do have a fair system of reporting, especially for financial reporting, for instance the regulatory Basel III disclosures, and reporting to RBI. But banks disclose very little in the public domain. The best way to address the issue of cronyism and the connected issue of irresponsible lending is to ensure transparent disclosures by banks so that the monitoring is a shared responsibility of all key stakeholder groups, including Government, RBI, civil society organisations, and of course bank customers.

The recent disclosure movement, led domestically by SEBI's mandate that top banks and other companies submit annual business responsibility reports, has certainly democratized opportunities significantly, providing civil society and wider citizenry with access to

[12] http://www.banktrack.org/show/dodgydeals/rampal#tab_dodgydeals_update

[13] Personal communication with bank representatives and civil society in Delhi, 2016

information online. Using these publically available resources, the authors have taken up a number of small-scale studies into bank policies that, together, flag up a way forward for how a concerned public can better hold their financial institutions accountable. Here we look at three possible approaches: (1) a study of policies listed in BRRs, (2) a study of policies of 10 banks in India, and (3) a study of 3 banks using methodology provided by the Fair Finance Guide.

As early as 2007 in a circular on *Corporate Social Responsibility, Sustainable Development and Non-Financial Reporting – Role of Banks*[14], the RBI expressed the need for banks to take holistic account of their impacts. Defining non-financial reporting (NFR) as "basically a system of reporting by organizations on their activities as regards the triple bottom line, that is environmental, social and economic accounting", it goes on to make a case for it, saying that "the urgency for banks to act as responsible corporate citizens in the society, especially in a developing country like ours, need be hardly overemphasized."

Encouragingly, an analysis of Business Responsibility Reports[15] indicates that most of the 18 FIs in the BSE Top 100 have policies for most of the principles (see Table 1, below) of the 2011 National Voluntary Guidelines on the Social, Environmental and Economic Responsibilities of Business (NVGs).

Table No. 1: Financial Institutions Reporting on existence of Policies on 9 principles of National Voluntary Guidelines (N=18)

S.No	**NVG Principles**	**Banks/Financial Institutions reported in their Business Responsibility Reports, 2013-14, that:**		
		They have policies	**Their Policies conform to any national /international standards**	**They Formally communicated to all relevant internal/ external stakeholders**
1	Ethics, Transparency and Accountability	17	17	17
2	Product lifecycle Sustainability	15	15	13
3	Employees' Well-being	17	17	16
4	Stakeholder Engagement	17	16	16

[14] Non-Financial Reporting and Corporate Social Responsibility-RBI Circular https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=3987&Mode=0

[15] Business Responsibility Reports were mandated by SEBI in 2012 for all Top 100 companies

5	Human Rights	17	16	15
6	Environment	16	16	15
7	Public Advocacy	12	11	10
8	Inclusive Growth	17	17	15
9	Consumer Value	17	16	15
Source: Corporate Responsibility Watch database, 2016				

However, whilst almost all the banks say that they formally communicate these policies to their stakeholders, we do not observe them on their websites to the same extent: raising the question of whether they consider their own customers as genuine stakeholders.

Today, it is clear that while most banks are abiding by the norms of financial reporting (FR), Non-Financial Reporting (NFR) and the disclosure obligations that go with it are not yet taken as seriously as they ought to be. Besides the RBI notification, Principle 1 of the 2011 National Voluntary Guidelines stresses ethics, transparency and the need for disclosure. To further explore banks non-financial reporting, a random sample of 10 banks operating in India was taken up in this study. It included 2 international banks, 3 PSBs and 5 private banks. A summary of the results are presented in Table 2, below.

Table 2: Banks disclosing their Policies on Key Themes in their Respective Website; (as on 31st July, 2016) (N=10)					
		Number of banks having policies on the following themes on their websites			
		Environment/ social risk assessment framework	**Whistle Blower Policy**	**Corporate Loan Policy**	**Individual Personal Loans Policy**
1	Have made policies available on public domain and provide updates on compliance	-	4	2	10
2	Have provided some information but not the policy itself	2	-	-	-
3	Have not mentioned anything about the policy	8	6	8	-
Source: Database on Policies of Banks, Partners in Change, 2016					

It is surprising that while all banks disclosed their personal loan policies in their website, none have corporate loan policies (as on 31st, July, 2016). When this was enquired about, at least two Banks stated that they had actually removed the policy in recent times for undisclosed reasons.

To add global perspectives on the policy disclosure situation of Indian banks, policies of three banks were analysed to find out whether their disclosures are in consonance with global standards. The Fair Finance Guide (FFG), globally respected disclosure guidelines,[16] was used for analysis.

Table 3: Public Disclosure by 3 Indian Banks of Policy instruments and Information identified by Fair Finance Guide (As on July 31, 2016)

Themes	**Number of Policy Instruments indicated by FFG**	**Number of policy instruments publically disclosed by the Bank**		
		Bank 1 (Govt)	**Bank 2 (Pvt)**	**Bank 3 (Pvt)**
Accountability and Transparency	18	4	2	11
Taxes and Corruption	13	2	2	2
Labour	12	2		
Human rights	13	4	2	4
Nature	14	0		1
Source: In-depth Analysis on 3 Banks done by research team (Lorina, Reena and Dikshit)				
Partners in Change, 2016				

The table above demonstrates that Indian Banks still have a long way to go in terms of public disclosure, with the 3 banks shown here only meeting a small proportion of the disclosures envisaged by these international guidelines.

Concluding remarks

Banks are very significant institutions that have instrumental value in promoting wider Corporate Social Responsibility, respecting human rights and enabling more equitable development in India. They are the key source of financing for most industrial projects. In that sense, responsible funding norms could be used as a vehicle for strengthening the social

[16] The Fair Finance Guide was originally developed by Oxfam Novib and other Dutch NGOs with technical support from Profundo. It is now active in 9 countries. The Fair Finance Guide captures a number of respected international benchmarks on responsible financing, responsible business, and reporting, including from the Equator Principles, the UN Global Compact, and GRI.

and environmental responsibility of the wider corporate sector. However, for that to happen, the Banks themselves need to be more transparent. The first step should be disclosure of information in the public domain, as well as their policies and means of compliance with them.

In the current climate, the public eye is a powerful means of keeping the banks responsible. There are a number of civil society groups that could play the role of a Watch on behalf of Indian citizens to ensure that Banks insist of responsible and sustainable use of public money. Together with Government, and the Banks themselves, they can help to create an environment of trust and transparency: hallmarks of the vibrant democracy we all want to achieve in India.