

**Report of the Technical Group to Review Legislations on**  
**Money Lending**

**C o n t e n t s**

Letter of Transmittal

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## **CHAPTER - 1**

### **Introduction**

1.1 The All-India Debt and Investment Survey as on June 30, 2002 (NSS Fifty-Ninth Round released in December 2005) had shown that the share of moneylenders in the total dues of rural households had increased from 17.5 per cent in 1991 to 29.6 per cent in 2002. Considering that high indebtedness to moneylenders can be an important reason for the distress amongst farmers, the Reserve Bank Governor announced in the Annual Policy Statement dated April 18, 2006 for the year 2006-07, that a Technical Group would be set up to review the efficacy of the existing legislative framework that governs money lending. The Group would also review the enforcement machinery in different States and make recommendations for its improvement.

### **Constitution of the Technical Group**

1.2 Accordingly, in May 2006, the Reserve Bank constituted a Technical Group under the chairmanship of Shri. S.C.Gupta, Legal Adviser-in-Charge, Reserve Bank of India as detailed below.

#### **Chairman**

Shri S.C.Gupta, Legal Adviser-in-Charge, Legal Department,  
Reserve Bank of India (since retired)

#### **Members**

1. Shri Girish Shankar, I.A.S., Secretary, (Cabinet Secretariat), Government of Bihar
2. Shri A.Giridhar, I.A.S., Secretary to Government (IF), Finance Department, Government of Andhra Pradesh
3. Shri Ashok Jain, I.A.S., Finance Secretary (II), Finance Department, Government of Rajasthan (later replaced by Shri Sanjay Malhotra,I.A.S.)
4. Shri P. Vijaya Bhaskar, Chief General Manager, Department of Banking Operations and Development , Reserve Bank of India
5. Shri P. Krishnamurthy, Chief General Manager-in-Charge, Department of Non-Banking Supervision, Reserve Bank of India
6. Shri K.U.B.Rao, Adviser, Department of Economic Analysis and Policy, Reserve Bank of India
7. Dr. K.S.Ramachandra Rao, Principal Adviser, Department of Statistical Analysis and Computer Services, Reserve Bank of India (since retired).

### **Member Secretary**

Shri G.Srinivasan, Chief General Manager, Rural Planning and Credit Department, Reserve Bank of India.

### **Invitees from the State Governments**

1. Shri Ashok Barnwal, Secretary, Finance , Government of Madhya Pradesh
2. Shri K.S. Pannu, I.A.S. , District Magistrate, Amritsar, Government of Punjab
3. Shri Anupam Kishore, Joint Secretary (DMU), Government of Goa
4. Shri Mara Pandiyan, Secretary, Taxes Department, Government of Kerala
5. Shri Murmu, Registrar of Co-operative Societies, Government of Gujarat
6. Shri Jayant Kawale, Secretary (Co-operation Marketing), Co-operation, Marketing and Textile Department, Government of Maharashtra
7. Dr. S. Subramanya, Secretary to Government (Budget & Resources), Finance Department, Government of Karnataka
8. Shri D.S.Misra, Secretary, Finance Department, Government of Chattisgarh
9. Shri P. Wangdi, Controller of Accounts, Finance, Revenue and Expenditure Department, Government of Sikkim.
10. Secretary, Co-operation Department, Government of Assam
11. Shri Lalmalsauma, I.A.S., Financial Commissioner, Government of Mizoram

### **Terms of Reference**

1. To study the functioning of moneylenders in the light of recent developments in the financial sector;
2. To review international practices in regulating money lending activities and suggest best practices for adoption in India;
3. To study the features, legal framework and enforcement mechanisms for money lending and similar activities in the different States of India;
4. To examine the linkages, if any, between money lending activities and formal credit channels.
5. To make recommendations to State Governments, in the light of above review/study, for improving the legal and enforcement machinery for money lending and similar activities in the interest of rural households.
6. Any other relevant matter.

## **Approach of the Group**

1.3 The Group adopted an extensive consultative approach for ascertaining the ground realities of money lending activities. Besides relying on the experience of State Government officials, the group also invited experts in the field to share their views on the subject.

1.4 Three sub-groups were constituted. While the Group had five formal meetings, the sub-groups visited different places *viz.*, Bangalore, Hyderabad, Thiruvananthapuram, Patna and Kolkata and held meetings with the State governments, bankers and groups/associations of moneylenders. They also interacted with experts. In addition, a survey was conducted using a structured questionnaire, through the Regional Offices of the Rural Planning and Credit Department of the Reserve Bank of India, covering 177 districts in 25 States through focus-group discussions with bankers, borrowers, moneylenders, MFI/NGOs and district administrations. A detailed questionnaire on money lending legislation was also forwarded to all the States, to which eight responded.

## **Organisation of the Report**

1.5 The Report is organised into eight chapters. Chapter One outlines the background, constitution, terms of reference, and the approach of the Group. Chapter Two elaborates the contextual significance of the setting up of the Group with reference to the distribution and composition of indebtedness of rural households, particularly farmer households. It also takes into account the efforts of the Government and the Reserve Bank to improve financial inclusion and to provide additional impetus to the flow of credit from the banking sector to rural areas. Chapter Three highlights the international experience with an overview of legislation in some countries. Chapter Four focuses on the existing legal framework that governs money lending in India. Chapter Five explores the possibility that moneylenders may have linkages with formal financial institutions. Chapter Six discusses the findings/results of the visits of the sub-groups and the survey conducted by the Regional Offices of the Reserve Bank. Chapter Seven attempts Model legislation on money lending covering the legal framework, the enforcement machinery, conclusions and the recommendations of the Group. Chapter Eight contains the summary of the recommendations.

## CHAPTER – 2

### The Context and the Focus

*"...We need more thinking on the credit front. While the financial system should do more for the credit needs of farmers, we need to raise some questions. What do farmers need – a lower rate of interest or reliable access to credit at reasonable rates? Is our existing institutional framework adequate for meeting the requirements of our farmers who are a diverse lot? Do we need to create new institutional structures such as SHGs, micro finance institutions, etc, to provide improved and reliable access to credit? Or do we need to bring in Moneylenders under some form of regulation? It is necessary that we find answers to these questions in the near future."*

**- Hon'ble Prime Minister of India, Dr. Manmohan Singh**

*(in his address at the 2nd Agricultural Summit, October 18, 2006)*

2.1 The issue of mainstreaming moneylenders has confronted the Government and policy makers for a long time. In 1971, the report of the Study Group on the Indigenous Bankers, which was one of the five study groups set up by the Banking Commission, made several recommendations that are still relevant. It noted that but for the services of these indigenous bankers, several segments of the neglected sectors would have been even more neglected. An extract of certain significant observations of the Group is given in Box-1 below:

#### Box-1

##### **Report of the Study Group of the Banking Commission on the Indigenous Bankers**

"...Today there is a network of financial institutions.... Would the commercial banks be in a position to supply funds to millions of small borrowers with comparable ease and informality, i.e., give loans on the basis of personal creditworthiness rather than tangible securities? Or would it be correct to say that indigenous bankers perform a gap-filling function in as much as they are catering to a class of borrowers whom the banks for various reasons cannot reach directly? And what follows as a corollary, is there need to forge a stronger link between the organised and the indigenous financial sectors? The broad conclusion of the Study Group's enquiry was that in many ways the indigenous bankers constitute an indispensable link between the organised banking system and the class of small borrowers who may not be in a position to obtain funds at the right time and in the right quantum from the organised banking system.... For instance, the discounting shroffs (the multanis) etc., act as the intermediary between the commercial banks and the small borrowers about whose creditworthiness the bank would not usually have adequate information..... In the view of the Study Group, the hundi could have provided an appropriate basis for the development of a truly integrated bill market adapted to the needs of the local environment. The hardening of attitudes on both sides, however, rendered any direct link or integration with the organised sector difficult. The indigenous bankers were reluctant to segregate their banking and non-banking activities. Another major difficulty was that the authorities were sceptical regarding the hundi as emanating from a particular trade transaction and therefore as a genuine trade bill. In their opinion, the advances were more often in the nature of accommodation paper and in the absence of documentary evidence to back the paper, it was difficult to say that the credit was in all cases used to support a genuine productive activity. In any event, with the nationalisation of major commercial banks and the emphasis of policy on the expansion of branches and direct financing of priority sectors like small-scale industry and agriculture, the urgency for a link between the two sectors appears to have receded into the background..... Although the Central Banking Enquiry Committee recommended that the indigenous bankers be linked directly with RBI and these bankers were also keen on such a link in the first half of this century, the Study Group is of the opinion that it is not now necessary or feasible to establish such a direct link..... The proper course would be for the Reserve Bank to exercise indirect influence over the business of indigenous bankers through the medium of commercial banks..... Because they remain outside the rigid cast-iron framework of rules and regulations and they are able to operate with a certain degree of flexibility which is what attracts the small borrower."

2.2 The Study Group was of the opinion that given the framework and functioning of the organized banking system, and the attributes of small borrowers and their typical needs, there is bound to be a disconnect between the two. The indigenous bankers, the Group opined, are necessary to fill this gap. Thus, the thrust of the recommendations of the Study Group was that indigenous bankers had a niche role to play and it would be advantageous to harness the synergies between them and the organized banking system. To this end, the Group had suggested linkage between the two, and recommended that commercial banks could finance indigenous bankers and Reserve Bank could extend refinance to the banks. However, the Group's recommendations, made mainly in the context of urban moneylenders, were not implemented.

2.3 The All India Debt and Investment Survey (NSS Fifty-Ninth Round) has revealed that share of institutional agencies in the total cash dues of urban households had increased from 72 per cent in 1991 to 75.1 per cent in 2002 and that of moneylenders had also increased during the period from 10.2 per cent to 14.1 per cent. In the case of rural households, on the other hand, the share of institutional agencies had in fact declined from 64 per cent in 1991 to 57.1 per cent in 2002. And more significantly, the share of moneylenders had increased in the same period from 17.5 per cent to 29.6 per cent in the case of rural households.

An analysis of source-wise distribution of outstanding loans taken by farmer households in different States is given in Table 1 below:

**Table 1**

**Per 1000 rupees distribution of outstanding loan taken by farmer households in different States <sup>1</sup>**

|                   | Sources of Loan |                |            |                                  |           |                     |                     |            |             |
|-------------------|-----------------|----------------|------------|----------------------------------|-----------|---------------------|---------------------|------------|-------------|
|                   | Govt.           | Co-op. society | Bank       | Agri./ professional money lender | Trader    | Relatives & friends | Doctor, lawyer etc. | Others     | All         |
| <b>Andhra Pr.</b> | <b>10</b>       | <b>104</b>     | <b>200</b> | <b>534</b>                       | <b>48</b> | <b>53</b>           | <b>9</b>            | <b>41</b>  | <b>1000</b> |
| Arunachal Pradesh | 61              | 0              | 208        | 0                                | 159       | 507                 | 0                   | 65         | 1000        |
| Assam             | 70              | 27             | 278        | 155                              | 120       | 247                 | 5                   | 99         | 1000        |
| <b>Bihar</b>      | <b>22</b>       | <b>25</b>      | <b>370</b> | <b>328</b>                       | <b>11</b> | <b>128</b>          | <b>12</b>           | <b>106</b> | <b>1000</b> |
| Chhattisgarh      | 13              | 206            | 505        | 130                              | 42        | 63                  | 7                   | 35         | 1000        |
| Gujarat           | 5               | 418            | 272        | 65                               | 44        | 177                 | 9                   | 10         | 1000        |
| Haryana           | 11              | 239            | 426        | 241                              | 31        | 34                  | 15                  | 4          | 1000        |

<sup>1</sup> NSS (59<sup>th</sup> Round)-Report on Indebtedness of Farmer Households

|                              | Sources of Loan |                |               |                                  |              |                     |                     |              |               |
|------------------------------|-----------------|----------------|---------------|----------------------------------|--------------|---------------------|---------------------|--------------|---------------|
|                              | Govt.           | Co-op. society | Bank          | Agri./ professional money lender | Trader       | Relatives & friends | Doctor, lawyer etc. | Others       | All           |
| Himachal Pr.                 | 61              | 116            | 476           | 72                               | 55           | 170                 | 1                   | 49           | 1000          |
| Jammu & Kashmir              | 131             | 2              | 543           | 11                               | 155          | 155                 | 0                   | 2            | 1000          |
| Jharkhand                    | 39              | 45             | 557           | 190                              | 17           | 136                 | 4                   | 12           | 1000          |
| Karnataka                    | 19              | 169            | 501           | 200                              | 19           | 68                  | 4                   | 21           | 1000          |
| Kerala                       | 49              | 283            | 491           | 74                               | 17           | 66                  | 10                  | 9            | 1000          |
| Madhya Pr.                   | 19              | 169            | 381           | 226                              | 90           | 101                 | 5                   | 8            | 1000          |
| Maharashtra                  | 12              | 485            | 341           | 68                               | 8            | 59                  | 3                   | 24           | 1000          |
| <b>Manipur</b>               | <b>15</b>       | <b>0</b>       | <b>167</b>    | <b>329</b>                       | <b>40</b>    | <b>401</b>          | <b>0</b>            | <b>49</b>    | <b>1000</b>   |
| Meghalaya                    | 60              | 0              | 0             | 128                              | 3            | 809                 | 0                   | 0            | 1000          |
| Mizoram                      | 243             | 31             | 499           | 0                                | 33           | 193                 | 0                   | 0            | 1000          |
| Nagaland                     | 75              | 77             | 536           | 3                                | 153          | 155                 | 0                   | 0            | 1000          |
| Orissa                       | 130             | 181            | 437           | 148                              | 8            | 84                  | 1                   | 10           | 1000          |
| <b>Punjab</b>                | <b>19</b>       | <b>176</b>     | <b>284</b>    | <b>363</b>                       | <b>82</b>    | <b>63</b>           | <b>6</b>            | <b>7</b>     | <b>1000</b>   |
| <b>Rajasthan</b>             | <b>13</b>       | <b>59</b>      | <b>270</b>    | <b>365</b>                       | <b>192</b>   | <b>69</b>           | <b>18</b>           | <b>14</b>    | <b>1000</b>   |
| Sikkim                       | 348             | 0              | 230           | 73                               | 221          | 67                  | 0                   | 61           | 1000          |
| <b>Tamil Nadu</b>            | <b>20</b>       | <b>233</b>     | <b>281</b>    | <b>397</b>                       | <b>4</b>     | <b>52</b>           | <b>1</b>            | <b>11</b>    | <b>1000</b>   |
| Tripura                      | 164             | 28             | 605           | 20                               | 39           | 119                 | 0                   | 25           | 1000          |
| Uttar Pr.                    | 24              | 67             | 512           | 191                              | 29           | 138                 | 19                  | 20           | 1000          |
| Uttaranchal                  | 315             | 48             | 398           | 59                               | 17           | 149                 | 0                   | 14           | 1000          |
| West Bengal                  | 103             | 192            | 285           | 130                              | 107          | 154                 | 7                   | 23           | 1000          |
| Group of UT's                | 307             | 147            | 136           | 103                              | 61           | 245                 | 0                   | 1            | 1000          |
| <b>All India</b>             | <b>25</b>       | <b>196</b>     | <b>356</b>    | <b>257</b>                       | <b>52</b>    | <b>85</b>           | <b>9</b>            | <b>21</b>    | <b>1000</b>   |
| <b>Estimated Number (00)</b> | <b>14769</b>    | <b>114785</b>  | <b>117100</b> | <b>125000</b>                    | <b>53902</b> | <b>77602</b>        | <b>7181</b>         | <b>14605</b> | <b>434242</b> |
| <b>Sample Number</b>         | <b>992</b>      | <b>5844</b>    | <b>6296</b>   | <b>6919</b>                      | <b>3018</b>  | <b>4528</b>         | <b>345</b>          | <b>872</b>   | <b>23935</b>  |

The survey reveals that out of every Rs 1,000 outstanding of farmer households in the country, Rs 257 was sourced from moneylenders. The share of moneylenders in the indebtedness of farmer households in Bihar, Manipur, Punjab, Rajasthan, Tamil Nadu and Andhra Pradesh were well above the national average, with Andhra Pradesh at the top. The penetration of moneylenders is significant even in States that are regarded as being adequately banked (Andhra Pradesh and Tamil Nadu).

### Initiatives in institutional credit in the rural sector

2.4 To provide an impetus to the flow of credit from the banking sector to rural areas, a host of measures have been initiated by the Government and the Reserve Bank. The progress in rural banking over the last several decades was described by Governor Y.V.Reddy in a recent speech<sup>2</sup>, extracts of which are given in Box-2.

#### Box-2

“.....Rural banking was traditionally a monopoly of the Moneylenders, till the colonial Government enacted Co-operative Societies Act in 1904 with a view to making the co-operatives as premier institutions for disbursement of credit. The process of a three-tier structure for co-operatives commenced in 1915. Government was also providing agricultural loans usually called Takkavi loans, which have since been discontinued. The RBI Act vested a unique responsibility of rural credit to the central bank. All India Rural Credit Survey (1951) of the RBI opined that the co-operatives were “utter failure” in providing rural credit, but added they had a vital role in agriculture credit. The Imperial Bank was nationalised as SBI, which was visualised as a vehicle for rural banking. ... Many State Governments legislated the registration and regulation of Moneylenders but with little emphasis on implementation. Nationalisation of banks in 1969 gave a boost to expansion of banks and banking in rural areas. The Reserve Bank hived off a part of its role in agricultural credit to a separate national level institution, viz. Agriculture Refinance and Development Corporation (ARDC) in 1975. Soon thereafter, a legislation was enacted to create Regional Rural Banks, with participation from Central and State Governments and the nationalised banks, which have their network spread almost all over the country. Subsequently, the ARDC was converted into NABARD..... Simultaneously, the directed credit in the form of priority sector lending continued and the administered interest rate regime lasted. During the reform period, capital was infused into the RRBs and the NABARD. While the priority sector lending continued, the administered interest rate regime was dismantled. To make up for the shortfall in the priority sector lending by the banks, the Rural Infrastructure Development Fund (RIDF) was initiated to ensure the envisaged flow of bank resources to agriculture through the intermediation of the NABARD and the State Governments. A system of Special Agricultural Credit Plan was also introduced. ....More recently, since 2004, vigorous efforts have been made to more than double the credit flow to agriculture. Emphasis has been laid on sound credit culture, effective credit delivery and appropriate credit pricing. Innovations in the area of rural credit have included introduction of Kisan Credit Cards and encouraging SHG-bank linkages. Further, new instruments for financial inclusion such as General Credit Cards and no-frills accounts were initiated. Micro finance programme was intensified and new guidelines for business-facilitator model were issued. Use of technology for rural banking is being encouraged. Special Area Plans for banking in several States such as Uttaranchal, North Eastern States, Chattisgarh and Bihar.... have been formulated to suit the local conditions. In terms of institutional development, consolidation of the RRBs, revamping of the urban co-

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<sup>2</sup>The first Smarajit Ray Memorial Lecture delivered by Dr. Y.V. Reddy, Governor, Reserve Bank of India, organised by the Andhra Pradesh Mahila Abhivruddhi Society, Hyderabad on December 16, 2006 at the Centre for Economic and Social Studies, Ameerpet, Hyderabad.

operative banks as per the vision document, revival of rural co-operative credit structure as per the Vaidyanathan Committee recommendations, a plan for restructuring of long-term lending institutions for agriculture, and a revisit of the prescriptions relating to the priority sector lending are underway. .... A Working Group was constituted by the Bank to look into the relief measures for the distressed farmers. Above all, as per the Government of India announcement in 2006, it has been decided to subsidise the commercial banks and NABARD to enable provision of short-term credit at 7% interest rate to the major segment of the farmers". (This has been extended for 2007 also). "Thus, there have been vigorous and determined efforts towards expansion of rural credit, especially through rural banking...However, an assessment of the position at ground level indicates that accessing non-institutional credit still continues as far as rural areas and agriculture sector are concerned. The credit-deposit ratio continues to be low in the rural areas, despite the intermediation of banks. The all-in costs of credit from banks, after factoring in timeliness, transaction-costs, access, etc, appears high for agriculture relative to private corporate sector even after accounting for the risks as reflected by the level of actual non-performing assets. The performance of some of the public sector banks in rural and agricultural lending is inadequate, while that of most of the private and foreign banks is even lower, despite considerable expansion of the scope of priority sector lending.....While there has been notable progress in micro finance, it is mostly confined to the States with fairly well-developed banking system. Further, the cost of credit at around 20 to 30% also appears high.....Though there has been significant growth in rural credit in the recent years, its medium-term sustainability is contingent upon growth in agriculture and improvements in the institutional settings. In brief, the perceptions on the outcomes of vigorous and varied efforts to expand the reach of rural banking seem to be less than expected."

2.5 The constraints faced by the formal financial system in reaching rural households in a flexible and hassle-free manner led, almost as a natural consequence, to emergence of various options like the SHG-bank linkage programme and the microfinance institutions (MFIs). MFIs range from fair-sized NBFCs to much smaller societies and trusts. The use of MFIs and other intermediaries as business facilitators and business correspondents was also allowed by the Reserve Bank in January 2006. Some banks are experimenting with using post offices as agents. In Andhra Pradesh, Village Organisations (VOs), which are set up as co-operatives through federated SHGs are being gainfully utilised for upscaling bank linkages because it is easy for bankers to deal with seven or eight VOs instead of a large number of SHGs. A pilot project in using VO as a business correspondent has commenced in Andhra Pradesh using IT solutions for ensuring necessary safeguards.

2.6 The SHG-bank linkage model has been quite successful in as much as 25.84 lakh groups have been linked to banks covering about 33 million women. The total credit cumulatively disbursed is about Rs14,479 crore. The current outstanding credit is at around Rs 4,000 crore. There is no doubt that in some regions these institutional arrangements have addressed the problem of the poor. Their success in empowerment of women, especially poor women, is remarkable. The access to savings and credit facilities provided by the SHG-bank linkage model would not have been possible by branch banking

alone. At the same time, it is important to note that the rates of interest paid by the borrower member of the SHG could be as high as 18 to 24 per cent *i.e.*, much higher than that charged by banks on their direct loans. In case of MFIs also, the interest rates are around 20 to 24 per cent. It should also be noted that these initiatives have generally been extensive in areas that are already served by banks and that their activities in the backward and tribal areas are limited. In the recent period, there have been initiatives by NABARD in extending the SHG model to some under-served areas.

2.7 Notwithstanding concerted and multi-pronged efforts to extend institutional credit to all sections of society as also other initiatives for increasing the outreach of banks by using SHGs and MFIs as intermediaries, the dependence on moneylenders has not decreased in rural areas and has, in fact, increased in several regions. Against this background, there is a case for looking at possibility of leveraging the presence of moneylenders who continue to operate despite century-long efforts by policy makers to find substitutes for them. Concerns regarding usurious rates of interest and harsh recovery practices are a reality and ways should be found by which the law can be enforced. The focus of the Technical Group was therefore, on whether there could be a way of incentivising good conduct and practices by moneylenders while simultaneously providing for a more effective enforcement of penalties for violations of the law.

## CHAPTER – 3

### Money Lending Legislation – The International Scenario

#### Introduction

3.1 The name<sup>3</sup> by which moneylenders are called may vary from country to country but they can be found performing similar activities all over the world. It is natural therefore that, with a view to having a level playing field, several governments should have attempted to regulate the activity. In this Chapter we analyse the main features of money lending legislation in the following countries<sup>4</sup>. The sample includes developed as well as the developing countries.

1. Hong Kong - Moneylenders' Ordinance, 1997
2. Singapore - Moneylenders' Act, 1959
3. Japan - Money Lending Business Control and Regulation Law, 1983<sup>5</sup>
4. Lesotho - Moneylenders' Order, 1989
5. United Kingdom - Consumer Credit Act, 1974<sup>6</sup>
6. West Pakistan - The Punjab Moneylenders Ordinance, 1960<sup>7</sup>
7. USA (S. Dakota) - Title 54 of the South Dakota State Laws (Debtor and Creditor)<sup>8</sup>
8. South Africa - The National Credit Act, 2005<sup>9</sup>

The administrative authorities empowered under the money lending laws in the above countries may be seen in Annex-II.

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<sup>3</sup> In many countries, the moneylenders (as we understand in India) are known as “consumer credit providers” (United Kingdom) or “credit providers” (South Africa)

<sup>4</sup> The selected countries are United Kingdom, United States (State of South Dakota), Hong Kong, Singapore, Lesotho, South Africa, Japan, West Pakistan. The object of selecting these said countries is to have a representative sample of countries having different legal and constitutional systems.

<sup>5</sup> Post amendment in December 2006, it will be known as Money Lending Business Law and major amendments are likely to come into effect from 01/12/2007 (Please see: <http://www.iflr.com/?Page=10&PUBID=33&ISS=23496&SID=677782&TYPE=20>). In view of the lack of statutory material pertaining to the Japanese law, the study of Japanese law is based on availability of secondary materials, like decisions of the Japanese Supreme Court and some write up on the said law from the website of the Financial Services Authority of Japan (<http://fsa.gov.jp>). Therefore, only the main features of the legislation are being discussed in this Chapter.

<sup>6</sup> The said Act has been extensively amended in the year 2005. The discussion in this Chapter takes into account the amendments also.

<sup>7</sup> <http://punjablaws.gov.pk/laws/126.html>. Considering the fact that receiving money in the form of interest is against the tenets of Islam, the said law was proposed to be repealed in so far as “private moneylenders” were concerned by introducing a Bill on Prohibition of Private Money Lending in the Assembly in the year 2003, which however could not be enacted due to changes in the political climate in Pakistan.

<sup>8</sup> <http://legis.state.sd.us/statutes/StatutesTitleList.aspx>

<sup>9</sup> Brought into force from 01/06/2006. The said Act is very elaborate. It tries to combine within itself all the aspects of regulation, protection of interests of the debtor as well as the creditor.

3.2 The nature of the money lending laws is regulatory<sup>10</sup>, with emphasis<sup>11</sup> being on protecting the interests of the borrowers<sup>12</sup> by providing definite upper limits on rates of interest<sup>13</sup> and curbing coercive recovery practices. The latter is sought to be done by penalizing such acts as also by denying the benefits of legal remedies to moneylenders to recover loans to the extent to which they are tainted with illegalities. Coercive recovery practices are also sought to be curbed by providing definite recovery procedures generally through Courts. Where there are violations, procedures are also prescribed to provide a remedy to the injured<sup>14</sup>. The prescription of fair practices is generally restricted to imposing certain obligations usually in the nature of requiring moneylenders to provide documents evidencing loan transactions containing detailed description, *inter alia*, of the amount of loan, date of payment of the loan and rate of interest.

### Definitions

3.3. The definition of the term 'moneylender' in legislation is generally all-inclusive, and means a person who is in the business of lending money (loans), whether as principal business or otherwise. However, nearly all legislations expressly exclude certain categories of persons from the definition. The excluded

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<sup>10</sup> All the legislations regulate the business of money lending by granting licences for conducting money lending business. Such business in some countries is not restricted to the traditional form of money lending but extends even to credit card business like the United Kingdom, South Dakota, South Africa, although in South Africa the law does not use the word "credit cards", the expression "credit facility" used therein covers credit card activities also.

<sup>11</sup> The object of the National Credit Act, 2005 of South Africa, says it all, in the following lines:

"To promote a fair and non-discriminatory marketplace for access to consumer credit and for that purpose to provide for the general regulation of consumer credit and improved standards of consumer information; to promote black economic empowerment and ownership within the consumer credit industry; to prohibit certain unfair credit and credit-marketing practices; to promote responsible credit granting and use and for that purpose to prohibit reckless credit granting; to provide for debt re-organisation in cases of over-indebtedness; to regulate credit information; to provide for registration of credit bureaux, credit providers and debt counselling services; to establish national norms and standards relating to consumer credit; to promote a consistent enforcement framework relating to consumer credit; to establish the National Credit Regulator and the National Consumer Tribunal..."

<sup>12</sup> **Instances of protection of borrower's interests:** Many legislations have clear cut provisions to prevent borrowers from being burdened by excessive borrowing. Under the South Dakota Law, there is a limitation on the number of times a borrower can borrow money from the lender (section 54-4-65), more particularly, in case of a short-term consumer loan. It also requires that at every such renewal / roll over etc., the principal amount should be reduced by not less than ten per cent. Similar provisions are also available under the South African law (Sections 79, 80, 81, 82, 83 etc., of the National Credit Act, 2005). Further, subsequent to the amendment which came to be enacted in December 2006, the Japanese law also has a provision which, *inter alia*, requires the moneylender to assess the borrower's repayment capacity and prohibits lending money exceeding one third of the borrower's annual income (Article 13). In addition to the same, the amended Japanese law has stricter provisions to ensure better compliance with provisions of the law.

<sup>13</sup> All the legislations provide rates of interest in the body of the Statutes themselves, thereby making its compliance mandatory. It would, however be interesting to note how interest is calculated in the case of loans in kind by the Courts under the West Pakistan Law. In terms of Section 16, the money value of the commodity at the time when, and the locality where the loan was advanced shall be deemed to be the principal of the loan and for determining the amount which may have to be repaid under the decree, the Court will take into consideration the market value of the commodity in the said locality at the date / dates of repayment. It is also interesting to note that under the said West Pakistan law, the interest rate ceiling is provided in the penal provision, rather than as a separate provision and it is, *inter alia*, linked to the bank rate (Section 20).

<sup>14</sup> Section 134 of the National Credit Act, 2005 (South Africa) provides for alternate dispute resolution mechanism whereby the National Credit Regulator may refer complaints of violation of the provisions of the Act to the Financial Services Ombud (if the credit provider is a financial institution) or to the consumer court / alternate dispute resolution agent (if the credit provider is not a financial institution). Similarly, the law in the United Kingdom was extensively amended in the year 2005 and, *inter alia*, the complaints concerning the credit providers has been brought under the jurisdiction of the Ombudsman.

categories are either incorporated bodies or institutions in the business of banking, insurance, dealing in securities *etc.*, which are otherwise regulated by formal regulatory bodies in those countries. There are certain other non-incorporated but registered bodies, such as, registered co-operative societies, which are also excluded from the definition of moneylenders. In addition to such individuals being expressly excluded, the laws abroad also exclude either a class of loans or loans provided by a class of persons from being regarded as “loans” for the purpose of the money lending legislation thereby taking them out of the purview of those laws. For example, under the **Hong Kong** Law, the following types of money lending are excluded from the applicability of the Ordinance:

- a. A bona fide loan made by an employer to his employee
- b. A loan made to a company secured by a mortgage
- c. A loan made by a credit card company to a credit card holder for purchase or refinance of immovable property
- d. A loan by a person whose ordinary or primary business does not include money lending
- e. A loan made by a pawn broker (since the pawn brokers in Hong Kong are regulated by a separate legislation, loans made by them are not covered under the Moneylenders’ ordinance)
- f. A loan made by a statutory corporation under the powers conferred upon it under the statute
- g. Loans from provident fund, chit fund, from holding company to subsidiary company, or by one subsidiary company to another subsidiary company
- h. Loans for transactions involving import into or export out of Hong Kong.
- i. Loans made to a company having paid up capital of not less than Hong Kong dollars one million, or whose shares or debentures are listed on the recognised stock exchanges in Hong Kong.

3.4. It was also seen that when a loan or a body or person making that loan came under a formal regulatory jurisdiction, it (or he or she) was excluded from the purview of the money lending legislation. But there are exceptions. For example, in **Lesotho**, certain transactions are exempted although these transactions are not formally regulated<sup>15</sup>. Similarly, in **Pakistan** trade loans are expressly excluded from the definition of “loan” and thereby from the purview of the legislation<sup>16</sup>. In Hong Kong, Singapore, and Lesotho, the law enables authorities to grant exemptions. The **Singapore** legislation provides that other than the persons expressly excluded from the purview of the law, any person who lends a sum of money in consideration of a larger sum being repaid shall be presumed to be a moneylender, until the contrary is proved<sup>17</sup>.

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<sup>15</sup> (a) any money lending transaction where the security for repayment of the loan and interest thereon is effected by execution of a chattels transfer in which the interest provided for is not in excess of 25 per centum per annum, (b) any transaction where a bill of exchange is discounted at a rate of interest not exceeding 25 per centum per annum, and (c) any money lending transaction where the security for repayment of the loan and interest thereon is effected by execution of a legal or equitable mortgage upon immovable property or of a charge upon immovable property or of any bona fide transaction of money lending upon such mortgage or charge.

<sup>16</sup> Section 2(l)(vi)

<sup>17</sup> Section 3 of the Moneylenders’ Act, 1959 (Singapore law)

3.5 In all the countries being discussed here, registration or obtaining a licence is compulsory. Such licences are generally valid for 12 months and can be renewed<sup>18</sup>. Procedures for obtaining licences are prescribed. The licence is for the business of money lending as a whole and restrictions generally tend to be geographical in nature, which means that the licence is valid only for a particular area. All these countries require a register of licensed moneylenders to be maintained. These registers also contain details of the licence, including whether the licence has been cancelled, suspended or revoked. In the **United Kingdom**, the Office of Fair Trading maintains a Consumer Credit Register wherein the details of everyone who holds a licence, has applied for one, or had one revoked, suspended or varied, is available and the same is made available to the public. Similarly, under the **Singapore** law, the list of licensed moneylenders is published in the Gazette by the Registrar from time to time. The presence of the name of a person is evidence that he or she is a licensed moneylender and the absence therefrom is evidence that he or she is not licensed.

3.6 If money lending is conducted without a valid licence, the lender becomes liable for criminal action and the offence can entail a fine or imprisonment or both. In the **South African** law, a credit agreement is rendered unlawful and amounts paid thereunder non-recoverable if at the time when the agreement was made, the credit provider was not properly registered<sup>19</sup>. Similarly, under the **Singapore** and **Hong Kong** laws, such person would not be entitled to recover the loan or loans, which has or have been provided without having a licence. Under the **Pakistan** law, such a licence should be in force or valid even at the time of filing a case before the Court<sup>20</sup> except in cases where the licence has been suspended or cancelled. However, the moneylender can still file a suit before the Court for the recovery of the loan (even though he is not technically in possession of a licence) if he has a certificate issued by the Collector specifying the loans in respect of which a suit may be instituted or the decree in respect of which an application for execution may be presented by him<sup>21</sup>.

3.7 In addition to the above, laws are sought to be enforced by restricting legal remedies available to the moneylender. In cases where a moneylender does not possess a valid licence, he or she loses the entitlement to recover the loans through the legal process<sup>22</sup>. Under the Singapore Law, by having 'residual' clauses<sup>23</sup> like deeming certain persons who lend money in consideration of receiving a higher

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<sup>18</sup> Interestingly, under the South Dakota Law the licence expires on a particular day, viz., July 1<sup>st</sup> of every year, irrespective of the date on which it was obtained in the previous year and has to be renewed by filing an application by June 15<sup>th</sup> (Section 54-4-45). In the United Kingdom the validity period of the licence is 5 years (Source: <http://oft.gov.uk>). In case of South Africa, the law does not limit the validity period. However, subject to the payment of annual renewal fees the registration remains effective until the registrant is deregistered or the registration is cancelled under the Act (as per Sections 51 and 52 of the National Credit Act, 2005)

<sup>19</sup> Section 89(2)(d) and 89(5). However, in terms of section 89(4), the provisions of section 89(2)(d) does not apply if the credit provider has at the time the credit agreement was made or within 30 days after that time, has applied for registration or holds a valid clearance certificate issued by the National Credit Regulator.

<sup>20</sup> Under the Hong Kong Law, if at the time of lending the money, the lender has a valid license, then he would be entitled to recover such loan through the Court, although at the time of filing a case before the Court, the lender does not possess a valid licence.

<sup>21</sup> Section 7 read with section 10.

<sup>22</sup> In addition to above, under the Lesotho law, a period of limitation has been prescribed, namely 12 months from the date on which the cause of action has accrued, within which suits for recovery have to be brought before the Courts of law by a moneylender.

<sup>23</sup> Section 3 read with section 15

money from the borrowers to be moneylenders, any person who seeks the help of the Court to enable him to recover such loan may have to either prove that he is not a moneylender or, if he is one, to produce a valid money lending licence. In cases where there are duties imposed under the law<sup>24</sup> in the event of non-compliance with those duties moneylenders are barred from recovering such loans, either in part or full, to which the acts of non-compliance relate<sup>25</sup>.

3.8 Overall, this comparison with international practice suggests that there is great deal of similarity with Indian laws. However, some features are peculiar to specific countries eg. the calculation of repayment amounts in the case of loans taken in kind, as in Pakistan; the prevention of over indebtedness of the borrower by restricting the amount of loans that could be provided to a particular borrower as in Japan, South Africa, South Dakota<sup>26</sup>; enabling persons to seek recourse to an alternate dispute resolution mechanism as in South Africa; requiring borrowers to obtain "credit insurance" in South Dakota and South Africa and provisions enabling the establishment of credit information agencies to obtain information about a borrower's indebtedness as in Japan.

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<sup>24</sup> Such duties may be in the form of requiring the moneylender to sign a note or memorandum containing the details of the loan, the date of payment, the rate of interest etc., and to provide the same to the borrower and also requiring the moneylender to provide such details as prescribed under the statutes to the borrower at prescribed intervals or as and when the borrower makes repayments.

<sup>25</sup> Under the South Dakota Law, a receiver may also be appointed for the business and property of the moneylender who shall be empowered to control the custody, collection, administration and liquidation of the property and business (Section 54-4-51). Similarly, under the Singapore law in case when any fine is imposed on an agent who is or has been licensed under the Act to carry on a money lending business on behalf of a principal not resident in Singapore, the fine, if it has been imposed in respect of an offence under the Act committed by the agent in the course of carrying on the business, unless the court imposing the fine otherwise directs, can be recoverable out of the property situate in Singapore belonging to the principal as well as out of the property belonging to the agent and any such property of the principal may be taken in execution and sold under any warrant issued against the agent for the levy of the amount of the fine (section 34).

<sup>26</sup> *Supra* Note 12

## CHAPTER – 4

### The Current Legal Framework

#### Introduction

4.1 The Constitution of India<sup>27</sup> has conferred the power to legislate on matters relating to money lending and moneylenders to the States. Most of them have enacted the laws (Annex-III). Many of these are comprehensive legislations providing detailed and stringent provisions for regulation and supervision of the money lending business. These legislations contain provisions aimed at protecting the borrowers from malpractices of the moneylenders. In Andhra Pradesh, there are two laws governing moneylenders, applicable to different parts of the State. The Andhra Pradesh (Telangana Area) Moneylenders Act, 1349 F (Act No. V of 1349 F) is applicable to the whole of the Telangana area, whereas the Andhra Pradesh (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960 (A. P. Regulation No.1 of 1960)<sup>28</sup> is applicable to the Andhra region. Efforts are being made by the State government to come up with a single Act that covers the whole State. Orissa also has two laws, which are made applicable in different parts. The Orissa (Scheduled Areas) Moneylenders' Regulation, 1967 has been made applicable to the Scheduled areas of the State, whereas the Orissa Moneylenders' Act, 1939 is applicable to rest of the State.

4.2 Some States have enacted separate legislations governing the business of pawn-broking<sup>29</sup>, while others have incorporated separate provisions for pawnbrokers within the money lending legislation itself<sup>30</sup>. For the purposes of this report, we have focused on the legislations dealing with money lending, leaving aside the laws governing pawn broking.

4.3 The history and object of enacting the money lending legislations can be inferred from the observations made by some High Courts. Thus, in *Sk. Abdul Sattar v. Sitaram Sah and Anr.*<sup>31</sup>, the Bihar High Court observed as under :

*"Before embarking upon this question, it is relevant to state at the outset that the Act was brought on the Statute book to consolidate and amend the law relating to regulation of money-lending transactions and to grant relief to the debtors in the State of Bihar."*

Similarly, in the case of *J.D. Nichani and Anr., v. State of Madras*<sup>32</sup>, the Madras High Court, while dealing with the challenge to the constitutional validity of certain provisions of the Madras Moneylenders Act, 1957, made observations to the effect that the Madras legislation had been enacted in order to cure the defects that were noticed in enforcing the provisions of the Section 51A of the City Police Act, 1888 which, in turn, was introduced in order to put an end to the malpractices followed by a special class of

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<sup>27</sup> Seventh Schedule, List II, Item 30 and Fifth Schedule, Paragraph 5 (2) (c).

<sup>28</sup> The Regulations (of both Andhra and Orissa) have been in exercise of the powers conferred by clause (c) of sub-paragraph (2) of paragraph 5 of the Fifth Schedule to the Constitution of India read with Article 244 of the Constitution of India.

<sup>29</sup> States of Karnataka, Tamil Nadu and Andhra Pradesh are examples.

<sup>30</sup> States of Kerala, Nagaland and Maharashtra are examples.

<sup>31</sup> AIR 1988 Pat 233; observations of Honourable Mr. Justice S.K. Jha

<sup>32</sup> AIR 1964 Mad 30; observation of Honourable Mr. Justice S. Ramachandra Iyer, C.J.

moneylenders known as pawnbrokers, and for the purpose of framing a legislation to regulate and control the business of moneylenders in the then State of Madras. In a case relating to the Bombay Money Lender's Act, 1946 the Bombay High Court held that the Act was a piece of social legislation<sup>33</sup>. In yet another case in Bihar, it was held that the Act was a measure of beneficial legislation intended to liberate agricultural debtors from shackles of the ever-continuing indebtedness<sup>34</sup>.

### **Salient features of the Money Lending Legislations**

4.4. An examination of the money lending legislations of 22 States<sup>35</sup> shows that the provisions are generally similar. The salient features are:

Requirement of registration/license for carrying on the business of money lending within a State/a portion of the State;

Duties of the moneylenders with respect to maintaining and providing statement of accounts to the debtors;

Penalties for carrying on business without licence<sup>36</sup> and for intimidating the debtors or interfering with their day-to-day activities, including the cognizability of such offences;

Maximum rates of interest that can be charged;

Matters that the Courts are required/empowered to decide in suits filed by moneylenders;

Applicability to companies engaged in the money lending business. However, some States in exercise of their general exemption powers, have granted exemptions to companies from the applicability of the legislations.<sup>37</sup>

Exemption to loans from a trader to another trader, loans by banks<sup>38</sup>, co-operative societies, financial institutions, etc.

Certain common features found in majority of the legislations are outlined in the following paragraphs.

### **Object and Coverage**

4.5 The object of legislation pertaining to money lending is to regulate and control the business of moneylenders. The various Moneylenders Acts define a moneylender as a person whose main or subsidiary occupation is the business of advancing and realising loans. Banks and Co-operative Societies are excluded from the purview of the Acts of many States. Generally, the laws have been made applicable to individuals, firms, association of individuals and companies. However, Nagaland and Andhra Pradesh (as applicable to the Andhra Region Scheduled Areas) have excluded companies from the purview of their respective enactments.

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<sup>33</sup> M. J. Brothers v. Amar Finance AIR 1992 Bom. 1

<sup>34</sup> Suresh Narain Pathak v. Ramakant Pathak 1992 (2) PLJR 815 (source: N.K. MALHOTRA, Commentary on Bihar Moneylenders Act, 1974, 2nd Edition, 1999)

<sup>35</sup> A list of the legislations referred to by the Technical Group is given at Annex -III

<sup>36</sup> The details of penalties for carrying on business without registration/license are given at Annex -IV

<sup>37</sup> Applicability of the money lending legislations to companies engaged in money lending business and provisions enabling exemptions are provided in Annex - V

<sup>38</sup> The applicability of the legislations to banks, trade credit etc. is given at Annex -VI

## Registration/Licensing

4.6 All the moneylending legislations provide that moneylenders are required to register and obtain a licence. All the State legislations, except those of Punjab and the National Capital Territory of Delhi, also provide for penalties if any person carries on business without registration/licence. The punishments range from a low fine of Rs.200 to imprisonment for a period of 3 years and maximum fine of Rs 50,000. Kerala prescribes a minimum punishment of imprisonment for 6 months. Some States<sup>39</sup> provide for enhanced punishments for second and subsequent offences.

4.7 Kerala and Karnataka provide for the payment of a security deposit by the moneylender at the time of applying for the licence, which is liable to be forfeited in the event of his contravening any of the provisions of the respective Acts/Rules, falsification of accounts, and commission of certain offences. Almost all laws, except of Kerala, Nagaland and Andhra Pradesh (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960, also impose a bar on suits filed by unregistered moneylenders.

## Loans in kind, goods and materials

4.8 Most State Acts include the advance of both money and kind within the definition of the term "loan". The AP (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960 defines a "loan" (section 2(10)) as advance of money or articles, goods or materials for interest and includes any transaction, which the Court finds in substance to amount to such an advance<sup>40</sup>. In Uttar Pradesh, the sale of goods on credit and hire purchase are not covered. In Kerala and Bombay<sup>41</sup>, a loan advanced in the regular course of business by a trader legitimately carrying on any business has been exempted from the definition of "loan". In Karnataka, loans from a landlord to a tenant for financing of crops or seasonal finance of not more than fifty rupees per acre of land held by the tenant have been exempted from the definition of the term "loan". Under the Orissa Moneylenders' Act, 1939, supply of goods (i) on *khata* carrying simple interest upto six and a quarter per cent per annum and (ii) on credit, are not treated as loans.

## Keeping, Filing and Furnishing of Accounts

4.9 Almost all the States have provisions requiring moneylenders to keep statement of accounts<sup>42</sup> in the form and manner prescribed in the Rules. Moneylenders are also required in Karnataka, Uttar Pradesh, Kerala, Maharashtra, Nagaland, Madhya Pradesh and Rajasthan to file statement of accounts with the registering/licensing authorities and generally they are required to do so annually<sup>43</sup>. Another requirement is to furnish a statement of accounts to the borrowers as prescribed under the Rules. Delhi, Punjab and Haryana do not contain provisions for the keeping of accounts, filing statement of

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<sup>39</sup> Bombay, Bengal and Karnataka

<sup>40</sup> Madhya Pradesh Moneylenders Act, 1934 contains a similar provision.

<sup>41</sup> In Bombay, the exemption is available only if the primary object of the business is not lending.

<sup>42</sup> Exception being the States of Punjab, Delhi and Haryana.

accounts/returns with registering authorities and furnishing of account details to the borrowers. Similarly, even though the Andhra Pradesh (Telangana Area) Moneylenders Act, 1349 F provides for keeping of accounts, it does not contain any provision requiring the lenders to file statements of accounts/returns to the registering authorities. In Bihar, the filing of accounts with registering authorities has been restricted to the accounts of scheduled castes and scheduled tribes only. Karnataka, Uttar Pradesh, Kerala, Maharashtra, Bengal, Orissa, Bihar, Andhra Pradesh, Rajasthan and Nagaland enable the State authorities to inspect the books of accounts and related documents. Some States even have powers of search and seizure of books of accounts and documents relating to money lending<sup>44</sup>. Most of the States also prescribe penalties for the falsification of accounts/entry of wrong sums in accounts<sup>45</sup>.

## Interest Rates

4.10 Interest rates chargeable by moneylenders are either fixed by Statute or the Statutes empower the respective Governments to fix the interest rate by issue of notification from time to time<sup>46</sup>. The same forms a bench-mark for the Courts to determine whether the interest rates charged are excessive in the given facts and circumstances of a case. The Courts are also empowered to examine whether or not interest rates charged on a loan transaction are excessive under a central legislation, namely, the Usurious Loans Act, 1918, wherein guidelines for determining what is 'excessive' have been provided in terms of Section 3(2) of the said Act.<sup>47</sup> Some States have provisions empowering the Courts to limit the

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<sup>43</sup> The State legislations of Punjab, Delhi, Haryana, Bengal, Orissa and Andhra Pradesh (Telangana Area) have no provisions for filing of accounts. In the case of Bihar, filing of accounts is restricted to Scheduled Castes/Scheduled Tribes accounts only.

<sup>44</sup> The money lending legislations of the States of Uttar Pradesh, Bombay, Tripura, Bihar, Punjab, Delhi, Haryana, Andhra Pradesh (Telangana Area), Madhya Pradesh, Gujarat and Rajasthan have no provisions enabling the State authorities to search and seize documents.

<sup>45</sup> Exception being the States of Uttar Pradesh, Punjab, Delhi, Haryana, Bihar, Andhra Pradesh (Telangana Area) and Madhya Pradesh

<sup>46</sup> The Moneylenders Acts applicable in the States of Haryana, Delhi, Punjab and Madhya Pradesh do not prescribe any interest rate ceiling. However, Section 6 of the Punjab Registration of Moneylenders' Act, 1938 (Punjab Act No. 3 of 1938) provides that a moneylender's license may be cancelled by the Collector, if it has been found by a Court that he has charged higher rates of interest than those prescribed under Section 5 of the Punjab Relief of Indebtedness Act in more than one suit.

<sup>47</sup> Section 3(2) of the Usurious Loans Act, 1918 (Central Act) reads as under:

"3. Re-opening of transaction –

...

(2) (a) In this section "excessive" means in excess of that which the Court deems to be reasonable having regard to the risk incurred as it appeared, or must be taken to have appeared, to the creditor at the date of the loan.

(b) In considering whether interest is excessive under this section, the Court shall take into account any amounts charged or paid, whether in money or in kind, for expenses, inquiries, fines, bonuses, premia, renewals or any other charges, and if compound interest is charged, the periods at which it is calculated, and the total advantage which may reasonably be taken to have been expected from the transaction.

(c) In considering the question of risk, the Court shall take into account the presence or absence of security and value thereof, the financial condition of the debtor and the result of any previous transactions of the debtor, by way of loan, so far as the same were known, or must be taken to have been known, to the creditor.

(d)..."

The High Court of Madras in the case of Sri Balasaraswathi Ltd., Tirunelveli v. A. Parameswara Aiyar and another (reported in AIR 1957 Mad 122, at page 129 para (28) gave some tests to determine when an interest could be termed as being usurious and observed as under:

"In normal cases, where the security is ample to cover the loan and there is no danger at all to the principal and interest, the Court will hold more than 12 per cent simple interest to be excessive,...where security is not so sound, ten per cent compound interest can be allowed,..."

amount of interest to a sum less than the principal of the loan while passing a decree<sup>48</sup> and also for reopening of transactions.

### **Molestation**

4.11 Karnataka, Kerala, U.P., Tamil Nadu, Bombay and Bengal have provisions defining an offence of 'molestation' and prescribing penalty for the commission or abetment to commit the same<sup>49</sup>. The term 'molestation' has been defined to include use of violence/intimidation against the debtor or family members/loitering near the house or work place/doing of any act calculated to annoy the debtor, etc.

### **Reopening of transactions by Court**

4.12 With the exception of Kerala, Punjab, Delhi, Haryana and AP (Telangana Area) all other States examined by the Group permit the Courts to reopen the transactions pertaining to the loan, settle accounts between the parties and reduce the amount charged to the debtor in respect of any excessive interest.

### **Trade credit**

4.13 Loans from one trader to another (trade credit) have been exempted, expressly or impliedly in Kerala, Andhra Pradesh (Telangana Area), Orissa, Karnataka, Rajasthan, Tamil Nadu, Maharashtra, Gujarat, Nagaland, Haryana, Punjab and Delhi. Even agricultural input credit appears to have been excluded from the purview of the legislations of the States of Karnataka, Maharashtra, Gujarat, Kerala and Madhya Pradesh.

### **Special features**

4.14 Apart from the general provisions common to the legislations of all the States, there are certain special features unique to some of them, which are noteworthy.

### **Commercial lending**

4.15 The Bengal Moneylenders Act, 1940 has a provision defining "commercial loan" (Section 2(4)) to mean a loan advanced to any person to be used by such person solely for the purposes of any business relating to trade, commerce, industry, mining, planting, insurance, transport, banking or entertainment, or to the occupation of wharfinger, warehouseman or contractor or any other venture of a mercantile nature, whether as proprietor or principal or agent or guarantor. Interest rate permitted is higher for such loans. The Andhra Pradesh (Telangana Area) Moneylenders Act, 1949 F has a provision (Section 2(9)) defining the meaning of "trader" and read with the provisions of Section 2(4)(g), providing for exemption to certain categories of loans, which include loan by a trader to another trader. The Kerala Act, while defining "loan", has excluded an advance made by a trader bona fide carrying on business, other than money lending, if such loan is advanced in the regular course of such business.

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<sup>48</sup> Bombay, Karnataka, Tamil Nadu and Rajasthan legislations are examples

### **Penalty for taking salami, batta, gadiana**

4.16 The Bihar Moneylenders Act, 1974 contains a provision<sup>50</sup> providing for penalty on moneylenders who takes from a debtor at the time of advancing loans or deducts out of the principal of such loan any *salami, batta, gadiana* or other extraction of a similar nature.

### **Composition of Offences**

4.17 Certain legislations<sup>51</sup> provide for compounding some of the offences<sup>52</sup> made punishable under the Moneylenders legislations.

### **Exemptions**

4.18 Generally all the legislations define a moneylender to be a person advancing loans. Exemptions from the applicability of the provisions of the money lending laws are of various types (i) exemption provided under the definition of moneylender (Rajasthan Moneylenders Act), (ii) exemption provided under the definition of loan (generally in many legislations); (iii) provisions expressly exempting persons / entities from the provisions of the legislations (Madhya Pradesh Moneylenders Act, 1934); (iv) Provisions empowering Government to exempt persons / entities from the provisions of the legislations; (v) limited exemption is granted under certain legislations (Bombay Moneylenders Act, 1946 – applicable to Maharashtra and Gujarat) to banks, companies, unincorporated bodies *etc.*

### **Debt collectors**

4.19 The AP (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960 has a provision for employing debt collectors by moneylenders after obtaining authorisation from the authority in terms of section 11. The Nagaland Moneylenders Act, 2005 prohibits employment of persons by moneylenders for the purpose of demanding or recovering any loan due to him unless such person is in possession of a certificate (issued by the designated authority of the State) authorising him to act as a debt collector.

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<sup>49</sup> Nagaland Moneylenders Act, 2005 also prescribes penalty for the offence of 'molestation'.

<sup>50</sup> Section 35 of the Bihar Moneylenders Act, 1974

<sup>51</sup> States of Kerala, Uttar Pradesh, Madhya Pradesh, Rajasthan etc.

<sup>52</sup> Under the Kerala and Uttar Pradesh legislations all offences under the Act are compoundable. However, Rajasthan, Madhya Pradesh and Gujarat legislations specify only certain offences which are compoundable.

### **Money lending to be carried on as a “business”**

4.20 The money lending laws of many States<sup>53</sup> specifically cover those who carry on money lending as a business.

### **Definition of “bank” and exemption to advances made by banks**

4.21 The term “bank” has been defined in certain laws<sup>54</sup> to mean a company carrying on the business of banking and registered under the enactment relating to companies. As regards Public Sector Banks, the above mentioned Acts are silent.

### **Loans by Cheque**

4.22 In UP there is a provision requiring that loans above Rs 1,000 are to be evidenced by a cheque<sup>55</sup>.

### **Board for Resolution of Disputes**

4.23 In Bihar Chapter IV deals with conciliation proceedings for resolving disputes pertaining to loans exceeding Rs 100 between the moneylender and the debtor, irrespective of the pendency of a suit for recovery of the loan before a court. In terms of these provisions, the State government can refer the dispute to a Board constituted by it consisting of three members – a chairman who has to be a person agreed upon by the parties or an officer not below the rank of a Sub-Deputy Collector, and one member each representing the parties to the dispute. The decision of the Board is final and cannot be called in question before any Court.

### **Security Deposits**

4.24 Kerala and Karnataka require registered moneylenders to keep security deposits with the Government. The law provides a detailed table specifying the amount of money required to be deposited by a moneylender, and it is linked to the amount of money lent in a year. The security deposits specified under the Kerala Moneylenders Act, 1958 range from a minimum of five thousand rupees to a maximum of two lakh rupees. The security deposits specified under the Karnataka Moneylenders Act, 1961 range from a minimum of five thousand rupees to a maximum of fifty thousand rupees.

### **Audit by Chartered Accountants**

4.25 The Kerala Moneylenders Act, 1958, is the only Act, which provides that the accounts of every moneylender be audited at least once in every year by a person who is a chartered accountant and the audit report submitted to the specified authority<sup>56</sup>.

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<sup>53</sup> Madhya Pradesh Moneylenders Act, 1934, Bengal Moneylenders Act, 1940, Bombay Moneylenders Act, 1946 (applicable to Maharashtra and Gujarat), Andhra Pradesh (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960, Rajasthan Moneylenders Act, 1963, Kerala Moneylenders Act, 1958, Karnataka Moneylenders Act, 1961, Punjab Registration of Moneylenders Act, 1938, Tamil Nadu Moneylenders Act, 1957, Orissa Moneylenders Act, 1939, The Assam Moneylenders Act, 1934 and Nagaland Moneylenders Act, 2005

<sup>54</sup> Andhra Pradesh (Telangana Area) Moneylenders Act, 1349 F, Andhra Pradesh (Andhra Region Scheduled Areas) Moneylenders Regulation, 1960, Madhya Pradesh Moneylenders Act, 1934

<sup>55</sup> Section 14. It may be observed that although the provision appears to have been enacted with a noble intention, the same has lost relevance in the present day.

### **The Rule of “Damdupat”**

4.26 Some of the State laws<sup>57</sup> contain a provision providing for the maximum amount of interest recoverable on loans made by moneylenders, incorporating the rule of *damdupat*. The rule of *damdupat* is a branch of the Hindu law of debt. According to this rule, the amount of interest recoverable at any one time cannot exceed the principal. The rule was applied not only to unsecured loans, but to loans secured by a pledge of movable property and those secured by a mortgage of immovable property.<sup>58</sup> The Rajasthan Moneylenders Act even has got a provision expressly stating that in cases where the moneylender has realised from the debtor an amount equal to or more than twice the amount of the principal, the debtor shall stand discharged and requiring the moneylender to refund the amount so realised in excess of twice the amount of the loan to the debtor.

### **Usurious Loans Act, 1918**

4.27 The Usurious Loans Act, 1918 is also currently applicable to transactions relating to money lending. The Usurious Loans Act, 1918 (ULA) was enacted with the object of preventing the Civil Courts being used for the purpose of enforcing harsh and unconscionable loans carrying interest at usurious rates<sup>59</sup>. The provisions of ULA enable the Courts to reopen transactions by way of money or grain loans in cases where the Court is satisfied (a) that the interest or other return is excessive and (b) that the transaction is substantially unfair and after investigation of the circumstances, both attendant and antecedent, to revise the transaction between the parties and, if necessary, to reduce the amount payable to such sum as the Court, having regard to the risk and all circumstances of the case, may decide to be reasonable. ULA has been made applicable to suits for (a) recovery of a loan, (b) enforcement of any security taken or any agreement, made in respect of any loan and (c) redemption of any security given in respect of any loan<sup>60</sup>. The State Government has been empowered to exempt, by way of notification in Official Gazette, any area, class of transactions or class of persons from the applicability of ULA<sup>61</sup>. ULA provides guidelines to the Court for examining whether a particular rate of interest can be considered to be excessive or not and also for considering whether a transaction is substantially unfair or not. The ULA is applicable to all suits as mentioned above irrespective of the parties involved in the disputes. Therefore, the Act is also applicable to suits in which a moneylender is a party. In view of the provisions of section 21A of the Banking Regulation Act, 1949, the provisions of the ULA are not applicable to banks. Some States like Madhya Pradesh and Maharashtra have made amendments to ULA specifically providing that charging of compound interest in excess of a particular percentage shall be deemed to be excessive. The State of Tamil Nadu has made an amendment to the effect that if compound interest is charged in case of loans to agriculturists, then the Court shall presume that the interest is excessive. Even if there is no prohibition under ULA against charging of compound interest, the Courts have a duty of examining the transaction as a whole and ascertaining whether in a given case, the transaction is

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<sup>56</sup> Section 9I

<sup>57</sup> Rajasthan, Assam, Bihar, Bengal and Orissa

<sup>58</sup> Chapter XXVIII of MULLA Principles of Hindu Law, 15th Edition, 1982, pp 680-684

<sup>59</sup> As stated in the Statement of Objects and Reasons

<sup>60</sup> Section 2 (3) of the Usurious Loans Act, 1918

<sup>61</sup> Section 1(3) of the Usurious Loans Act, 1918

unfair or the rate of interest is usurious.<sup>62</sup> The Bengal Moneylenders Act, 1940 has repealed the Usurious Loans Act, 1918 in respect of money lending transactions falling within the purview of the Bengal Moneylenders Act<sup>63</sup>.

### **Interest Act, 1978**

4.28 Though not a part of the overall body of laws relating to money lending, there is one more Act, viz, the Interest Act, 1978 which can also be applied by Courts while granting interest in suits. The Act is a Central Act and it was enacted with a view to consolidate and amend the law relating to allowing of interest in certain cases. Its provisions<sup>64</sup> empower the Court to allow interest in any proceeding for the recovery of any debt or damages or in any proceedings in which a claim for interest is made in respect of any debt or damages already paid to the person entitled to the debt or damages at a rate not exceeding the "current rate of interest"<sup>65</sup> for the period specified in the provisions<sup>66</sup>.

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<sup>62</sup> AIR 1982 Mad 296 (303)

<sup>63</sup> Section 45 A of the Bengal Moneylenders Act, 1940

<sup>64</sup> Section 3

<sup>65</sup> "current rate of interest" has been defined as "the highest of the maximum rates at which interest may be paid on different classes of deposits (other than those maintained in savings account or those maintained by charitable or religious institutions) by different classes of scheduled banks in accordance with the directions given or issued to banking companies generally by the Reserve Bank of India under the Banking Regulation Act, 1949".

<sup>66</sup> If the proceedings relate to a debt payable by virtue of a written instrument at a certain time, then, from the date when the debt is payable to the date of institution of the proceedings and if the proceedings do not relate to any such debt, then, from the date mentioned in this regard in a written notice given by the person entitled or the person making the claim to the person liable that interest will be claimed, to the date of the institution of the proceedings.

## CHAPTER – 5

### Linkages between Moneylenders and Formal Credit Channels

5.1 Various studies in India and abroad show that the informal sector is better at serving the sectors neglected by banks such as small businessmen, traders, poor transport operators, handloom weavers, small farmers, self-employed people and women. They are also better at recovering loans. They have better market knowledge and lower transaction costs. They are flexible and can customise the products to suit the needs of individual borrowers. They respect the borrowers' privacy. On the other hand, the formal sector has strengths in terms of its access to low cost funds, providing safe avenues for savings and access to payments system. But their procedures and practices deter the poor.

#### Review of Literature

5.2 A review of the available literature suggests that moneylenders continue to provide financial intermediation in areas that are underserved by formal institutions. The very small scale is the critical determining factor, as they are able to provide very tiny sums as loans. J. Howard M. Jones<sup>67</sup>, Professor in University of Reading, U.K. who had examined micro-finance in a tribal village in Rajasthan found that moneylenders continued to cover both consumption and production needs which, given the small scale of finance required, are unlikely to be met by formal financial intermediaries or MFIs. The inherent flexibility in loan use, along with the speed with which the transaction is completed, has ensured continued demand. In contrast to the attitudes of bank managers towards the rural poor, clients were treated with respect by the moneylender. Interestingly, although the interest rates charged by the moneylenders had not come down with the advent of bank credit in the village, additional charges levied by the moneylenders had. This was attributed to the greater financial awareness in the population. Jones concludes that once recognised and understood in all their diversity, the moneylender might have new and different roles to play in future implementations of policy to provide financial services to the rural poor. Supporting Jones is the view that the informal sector serves as lender of last resort to those who are unable to obtain finance in the formal sector because the transaction costs of lending to this group are prohibitive, as the loans they demand are so small<sup>68</sup>.

5.3 A.K. Garg, MD Agricultural Finance Corporation suggests that a comprehensive financial system based on bank-moneylender linkages is required<sup>69</sup>. He notes that if a comparison is made between the credit card interest rates and interest rates charged by moneylenders, the latter are clearly less exploitative. Prof. R. Vaidyanathan, IIM Bangalore, is of the opinion that it is important to recognise moneylenders as legitimate agents of economic activity, and that banks must treat them as channel partners and provide them with credit.<sup>70</sup> It has been suggested by him that banks might consider adopting a policy of encouraging the informal sector with refinance wherever possible (for example, chit

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<sup>67</sup> J. Howard M. Jones- Some Issues in Informal Finance-Perspectives from a Rajasthan Village

<sup>68</sup> Besley, Timothy (1994) How do market failures justify interventions in rural credit markets? *World Bank Research Observer*, 9 (1), pp. 27-47. ISSN 0257-3032

<sup>69</sup> A.K. Garg- 'Making Money Work for Poor - Inclusive Finance through Bank-Moneylender Linkages'

<sup>70</sup> Prof. R. Vaidyanathan, IIM Bangalore- 'Why financial system must legitimise moneylenders'

funds and nidhis). In respect of nidhis, for instance, which extend loans only against tangible security, deposit insurance by the Deposit Insurance and Credit Guarantee Corporation of India could be extended. With such refinance and liberal credit facilities to the deserving informal financial institutions, the banks will be helping the poor indirectly without undertaking a direct risk of default.<sup>71</sup>

5.4 Citing the experience of Bangladesh, P.B. Ghate mentions that, the 'recovery agents' help borrowers roll over bank loans for a fee, after which borrowers obtain a fresh bank loan. It was seen that even after paying the fee, they found the loans worthwhile (Ghate, 1992)<sup>72</sup>. Alternatively, K.G.Karmakar (1999)<sup>73</sup> observes moneylenders in India also disburse loans to borrowers who have bank sanctioned loans but wait to receive them. These anecdotes imply that linkages provide an appealing option (Varghese, 2004)<sup>74</sup>. Using a micro data set from Indian villages, Varghese provides the evidence that those borrowers who borrow also from moneylenders repay banks with greater ease. Thus, borrowers can use moneylenders to smooth cash flows so as to meet bank obligations better. In another interpretation of this linkage, banks provide production loans and moneylenders provide bridge loans in order to ensure continuing access.

5.5 But there are concerns as well. K. Hoff and J. E. Stiglitz (1997) provide evidence that infusion of government subsidised formal credit have not improved the terms offered by the moneylenders. Subsidy induces new entry, which reduces the market of each moneylender and forces him to operate at a higher marginal transacting cost.<sup>75</sup> Thus, interest rates charged by moneylenders rise. An increase in entry also adversely affects borrower's incentive to repay, which increases the enforcement effort that each moneylender must expend per borrower to ensure repayment.

5.6 D.Hulme and P. Mosley argue that the Indonesian system, often quoted as the example of successful linkage, works because of a clear system of control which may not work in all places<sup>76</sup>. Careful consideration must, therefore, be given to the credit market structure that determines the division of surplus among banks, borrowers, and moneylenders. In a monopolistic market, the moneylender can extract the maximum amount and keep borrowers at their lowest reservation utility. In those linkages, borrowers may collude with informal lenders.

5.7 One of the difficulties in the linkage model is the need for banks to ensure that the informal lender continues to lend in an informal manner. In the context of banks lending to Praja Naya Niyamakass (PNNs) of Sri Lanka, the warning is that since the PNNs bear the risk of lending they should be free to lend in any

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<sup>71</sup> Nayar.C.P.S., (1992), "Strengths of Informal Financial Institutions: Examples from India", Westview Press.

<sup>72</sup> Ghate, P.B. (1992) Informal Finance: Some Findings from Asia. Hong Kong: Oxford University Press

<sup>73</sup> Karmakar, K.G. (1999). Rural Credit and Self-help Groups. Delhi: Sage Publications.

<sup>74</sup> Varghese A., (2004), "Can Moneylenders Link with Banks? Theory and Evidence from Indian Villages", Bush School Working Paper.

<sup>75</sup> K. Hoff and J.E. Stiglitz (1997) "Moneylenders and Bankers: Price-increasing Subsidies in a Monopolistically Competitive Market", *Journal of Development Economics*, Volume 52, Number 2, pp. 429-462(34).

<sup>76</sup> . Hulme, D. and P. Mosley (1996). Finance Against Poverty, New York : Routledge.

manner they wanted. Banks should only use moral suasion to achieve the objectives of the scheme, "otherwise this linking would be a kiss of death" (Sanderatne, 1992)<sup>77</sup>.

5.8 Also both theoretically and empirically, linkages are at an embryonic stage in many countries. Issues of mechanism, design, institutions, and incentives are relatively new areas to explore. Furthermore, historically, policymakers have viewed moneylenders as exploitative. This adds a moral and equity dimension that acquires political weight. Indeed, in certain cases, banks may not find it worthwhile since normally, one bank would not like to provide another with borrower training and management skills gratis. Though no study provides independent evaluation on the effectiveness of moneylenders with respect to non-moneylenders, if banks hire moneylenders, they need not expend resources on training since moneylenders are already experienced in this field. Therefore, both commercial banks and the informal institutions would need additional incentives for these linkages. (Verghese 2004).

5.9 In India, initiatives have been taken to bridge the gap in lending by banks. Guidelines have been issued to the effect that the services of Banking Correspondent (BC)/Banking Facilitator (BF) model may be utilised by banks for expanding their outreach in rural areas and in previously unbanked areas. However, only a few banks have adopted these innovations, and there have been reservations in widely expanding/implementing the models. One of the reasons for the scheme not taking off is reported to be the restriction on the BC/BF to recover charges directly from the ultimate borrower.

#### **International Experience of Linkage**

5.10 Africa, Asia and Latin America show a rich variety of linkages between the formal and informal sectors. These financial linkage services include rural smallholders, enterprises, households, small traders and local organisations and associations, and any previously unbanked rural people, such as subsistence farmers and women. One of the schemes adopted by Agricultural Bank of **Malaysia**, involved using co-operatives, farmer's organisations and private traders as local credit agents of the bank. The Praja Naya Niyamaka (PNN) scheme inaugurated by the two state banks in **Sri Lanka** has attempted to link informal credit sources to the institutional banking system. Here banks lend funds to persons of proven credit worthiness, often on the basis of collateral, at an interest rate of 18 per cent per annum and expect the PNNs to lend at an interest rate not exceeding 30 per cent per annum. The banks give the PNNs guidelines on how to lend but do not require them to provide documentation and other proof of their lending. The regional development banks in **Indonesia** have established village units, which disburse loans at weekly mobile bank offices. In order to monitor these transactions, the village units actually hire ex-moneylenders as commission agents to monitor repayments. The lenders receive four per cent of collected loan instalments. The whole system builds a web of incentives, with other participants such as the village headman, who provides some of the linkage advantage, screening borrowers and receiving one and a half percent of pre-tax profits. Another Indonesian bank (BUPB) offers field officers minimum guarantees *plus* two percent of fully repaid loans and seven and a half percent of savings. In eight other

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<sup>77</sup> Sanderatne N., (1992), *"Informal Finance in Sri Lanka"*, Westview Press.

financial intermediaries in Indonesia, village agents screen and collect loans. The agents' wages depend on observable variable such as collected repayments, loan instalments and primarily adjusted profits. This flexible system varies in its implementation across villages in that wages are village specific. The **Philippines** Government has actively intervened to incorporate the informal sector into the overall strategy of agricultural development. When the Masagna-99<sup>78</sup> formal credit programmes expanded, repayments deteriorated, borrowers were excluded and they therefore shifted back to informal lenders. The same phenomenon occurred in rural **Thailand** when the Bank for Agriculture and Agricultural Cooperatives (BAAC) attempted to expand credit. A more proactive and inclusive attitude towards moneylenders has resulted in success for the new credit programmes. In recent years, there have been an increasing number of financial institutions in **Ghana** seeking to establish more formal, purposive linkages with informal financial agents. Evidence suggests a complex set of relationship between a wide range of players in the formal, semi formal and informal financial sectors. Recent examples are (i) Accra based non-bank financial institution had linkage with susu collectors (ii) Accra based Commercial Bank had linkage with Rotating Savings and Credit Associations (ROSCAs), and (iii) another Rural Bank had established links with ROSCAs. Linkage to susu groups and susu collectors offers the potential for reaching even more women clients. The outreach potential of linkage for the formal financial institutions is very apparent in Ghana. These links were all established in the last 5 years. The non-regulated **Bolivian** NGO FADES entered into strategic linkages with private and public sector organisations in an effort to increase its rural outreach. Between 2000 and 2004, a very rapid expansion of its branch network caused FADES to experience a decline in the average number of rural clients per branch, which motivated them to find innovative solutions to sustain their extensive branch network. FADES decided to opt for linkages with several non-financial institutions, and offered to facilitate electricity payments, pension transfers and to sell several utility cards on behalf of Government institutions. This broader array of services led to an increase in the flow of people at the branch, it ensured a flow of funds at the branch level that reduced the need for transfers within the network, and the fees charged were sufficient to pay for several expenses at the branch. In **Rwanda**, as both the formal and informal financial sectors are relatively weak the potential for linkages is extremely low. However, more than 20,000 individuals living deep in the countryside of Rwanda now access credit and other financial services of the Peoples Bank on a regular basis. Also training of SHGs on savings and credit operations, is taking place.

### **Survey findings relating to linkages**

5.11 The results of the survey conducted in various districts across the country were mixed. While many saw advantage in forging formal links either as agent or for on-lending, their concerns were on the adequacy of the remuneration. Registered moneylenders/pawn brokers and unregistered moneylenders

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<sup>78</sup> The Masagana 99 program was initiated in the early 1970s to encourage adoption of new, high-yielding rice varieties. Non-collateral, low-interest loans were made available to small farmers, mainly by privately owned, rural banks, with the government guaranteeing 85 percent of any losses suffered by the banks.

who were big farmers or had a huge volume of business, expressed their unwillingness to work as agents/correspondents of the banks. In urban areas, there had been a decrease in the business of moneylenders with the advent of Credit Cards and ATMs. Branch managers, while welcoming the suggestions from point of view of better outreach, credit appraisal, supervision and recovery in the context of their limited staff constraints, perceived the downside as essentially one of reputation risk.

5.12 The advantages of forging links with moneylenders for more efficient credit delivery according to the branch managers are:

- (i) Better identification of prospective customers in view of better information with moneylenders;
- (ii) Better coverage of remote and unbanked rural areas;
- (iii) Facilitate better recovery;
- (iv) Increase in the portfolio of banks;
- (v) Availability of credit at lower rates compared to what is presently being paid by borrowers to moneylenders;
- (vi) Help in avoiding multiple lending to same borrowers against same assets by both the banks as well as moneylenders;
- (vii) Save the time and effort of banks in credit appraisal, making pre-sanction visits, documentation processes, credit supervision, and recovery, etc., thereby facilitating better credit flow especially in the context of staff shortages at rural branches;
- (viii) Provision of services during the bank holidays as well as after banking hours, which would prove beneficial to people in need of funds in emergency situations.

5.13 The disadvantages are:

- (i) The inability of the banks to enforce end-use of funds, reasonableness of interest rates and ensure fair recovery practices;
- (ii) The likelihood of monopolistic practices if banks withdraw and lend only through moneylenders;
- (iii) Scope for increased political influence;
- (iv) High interest rates, diversion of funds for furtherance of moneylenders' own businesses leading to further malpractices as more funds are made available to them;
- (v) Adverse affect on direct lending and possibility of deterioration of direct relationship between banks and customers and continuance of coercion in recovery, ultimately resulting in tarnishing the bank's image.

5.14 Most moneylenders felt they needed commission of at least 6 per cent to cover their transaction cost as they were dealing with very small loans. They were also concerned about the non-availability of relief/concessions in the event of non-wilful defaults. They feared that banks might not allow the facility of automatic rescheduling of loan and they would be forced to repay on behalf of the farmer-borrowers as per the original repayment schedule, which might lead to recovery risk. They also apprehended that formal linkages might attract adverse attention from income tax and police authorities, and feared harassment from the co-operative department if registration under money lending were made compulsory for accessing bank finance; instead some moneylenders preferred regulation/inspection by some outside agencies, such as NABARD.

## Models for linkage

5.15 The literature reviewed<sup>79</sup> suggests that financial linkages can be grouped into two broad categories: direct and facilitating. Direct financial linkages refer to linkages between financial institutions in which the main purpose of the linkage is to help informal institutions diversify their sources of funding, expand their loanable funds and balance liquidity shortages and excesses. A typical example of this type of linkage is a bank or apex organization offering bulk loans to MFIs for on-lending to clients. Facilitating linkages, on the other hand, refer to linkages between institutions in which the formal institution hires the informal institutions to act on its behalf. This type of linkage facilitates the transactions, such as remittances, payment of utilities, and mobilisation of savings or even facilitates loan payouts. Typically, one partner or financial institution will pay the other partner a fee to facilitate the transaction.

5.16 The search for effective linkages forms part of a wider program in the microeconomics of development. Linkages can help bridge the persistent dualism in many developing countries like India by providing a step in the development process. The linkages suggest that banks should compensate moneylenders according to the moneylenders' opportunity costs and information contribution. Learning from the cross-country experiences, there appears to be potential for linkages between informal and formal financial system in India, which has a strong formal financial sector, but a relatively weaker informal sector. Anecdotal evidence suggests that commercial banks have already been lending to the artisans in Punjab and Chandigarh in a small way, who in turn lend to the farmers and traders, which may be formalised. In the South also, an attempt at linkage has been made by the Indian Bank which has initiated a scheme of lending through rural credit franchisers (RCF) viz. pawn brokers to meet the working capital requirements against gold ornaments through RCF for agricultural purposes.

5.17 Thus, linkages would exploit the advantages of each sector. For example, banks could issue large production loans and request moneylenders to monitor and enforce that loan. In monitoring the loan, moneylenders adopt their own flexible practices. In this manner, banks access borrowers to whom they would otherwise not lend and borrowers access loans that would otherwise be beyond their reach.

5.18 The essential lesson from the international and theoretical studies and the Group's survey is that any attempt in the linkage model to put too many onerous oversight obligations on banks in terms of processes and procedures will be counterproductive as the moneylenders will not be happy. There is need for considerable flexibility, judging only by outcomes and whether objectives achieved compared to the pre-linkage position. It is equally important to recognise that any model can be successful only if more credit flows at lower cost and in timely fashion.

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<sup>79</sup> Maria Pagura & Marié Kirsten, "Formal-informal financial linkages: Lessons from developing countries

## CHAPTER - 6

### Functioning of Moneylenders

6.1 The Technical Group formed sub-groups to solicit the views of the State Governments, bank officials and moneylenders' associations on money lending legislation and the linkages between formal sector and informal credit markets in different parts of the country. The groups toured southern centres including Bangalore, Hyderabad and Thiruvananthapuram and the eastern centres of Patna and Kolkata.

#### Survey results

6.2 In addition to the visits of the sub-group, 16 Regional Offices (ROs) of RBI carried out a survey on the role of informal credit providers (including moneylenders) in rural areas covering 177 districts in 25 States through their Lead District Officers. An important objective of the survey was to identify the downside as well as the upside of such linkages.

The survey was done through focus group discussions, using a structured questionnaire, with cross section of borrowers, rural branch managers, officials from the district administration, different types of informal credit providers, MFIs/SHGs etc., during September-October 2006. The districts were selected taking into account geographical representation, the prevalence of money lending activity and the scale of agricultural operations.

The objective of the meetings of the sub-group and the survey was to understand why, despite the expansion of co-operatives and banks in the rural areas, the dependence of rural households on moneylenders was still so high and had, in fact, increased. The survey also wanted to get a feedback on/from the district administration and moneylenders on the enforcement of existing legislation, suggestions for improvements that would encourage registration and the kind of linkages that could be forged between the formal sector and the informal sector.

#### Findings

6.3 A profile of the prevailing practices of the various types of informal credit providers gleaned from the survey is given in Box-3. While there is considerable variety of practices in various regions, the common features have been depicted.

**Box 3****Profile of Informal Credit Providers**

Various categories of informal credit providers are in existence in most of the States where the survey was conducted. The categories of informal credit providers in order of frequency are pawnbrokers followed by input suppliers, arthiya/commission agents, kirana shopkeepers, lender against land, etc. According to what was reported by the 11 Regional Offices of the RBI there were 12,601 registered moneylenders as on March 1995. This number has increased to 19,627 as on March 2006. Anecdotal evidence suggests that there is a corresponding increase in unregistered moneylenders.

Their mode of operations, viz, maintaining inter-personal relationship with the borrowers, their informal approach, round-the-clock availability of finance, etc., have made them the most important lenders in the villages. Their policy of 'any time, anywhere, any amount', which is borrower-friendly, has strengthened their position in the villages, thus reducing the role of banks. They offer a variety of products tailor-made to the needs of the borrowers.

**Amount lent by moneylenders:** District officials from only five States could furnish the data on the amount of loan advanced by the moneylenders in their jurisdiction as under:

Amt. in Rs. Crore

| Name of State | As on March 1995 | As on March 2006 |
|---------------|------------------|------------------|
| Gujarat       | 38.34            | 139.65           |
| Maharashtra   | 29.90            | 82.28            |
| Kerala        | 25.00            | 138.00           |
| Karnataka     | 19.22            | 87.70            |
| Uttar Pradesh | 34.22            | 181.92           |

b) **Size of the loan:** The average size of the loan varied widely from Rs 1,000 to 30,000. In some cases, it could be as low as Rs 10 and as high as Rs 5 lakh.

c) **Purpose:** The loans provided by the informal credit providers were generally short-term in nature and mainly for the purpose of meeting social obligations associated with weddings, birth or death ceremonies. Loans for farming and livelihood were also common.

d) **Security obtained:** Mostly all the loans were granted against the security of gold jewellery, land documents, cultivation rights, promissory notes and even against utensils. Many of the informal credit providers lent money/inputs-consumption and production credit to farmers/small businessmen without any security/documents and with only a signature in their cashbook register for having taken the loan.

e) **Savings products offered by moneylenders:** Though most moneylenders do not offer any savings products, some operate "Chit Funds" and Bishis.

f) **Innovative Products:** Some moneylenders in Karnataka and Rajasthan had introduced a new product viz. 100 days loan. Under the scheme, the principal amount of Rs.1,000 is lent after deducting an interest amount of Rs120 (upfront) and a sum of Rs10 is collected on a daily basis for the next 100 days. The interest collected works out to 44 per cent per annum. Similarly, a sum of Rs 20,000 is lent deducting an amount of Rs 2,400 as interest (upfront) towards the purchase of vehicles etc., and Rs.200 is collected on a daily basis for the next 100 days. In Karnataka in the Gangavati taluk of Koppal district, it was observed that informal credit providers (who were also rice mill owners and commission agents) have formed co-

operative society (the Tungabhadra Co-operative Society) under the Karnataka Souharda Co-operative Societies Act. They accept deposits and lend to farmers with an informal agreement that the farmers will sell the produce only to the directors of the cooperative societies for liquidating the loan. These societies collect pigmy deposits and also disburse loans with daily/weekly repayment schedules. Under the Souharda Co-operative Societies Act, the supervision and control of the Co-operation Department of Government of Karnataka is minimal and the accounts of the society are audited by a chartered accountant firm.

g) Rates of interest: The rates of interest charged by the creditors ranged from 12 per cent to 150 per cent per annum although the average rate of interest ranged from 18 per cent to 36 per cent per annum. In some cases, it was observed that the input suppliers did not charge any interest explicitly though such interest was subsumed in the cost of the input itself. Also all moneylenders invariably deducted interest upfront from the principal amount and the balance amount was given to the borrower.

h) Collection of Interest: There was no fixed or specific period for the collection of interest by the lenders. They adopted their own practices which were binding on the borrowers. The interest was collected either upfront or on redemption of the loan as per the terms and conditions or after harvest or daily/monthly/half-yearly. In some of the districts of West Bengal it was observed that the interest was collected by the lenders by way of taking the cultivation rights of the mortgaged land which is known as "Sudha-varna System" till the loan amount was repaid. This practice was also prevalent in Punjab. The lenders were not charging any additional interest except in few cases where penalties were imposed on borrowers for delayed repayment of the loan.

#### **6.4 Reasons for continued dependence on moneylenders**

Limited outreach of formal credit institutions: One of the important reasons for continued dependence on moneylenders is that despite its penetration, the formal credit delivery structure has not percolated down to the villages. The villagers, especially the poor, have to necessarily depend on moneylenders for their survival. It would seem from this that any attempts to stop money lending will affect the poor people in the villages by cutting off all access to credit. The main problem seems to be that the credit institutions that were created to replace the moneylenders have become very formal with cumbersome procedures. Equally importantly, the formal credit delivery channels also lack the personal bonds that moneylenders enjoy with the borrowers.

Banks do not like to deal with marginal farmers: More than 50 per cent of the farmers belong to this category, with cultivable areas of less than one hectare. They did not get loans from the banks and were therefore, compelled to approach moneylenders for their needs.

Moneylenders do business at "doorstep" and respect privacy: Moneylenders provide 24/7 service and maintain confidentiality. They even visit households and give money and collect interest and also principal periodically, maintaining one-to-one business relationships.

They lend for consumption purposes without hesitation: Apart from agricultural operations, farmers are dependent on moneylenders for their requirements like weddings, illnesses in the family, education of children, etc. As consumption needs are not met by the formal sector, people approach moneylenders, even at centers where branches of commercial and co-operative banks are present. The rate of indebtedness is more in Kerala particularly among non-asset owning classes, because people tend to

borrow more for consumption (sometimes of the conspicuous variety) and not for farming activities alone.

Inadequate and delayed credit: Under-financing coupled with the delay in sanctioning of loans by banks often forced the borrowers to approach moneylenders even though they charged much higher rates of interest. In Karnataka, even farmers owning 10-15 acres of land were indebted to moneylenders for their emergency requirements. Owing to the high rate of interest charged, and the coercive methods used by them, clearing debts to moneylenders is given higher priority by the borrowers compared to bank loans. The result is that bank loans become overdue and sometimes turn into Non- Performing Assets (NPAs).

### **Enforcement of the money lending legislation**

6.5 Overall, it is very difficult to enforce legislation. The reasons are given below. In most areas, very few moneylenders have a valid licence and no new licence has been issued for a number of years. The common observation heard was that moneylenders operated covertly. In West Bengal, applications for licences were pending for consideration with SDOs/Collectors for over 3 to 5 years. In Jharkhand, an official from one of the districts said that there were no registered moneylenders in his district because the activity was completely informal. The landless labourers get loans from moneylenders through middlemen, who act as a sort of guarantor.

Very few complaints against moneylenders were received by the district administration. But those complaints that were received were mainly about unlicensed money lending, charging of high rates of interest, land grabbing, taking blank pro-notes, etc. (The last pertains to the district of Bhatinda, Punjab, where the administration reported that they had received one complaint each on land grabbing and taking blank pro-notes). Action taken by the authorities varied from the imposition of a penalty, warning to cancel the licence and filing the cases with police.

One of the Divisional Commissioners in Bihar stated that till the 1980s regular reports about money lending were being sent to the State Government. But that has been discontinued over a period of time and as such no data is available on the moneylenders. Even the registered moneylenders do not submit the returns.

In Kerala, where indebtedness to moneylenders is very high, the role of the police in administering the Kerala Moneylenders Act, 1958 was very limited because none of the sections of the Act were effective mainly because the punishment imposed was not severe enough. The concern of the police was that suicides had been taking place because of the pressure tactics adopted by moneylenders. It was proposed that the offences under the Act should be made cognizable and stringent punishment should be awarded to offenders.

When queried about the ineffective implementation of the Act, some of the important reasons given were the lack of adequate administrative infrastructure, lack of awareness about provisions of the Act, absence of complaints, inadequate guidelines, interference of political leaders in local areas, and the fear of registering complaints. Disputes relating to money lending were settled locally by a group of people in the village without having to approach the authorities. As a result, the Kerala administration did not receive any complaint against any moneylender. In Bihar, there was no reported case of illegal money lending as there were no complaints from the public. In West Bengal also the authorities said there were no complaints.

### **Why moneylenders do not register themselves**

6.6 Moneylenders do not register for many reasons. District Officials felt that most of the moneylenders did not register because of:

- (i) the ceiling on the interest rate on lending
- (ii) the cumbersome process of registration
- (iii) The high registration and renewal fee
- (iv) the fear of disclosure of unaccounted money, and audit
- (v) the fear of penalties and
- (vi) the need to compulsorily submit statements/returns at periodic intervals etc.

### **Advantages of registration**

6.7 The advantages of registration as perceived by moneylenders were:

- (i) Registration would help them carry on business lawfully and have legal recourse against defaulters
- (ii) Registration would enable them to exhibit their names over shops, which would enhance their status in society and also bring new customers and help in warding off undue harassment by police authorities

### **Possible incentives for registration.**

6.8 Moneylenders suggested the following incentives to encourage more moneylenders to register:

- (i) Simplification of procedures
- (ii) Exemption from submission of certain types of returns
- (iii) Allowing registered moneylenders to file suits for recovery
- (iv) Government assistance in recovery of their dues
- (v) Access to loan facilities of the banking system with the provision of adequate spread
- (vi) Putting in place a proper mechanism of arbitration to resolve disputes and the implementation of Execution Petitions by government departments for effective recovery
- (vii) Removal of restrictive clauses regarding rate of interest charged by the moneylenders
- (viii) Creation of awareness among moneylenders about the legal framework by publicity/notification
- (ix) Extension of the area of operation to the entire district

- (x) Giving financial incentives
- (xi) Providing legal backing and protection
- (xii) Spreading the word that money lending is not an illegal business provided a licence is obtained

6.9 Moneylenders suggested the following changes in regulations to incentivise registration:

- (i) The removal of restrictions regarding the area of operation in order to increase their customer base
- (ii) Increase in the validity period of the licence
- (iii) Dispensing with cumbersome procedures of submitting details of each and every transaction to the Registrar of Money Lending. Instead, half-yearly or yearly statements of all transactions should suffice.
- (iv) Offering interest on the security deposits kept with the State governments
- (v) Establishing a separate court for the speedy disposal of disputes
- (vi) Extension of some of the facilities such as seizure of mortgaged property etc., as provided to co-operative societies
- (vii) Amending the Act to permit moneylenders to function as agents of banks
- (viii) Popularising money lending legislation and making it hassle-free so that moneylenders can operate like formal financial institutions

6.10 District officials from Karnataka said that security deposits kept with the State government under the Karnataka Moneylenders' Act, 1961 was in the form of investment. Despite a court ruling in favour of the depositors, the payment of interest on such deposits which was in vogue earlier was discontinued in 1998. This may need to be restored. Further, they wanted the recovery mechanism facilities available to co-operative societies under Co-operative Societies Act to be extended to registered moneylenders. Some officials from Madhya Pradesh said not imposing the penalty for non-registration in the past could encourage registration.

6.11 According to the Registrar of Moneylenders (RML) in West Bengal, money lending legislation did not get proper attention from the SDOs/Collectors because they had other pressing matters to attend to. He said that informal interest rates charged by the moneylenders were probably very high and many a times the value of the goods (such as ornaments) pawned by the borrowers, which could not eventually be redeemed. Representatives of the West Bengal Swarnakar Development Association stated that 1.5 per cent per month was their official rate of interest. They said that new customers bargained for even lower rates stating that the banks were offering lower rates. According to the Association, the applications for renewal of licences tended to remain pending with the authorities for long periods. As a result, their business suffered. Their view is the opposite of the State government's view which thought moneylenders fleece the people. On the contrary, they were doing a service to the people and demanded that the government should exempt them from professional tax. They all claimed to be licence holders with Income Tax Permanent Account Numbers, trade licences, VAT and sale tax registration numbers, etc. They demanded that the system should provide for issue of one-time licence and simplified so that they could conduct their business freely.

6.12 One common suggestion was that the licence fee should be made uniform in all the States. Spurious gold also was a problem. It was felt that unregistered entities should be curbed, because they impaired the image of registered moneylenders. In the South, the moneylenders were prepared to give collateral in case bank finance was extended, and to abide by the rules and regulations. However, most of them were not willing to extend unsecured loans to their borrowers as banks do up to some limit and for certain purposes.

### **Suggestions for improvement**

6.13 Officials from Karnataka felt that the existing Act was effective and powerful but needed to include certain penal provisions if it was to be more effective. Pro-active measures by the State government *viz.*, establishing special squads to check the menace of unregistered moneylenders, of charging very high rates of interest, and curbing unlawful and oppressive methods for recovery of dues, would go a long way in effective enforcement of Money Lending Act provisions.

6.14 The registration officials from Uttar Pradesh said that the Act was not effectively enforced because of the lack of adequate manpower and infrastructural support at the district level. To ensure its effectiveness, more teeth should be added to the Act so as to make it a deterrent for moneylenders to violate the cap on interest rates.

6.15 While some of the district authorities from West Bengal were in favour of repealing the Bengal Money Lending Act, 1940, other officials felt that it was not possible to curb the money lending due to the lack of adequate administrative infrastructure. According to some others, the legislation was irrelevant because of the penetration by banks which had a large branch network across the length and breadth of the State.

6.16 The Registrar from Gujarat reported that the amendments carried out in Maharashtra to the Bombay Money Lending Act, 1946 have not been implemented in Gujarat. An increase in penalties, delegation of search and seizure powers, and adequate infrastructure could ensure the effective enforcement of the Act.

6.17 In Nagaland, the district administration, proposed that the activities of the Village Development Board could be included in money lending legislation. They also suggested that the registered moneylender may be allowed to file suits for recovery. The Act in Nagaland is yet to be put in practice.

6.18 District Administration officials from Tinsukia, Assam said that the Act was very old.

6.19 In general, most officials were of the view that the following suggestions would help in the effective enforcement of the Act:

- (i) Increase in penal provisions
- (ii) Specific definition of 'traders' in the Act
- (iii) Involvement of Gram Panchayats/Gram Sabhas in enforcing registration through its collective pressure.
- (iv) Incorporation of quasi judicial powers in the existing Act
- (v) Amendment of the Complaint Redressal Authority Act
- (vi) Creation of awareness among the people and district administration about the Act.

6.20 All the moneylenders interviewed stated that the present interest rate cap under the Money Lending Act was not practical and viable as it did not offset adequately the cost of funds. It is interesting to note that some of the moneylenders from Orissa stated that the Act should be scrapped or removed.

6.21 In general, officials who were interviewed did not wish to include any other activity under Money Lending legislation. They said that the lack of administrative infrastructure, changes in the perception about the evils involved in the transactions in money lending and changes in the State policies were some of the reasons for laxity.

#### **Are MFIs an alternative?**

6.22 The crucial finding here is that in the districts surveyed, and where the presence of MFI-SHG was significant, the incidence of money lending by traditional moneylenders has come down. However, this has not prompted moneylenders to reduce their interest rates. This could be because MFIs do not have a sufficiently large network.

6.23 In general, rural borrowers prefer to approach moneylenders for their credit needs because of the "anytime" availability of loans, that too with minimum formalities. They will turn to the banks only if timely and adequate credit is made available to them with simplified/hassle-free procedures/documentation, and a minimum gap between sanction and disbursement. In other words, the service aspect is crucial.

6.24 The majority of MFIs stated that their presence would replace the activities of moneylenders, while a few of them said that total replacement was not possible but that dependency on moneylenders could be reduced substantially.

6.25 Some MFIs were offering various types of flexible and need-based loan products. Illustratively, an MFI in Deogarh district in Jharkhand provided health insurance to the members of SHG on payment of premium of Rs. 346 and medical insurance up to Rs.20,000 could be availed of, provided the treatment was in the MFI empanelled hospitals.

6.26 One MFI in Davangere district of Karnataka said that they could replace the informal/unorganised moneylenders by providing finance to individuals if adequate finance was made available/extended to them by banks.

6.27 The following suggestions were made by the branch managers for increasing the outreach of MFIs:

- (i) Introduction of a rating system for MFIs to facilitate the disbursement of loans without security/charge
- (ii) Promotion of SHGs - especially women SHGs - to ensure cheaper credit to rural poor and farmers
- (iii) Need to be more tolerant towards defaults
- (iv) Increase the loan period from 11 months to 2-3 years
- (v) Training field staff to be courteous and sensitive to borrowers
- (vi) Giving wider publicity, as most of the persons were not aware of the existence of such entities in their district
- (vii) Encouraging venture capital funding in the initial stages of operation as some of the MFIs are confident of equity funding say after three years
- (viii) Provision of soft loans, say at 5-6 percent per annum, so that they have reasonably higher margins to cover cost;
- (ix) Clear guidelines for MFI including service charges collected by them
- (x) The need for the expertise and guidance from banks and others for introduction of Information Technology
- (xi) Encouraging NGOs with adequate remuneration to form and develop quality SHGs instead of proliferation of SHGs
- (xii) Removal of MFIs from the purview of the State Act on money lending

6.28 MFIs reported that they have taken the following steps to ensure transparency/fairness in interest *plus* charges, fair collection/recovery practices and code of conduct:

- (i) Conducting monthly meetings and regularly visiting the targeted groups
- (ii) Providing proper literature, application forms for loans, passbooks/statements of accounts periodically, repayment schedule to borrowers
- (iii) Subjecting the books of accounts to audit and inspection
- (iv) Clarity in by-laws and interest rates
- (v) Charging interest on loans on flat basis and on reducing balances
- (vi) No hidden charges
- (vii) Sensitising and training the field level staff to be courteous with regard to recovery of loans
- (viii) Recovery at door step and collection against money receipts
- (ix) Rules, regulations and procedures to be followed for assessment, meeting the clientele, recovery procedure, *etc.*, are well documented in a Manual

6.29 In Andhra Pradesh, the MFIs are reported to have voluntarily agreed to adhere to the code of conduct evolved by Sa-Dhan (An association of community development financial institutions).

6.30 A majority of MFIs that were interviewed stated that they did not come under the purview of Money Lending Act. In Karnataka, the MFIs were either registered under Section 25 of the Companies Act or as a trust or as a NBFC. Registration under money lending legislation of the state was not considered necessary or obligatory. However, one MFI in Gulbarga District was registered under Money Lending Act in the State.

6.31 An alternate suggestion received from Karnataka was that PACS can provide an alternative conduit if they can partner with RRBs and banks. As per existing instructions, these societies can only operate with DCCBs. If these societies are ceded to Rural/Semi-urban branches of the RRBs/banks, they can play an effective role in delivering credit to petty businessmen, farmers and other people.

## CHAPTER- 7

### Model Legislation on Money Lenders and Accredited Loan Providers

#### Need for money lending legislation

7.1 The majority of legislations relating to money lending were passed by the various States of India several decades ago. It is, therefore, pertinent to examine whether the legislations are still relevant in the modern context with the spread of banking, changes in the financial sector and the increase in awareness among the rural households in the country. The recent NSSO survey has brought out the significant role played by the moneylenders in the credit delivery system of the country especially in the rural areas. The survey conducted by the Reserve Bank also brought out that the number of moneylenders and quantum lent by them has increased manifold between 1995 and 2006. In spite of there being a legislation, a large number of moneylenders continue to operate without licence and even the registered moneylenders charge interest rates much higher than permitted by the legislation apart from not complying with other provisions of the legislation. Signs of effective enforcement of the legislation are absent. Absence of interest to get registered together with ineffective enforcement implies that the legislation does not reflect the ground realities. There are no incentives for registration or conviction on the part of the State to implement the legislation. Officials of several State Governments, who are administering the legislations at the ground level, admitted that if the legislations are strictly enforced, moneylenders would go out of business and this would adversely affect the interests of the rural borrowers who would have no other source to meet their immediate personal needs. Considering the significance of moneylenders especially in the rural credit delivery system, there is a need for a suitable and effective legislation. While having enabling provisions in the legislation so that there are incentives for registration and mainstreaming the activity of money lending, there is a need for disincentives to those that escape the law in the form of more stringent action against unregistered lenders.

#### Changes in existing legislation

7.2 The legislations concerning money lending presently in force in the States vary from each other in respect of details such as entities covered under the legislation, inclusion/exclusion of trade credit, method of fixing maximum rates of interest that can be charged by moneylenders, powers available to the licensing/registering authorities for production of documents, search and seizure, the consequences of carrying on business without licence, etc. The Technical Group has tried to include the best features of legislation internationally and domestically. It recommends a model legislation for the consideration and adoption by those States that do not presently have a comprehensive legislation in place (Annex-I). The Technical Group also recommends some modifications in the existing legislations like a quick, informal and easy dispute resolution mechanism for better enforcement and mandatory provision for registration to undertake money lending activity in States that have no such provisions.

## **Registration**

7.3 Internationally, informal non-institutional credit providers like moneylenders, loan providers, credit providers, etc. are required to be licensed or registered with a regulatory authority.<sup>80</sup> The legislation by some of the States like Punjab and Haryana do not provide for compulsory registration of moneylenders. The expression 'registration' is found in many State legislations, while some of the State legislations provide for licensing of money lenders. The expression "licence" may be substituted by "registration" as the expression "licence" is perceived as the State control over the entity. Further it is recommended to make registration compulsory by penalising conduct of business without registration. Almost all the legislations prescribe for licence/registration to be issued for a specified period. During the interactions with the sub-groups, many moneylenders and State Government officials felt that registration should be a one time activity as the same would reduce the administrative difficulties faced by them and also that the periodic renewal acted as a disincentive for those engaged in money lending as it brings in avoidable cost and other issues. The Technical Group has noted that internationally also, the money lenders are periodically required to renew their registration. Therefore, the Technical Group is not inclined to make any recommendation for doing away with the legal provisions regarding renewal of registration. The requirement of periodic renewal of registration at less frequent intervals would give an opportunity to the registering authorities to have a look at the activities of moneylenders at regular intervals. The Technical Group recommends that the procedure for registration (and renewal) to be prescribed by the State Government should be made simple and hassle free, encouraging the unregistered money lenders to come forward and register, thereby legitimising their business. Renewal of registration may be at less frequent intervals, say once in three years.

## **Registering authority**

7.4 Even though the draft legislation contemplates appointment of registration authority from amongst the officers of the State Government, the State Governments should be empowered also to appoint persons other than public officers as registering authorities. This would facilitate appointment of non-governmental persons (but suitable persons) as registering authorities, who would have a better idea about the moneylenders and accredited loan providers in that locality.

7.5 Further, for the purpose of bringing in more transparency, the register of money lenders is recommended to be put in the public domain.

## **Exemptions**

7.6 Many international legislations on money lending like those of Hong Kong, Singapore and Lesotho provide for exemptions to certain entities from the applicability of those legislations. Globally, in general, regulated entities like banks, financial institutions and co-operative societies are exempted from the purview of money lending legislations. The Group has observed that the existing State legislations give exemption to banks, statutory corporations, co-operatives and financial institutions like Small Industries

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<sup>80</sup> United Kingdom, Hong Kong, South Africa, Singapore, Japan, Lesotho, United States (South Dakota)

Development Bank of India, State Financial Corporations, etc. The Group has also observed that in certain State legislations, Reserve Bank of India has been given specific exemption from the purview of such legislation<sup>81</sup>. After due deliberation, the Technical Group recommends that the exemption to RBI and banks from the applicability of all the provisions of the money lending legislation should be expressly provided in the legislation itself. Accordingly, a suitable provision has been incorporated in the preliminary Chapter of the legislation. The Group recommends that the term “bank” may include all banking companies, nationalised banks (corresponding new banks), State Bank of India, its subsidiary banks, Regional Rural Banks as also co-operative banks<sup>82</sup>. Also being registered with and regulated by RBI, NBFCs should be exempt from the money lending legislation. Similarly, lending transactions by registered charitable societies and public trusts should also be exempted from the purview of the legislations. The Group also recommends that the State Government should be empowered to notify any other financial institution in consultation with the Reserve Bank for exemption from the provisions of the legislation.

7.7 As regards, inclusion of trade credit (loans by traders in the ordinary course of their business), within the scope of the proposed legislation, the Technical Group deliberated upon the same and is of the view that while both these activities involve credit, interest rates can be subsumed in the price and could be difficult to regulate / enforce. The Technical Group hence recommends that Trade Credit should be kept outside the purview of the proposed legislation. Similarly, credit provided by input suppliers, for the purchase of inputs, may be kept outside the purview of the legislation. However, in some States the level of money lending activities by agriculture input suppliers in the guise of input supplies is very high. As such, those States, may, if they so desire, include input suppliers also within the purview of the legislation.

7.8 In some of the legislations like Andhra Pradesh (Telangana Areas) Money Lenders Act, 1349F, Bombay Money Lenders Act, 1946, the Bengal Money Lenders Act, 1940, Karnataka Money Lenders Act, 1961., loans against negotiable instruments (other than promissory notes) as defined in the Negotiable Instruments Act, 1881, have been exempted from the definition of the term “loan” for the purposes of those legislations<sup>83</sup>. The Group recommends that a provision may be incorporated in the legislations of all the States exempting loans against negotiable instruments (other than promissory notes) from the definition of the term "loan", as these lending transactions are more in the nature of commercial transactions than pure money lending transactions.

7.9 The Technical Group feels that the above measures would narrow down the scope of the legislation, allowing the administering authorities to concentrate on the regulation of pure money lending transactions by individuals and entities conducting business with a profit motive.

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<sup>81</sup> Bihar has granted exemption to Reserve Bank of India by way of a notification under section 3 of the Bihar Money Lenders Act, 1974

<sup>82</sup> Lending transactions by co-operative banks would be exempt as all loans by co-operative societies have been proposed to be kept out of the purview of the money lending legislation.

<sup>83</sup> Some of the legislations have monetary ceilings and lending against instruments above those ceilings are not considered as "loans".

7.10 The Technical Group, while reviewing the existing legislations, observed that only a few State legislations empower the respective State Governments to exempt moneylenders from all or any of the provisions of the Act, although many State legislations have provisions to exempt certain specific institutions from the purview of the Act either by excluding them from the definition of 'moneylender' or by excluding the loans provided by such institutions, from the definition of "loan". The Technical Group recommends that all the State Governments should have a general enabling power to exempt moneylenders from all or any of the provisions of the legislation.

### **Interest rates**

7.11 Internationally as also in the case of the various State legislations in India, the money lending legislations<sup>84</sup> empower the Governments to notify the maximum rates of interest that can be charged by moneylenders. From a survey of the State legislations, it was found that some of the legislations themselves prescribe the maximum rates of interest that can be charged by moneylenders. The Group is of the view that the existing ceilings prescribed under the legislations are out of sync with market reality. Prescription of interest rates in the statute itself is not desirable as the interest rates prescribed for moneylenders should be related to the prevailing market conditions, which would require amendment to the legislation from time to time. Therefore, to provide the State Governments with the flexibility of adjusting the rates of interest in accordance with the market realities, the Technical Group recommends that the prescription of interest rates under the statute itself may be done away with and a provision be made to the effect that the maximum rates of interest that could be charged by moneylenders shall be notified by the State Government from time to time. As this may become cumbersome in a fast changing scenario, the State Government in consultation with the State Level Bankers' Committee (SLBC) could link the rate to a bench-mark with a maximum mark up permitted over the bench mark to factor in other costs, ease of access, doorstep delivery and reasonable margin. While determining the maximum mark up, it would also be reasonable to look at the range of interest rates being charged by micro finance entities in the area as well. Fixing of rates linked to market determined bench-mark, the Group feels, will make more and more unregistered moneylenders view the legislation favourably.

### **Damdumat**

7.12 The money lending legislations of at least five States<sup>85</sup> provide for the rule of *damdumat*, restricting the maximum amount of interest chargeable by the lender to the principal amount. This rule discourages excessive interest on loans and limits the scope for compounding of interest and for penalizing premature repayments in excess of twice the amount of the loan. The Technical Group recommends that the rule of *damdumat* should be incorporated in the legislations by all the States restricting the maximum amount of interest chargeable by the lender to the principal amount. The Technical Group further recommends that there should be a provision requiring the moneylender to refund to the borrower, any excess money paid.

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<sup>84</sup> Hong Kong, Singapore, Japan, United States (South Dakota), South Africa contain provisions regarding interest rate ceiling.

<sup>85</sup> States of Rajasthan, Bihar, Bengal, Assam and Orissa

## **Maintenance of accounts and audit**

7.13 The money lender should be required to maintain proper accounts as is done internationally<sup>86</sup>. The majority of the State legislations in India also have such a provision. As regards furnishing of accounts to borrowers, it has been proposed that while the initial accounts and receipts have to be furnished<sup>87</sup> free of charge, the borrower may have to pay a nominal fee if he wants the statement any time during the year.

7.14 The Technical Group discussed whether there was a need to prescribe any audit by Chartered Accountants<sup>88</sup> of the books of all moneylenders. However, as the majority of the moneylenders are based in the villages having small volume of business, imposing statutory obligation on them to get their accounts audited, is impractical and further audit may not necessarily add value.

## **Powers to inspect, seize and search**

7.15 Many State legislations like those of Bengal, Kerala, Karnataka, Orissa, Tamil Nadu provide for inspection of books of accounts/documents of the moneylenders and their search/seizure, by the regulatory authorities. However, certain State legislations like those of Uttar Pradesh, Bombay and Bihar provide powers only with respect to inspection of documents/books of accounts and not their search and seizure. The Technical Group recommends that the provisions empowering the regulatory authorities to inspect the books of accounts and other documents of the moneylenders should be incorporated in all the State legislations. The power to search and seize accounts should however be exercised at higher level of administration – i.e. higher than those given powers to inspect, so as to avoid undue harassment. It has therefore been proposed that power to search and seize accounts can be exercised only by the registering authority.

## **Dispute resolution**

7.16 Another area of concern with respect to the business of lending has been the lack of a cheap and quick dispute resolution mechanism for the borrowers and lenders. There is a heavy backlog of cases with the Civil Courts resulting in inordinate delay in disposal of the cases. In order to remedy this situation, the Technical Group recommends alternate dispute resolution mechanisms like Lok Adalat and Nyaya Panchayat for speedy and economical dispensation of justice. The Technical Group recommends that disputes on loans upto an amount of Rs.50,000/- should be decided by the Nyaya Panchayats and cases involving loans of more than Rs.50,000/- and also in places where there are no Nyaya Panchayats should be decided by the Lok Adalats. Alternatively, State Governments may think of setting up fast-track Courts/designated Courts to deal with disputes relating to lending transactions by moneylenders and accredited loan providers. The choice of the forum can be decided by the State Governments depending upon the local conditions.

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<sup>86</sup> Hong Kong, Singapore etc.

<sup>87</sup> Internationally also money lenders are required to provide statement of account to the borrower

<sup>88</sup> As provided in the Kerala Money Lenders Act, 1958

7.17 The Technical Group recommends that punishments for specific offences may be provided to take care of the major malpractices, viz, "molestation" (intimidatory tactics and use of force/violence for recovery of the loan, grabbing the property etc.), entry of wrong sums in bonds, promissory notes, taking salami, batta or extractions of similar nature and obtaining blank documents with signature of the borrower and for carrying on the business of money lending without registration. The punishments for these offences should be made stringent. For other offences, the punishment should be a fine upto a maximum amount of Rupees ten thousand. Also all offences have been proposed to be made non-cognizable except the offence of "molestation". Also the offences, except the offence of "molestation", should be compoundable by officials of the State Government or other authorised persons on payment of specified amounts by the accused.

7.18 In order to ensure that the enforcement / administration of the legislation is properly monitored, a new section has been proposed casting an obligation on the State Government to place the Annual Report of administration of the legislation, before the Legislature, thereby ensuring that the State will take proper interest in monitoring the money lending law.

#### **Awareness programmes**

7.19 The State Governments should take adequate steps to spread awareness among the moneylenders of the advantages in registering under the legislation and the intention to enforce the legislation more stringently. The maximum rates of interest notified, the offences under the Act and the dispute redressal machinery provided thereunder must also be publicised. Public should be encouraged to file complaints with the registering authorities if they have a grievance against the persons engaged in money lending activities without registration and / or charging excessive rates of interest. It is found that in many States, the role of the registering and supervisory authority has been given to departments like revenue, who give very little importance to the implementation of the provisions of the legislation. The Reserve Bank survey has indicated that lack of administrative infrastructure, change in the perception about the evils involved in the transactions in money lending and changes in the State policies were some of the reasons cited for the laxity on the part of administration authorities. The State Governments should take pro-active measures like obtaining feedback from the grass-root level especially from NGOs/community based organisations regarding excessive interest rates and adoption of oppressive practices. The State Governments may also consider involving the Gram Panchayats/Gram Sabhas in the implementation of the legislations relating to money lending.

#### Recommendations of Johl Committee

7.20 The Technical Group has been asked to examine certain recommendations made by a High Power Working Group constituted by the Reserve Bank of India under the Chairmanship of Shri S. S. Johl, "to Suggest Measures to Assist Distressed Farmers". The High Powered Working Group, while taking note of the huge percentage of outstanding debt from moneylenders and the usurious rates of interest charged by the moneylenders, has, *inter alia*, suggested certain changes to be made in the legislation governing moneylenders.

7.21 The first suggestion made was that the total liability of the borrower should not exceed double the amount borrowed. The Technical Group has noted that the legislations of at least five States<sup>89</sup> already provide for the rule of *damdupat*, which restricts the maximum amount of interest chargeable by the lender to the principal amount as a result of which the total liability of the borrower is not to exceed double the amount borrowed. The Technical Group has already recommended incorporation of a similar provision in all the State legislations.

7.22 The second suggestion was that a ceiling on the rate of interest may be fixed say, at SBI's Benchmark Prime Lending Rate plus 4 per cent. The legislations relating to money lending that are in force contain provisions either prescribing the maximum interest rates that can be levied by the money lenders or enabling the State Governments to notify the maximum chargeable interest rates from time to time. The Technical Group has, after detailed deliberations, recommended that the State legislations on money lending should empower the State Governments to notify the rate of interest in accordance with the market related bench-marks in the banking and non banking sector. Based on the recommendations of the Technical Group, it is perceived that the rate of interest notified by the State Governments may work out to somewhat more than what was suggested by the High Powered Working Group, but would be much less than what is actually charged by some money lenders at present. It may be noted that some studies have worked out transaction cost at 5 to 6 per cent for small loans (Rs 15000 to Rs 20000) and this would have to be part of the margin apart from risk cost and normal profits for continuing in the business.

7.23 The third suggestion relates to the Court's jurisdiction to scrap all residual liabilities with retrospective effect if repayments have been made, up to double or more than the amount borrowed. This suggestion is an extension of the first suggestion. As already stated, some of the legislations<sup>90</sup> specifically contain provisions requiring the moneylender to return any money paid in excess while applying the rule of *damdupat*. The Technical Group has already included this recommendation in its report.

7.24 The last two suggestions are that one residential house and land up to 5 acres should not be attached under any circumstances and should not be taken as collaterals and that the land and residential house may be used only to assess the worth of the borrower and to assess reasonable credit needs of the person. In this connection, it is noted that the provisions of clause (c) of the proviso to sub-section (1) of Section 60 of the Code of Civil Procedure, 1908 specifically exempts "houses and buildings (with materials and sites thereof and the land immediately appurtenant thereto and necessary for their enjoyment) belonging to an agriculturalist or a labourer or a domestic servant and occupied by him". Thus, even presently, the residential house of an agriculturalist is statutorily exempt from attachment and sale. As regards the recommendation to exempt agricultural land upto five acres from attachment, there is a risk that having such a provision may actually result in denial of credit to the small farmer. The Technical Group is, therefore, not in favour of incorporating any such provision in the money lending legislation.

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<sup>89</sup> States of Rajasthan, Bihar, Bengal, Assam and Orissa

<sup>90</sup> For example Rajasthan Money Lenders Act,

### **Addition of a new chapter to enable registration of accredited loan provider**

7.25 During the survey conducted by the Reserve Bank and the meetings of the sub- groups, many informal credit providers (moneylenders and non-governmental organizations) stated that they were agreeable to enter into linkages with banks as agents or as intermediaries for on lending, if the fee/spread offered to them were reasonable. However, moneylenders who were big farmers or having huge volume of business expressed their unwillingness to work as agents or intermediaries of banks as they had enough capital of their own and would not like the banks to have an oversight on their business. The response to the survey also indicated that a number of money lenders expressed apprehensions on formalisation of their relationship with bankers. These apprehensions were largely with regard to excessive documentation for securing loans, adhering to rigid accounting practices, likely requirement of collateral, possibility that there will be no relief provided to them from institutional creditors in case of non-willful default or untimely death of borrowers, *etc.* The bankers interviewed during the survey were of the opinion that keeping in view the requirements of the rural clientele, there was a need for more flexible approaches that were inhibited by the formal institutional structures. To take advantage of the knowledge base, informality and easy access of the moneylender, formalising the relationship with the informal credit providers might prove beneficial to farmers, rural households, banks and to the informal credit providers themselves. They also felt that linkage might help in identification of prospective borrowers, coverage of remote rural and unbanked areas, avoidance of multiple lending to same borrower, *etc.* However, the bankers had concerns regarding the nature of security, end use of bank's funds, conflict of interest, high rates of interest, discriminatory lending, NPA risk, tarnishing of bank's image, *etc.* In general the borrowers wanted more competitive rates and transparent and fair practices in recovery.

7.26 The Technical Group is of the view that there will be considerable advantage in having a separate chapter in the States' money lending legislations for establishing linkage between the formal and informal credit providers to leverage on dominant presence of moneylenders while providing incentives for more competitive rates and fair practices. Such linkages could provide yet another credit delivery channel to rural households and increase the flow of such credit especially to the rural poor. Such an arrangement may also give an added thrust to the initiatives towards "financial inclusion" through the formal lending institutions. Many of the apprehensions expressed by the informal lenders with respect to linkage with formal institutions can be addressed in the agreements between the banks and the informal lenders, monitoring of activities of the lenders involved in onlending activities by the banks and restricting the linkage to those with whom the bankers have comfort. With this intention in mind, the Technical Group has proposed introduction of a new class of loan providers in the proposed model legislation - Accredited Loan Providers, to differentiate between the sources of funds and the presence or absence of linkage with the formal credit delivery institutions. The draft legislation thus, provides for two sets of regulatory provisions, *i.e.*, one for the ordinary money lenders and another for the accredited loan providers.

7.27 The Technical Group recommends that States that have comprehensive legislations relating to money lending may consider amendment to incorporate a separate chapter relating to accredited loan providers, who will be loan providers having linkage with banks. A definition of the term "institutional creditor" has been incorporated in the proposed legislation and the banks that provide credit to accredited loan providers for the purpose of on-lending have been defined as "Institutional Creditors". The provisions in the Chapter dealing with accredited loan providers as proposed in the draft legislation would encourage existing moneylenders, input dealers, agricultural traders, commission agents, agricultural output processors, vehicle dealers, oil/petrol dealers, retired postmen /schoolteachers, educated youth or any other person who may be considered by institutional creditors as suitable for the purpose, to register themselves as accredited loan providers for on-lending purposes. Such accredited loan providers would be expected to be monitored by those banks. The accredited loan providers would be doing business independent of the banks, at their own risk and the banks would facilitate them to set up the business by giving them the required funds for on-lending with risk on borrowers being taken by such accredited loan provider. Unlike banks where the lending is done only during working hours, accredited loan providers would be accessible to the public round the clock. The accredited loan providers would also act as competitors to more established money lenders, thereby bringing in discipline in the informal credit delivery structure.

#### **Eligibility for accredited loan providers**

7.28 The Technical Group is of the opinion that the persons eligible for linkage with the institutional creditors should be residents of the area of operation, having intimate knowledge of the population and with sufficient education to be able to maintain accounts. Existing moneylenders, input dealers, agricultural traders, commission agents, agricultural output processors, vehicle dealers, oil/petrol dealers, or any other person may be considered by institutional creditors as accredited loan providers for on-lending purposes. The State Government could offer a short duration certification course which could be in local language and which will have to be completed within one year of linkage with the bank. Institutes such as the Indian Institute of Banking and Finance could offer their services in designing such a course and providing accreditation.

#### **Registration of accredited loan providers**

7.29 The accredited loan providers would also be required to obtain a registration from the registering authority. The application for such registration should be counter signed by the institutional creditor to assure the registering authority that the accredited loan provider will be linked to a specific bank branch. An accredited loan provider can be linked only to one bank at any point of time. The process of counter signing would also help the bank to ascertain the details stated in the application form submitted by the accredited loan provider.

## **Incentives to Accredited Loan Providers**

7.30 In order to incentivise registration as accredited loan providers, the Group recommends that

(i) The process of registration should be simplified requiring mere countersignature by the branch manager of the bank with whom such accredited loan provider seeks to be linked. Unlike in the case of money lenders, the registration of accredited loan providers should be a one time event, which could be cancelled or suspended by the registering authorities for sufficient reasons like prosecution or conviction of the accredited loan providers or on the information of institutional creditor about the termination of relationship between the accredited loan provider and the institutional creditor.

(ii) While the designated State Government officials should have the power to inspect the books of accounts of traditional money lenders and if necessary seize such books, the Technical Group recommends and proposes that in case of accredited loan providers, if there is an issue warranting such inspection, the institutional creditor could be requisitioned to furnish the details of loans, *etc.*, and the information could be provided to the registering authority for taking action as warranted for non-compliance of any regulation by such accredited loan provider. The Technical Group has been prompted in making this recommendation as activities of accredited loan providers are expected to be closely monitored by the institutional creditors.

7.31 As regards the applicability of the Usurious Loans Act, 1918, to such accredited loan providers, the Technical Group has noted that all banks including co-operative banks are, by virtue of Section 21 A of the Banking Regulation Act, 1949, exempt from the provisions of the Usurious Loans Act, 1918. They deliberated as to whether the provisions of Usurious Loans Act, 1918 or any other similar law should be made inapplicable to the interest charged on the loans provided by them, thus barring the Courts from examining the excessiveness or otherwise of the interest rate charged. The Group feels that keeping in view the factors recommended by the Group for fixing market related interest rates taking into account costs and risks, there is merit in retaining the applicability of the Usurious Loans Act 1918 to accredited loan providers.

## **Safeguards through agreement between bank and accredited loan provider**

7.32 For the new system of accredited loan providers to succeed, it is imperative to have certain conditions in the agreement between the banks/financial institutions and the accredited loan providers. To ensure that the accredited loan providers pursue good practices, the agreement by the banks with the accredited loan providers should enable the banks to inspect the books of the accredited loan provider, cross verify lending, interest rates charged, *etc.* The agreement may also provide for the rate of interest at which the accredited loan provider would on-lend. The institutional creditors can fix a limit upto which they would finance an accredited loan provider. The agreement should make it mandatory for the accredited loan provider to conduct a large portion, in any case not less than fifty per cent, of his business of lending, by utilizing the funds obtained from the institutional creditor under the agreement. The agreement can also consider providing for rescheduling of the loan/ its repayment schedule to the accredited loan provider in case of untimely death of the ultimate borrower or other genuine emergencies. The agreement

may also contain a clause enabling the institutional creditor to terminate the agreement with, say, three months prior notice, if any violation of the agreement is detected in the on-lending process. The institutional creditors may be required to review the accounts of the accredited loan provider at least once every six months and should assist the accredited loan provider to adhere to best practices. The institutional creditor should ensure that the documentation in the linkage process is kept to a minimum.

7.33 Since the accredited loan providers would be acting independently of the institutional creditors (and not as their agents), the risk involved in such on-lending should naturally fall only on those accredited loan providers. However, as an optional mutually agreed arrangement, the institutional creditor could enter into an agreement for sharing a part of the credit risk, in order to attract more persons to take up the business of accredited loan providers.

7.34 The advances made by institutional creditors to accredited loan providers, may be treated as priority sector lending. This would encourage the banks to take up the role of institutional creditors and disburse loans through the linkage with accredited loan providers as an additional business.

7.35 While the Group interacted with moneylenders there was some preference for linkage with the banks as agents. The Group has noted that the Reserve Bank has framed a policy vide Reserve Bank's Circular DBOD No. BL.BC. 58 / 22.01.001 / 2005-2006 dated 25th January 2006, which allows banks to use the services of certain entities as 'business facilitator' and utilise the services of societies, trusts, cooperatives and Section 25 companies apart from Post Offices as 'business correspondents'. On the issue of whether accredited loan providers could act as "business correspondents", the Group is of the view that there could be a possible conflict of interest if the accredited loan provider, as an on-lending entity having principal to principal relationship with banks, also acts as an agent (business correspondent). Hence, enabling policy changes could be considered by RBI to allow banks to use accredited loan providers as agents viz. business correspondents after gaining experience with implementation of the scheme of accredited loan provider for on-lending purposes.

7.36 The issue whether business correspondents and business facilitators would get covered within the scope of the money lending legislations and whether any provision was needed to be proposed was also considered. The Technical Group is of the view that in terms of the aforesaid circular, business correspondents would be undertaking activities which would be within the normal course of the banking business and thus would be outside the purview of the money lending legislations. Similarly, the business facilitators would not be undertaking any lending activity and hence, the question of bringing them within the scope of the money lending legislation does not arise. As such, no provision is proposed to be recommended in the draft legislation regarding business correspondents and business facilitators.

#### **State Specific modifications**

7.37 The Technical Group recommends that the provisions in the model legislation may be adopted by all States by making suitable amendments to the respective State legislations relating to money lending, after taking into account any unique conditions exclusively applicable to the State concerned and after putting its intentions in public domain.

## CHAPTER- 8

### Summary of Recommendations

8.1 Considering the significance of moneylenders especially in the rural credit delivery system, there is a need for a suitable and effective legislation in the interest of the borrower. While having enabling provisions in the legislation so that there are incentives for registration and mainstreaming the activity of money lending, there is a need for disincentives to those that escape the law in the form of more stringent action against unregistered lenders (para 7.1).

8.2 The Technical Group recommends a model legislation for the consideration and adoption by the State Governments that do not presently have a comprehensive legislation in place (Annex-I). The Technical Group also recommends some modifications in the existing legislations like a quick, informal and easy dispute resolution mechanism for better enforcement and mandatory provision for registration to undertake money lending activity in States that have no such provisions (para 7.2).

8.3 The word “licence” may be substituted by “registration” as the expression “licence” is perceived as the State control over the entity. Further, it is recommended that registration should be made compulsory by penalising the conduct of business without registration (para 7.3).

8.4 The procedure for registration (and renewal) to be prescribed by the State Government should be made simple and hassle free, encouraging the unregistered money lenders to come forward and register, thereby legitimising their business. Renewal of registration may be at less frequent intervals say once in three years (para 7.3).

8.5 The State Governments should be empowered also to appoint persons other than public officers as registering authorities. This would facilitate appointment of non-governmental persons (but suitable persons) as registering authorities, who would have a better idea about the moneylenders and accredited loan providers in that locality (para 7.4).

8.6 Further, for the purpose of bringing in more transparency, the register of moneylenders is recommended to be put in the public domain (para 7.5).

8.7 Exemption to RBI and banks from the applicability of all the provisions of the money lending legislation should be expressly provided in the legislation itself. Also being registered with and regulated by RBI, NBFCs should be exempt from the money lending legislation. Lending transactions by registered charitable societies and public trusts should also be exempted from the purview of the legislations. (para 7.6).

8.8 The Technical Group recommends that trade credit should be kept outside the purview of the proposed legislation. Similarly, credit provided by input suppliers for the purchase of inputs may be kept outside the purview of the legislation. In some States the level of money lending activities by agriculture input suppliers in the guise of input supplies is very high. As such, those States, may, if they so desire, include input suppliers also within the purview of the legislation. (para 7.7).

8.9 A provision may be incorporated in the legislations of all the States exempting loans against negotiable instruments (other than promissory notes) from the definition of the term "loan", as these lending transactions are more in the nature of commercial transactions than pure money lending transactions (para 7.8).

8.10 The Technical Group recommends that all the State Governments should have general enabling power to exempt money lenders from all or any of the provisions of the legislation (para 7.10).

8.11 To provide the State Governments with the flexibility of adjusting the rates of interest in accordance with the market realities, the prescription of interest rates under the statute itself, may be done away with and a provision be made to the effect that the maximum rates of interest that could be charged by money lenders shall be notified by the State Government from time to time. As this may become cumbersome in a fast changing scenario, the State Government in consultation with the SLBC could link the rate to a bench mark with a maximum mark up permitted over the bench mark to factor in other costs, ease of access, doorstep delivery and reasonable margin. While determining the maximum mark up, it would also be reasonable to look at the range of interest rates being charged by micro finance entities in the area as well (para 7.11).

8.12 The Technical Group recommends that the rule of damdupat should be incorporated in the legislations by all the States, restricting the maximum amount of interest chargeable by the lender to the principal amount (para 7.12).

8.13 The moneylender should be required to maintain proper accounts as is done internationally. The initial accounts and receipts have to be furnished free of charge, the borrower may have to pay a nominal fee, if he wants the statement any time during the year (para 7.13).

8.14 Provisions empowering the regulatory authorities to inspect the books of accounts and other documents of the moneylenders should be incorporated in all the State legislations. The power to search and seize accounts should, however, be exercised at higher level of administration *i.e.* higher than those given powers to inspect, so as to avoid undue harassment. The power to search and seize accounts may be exercised only by the registering authority (para 7.15).

8.15 In order to remedy the situation of inordinate delay in disposal of the cases by Civil Courts, the Technical Group recommends alternate dispute resolution mechanisms like Lok Adalat and Nyaya Panchayat for speedy and economical dispensation of justice (para 7.16).

8.16 The Technical Group recommends that disputes on loans upto an amount of Rs.50,000/- should be decided by the Nyaya Panchayats and cases involving loans of more than Rs.50,000/- and also in places where there are no Nyaya Panchayats should be decided by the Lok Adalats. Alternatively, State Governments may think of setting up of fast-track Courts/designated Courts to deal with disputes relating to lending transactions by money lenders and accredited loan providers. The choice of the forum can be decided by the State Governments depending upon the local conditions (para 7.16).

8.17 The Technical Group recommends that punishments for specific offences may be provided to take care of the major malpractices, viz, "molestation" (intimidatory tactics and use of force/violence for recovery of the loan, grabbing the property etc.), entry of wrong sums in bonds, promissory notes, taking salami, batta or extraction of similar nature, and obtaining blank documents with signature of the borrower and for carrying on the business of money lending without registration and the punishments for these offences should be made stringent. For all other offences, the punishment should be fine upto a maximum amount of Rupees ten thousand (para 7.17).

8.18 All offences have been proposed to be made non-cognizable except the offence of 'molestation'. The offences, except the offence of "molestation", should be compoundable by officials of the State Government or other authorised persons on payment of specified amounts by the accused (para 7.17).

8.19 In order to ensure that the enforcement / administration of the legislation is properly monitored, a new section has been proposed casting an obligation on the State Government to place the Annual Report of administration of the legislation, before the Legislature, thereby ensuring that the State will take proper interest in monitoring the money lending law (para 7.18).

8.20 The State Governments should take adequate steps to spread awareness among the moneylenders of the advantages in registering under the legislation and the intention to enforce the legislation more stringently. The maximum rates of interest notified, the offences under the Act and the dispute redressal machinery provided thereunder must also be publicised and public should be encouraged to file complaints with the registering authorities if they have a grievance against the persons engaged in money lending activities without registration and / or charging excessive rates of interest (para 7.19).

8.21 The State Governments should take pro-active measures like obtaining feedback from the grass-root level especially from NGOs/community based organisations regarding excessive interest rates and adoption of oppressive practices (para 7.19).

8.22 There will be considerable advantage in having a separate chapter in the States' money lending legislations for establishing linkage between the formal and informal credit providers to leverage on dominant presence of moneylenders, while providing incentives for more competitive rates and fair practices. With this intention in mind, the Technical Group has proposed introduction of a new class of loan providers - Accredited Loan Providers, to differentiate between the sources of funds and the presence or absence of linkage with the formal credit delivery institutions (para 7.26).

8.23 States that have comprehensive legislations relating to money lending may consider amendment to incorporate the separate chapter relating to accredited loan providers, who will be loan providers having linkage with banks (para 7.27).

8.24 Persons eligible for linkage with the institutional creditors should be residents of the area of operation, having intimate knowledge of the population and with sufficient education to be able to maintain accounts. Existing moneylenders, input dealers, agricultural traders, commission agents,

agricultural output processors, vehicle dealers, oil/petrol dealers, or any other person may be considered by institutional creditors as accredited loan providers for on-lending purposes. The State Government could offer a short duration certification course which could be in local language and which will have to be completed within one year of linkage with the bank. Institutes such as the Indian Institute of Banking and Finance could offer their services in designing such a course and providing accreditation (para 7.28).

8.25 In order to incentivise registration as accredited loan providers, the Technical Group recommends that –

(i) The process of registration should be simplified requiring mere countersignature by the branch manager of the bank with whom such accredited loan provider seeks to be linked. The registration of accredited loan provider should be a one time event.

(ii) If there is an issue warranting inspection, the institutional creditor could be requisitioned to furnish the details of the loans, *etc.* (para 7.30).

8.26 To ensure that the accredited loan providers pursue good practices, the agreement by the banks with the accredited loan providers should enable the banks to inspect the books of the accredited loan provider, cross verify lending, interest rates charged, *etc.* The agreement may also provide for the rate of interest at which the accredited loan provider would on-lend. The institutional creditors can fix a limit upto which they would finance an accredited loan provider. The agreement shall make it mandatory for the accredited loan provider to conduct a large portion, in any case not less than fifty per cent, of his business of lending, by utilizing the funds obtained from the institutional creditor under the agreement. The agreement can also consider providing for rescheduling of the loan/ its repayment schedule to the accredited loan provider in case of untimely death of the ultimate borrower or other genuine emergencies (para 7.32).

8.27 As an optional mutually agreed arrangement, the institutional creditor could enter into an agreement for sharing a part of the credit risk, in order to attract more persons to take up the business of accredited loan providers (para 7.33).

8.28 The advances made by institutional creditors to accredited loan providers, may be treated as priority sector lending. (para 7.34).

8.29 There could be a possible conflict of interest if the accredited loan provider as an on-lending entity having principal to principal relationship with banks also acts as an agent (business correspondent). Enabling policy changes could be considered by RBI to allow banks to use accredited loan providers as agents viz., business correspondents after gaining experience with implementation of the scheme of accredited loan provider for on-lending purposes (para 7.35).

8.30 The provisions in the model legislation may be adopted by all States by making suitable amendments to the respective State legislations relating to money lending, after taking into account any unique conditions exclusively applicable to the State concerned and after putting its intentions in public domain (para 7.37).

**ANNEX – I**

**Money Lenders & Accredited Loan Providers' Bill, 2007  
(Model Legislation)**

| <b>Section</b> | <b>Heading</b>                       | <b>Provisions</b>   |
|----------------|--------------------------------------|---|
|                | Preamble                             | An Act to amend and consolidate the law relating to money lending in the State of ___ and for matters connected therewith and incidental thereto.<br><br>Whereas, it is expedient to make provisions for protecting the interests of borrowers, for regulating the transactions of money lending and to secure more transparency in such transactions in the State of _____;<br><br>Be it enacted by the Legislature of the State of ___ in the Fifty-Eighth Year of the Republic of India as follows:-   |
|                | <b>Chapter I</b>                     | <b>Preliminary</b>  |
| 1              | Short title, extent and commencement | (1) This Act may be called the _____ Money Lenders and Accredited Loan Providers Act, 2007.<br><br>(2) It will extend to the whole of the State of _____.<br><br>Provided that the State Government, may by notification, exclude the operation of this Act to the Scheduled areas or extend the operation of this Act to such areas, with such modification, as it may deemed fit. <sup>91</sup><br><br>(3) It shall come into force on such date as the State Government may by notification, appoint.<br><br>Provided that different dates may be appointed for different sections of the Act.<br><br>(4) Nothing contained in this Act shall apply to the Reserve Bank or any bank. |
| 2              | Definitions                          | In this Act, unless the context otherwise requires -<br><br>(1) "Accredited Loan Provider" means a person who has a contractual arrangement with an institutional creditor for receiving finance from such institutional creditor for the purpose of onlending to the borrowers in his or its own name;   |

<sup>91</sup> The proviso is meant for the States which may have scheduled areas.

| Section | Heading | Provisions  |
|---------|---------|---|
|         |         | <p>(2) "bank" means -</p> <p>(i) a banking company or a cooperative bank to which the Banking Regulation Act, 1949 (Central Act 10 of 1949) applies;</p> <p>(ii) the State Bank of India constituted under the State Bank of India Act, 1955 (Central Act 23 of 1955);</p> <p>(iii) a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 (Central Act 38 of 1959);</p> <p>(iv) a corresponding new bank constituted under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (Central Act 5 of 1970);</p> <p>(v) a corresponding new bank constituted under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (Central Act 40 of 1980); and</p> <p>(vi) a regional rural bank established under the Regional Rural Banks Act, 1976 (Central Act 21 of 1976);</p> <p>(3) "borrower" means a person to whom a loan is advanced and includes a successor-in-interest or surety;</p> <p>(4) "co-operative society" means a society registered or deemed to have been registered under the _____ Co-operative Societies Act__ or any other Act relating to Co-operative societies and includes a multi state co-operative society registered under the Multi-State Co-operative Societies Act, 2002 (Central Act 39 of 2002);</p> <p>(5) "institutional creditor" means any bank which has advanced or agreed to advance monies to accredited loan providers for the purpose of on-lending.</p> <p>(6) "interest" includes the return to be made over and above what is actually lent, whether the same is charged or sought to be recovered specifically by way of interest or otherwise, but does not include any sum lawfully charged by a money lender or accredited loan provider as costs, charges, expenses towards evaluation, assessment and creation of the security.</p> |

| Section | Heading | Provisions   |
|---------|---------|--|
|         |         | <p>7) "Loan" means an advance whether of money or kind at interest, with or without security, and includes advance, discount, money paid for or on account of or on behalf of or at the request of any person, or the forbearance to require payment of money owing on any account whatsoever, and every agreement (whatever its terms or form may be) which is in substance or effect a loan of money, and also an agreement to secure the repayment of any such loan, but does not include,-</p> <p>(a) a deposit of money or other property in a Government Post Office Bank or in a Government Savings Bank;</p> <p>(b) a loan advanced by the State Government or by any local authority authorised by the State Government;</p> <p>(c) a deposit of money with or a loan advanced by a co-operative society;</p> <p>(d) a loan advanced by the National Bank for Agriculture and Rural Development established under the National Bank for Agriculture and Rural Development Act, 1981 (Central Act 61 of 1981);</p> <p>(e) a loan advanced by the Export-Import Bank of India established under the Export-Import Bank of India Act, 1981 (Central Act 28 of 1981);</p> <p>(f) a loan advanced by the Small Industries Development Bank of India, established under the Small Industries Development Bank of India Act, 1989 (Central Act 39 of 1989)</p> |

| Section | Heading | Provisions  |
|---------|---------|---|
|         |         | <p>(g) a loan advanced by the National Housing Bank, constituted under the National Housing Bank Act, 1987 (Central Act 53 of 1987)</p> <p>(h) a loan advanced by State Financial Corporations established under the State Financial Corporation, Act, 1951 (Central Act 63 of 1951); and</p> <p>(i) a loan advanced by any institution</p> <p>(1) established by or under an Act of Parliament or the legislature of a State, which grants any loan or advance in pursuance of the provisions of that Act; or</p> <p>(2) notified in this behalf by the State Government, in consultation with the Reserve Bank;</p> <p>(j) an advance made to a subscriber, or a depositor in a Provident Fund from the amount standing to his credit in the fund in accordance with the rules of the fund;</p> <p>(k) a loan to or by an insurance company as defined in the Insurance Act, 1938 (Central Act IV of 1938);</p> <p>(l) a loan or debenture in respect of which dealings are listed on any Stock Exchange;</p> <p>(m) a loan or deposit to or by a non-banking financial company registered with Reserve Bank under chapter III B of the Reserve Bank of India Act, 1934 (Central Act 2 of 1934);</p> <p>(n) a loan to, or by, or a deposit with, any charitable society or association registered under the ___ Societies Registration Act, ___ or the Public Trusts Act, ___, as the case may be;</p> <p>(o) an advance made on the basis of a negotiable instrument as defined in the Negotiable Instruments Act, 1881 (Central Act XXXVI of 1881) other than a promissory note;</p> <p>(p) a loan or advance made by a trader bonafide carrying on any business, other than money lending, if such loan is advanced in the regular course of such business;</p> <p>Explanation: For the purposes of clause (p), "trader" means a person who in the regular course of business buys and sells goods or other property, whether movable or immovable and includes a wholesale or a retail merchant.</p> <p>(8) "Lok Adalat" means the Lok Adalat established under the provisions of the Legal Services Authority Act, 1987 (Central Act 39 of 1987) and includes a Permanent Lok Adalat ;</p> |

| Section | Heading                              | Provisions  |
|---------|--------------------------------------|---|
|         |                                      | (9) "money lender" means a person whose main or subsidiary occupation is the business of advancing and realising loans in the State;  |
|         |                                      | (10) "Nyaya Panchayat" means the body constituted at the panchayat level by the _____ Act (Panchayat Act of the State concerned)  |
|         |                                      | (11) "prescribed" means prescribed by rules made under this Act;  |
|         |                                      | (12) "principal" means in relation to a loan, the advance actually made to a borrower;  |
|         |                                      | (13) "register" means a register of money lenders or accredited loan providers maintained under this Act;   |
|         |                                      | (14) "registering authority" means a person or an officer appointed by the Government to perform the functions of a registering authority under this Act;   |
|         |                                      | (15) "registration" means a money lender's registration or accredited loan provider's registration granted under this Act;  |
|         |                                      | (16) "Reserve Bank" means the Reserve Bank of India constituted under Section 3 of the Reserve Bank of India Act, 1934 (Central Act 2 of 1934);   |
|         |                                      | (17) "rules" means rules made under this Act;   |
|         |                                      | (18) "State Government" means the Government of the State of _____;   |
|         | <b>Chapter II</b>                    | <b>Appointment and Powers of Registering Authority, Registration of Money Lenders etc.</b>  |
| 3       | Appointment of registering authority | The State Government may, by notification in the Official Gazette, appoint such persons, whether public officers or not, as it thinks proper, to be registering authorities of the money lenders and accredited loan providers for the purposes of this Act and may define the areas within which each such authority shall exercise his powers and perform his duties.   |
| 4       | Register of Moneylenders             | (1) Every registering authority shall maintain for the area under its jurisdiction the registers of all money lenders having valid registration in such form as may be prescribed.<br><br>(2) The registers maintained under sub-section (1) shall be published in such manner and at such intervals as may be prescribed.  |
| 5       | Moneylender to obtain registration   | (1) No money lender shall commence or carry on the business of providing loan at any place to which this Act applies without obtaining a registration under this Act.<br>(2) Every application for a money lender's registration and for a renewal of money lender's license shall be in writing in the prescribed manner and form and shall be made to the registering authority along with the prescribed fee;<br>(3) Every registration granted by the registering authority shall be in such form and subject to such conditions as may be prescribed;<br>(4) A registration shall be valid within the local area as specified in the registration for a period of three years :<br>Provided that when an application for renewal of a registration has been received by the registering authority within the prescribed period, the registration shall, until the application is finally disposed of, be deemed to be valid; |

| Section | Heading  | Provisions  |
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|         |  | <p>(5) The registering authority may, at any time for sufficient cause, suspend or cancel a registration granted under sub-section (3) Provided that no order suspending or cancelling the registration shall be passed except after giving the money lender an opportunity of showing cause against the proposed action;</p> <p>Explanation: For the purposes of sub-section (5), prosecution or conviction of a money lender for violating any of the provisions of this Act shall be sufficient cause for suspension or cancellation of his registration.</p>  |
|         | <b>Chapter III</b>   | <b>Maintenance of Books of Accounts and Submission of Returns</b>   |
| 6       | Duty of money lender to maintain accounts and furnish copies | <p>(1) Every money lender shall keep and maintain a cash book, a ledger, register of securities and such other books of accounts in such form and in such manner as may be prescribed.</p> <p>(2) Every money lender shall,-</p> <p>(a) deliver or cause to be delivered, to the borrower within seven days from the date on which a loan is made, a statement in the prescribed form showing in clear and distinct terms the amount and date of the loan and of its maturity, the nature of the security, if any, for the loan, the name and address of the borrower and of the money lender and the rate of interest charged:</p> <p>Provided that no such statement shall be required to be delivered to a borrower if he is supplied by the money lender, with a pass book in the prescribed form containing an up-to-date account of the transactions with the borrower;</p> <p>(b) upon repayment of a loan in full, mark indelibly every paper signed by the borrower with words indicating payment or cancellation, and discharge every mortgage, restore every pledge, return every document or note and cancel or reassign every assignment given by the borrower as security for the loan.</p> <p>(3) No money lender shall receive any payment from a borrower on account of any loan without giving him a duly signed receipt for the payment.</p> <p>(4) No money lender shall accept from a borrower any article as a pawn, pledge or security for a loan without giving him a signed receipt for the same with its description, estimated value, the amount of loan advanced against it and such other particulars as may be prescribed.</p> <p>(5) A money lender shall, on a demand in writing by the borrower, and tender of the prescribed sum of expenses, supply a copy of any document relating to a loan made by him or any security therefor, to the borrower, or if the borrower so requires, to any person specified in that behalf in the demand.</p> |
| 7       | Submissions of accounts, returns etc.                        | Every money lender shall file such statements of accounts and submit returns to the registering authority, at such intervals and on or before such dates as may be prescribed.  |
| 8       | Power to require production of records or documents and      | (1) The registering authority or any officer authorised by the State Government in this behalf may, to verify whether the business of the money lender is carried on in accordance with the provisions of this Act, enter the premises of the money lender or any person who in his opinion is carrying on the business of a money lender and call upon him to produce any record or document relating to such business and every   |

| Section | Heading   | Provisions  |
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|         | power of entry, inspection and seizure                | <p>such money lender or person shall allow such inspection and produce such record or document.</p> <p>(2) The registering authority may, for the purposes of the said sub-section, search the premises and seize any record and document as may be necessary and the record or document seized shall be retained only for such period as may be necessary for the purposes of examination, prosecution or other legal action:</p> <p>Provided that the provisions of Sections 100 and 102 of the Code of Criminal Procedure, 1973 (Central Act 2 of 1973) shall, so far as may be, apply to such search and seizure:</p> <p>(3) The registering authority or the other officer referred to in sub-section (1) shall also have power to summon and examine the money lender or any person who in his opinion is in a position to furnish relevant information.</p>  |
| 9       | Borrowers not bound to admit correctness of accounts. | A borrower to whom a statement of accounts or a pass book has been furnished under this Act shall not be bound to acknowledge or deny its correctness and his failure to do so shall not, by itself, be deemed to be an admission of the correctness of the accounts.   |
|         | <b>Chapter IV</b>                                     | <b>Dispute Resolution</b>   |
| 10      | Procedure in disputes regarding loan.                 | <p>(1) In case of any dispute relating to the transactions involving a loan of upto Rs. 50,000/- or equivalent value (excluding interest), the aggrieved person may file an application in the prescribed form along with the prescribed fee, before the Nyaya Panchayat and on receipt of such application, the Nyaya Panchayat shall cause a notice of the application to be given to the other party.</p> <p>(2) Where in any area there is no Nyaya Panchayat and in every dispute relating to the transactions involving a loan exceeding Rs. 50,000/- or equivalent value (excluding interest), the aggrieved person may file an application in the prescribed form along with the prescribed fee, before the Lok Adalat and on receipt of such application, the Lok Adalat shall cause a notice of the application to be given to the other party.</p> <p>(3) The orders passed by the Nyaya Panchayat or Lok Adalat, as the case may be, after hearing the parties shall be binding on all the parties to the dispute.</p> <p>(4) Notwithstanding anything contained in any law for the time being in force, in any suit to which this Act applies,—</p> <p>(a) a Lok Adalat or Nyaya Panchayat shall, before deciding the claim on merits, frame and decide the issue whether the money lender has complied with the provisions of section 6;</p> <p>(b) if the Lok Adalat or Nyaya Panchayat finds that the provisions of section 6 have not been complied with by the money lender, it may, if the money lender's claim is established, in whole or in part, disallow the whole or any portion of the interest found due as may seem reasonable to it in the circumstances of the case and may disallow costs.</p> <p>Explanation.—A money lender who has given the receipt or furnished a statement of accounts or a pass book in the prescribed form and manner, shall be held to have complied with the provisions of section 6, as the case may be, in spite of any errors and omissions if the Lok Adalat or Nyaya Panchayat finds that such errors and</p> |

| Section                         | Heading   | Provisions   |
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|                                 |   | <p>omissions are not material or not fraudulent.</p> <p>(5) Notwithstanding anything contained in the Code of Civil Procedure, 1908 (Central Act 5 of 1908), the Nyaya Panchayat or Lok Adalat, as the case may be, shall have jurisdiction to hear and decide disputes relating to loan between a money lender and borrower at the place where the borrower resides.</p> <p>(6) The Nyaya Panchayat or Lok Adalat, as the case may be, while hearing a dispute under this Act shall have all the powers as are vested in a civil Court under the Code of Civil Procedure, 1908 (Central Act 5 of 1908) while trying a suit in respect of the following matters, namely-</p> <p>(i) the summoning and enforcing the attendance of any defendant or witness and examining the witnesses on oath;</p> <p>(ii) the discovery and production of any document or other material object producible as evidence;</p> <p>(iii) the reception of evidence on affidavits;</p> <p>(iv) issuing of any commission for the examination of any witness; and</p> <p>(v) any other matter which may be prescribed.</p> |
| <p><b>Alternate Sec. 10</b></p> | <p><b>Settlement of Disputes</b></p>  | <p><b>(1) For the protection of debtors and for the settlement of disputes under the Act, the State Government after consultation with the High Court, and by notification, -</b></p> <p><b>(a) shall, as soon as may be after the commencement of this Act, establish for every district in the State a Fast-Track Court;</b></p> <p><b>(b) may establish Fast-Track Court for such other areas in the State, as it may deem necessary.</b></p> <p><b>(2) The State Government shall, after consultation with the High Court specify, by notification, the local limits of the area to which the jurisdiction of a Fast-Track Court shall extend and may, at any time, increase, reduce or alter such limits.</b></p> <p><b>(3) The cases that are filed before the fast-Track Court shall be disposed of within a period of three months.</b></p>  |
| <p>11</p>                       | <p>Power of Nyaya Panchayat or Lok Adalat to deposit money due on loan in Nyaya Panchayat or Lok Adalat</p> | <p>(1) The Nyaya Panchayat or Lok Adalat may, at any time, on application of a judgment-debtor, after notice to the decree-holder, direct that the amount of any decree passed against him, whether before or after the date on which this Act comes into force, in respect of a loan, shall be paid in such number of installments and subject to such conditions, and payable on such dates, as, having regard to the circumstances of the judgment-debtor and the amount of the decree, it considers fit.</p> <p>(2) (a) Where a money lender refuses to accept the whole or any portion of the money due in respect of his loans, the borrower may deposit the said money into the Nyaya Panchayat or Lok Adalat, having jurisdiction in the matter and apply to the Nyaya Panchayat or Lok Adalat, as the case may be, to record full or part satisfaction of the loan</p> <p>(b) Where any such application is made, the Nyaya Panchayat or Lok Adalat, as the case may be, shall, after due inquiry pass orders recording full or part satisfaction of the loan, as the case may be.</p>        |
| <p>12</p>                       | <p>Suits and applications by unregistered money lenders</p>   | <p>Notwithstanding anything contained in any other enactment for the time being in force-</p> <p>(i) a suit by a money lender for the recovery of a loan ; or</p>  |

| Section | Heading                                   | Provisions  |
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|         | barred                                    | (ii) an application by a money lender for the execution of a decree relating to a loan; or<br>(ii) an application for resolution of dispute through a Lok Adalat or Nyaya Panchayat, shall be dismissed, unless at the time when the loan was advanced, the money lender held an effective registration.  |
|         | <b>Chapter V</b>                          | <b>Accredited Loan Providers</b>  |
| 13      | Registration of accredited loan providers | (1) Any person or institution intending to engage himself or itself as an accredited loan provider shall apply to the registering authority constituted under section 3 of this Act for registration to carry on the business as an accredited loan provider.<br><br>Provided that only such persons who have the necessary educational qualification or knowledge of agriculture and rural economy, knowledge of maintenance of books of accounts and such other conditions as may be specified in the order issued by the State Government in this behalf shall be eligible to become accredited loan providers.<br><br>(2) No such application by an accredited loan provider shall be entertained by the registering authority unless such application is counter signed by an institutional creditor having credit link with the accredited loan provider.<br><br>(3) No accredited loan provider shall commence or carry on the business of providing loan without obtaining a registration under the provisions of this chapter;<br><br>(4) Every registration granted by the registering authority shall be in such form as may be prescribed.<br><br>(5) Every registering authority shall maintain for the area under its jurisdiction the registers of all accredited loan providers having valid registration in such form as may be prescribed.<br><br>(6) The registers maintained under sub-section (5) shall be published in such manner and at such periodic intervals as may be prescribed. |
| 14      | Submissions of accounts, returns etc.     | (1) Every accredited loan provider shall maintain such books of accounts and file such statements of accounts and returns as may be prescribed to the registering authority and a copy of such statement of accounts and returns shall also be furnished to the institutional creditor.<br><br>(2) The institutional creditor shall, on a requisition from the registering authority, furnish the information concerning the loans provided by an accredited loan provider within such time as may be specified in the requisition.   |
| 15      | Settlement of disputes                    | The provisions of Section 10 shall <i>mutatis mutandi</i> apply to any dispute between the accredited loan provider and the borrower.   |
| 16      | Cancellation of registration              | (1) If the institutional creditor has informed the registering authority about the termination of its relationship with the accredited loan provider, the registering authority shall cancel the registration of the accredited loan provider.<br><br>Provided that if within a period of thirty days from the cancellation of the registration, such accredited loan provider enters into an agreement with another institutional  |

| Section | Heading   | Provisions  |
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|         |   | <p>creditor and his application is countersigned by the new institutional creditor, the registering authority shall restore the registration of such accredited loan provider.</p> <p>(2) The registering authority may, at any time for sufficient cause, suspend or cancel a registration granted under Section 13;</p> <p>Provided that no order suspending or cancelling the registration shall be passed except after giving the accredited loan provider an opportunity to show cause against the proposed action.</p> <p>Explanation : For the purposes of sub-section (2), prosecution or conviction of a accredited loan provider for violating any of the provisions of this Act shall be sufficient cause for suspension or cancellation of the registration.</p>  |
|         | <b>Chapter VI</b>   | <b>Interest Rate Ceiling</b>  |
| 17      | Limitation on rates of interest charged by money lenders and accredited loan providers  | <p>(1) The State Government may from time to time by notification specify the maximum rates of interest for any local area chargeable by money lenders and accredited loan providers and separate rates of interests may be specified in respect of secured and unsecured loans.</p> <p>(2) If any money lender or accredited loan provider charges or receives from a borrower interest at a rate exceeding the maximum rate fixed by the State Government under sub-section (1), he shall be liable for punishment under this Act.</p> <p>(3) The maximum rate of interest notified by the State Government under sub-section (1), shall be calculated by taking into account the interest rate trends, cost of transactions, cost of the capital, the risk premium and the administrative expenses associated with such loans.</p> <p>(4) All money lenders and accredited loan providers shall display the rates of interest charged by them, both on secured as well as unsecured loans, in a conspicuous place in their premises.</p> |
| 18      | Maximum amount of interest recoverable on loans and discharge of loans in certain cases | <p>(1) No money lender or accredited loan provider shall recover towards the interest in respect of any loans advanced by him, an amount in excess of the principal amount.</p> <p>(2) Any loan in respect of which the money lender or accredited loan provider has realized from the debtor an amount equal to or more than twice the amount of the principal, shall stand discharged and the amount, if any, so realized in excess of twice the amount of the loan shall be refunded by the money lender or accredited loan provider, as the case may be, to the debtor.</p>   |
|         | <b>Chapter VII</b>  | <b>Offences and Penalties</b>   |
| 19      | Entry of wrong sum in bond, etc., to be an offence                                      | <p>(1) No money lender or accredited loan provider shall take any promissory note, acknowledgment, bond or other writing which does not state the actual amount of the loan, or which states such amount wrongly or obtains any instrument in which blanks are left to be filled after execution.</p> <p>(2) Whoever contravenes the provisions of sub-section (1) shall, on conviction, be punished with fine which may extend to twenty thousand rupees or with imprisonment which may extend to one year or with both.</p>   |
| 20      | Penalty for salami, batta,  | If any Loan Provider or accredited loan provider or his agent takes from a borrower at the time of advancing a loan or deduct out of the principal of such loan any salami,   |

| Section | Heading  | Provisions  |
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|         | dharmada etc.  | batta, dharmada or other extraction of similar nature by whatever name called, he shall be punishable with fine which may extend to twenty thousand rupees.   |
| 21      | Penalty for molestation                                | <p>(1) Whoever molests, or abets the molestation of, a borrower for the recovery of a debt due by him to a money lender or accredited loan provider or his assignee, as the case may be, shall, on conviction, be punished with imprisonment which may extend to two years or with fine which may extend to one lakh rupees or with both.</p> <p>Explanation.—For the purposes of this section, a person who, with intent to cause another person to abstain from doing any act which he has a right to do or to do any act which he has a right to abstain from doing,—</p> <p>(a) obstructs or uses violence to or intimidates such other person, or</p> <p>(b) persistently follows such other person from place to place or interferes with any property owned or used by him or deprives him of, or hinders him in, the use of any such property, or</p> <p>(c) loiters at or near a house or other place where such other person resides or works, or carries on business, or happens to be, or</p> <p>(d) does any act calculated to annoy or intimidate such other person or the members of his family, or</p> <p>(e) moves or acts in a manner which causes or is calculated to cause alarm or danger to the person or property of such other person,</p> <p>-shall be deemed to molest such other person:</p> <p>Provided that a person who goes to the house or place referred to in clause (c) in order merely to obtain or communicate information shall not be deemed to molest.</p> <p>(2) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, offence punishable under sub-section (1) shall be cognizable.</p> |
| 22      | Penalty for carrying on business without registration  | Whoever carries on the business of providing loans without obtaining registration or otherwise than in conformity with the terms and conditions imposed by the registering authority shall be punished with imprisonment for a term which may extend to one year and with fine which may extend to fifty thousand rupees.   |
| 23      | Penalty for contravention of the provisions of the Act | If any person contravenes any other provision of this Act, he shall be punishable with fine which may extend to ten thousand rupees.  |
| 24      | Composition of offences                                | <p>(1) The Registering Authority or any other officer or authority authorised by the State Government in this behalf, may accept from the person who has committed or is reasonably suspected of having committed an offence under this Act, by way of composition of such offence-</p> <p>(a) a sum of money equal to the maximum amount prescribed as fine under this Act, if the offence is committed for the first time; and</p> <p>(b) in other cases, twice the amount of such fine prescribed under the respective sections.</p> <p>Provided that an offence with respect to which a proceeding is pending before the Court shall not be compoundable.</p>   |

| Section | Heading   | Provisions   |
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|         |   | (2) Notwithstanding anything contained in sub-section (1), offence punishable under Section 21 of this Act shall be cognizable and shall not be compoundable.  |
| 25      | Cognisance of certain offences                          | No Court shall take cognizance of any offence, except the offence under Section 21, save on a complaint made by Registering Authority or any other officer duly authorized in this behalf by the State Government.   |
|         | <b>Chapter VIII</b>                                     | <b>Miscellaneous</b>   |
| 26      | Every officer to be public servant                      | Every officer of the Government and every person acting under the provisions of this Act shall be deemed to be a public servant within the meaning of section 21 of the Indian Penal Code.   |
| 27      | Saving of laws relating to agriculturists' indebtedness | Nothing in this Act shall affect any of the provisions of any enactment relating to relief of agriculturists' indebtedness.  |
| 28      | Power to make rules                                     | <p>(1) The State Government may, by notification in the Official Gazette, make rules for carrying out the purposes of this Act.</p> <p>(2) In particular and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:-</p> <p>(a) the form of the register under section ___;</p> <p>(b) the form of the application for registration, the further particulars to be included therein and the manner of payment of registration fee under section ___;</p> <p>(c) the form of cashbook, ledger and other books and the manner in which they shall be maintained under Section ___ and the other particulars to be prescribed under ___ of that section;</p> <p>(d) the form of the statement of accounts and pass books to be furnished or delivered and the date before which it is to be furnished or delivered under ___, the fee to be paid under ___, and the sum of expenses to be paid under ___ of section ___;</p> <p>(e) the procedure to be followed by the officers while compounding offences under this Act;</p> <p>(f) any other matter which has to be or may be prescribed under this Act or any matter for which there is no provision or insufficient provision in this Act and for which provision is, in the opinion of the State Government, necessary for giving effect to the provisions of this Act.</p> <p>(3) Every rule made under this Act, shall be laid, as soon as may be after it is made before each House of the State Legislature while it is in session for a total period of thirty days which may be comprised in one session or in two successive sessions, and if before the expiry of the session in which it is so laid or the session immediately following, both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be; so however that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.</p> |
| 29      | Power to  | The State Government may, after consultation with the Reserve Bank, by notification in the Official Gazette, exempt such money lenders or accredited loan providers,   |

| Section | Heading  | Provisions  |
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|         | Exempt   | from all or any of the provisions of this Act, subject to such conditions as it may deem fit and for such period as may be specified.   |
| 30      | Annual Report on the administration of the Act | The State Government shall prepare an annual report on the administration of this Act and the same shall be placed before the State Legislature.  |
| 31      | Repeal and savings                             | <p>(1) The ____ Act,____, is hereby repealed.</p> <p>(2) Notwithstanding such repeal, anything done or any action taken under the provisions of the said Act shall, in so far as such thing or action is not inconsistent with the provisions of this Act, be deemed to have been done or taken under the provisions of the Act as if the said provisions were in force when such thing was done or such action was taken and shall continue in force accordingly until superseded by anything done or any action taken under this Act.</p> |

**Enforcement Machinery under the Laws of various Countries**

| Country / State | Law   | Licensing Authority   |
|-----------------|---|---|
| United Kingdom  | Consumer Credit Act, 1974                               | Office of Fair Trading<br>( <a href="http://www.offt.gov.uk">http://www.offt.gov.uk</a> ) |
| Hong Kong       | Money Lenders Ordinance, 1997                           | Office of the Registrar (under the Financial Secretary)                                   |
| Singapore       | Money Lenders Act, 1959                                 | Office of the Registrar (under the Minister)  |
| Japan           | Money Lending Business Control and Regulation Law, 1983 | Financial Services Authority<br>( <a href="http://fsa.gov.jp">http://fsa.gov.jp</a> )     |
| Lesotho         | Money Lenders Order, 1989                               | Commissioner of Financial Institutions  |
| South Dakota    | Title 54 of the State Laws of South Dakota              | Division of Banking of the Department of Revenue and Regulation                           |
| West Pakistan   | Punjab Money Lenders Ordinance, 1960                    | Collector   |
| South Africa    | National Credit Act, 2005                               | National Credit Regulator   |

**List Of Money Lending Laws In India**

| <b>SI No.</b> | <b>State</b>   | <b>Legislation</b>   |
|---------------|----------------|--|
| 1             | Karnataka      | Karnataka Money Lenders Act, 1961  |
| 2             | Kerala         | Kerala Money Lenders Act, 1958   |
| 3             | Uttar Pradesh  | Uttar Pradesh Regulation of Money Lending Act, 1976  |
| 4             | Tamil Nadu     | Tamil Nadu Money Lenders Act, 1957   |
| 5             | Maharashtra    | Bombay Money Lenders Act, 1946   |
| 6             | Punjab         | The Punjab Registration of Money-Lenders Act, 1938   |
| 7             | NCT Delhi      | Adopted the Punjab Legislation   |
| 8             | Haryana        | Adopted Punjab Legislation vide Haryana Adaptation of Laws Order, 1968   |
| 9             | West Bengal    | Bengal Money-Lenders Act, 1940   |
| 10            | Orissa         | Orissa Money Lenders Act, 1939   |
| 11            | Bihar          | Bihar Money Lenders Act, 1974  |
| 12            | Rajasthan      | Rajasthan Money Lenders Act, 1963  |
| 13            | Gujarat        | Adopted Bombay Money Lenders Act, 1946   |
| 14            | J & K          | No legislation   |
| 15            | Madhya Pradesh | Madhya Pradesh Money Lenders Act, 1934   |
| 16            | Chhattisgarh   | Same as M.P.   |
| 17            | Andhra Pradesh | Andhra Pradesh (Telangana Area) Money Lenders Act, 1349 F<br><br>Andhra Pradesh (Andhra Region Scheduled Areas) Money Lenders Regulation, 1960 |
| 18            | Assam          | The Assam Money Lenders Act, 1934  |
| 19            | Meghalaya      | Adopted the Assam Legislation  |
| 20            | Tripura        | Adopted Maharashtra Legislation  |

|    |             |                                  |
|----|-------------|----------------------------------|
| 21 | Nagaland    | Nagaland Money Lenders Act, 2005 |
| 22 | Uttarakhand | Same as Uttar Pradesh            |

## Provisions requiring Registration/Licensing and Penalties

| State          | Whether license/ registration is required for carrying on the business of money lending  | Whether non-registration/ unlicensed conduct of business attracts penalty | Penalty  |
|----------------|--|---|--|
| Bihar          | Yes. Section 5   | Yes. Section 34   | <b>Imprisonment</b> which may extend to <b>1 year</b> or with <b>fine</b> not exceeding <b>500</b> rupees or with <b>both</b>  |
| Uttar Pradesh  | Yes. Section 7 read with Section 10  | Yes. Section 22 read with section 10                                      | <b>Imprisonment</b> which may extend to <b>6 months</b> or with <b>fine</b> not exceeding <b>5,000</b> rupees or with <b>both</b>  |
| Kerala         | Yes. Section 3   | Yes. Section 17 (Cognisable Offence)                                      | <b>Imprisonment</b> which, in the absence of special reasons to be recorded, shall <b>not be less than 3 months</b> , but which may extend to <b>3 years</b> and with <b>fine</b> which may extend to <b>50,000</b> rupees   |
| Karnataka      | Yes. Section 5   | Yes. Section 39 read with Section 5 (Cognisable Offence)                  | <b>First offence: Simple Imprisonment</b> which may extend to 3 months or with <b>fine</b> which may extend to <b>1000</b> rupees or with <b>both</b> .<br><br><b>Second/Subsequent Offence: Imprisonment</b> which may extend to <b>6 months</b> or with <b>fine</b> which may extend to <b>2000</b> rupees or with <b>both</b> . |
| Punjab & Delhi | In terms of section 3 only registered money lenders can maintain a suit for recovery of loan and Section 4 provides for registration | No offence defined  |  |
| Haryana        | Yes. Section 4 (2)   | Yes. Section 4 (3)  | <b>First offence: Fine</b> not exceeding <b>1000</b> rupees.<br><br><b>Subsequent Offence: Fine</b> not exceeding <b>2000</b> rupees.  |
| Orissa         | Yes. Section 4   | Yes. Section 19(1)(a)   | <b>Imprisonment</b> for a term which may extend to <b>1 year</b> or with <b>fine</b> which may extend to <b>1000</b> rupees or with  |

| State  | Whether license/ registration is required for carrying on the business of money lending | Whether non-registration/ unlicensed conduct of business attracts penalty | Penalty  |
|--|---|---|--|
|  |   |   | <b>both.</b>   |
| Tamil Nadu                                     | Yes. Section 3  | Yes. Section 17   | <b>Fine</b> which may extend to <b>1000</b> rupees   |
| Maharashtra & Gujarat                          | Yes. Section 6 read with Section 5  | Yes. Section 34 read with Section 5 (Cognizable)                          | <b>First offence: Simple Imprisonment</b> which may extend to <b>2 months</b> or with <b>fine</b> which may extend to <b>500</b> rupees or with <b>both</b> .<br><br><b>Second/Subsequent Offence: Imprisonment of either description</b> which may extend to <b>6 months</b> or with <b>fine</b> or with <b>both</b>    |
| Bengal   | Yes. Section 8  | Yes. Section 42   | <b>First offence: Fine</b> which may extend to <b>200</b> rupees.<br><br><b>Second Offence: Fine</b> which may extend to <b>500</b> rupees.<br><br><b>Subsequent Offence: Rigorous Imprisonment</b> which may extend to <b>3 months</b> and also liable for <b>Fine</b> .  |
| Andhra Pradesh (Telangana Area)                | Yes. Section 3 (5) (a)  | Yes. Section 3 (5) (b)  | <b>Rigorous Imprisonment</b> which may extend to <b>6 months</b> or with <b>fine</b> or with both  |
| Andhra Pradesh (Andhra Region Scheduled Areas) | Yes. Section 3  | Yes. Section 24   | <b>Imprisonment</b> which may extend to <b>6 months</b> or with <b>fine</b> which may extend to <b>1000</b> rupees or with both  |
| Madhya Pradesh                                 | Yes. Sections 11 B & 11 F   | Yes. Section 11 F (2) & (3)   | <b>Scheduled Areas - Imprisonment</b> which may extend to <b>2 years</b> or with <b>fine</b> which may extend to <b>10,000</b> rupees or both.<br><br><b>Other Areas - First offence - Fine</b> which may extend to <b>2000</b> rupees.<br><br><b>Subsequent offences - Fine</b> which may extend to <b>5000</b> rupees. |
| Assam  | Yes. Section 7C (1)   | Yes. Section 7C (2)   | <b>First offence: -Simple Imprisonment</b> which may extend to <b>3 months</b> or with <b>fine</b> which may   |

| State | Whether license/ registration is required for carrying on the business of money lending | Whether non-registration/ unlicensed conduct of business attracts penalty | Penalty   |
|-------|---|---|---|
|       |   |   | <p>extend to <b>500</b> rupees or with both.</p> <p><b>Second/Subsequent Offence:-</b><br/> <b>Imprisonment of either description</b> which may extend to <b>6 months</b> or with <b>fine</b> which may extend to <b>1000</b> or with <b>both</b></p> |

**Applicability / Exemption To Companies**

| <b>S. No.</b> | <b>STATE</b>                 | <b>LEGISLATION</b>                             | <b>PROVISION</b>                   | <b>APPLICABLE</b> | <b>EXEMPTION</b>  |
|---------------|------------------------------|--|------------------------------------|-------------------|---|
| 1             | Rajasthan                    | Rajasthan Money Lenders' Act, 1963             | 2(10)(iii) (defn. of money lender) | Yes               | By St. Govt., by Notification in Gazette  |
| 2             | Kerala                       | Kerala Money Lenders act, 1958                 | 2(7)(g) (defn. of money lender)    | Yes               | Instn. in Public sector by Govt. by notfn.  |
| 3             | Bihar                        | Bihar Money-Lenders Act, 1974                  | 2(k) (defn. of money lender)       | Yes               | By St. Govt. by Notification (section 3)  |
| 4             | West Bengal                  | Bengal Money-Lenders Act, 1940                 | 2(13) (defn. of money lender)      | Yes               | To loans by a bank (sec. 2(12)(d)) and bank includes FI notified by St. Govt. 2(1)(iii)   |
| 5             | Assam                        | Assam Money Lenders Act, 1934                  | 2(1) (defn. of money lender)       | Yes               | No provision for exemption except for banks (section 2A)  |
| 6             | Punjab, UT of Delhi, Haryana | Punjab Registration of Money-Lenders Act, 1938 | 2(8) – money lender                | Yes               | To loans given by companies 2(7)(v)   |
| 7             | Maharashtra, Tripura         | Bombay Money Lenders Act, 1946                 | 2(10) – money lender               | Yes               | 2(10)(v) – St. Govt. empowered to exempt and partial exemption in respect of keeping of accounts etc., could be granted under section 22. |
| 8             | Gujarat                      | --do--   | --do--                             | --do--            | No provision to grant full exemption,   |

| S. No. | STATE          | LEGISLATION  | PROVISION  | APPLICABLE   | EXEMPTION   |
|--------|----------------|--|--|--|---|
|        |                |  |  |  | although the partial exemption as aforesaid is possible   |
| 9      | Orissa         | Orissa (Sch. Areas) Money Lenders' Regulation, 1967<br><br>Orissa Money Lenders Act, 1939                              | Regulation 2(x) – money-lender<br><br>2(1)(j) – money-lender | Yes<br><br>Yes   | Banks not included<br><br>Banks not included  |
| 10     | Andhra Pradesh | AP (Telangana Area) Money-Lenders Act, 1349 F<br><br>AP (Andhra Region Scheduled Areas) Money Lenders Regulation, 1960 | 2(7) – money lender<br><br>2(11) – money lender              | Yes<br><br>No  | Loans by companies exempted (section 2(4)(d))<br><br>Companies as well as loans by companies exempted (2(11) and 2(10)(ii)) |
| 11     | Karnataka      | Karnataka Money-Lenders Act, 1961  | 2(10) – money lender   | Yes  | St. Govt. by notification may specify non-inclusion of company  |
| 12     | Tamil Nadu     | Tamil Nadu Money-Lenders Act, 1957   | 2(8) – money lender  | Yes, but excludes bank   | St. Govt. may notify financial or banking institution under section 2(1)(k) [defn. of "bank"]                               |
| 13     | Uttar Pradesh  | UP Regulation of Money Lending Act, 1976   | Section 2(1)(b)  | Not applicable to loan by public company (as defined in Co. Act, 1956) | Section 3(1)(g) (defn. of "bank") – power of St. Govt. to notify a banking / Financial institution as                       |

| S. No. | STATE          | LEGISLATION                            | PROVISION                                   | APPLICABLE | EXEMPTION  |
|--------|----------------|--|---|------------|--|
|        |                |  |   |            | "bank" – r/w 2(1)(a) – the Act becomes inapplicable  |
| 14     | Madhya Pradesh | Madhya Pradesh Money Lenders Act, 1934 | Section 2(v)- defn. of money lender         | Yes        | 2(vii) – defn. of loan excludes loan by company whose accounts are subject to audit by a certified auditor |
| 15     | Nagaland       | Nagaland Money Lenders Act, 2005       | Section 2 (10) - Definition of money lender | No         | Companies and banks have been excluded from the definition of money lender                                 |

**Applicability of State Legislations to banks and to certain transactions**

| <b>State</b>                         | <b>Banks</b>                    | <b>Other entities</b>                           | <b>Trade Credit</b>  | <b>Agricultural input credit</b>   |
|--------------------------------------|---------------------------------|---|--|--|
| UP                                   | Excluded                        | Exclusion by notification                       | Excluded   |  |
| AP (Telengana Area)                  | Excluded                        | Excluded  | Excluded   | Not Excluded   |
| AP (Andhra Region – Scheduled Areas) | Excluded                        | Excluded  |  | A person advancing money on the security of any standing crop or produce has been specifically included. |
| TN                                   | Excluded                        | By notification may be excluded                 | By implication excluded  |  |
| Bengal                               | By notification may be excluded | By notification may be excluded                 | Not excluded although commercial loan has been defined and the Act enables higher rates of interest to be charged for such loans |  |
| Orissa                               | Excluded                        | By notification may be excluded                 | Certain types and to certain extent are excluded   |  |
| Karnataka                            | Excluded                        | Included but FI by notification may be excluded | Excluded subject certain limitations   | Excluded subject certain limitations   |
| Maharashtra                          | excluded                        | FI by notification may be excluded              | Excluded by implication  | Excluded subject certain limitations   |
| Kerala                               | Excluded                        | Institution in public sector                    | Excluded   | By implication   |

| State                     | Banks   | Other entities                                    | Trade Credit  | Agricultural input credit  |
|---------------------------|---|---|---|--|
|                           |   | by notification may be excluded                   |   |  |
| Bihar                     | Not excluded, but by notification may be excluded | Not excluded, but by notification may be excluded |   |  |
| Rajasthan                 | Excluded  | Not excluded, but by notification may be excluded | Excluded subject certain limitations, but credit artisan or a person who sells his agricultural produce or cattle or buys agricultural produce or cattle for his use not excluded |  |
| Nagaland                  | Excluded  | Excluded  | Excluded  | money advanced on the security of standing crops or produce have been included                                     |
| Haryana, Punjab and Delhi | Excluded  | Excluded  | Excluded but credit to person who sells only his own agricultural produce or cattle, or buys agricultural produce or cattle for his own use                                       |  |
| M.P.                      | Excluded  | Excluded  |   | Excluded where proprietor advances grains or money exclusively to any of his tenants for seed, land improvement or |

| <b>State</b> | <b>Banks</b> | <b>Other entities</b> | <b>Trade Credit</b> | <b>Agricultural input credit</b> |
|--------------|--------------|-----------------------|---------------------|----------------------------------|
|              |              |                       |                     | agricultural operations          |