



ICRA

ICRA Limited

CONFIDENTIAL

May 05, 2017

Mr. Subrata Pradhan
Company Secretary
Annapurna Microfinance Private Limited
Plot No. 1215/1401, Khandagiri Bari
Infront of Jayadev Vatika, Khandagiri
Bhubneswar – 751 030
Odisha

Dear Sir,

Re: Review of ICRA-assigned Code of Conduct Assessment Grading of Annapurna Microfinance Private Limited

Please refer to our letter dated April 21, 2017 communicating the "C3" (pronounced C three) Code of Conduct Assessment grading assigned to your entity and also your subsequent email dated April 29, 2017 requesting a review of the same.

Please note that the Rating Committee of ICRA, after due consideration has revised the Code of Conduct Assessment grading at "C2" (pronounced C two) to the captioned entity. This grading indicates that in ICRA's current opinion, MFIs with this grade have **good** performance on Code of Conduct dimensions.

Please find appended revised grading letter. The annexed letter (ICRA/KOL/RA/2017-18/081) dated May 05, 2017 supersedes previous letter dated April 21, 2017.

We thank you for your kind cooperation extended during the course of the grading exercise.

With kind regards,

Yours sincerely,
for ICRA Limited

Sujoy Saha
Vice President
sujoy.saha@icraindia.com

Niraj Jalan
Assistant Vice President
niraj.jalan@icraindia.com



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Ref: ICRA/KOL/RA/2017-18/081

Date: May 05, 2017

Mr. Subrata Pradhan
Company Secretary
Annapurna Microfinance Private Limited
Plot No. 1215/1401, Khandagiri Bari
Infront of Jayadev Vatika, Khandagiri
Bhubneswar – 751 030
Odisha

Dear Sir,

Re: ICRA Code of Conduct Assessment Grading of Annapurna Microfinance Private Limited

Please refer to your rating agreement dated April 18, 2017 for Code of Conduct Assessment grading of the aforesaid entity. Our Rating Committee, after due consideration, has assigned "C2" (pronounced C two) grade to the captioned entity. In ICRA's opinion, MFIs with this grade have **good** performance on Code of Conduct dimensions.

In any of your publicity material or other documents wherever you are using the above grading, it should be stated as "C2". We would appreciate if you can sign on the duplicate copy of this letter and send it to us as a token of your acceptance and use of the assigned grade. The draft report for assigning the above mentioned grade is enclosed along with this letter for your feedback. Any intimation by you about the above mentioned grade to any Banker / Lending Agency / Government Authorities / Stock Exchange / Project Promoter / Consultant / Customers would constitute use of this grading by you.

The grading along with any subsequent revisions/changes is valid till April 20, 2018, unless revalidated by a fresh mandate. ICRA reserves the right to suspend, withdraw or revise the above at any time on the basis of new information or such other circumstances, which ICRA believe, may have an impact on the grade assigned to you.

The grading, as aforesaid, however, should not be treated as a recommendation to lend or not to lend or to do business with any such graded entity.

You are required to keep us informed of the progress details of your company and any developments, which may have a direct or indirect impact on the performance of the company.

We thank you for your kind cooperation extended during the course of the grading exercise.

With kind regards,

Yours sincerely,
for ICRA Limited

Sujoy Saha
Vice President
sujoy.saha@icraindia.com

Niraj Jalan
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R A T I N G • R E S E A R C H • I N F O R M A T I O N

Comprehensive MFI Grading

Annapurna Microfinance Private Limited

Comprehensive Grade Assigned: *mfR2 C2*

Date assigned: *May 5, 2017*

Scale	C1	C2	C3	C4	C5
mfR1					
mfR2		mfR2 C2			
mfR3					
mfR4					
mfR5					
mfR6					
mfR7					
mfR8					

The MFI has been assigned a comprehensive MFI grade of **mfR2 C2**.

Grading Rationale

Microfinance Capacity Assessment Grade	Annapurna has obtained " mfR2 " grading from CRISIL.
Code of Conduct Assessment Grade	Annapurna obtains " C2 " as its Code of Conduct Assessment Grade which signifies good performance on COCA dimensions.

*Comprehensive MFI Grading provides opinion of the Rating Agency on MFI's capacity to carry out its microfinance operations in a sustainable manner and its adherence to Industry code of conduct. MFI Capacity Assessment Grading has been done on the dimensions of **Capital Adequacy, Governance, Management Quality and Risk Management Systems**. Assessment on Code of Conduct has been done on the indicators pertaining to **Transparency, Client Protection, Governance, Recruitment, Client Education, Feedback & Grievance Redressal and Data Sharing**. Some of these indicators have been categorized as Higher Order indicators consisting of indicators on **Integrity and Ethical Behaviour and Sensitive Indicators**.*

Conflict of Interest Declaration

The Rating Agency has not been involved in any assignment of advisory nature with the MFI, for a period of 12 months preceding the date of the comprehensive grading. None of the employees or the Board members of the Rating Agency have been a member of the Board of Directors of the MFI during for a period of 12 months preceding the date of the comprehensive grading.

Disclaimer

ICRA does not undertake unsolicited ratings or gradings. The MFI grading exercise for this entity was not carried by ICRA Limited and ICRA has relied on the grading report and letter provided by the MFI for the same. Therefore, the grading mentioned above does not reflect ICRA's opinion on the relative capability of the MFI concerned to manage its microfinance activities in a sustainable manner.

Disclaimer

The objective of the Code of Conduct assessment exercise is to assess the extent of adherence to common Code of Conduct by MFIs during the period of assessment. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the graded entity. ICRA however has not conducted any audit of the graded entity or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than grading to the entity graded. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.

Historical Rating Grades

Date	Rating Agency	Comprehensive rating grade
03-Oct-2016	CRISIL	mfr2

Code of Conduct Assessment scale and definitions

C1	MFIs with this grade have excellent performance on Code of Conduct dimensions
C2	MFIs with this grade have good performance on Code of Conduct dimensions
C3	MFIs with this grade have average performance on Code of Conduct dimensions
C4	MFIs with this grade have weak performance on Code of Conduct dimensions
C5	MFIs with this grade have weakest performance on Code of Conduct dimensions

MFI's profile (March 2017)	
Name of the MFI	Annapurna Microfinance Private Limited
Legal form	NBFC-MFI
Operational Head	Mr. Sanjay Pattanaik
Year of starting microfinance	2009
Branches	246
Active borrowers	8,96,699
Total staff	2432
Operational area	Assam, Bihar, Chhattisgarh, Jharkhand, Madhya Pradesh, Maharashtra, Meghalaya, Odisha, Rajasthan, Tripura
Visit of the Assessment team	Odisha, Maharashtra and Bihar
Correspondence address	Plot 1215/1401, Khandagiri Bari, Opposite Jayadev Vatika, Khandagiri, Bhubaneswar, Odisha -751030

Details of Loan Products (February 2017)						
Product	Ticket Size (Rs.)	Purpose	Interest Rate	Average Tenure	Processing Fees	Group Guarantee/ Individual Loan
SHG Loan	10,000 - 60,000	Agri & Agri Allied,Business	23%-24%	22 Months	1%	Group Guarantee
Crop Loan	25,000	Crop Loan	23%	16 Months	1%	Group Guarantee
Swasth	10,000 - 25,000	Water and Sanitation Facilities	22%	19 Months	1%	Individual Loan
MEL	25,000 - 3,00,000	For new business or expanding existing business.	26%	22 Months	1%	Individual Loan
HIL	20,000 - 1,20,000	Repair/upgradation of housing units of existing member's households	22%	29 Months	1%	Individual Loan
Dairy	10,000 - 1,28,000	To buy cross breed cows. It is provided to those who are already involved in the dairy business	23%	24 Months	1%	Individual Loan

Solar	4,000	Solar Power Lighting System for rural household.	18%	15 Months	1%	Individual Loan
PWD	25,000	Loans for persons with disability	18%	12 Months	1%	Individual Loan

Shareholding Pattern (March 2017)	
Shareholder	% Shareholding
Gobinda Chandra Pattanaik	17.31%
Dibyajyoti Pattanaik	0.18%
RIF East 2	7.61%
BIO	22.09%
SIDBI	2.75%
SIDBI Venture Capital Ltd, STCL , A/c - Samridhi Fund	15.41%
DCB Bank Ltd.	5.02%
Oikocredit Ecumenical Development Cooperative Society U.A.	13.67%
Women's World Banking Capital Partners, LP	15.95%
Total	100.00%

Preference Shareholding (March 2017)	
Shareholder	% Shareholding
SIDBI	25.00%
AIDS Awareness Trust of Orissa	75.00%
Total	100.00%

Key Performance Ratios		
	March 2016	December 2016
Portfolio at Risk (>30 days)	0.08%	0.50%
Capital to Risk Weighted Capital Adequacy Ratio (CRAR)	19.43%	23.13%
Operating Expense Ratio (OER)	6.58%	6.62%
Funding Expense Ratio (FER)	12.12%	13.01%
Write-offs to average portfolio	0.05%	0
Return on Assets (RoA)	2.75%	3.23%
Return on Equity (RoE)	17.54%	21.84%
Active borrowers per staff	370	346
Active borrowers per branch (Own)	2594	2536

Compliance with RBI's Directions for MFIs

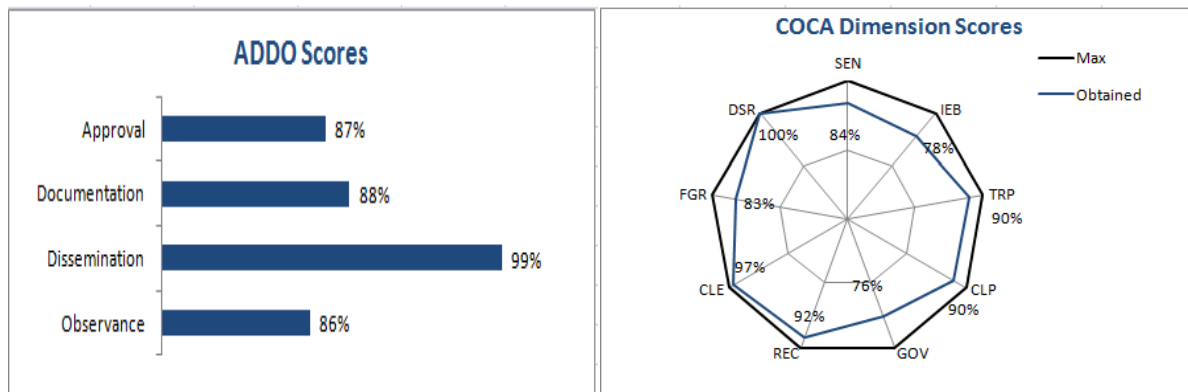
Sr No	RBI's Direction	Status
1	85% of total assets to be in the nature of qualifying assets	94.32% of total assets (excluding cash, balances with banks and financial institutions, government securities and money market instruments), comprise 'Qualifying Assets', as on Dec.16
2	Net worth to be in excess of Rs 5 Crore	Complied. Net worth of Rs. 179.07 Cr. as on Dec. 16.
3	Income of borrower not to exceed Rs 100,000 in the rural areas and Rs 160,000 in the urban and semi-urban areas*	AMPL verifies the household income at three levels i.e. by Field Credit Officer, Branch Manager and Appraisal Officer prior to disbursement. AMPL takes a declaration from the loanee regarding their household income.
4	Loans size not to exceed Rs 60,000 in first cycle and Rs 100,000 in subsequent cycles*	Complied. Highest loan amount given to an individual borrower in the first cycle has not exceeded Rs. 40,000, similarly maximum loan given on the third cycle till date is Rs. 60,000. In future also AMPL will strongly follow upper caps of loan amounts while sanctioning loans
5	Total indebtedness of the borrower not to exceed Rs 100,000 (excl medical and education loans)*	Complied. AMPL depends upon its field staff as well as its appraisal team to know about the total indebtedness of the borrower. AMPL is also a partner to High Mark and Equifax MFI Credit Information Bureau & checks borrower's credit information prior to the sanction.
6	Tenure of loans not to be less than 24 months for loan amount in excess of Rs 30,000, with prepayment	Complied. AMPL is complying with these

Sr No	RBI's Direction	Status
	without penalty*	norms and disbursing for 24 month in case of loan amount more than Rs.30,000. AMPL do not charge prepayment penalty.
7	Pricing guidelines are to be followed	Complied. AMPL is abiding the 10% margin as its loan portfolio has exceeded 100 crores. With its reduced cost of borrowing and maximum margin of 10%, AMPL is charging interest to the borrowers at 24% reducing for first and second cycle & 23% reducing (for third cycle) (from June 16 onwards.)
8	Transparency in interest rates to be maintained	Complied. There are only three components in the pricing of the loan product of AMPL i.e Interest cost of 24% reducing (for first and second cycle) & 23% reducing (for third cycle) , 1% of the loan amount as processing fees & actual cost of group life insurance premium.
9	Not more than two MFIs lend to the same client	Complied. AMPL does not lend where the borrower has taken loan from two other NBFC-MFIs. It checks the indebtedness also through credit bureau from Highmark and Equifax.

* For the assets classified as qualifying

Source: Company data

Section 1: Code of Conduct Assessment



SEN: Sensitive Indicators; IEB: Integrity and Ethical Behaviour; TRP=Transparency; CLP=Client Protection; GOV=Governance; REC=Recruitment; CLE=Client Education; FGR=Feedback and Grievance Redressal; DSR=Data Security

Code of Conduct Assessment Summary

Annapurna's performance on the code of conduct takes into account MFI's strong performance on Transparency, Client Protection, Client Education, Recruitment and Data Sharing. The overall score is further enhanced by Annapurna's high score on sensitive parameters. There is scope of improvement across Governance and Feedback and Grievance Redressal Mechanism. Annapurna's overall score is impacted by low scores in Integrity and Ethical Behaviour.

MFI Strengths and Weaknesses pertaining to Code of Conduct

Strengths

- Annapurna communicates with borrowers in a transparent and professional manner. The MFI informs the clients about interest rates and other costs and issues receipts for all payments. All client communication is in the vernacular language.
- Operational staff is punctual and courteous towards borrowers. None of the borrowers complained about operational staff's behaviour during our field visits.
- Annapurna disseminates a single, effective annual rate to its borrowers. The processing fees charged is 1%, which is in line with the prescribed guidelines.
- Discussion with borrowers does not reveal any incidence where they been charged a processing fee of more than 1%. However, the company informed that they facilitate the 1st cycle clients for buying register and diary from third party. Further, the company informed that Annapurna financials doesn't reflect any amount which is received from sale of register and diary.
- All borrowers undergo training (compulsory group training, CGT and group recognition test, GRT). During training, clients are informed about the products, terms and conditions, and responsibilities.
- Key financial and operational performance data for FY2016 are displayed on Annapurna's website.
- No instances of collateral or security deposit being taken from the borrowers were observed. The same has been documented in the operational manual as well. Interviewed branch managers were aware regarding the guidelines.
- Annapurna undertakes review of its margin regularly and tracks the prevailing base rates of five largest banks. The company also gets compliance with RBI pricing guidelines certified by an independent CA agency on a quarterly basis.
- Annapurna has a policy stating that any non-credit product offered will be voluntary for the client and would not be a precondition for loans and the same has been documented. Branch staff interviewed was found to be aware of the policy regarding the same.
- No instances came to notice where a borrower had been made to pay for a service or product as a precondition for loan.
- Annapurna has a HR policy restricting the posting of new joiners at the same geography where they were associated with their previous organization.
- Before entering a particular state or district, Annapurna performs state, district and village surveys where micro credit saturation profile of the area is analysed.

Weaknesses

- Of the ADDO parameters, the company needs to improve on the approval policies/updates related to Board matters like review of code of conduct compliance report, recruitment policy, progress made on Aadhaar coverage, credit bureau checks post disbursement.
- Branch managers' awareness with respect to RBI directions regarding loan tenures, loan purpose and income level of borrowers could be improved through refresher trainings.
- Clients' awareness was particularly low on processing charges, insurance premium, grievance redressal mechanism of MFIN and that their data can only be shared for authorized purposes.
- Annapurna is a member of all four credit bureaus and shares data with all the four bureaus on a weekly and monthly basis. Review of loan files indicated that credit bureau checks had been made not more than 15 days prior to disbursement in all cases. Though Annapurna has a policy for CB check validity of 15 days before disbursement, however there is no automatic mechanism to restrict the disbursement if the CB report is more than 15 days which provides a chance for the same. However, Annapurna stated that there were few instances where company withdrew cash for disbursement but the process was delayed due to client's inconvenience to visit branches for disbursement.
- Annapurna does not have a structured compliance report on code of conduct parameters.
- The board is chaired by an executive chairperson (Chairman cum Managing Director) and 3 of the 10 board members are independent directors.
- During field visits ICRA noticed that the client's awareness level was low on the grievance redressal mechanism established by industry associations.
- Annapurna has developed acknowledgement and acceptance format for clients when they apply for a loan. However, clients interviewed revealed that loan application acknowledgement was not shared.
- It is not compulsory that for second and subsequent cycle loans, clients are identified through their UIDAI (Aadhaar) numbers for the purpose of credit bureau reports.

Significant Observations - Higher Order Indicators

1. Integrity and Ethical Behaviour

Strengths

- The scope of internal audit was reviewed by the audit committee of the Board.
- Internal audit report has been reviewed by the board, regarding non occurrence or otherwise of the following:
 - Abusive language or threats
 - Visiting borrowers at odd hours
 - Forcible entry into dwelling and forced seizure of property without the legal orders
- There is a board approved policy on handling delinquent loans.
- There is documentary evidence that the MFI has provided NOC or relieving letter to all employees who have given adequate notice before quitting.
- The staff members were trained by senior branch staff on the various processes to be followed including CGT and GRT and the disclosures to be made to the borrowers.
- The operational staff confirmed that they have received training on the following:
 - Conducting client meetings
 - Collecting repayments
 - Recovering overdue loans
- The staff confirmed receiving training from seniors on the grievance redressal mechanism.
- The total compensation of field staff (BM, AM, LO) remains the same whether the repayment rate attributed to the staff is 98% or 100%. The incentive is not linked with the portfolio quality. The incentive depends on monthly client enrolment but there is no incentive for number of client managed.
- The board has reviewed the recruitment policies or resource planning policy during board meeting held in September'16. The recruitment process is documented in the HR manuals.
- The MFI has a policy of providing sufficient notice to employees whose employment is being terminated. The notice period for field officer to Branch manager is 1 month while for Area Manager and above is 2 months.
- Submission of relieving letter from the previous employer is mandatory for new joiners.
- There is documentary evidence that the MFI has provided relieving letter to all employees who have given adequate notice before quitting.
- Grievance redressal mechanism established by industry associations is disseminated to the borrowers during training and is also displayed in the branches.
- The Group Nurturing of the SHGs is a 3 day process which includes training on the mechanism of Grievance Redressal Mechanism.
- Annapurna prepares monthly reports about the number, nature and resolution of grievances and feedback received for management review which is also shared SPM committee and MFIN on a quarterly basis.
- Annapurna's incentive policy specifies an upper limit for incentives related to monthly client enrolment targets. The maximum a field officer gets for enrolling clients is Rs 3,500 per month for adding 120 clients. The Branch Manager gets 30% incentive of the total incentive given to all the field officers in his branch.
- Annapurna does not have an incentive policy stating an upper limit for incentives related to number of clients managed.

1. Integrity and Ethical Behavior

Weaknesses

- Annapurna does not present regular compliance report on code of conduct parameters to the Board.
- The internal audit does not cover staff satisfaction related to compensation and incentive.
- All the branches visited had not displayed, the contact number and address of SRO nodal official (as applicable), in a manner that made it clear that a client could approach the official in case she is dissatisfied with the way her grievance has been handled.
- There is a documented HR policy that shortfall in collections like miscalculation of funds during collection will make the employee liable for disciplinary action such as penalty, termination. However, Annapurna stated that this is a precautionary measure only and any disciplinary action or punishment is given only after repeated occurrence of such event and proper investigation.
- During field visits ICRA noticed that the client's awareness level was low on the grievance redressal mechanism established by industry associations. However, the management has sent circulars presenting the MFIN grievance redressal number to all branches to be displayed.
- The borrowers confirmed that the central toll number was explained to them during the loan disbursement however some of the borrowers (~28%) were aware of the process to be followed in case of any grievance except reaching out to the field officer and branch manager.

2. Sensitive Indicators

Strengths

- Around 95% of borrowers were found to be aware of the amount and number of instalments they were required to pay.
- No instances of the following were found:
 - A borrower being made to pay for a service or product as a precondition for loan.
 - Fine or penalty being levied or collected from the borrowers.
 - Collateral or security deposit being taken from the borrowers.
 - Loan size or tenure being in non-compliance with RBI directions.
 - Annapurna charging clients additionally for insurance, apart from premium payable.
 - Clients had to make payment to informal agents or bribes.
 - Unauthorised sharing of client data by Annapurna.
- Annapurna's policy allows the borrowers to prepay loans and it does not lead to a change in the effective rate of interest.
- Discussion with borrowers does not reveal any incidence where they been charged a processing fee of more than 1%. However, the company informed that they facilitate the 1st cycle clients for buying register and diary from third party. Further, the company informed that Annapurna financials doesn't reflect any amount which is received from sale of register and diary.
- The difference between the interest rate charged on any two loan products is not more than 4%.
- Annapurna undertakes review of its margin regularly and gets the prevailing base rates of five largest banks from RBI. The company also gets compliance with RBI pricing guidelines certified by an independent CA agency on a quarterly basis.
- Clients receive sanction letters with all terms and conditions of the loan including annualized interest rates.
- During interviews with borrowers, loan utilisation was found to be in line with RBI's directions. Most of the loans were taken for income generation purpose.
- Not a single case was found during interview with clients and review of loan records, where a client had to make the first repayment on her loan before seven days had passed on a weekly repayment product or 14 days had passed on fortnightly repayment product or a month had passed on a monthly repayment product.
- Annapurna has a clear policy regarding documents to be collected for identity and address proof. The company requires borrowers to have either Aadhaar Card or Voter ID. The copy of KYC collected from clients will need to be verified with original documents by the field staff. No instances of KYC documents not being taken from borrower where a loan classified as qualifying microfinance loan, identity proof (with a verified with original declaration) had not been obtained.
- Annapurna as a policy collects either Aadhaar card or Voter ID for all loan cycles. As a company policy, the benchmark for minimum Aadhaar requirement is state level Aadhaar penetration (published by MFIN) plus 5%. However, Aadhaar is not mandatory for second cycle loans.
- Interviews with borrowers revealed that the staff did not indulge in the following:
 - Abusive language or threats
 - Visiting borrowers at odd hours
 - Forcible entry into dwelling and forced seizure of property without the legal orders.
- All clients revealed that they receive accurate receipts for all transaction.
- There were no adverse observations in the Auditor's report for the year 2015-2016 regarding accounting standards followed by the MFI.
- Annapurna is a member of all four credit bureaus and reports data to all of them on a weekly and monthly basis.

2. Sensitive Indicators

Weaknesses

- Most of the borrowers interacted with were found to be in compliance with respect to economic status and the income mentioned in the application forms was in compliance with the norms.
- Annapurna does not lend as a 3rd MFI and extends a maximum loan of Rs.60,000 under SHG model. However, in some cases ICRA noticed that indebtedness of borrower was more than that stipulated by RBI. Also, in 2QFY17 internal audit it was observed that 66 cases or 0.07% of the disbursed members were having over-indebtedness more than the stated guideline. At the time of lending, Annapurna was not the third lender, and the indebtedness was under prescribed norms.
- Review of loan files indicated that credit bureau checks had been made not more than 15 days prior to disbursement in all cases. However, the internal audit report of 2QFY17 states that there were 451 (0.45%) groups where member's KYC id was not resent for CB check after 15 days. There is no stated mechanism for credit bureau check which automatically restricts the disbursement post 15 days of CB check. However, Annapurna stated that there were few instances where company withdrew cash for disbursement but the process was delayed due to client's inconvenience to visit branches for disbursement.
- It is not compulsory that for second and subsequent cycle loans, clients are identified through their UIDAI (Aadhaar) numbers for the purpose of credit bureau reports.

Significant observations – Building Blocks

1. Transparency

Strengths

- Annapurna's board takes into consideration the guidelines and directions issued by Reserve Bank of India (RBI) with respect to vernacular language being used in communication, use of only single and effective interest rate, issue of receipt for any payments. The same have been documented in manuals. In June 2016, board meeting reviewed the RBI's directions on KYC and AML Policy.
- Circulars with the most recent RBI directions were available in the branches visited.
- Annapurna field staff was given training from a senior officer regarding RBI's direction through structured training programs.
- Around 90% of the branch managers and field staff were aware of the terms and conditions that need to be communicated in a transparent manner with the borrowers and were given training on the same.
- Discussion with borrowers does not reveal any incidence where they been charged a processing fee of more than 1%. However, the company informed that they facilitate the 1st cycle clients for buying register and diary from third party. Further, the company informed that Annapurna financials doesn't reflect any amount which is received from sale of register and diary.
- The difference in the effective interest rate between any two products is not more than 4%.
- Various forms and documents used by Annapurna are in the vernacular language which is covered in the Fair Practice Code and has been reviewed by the board in the past 1 year.
- The loan documents are maintained in local languages which were verified during branch visits.
- Discussions with clients revealed that they or someone in their families were able to read and understand the text in documents, such as loan cards, loan agreements etc, shared by Annapurna.
- Annapurna displays the effective rate of interest on its products in all its offices including branches.
- Almost all borrowers were found to be aware of the amount and number of instalments they were required to pay.
- Almost all the clients interacted with revealed that charges and price for all services (which should be voluntary) have been communicated in written.
- There is no significant difference between nominal interest rates and the APR. The processing fee charged by Annapurna is 1%, so the APR is only 1% higher than the nominal interest rates.
- Annapurna's policy allows the borrowers to prepay loans and it does not lead to a change in the effective rate of interest. Annapurna charges interest only for the duration of the loan.
- No instances of fine or penalty being levied or collected from the borrowers were observed. The borrowers also confirmed that no fine has been paid by them.
- Annapurna has a board approved policy stating that no security deposit will be collected, or collateral will be obtained for loans meant to qualify under priority sector classification and company's position on the same has been reviewed by the board in the past year.
- Not a single instance of collateral or security deposit being taken from the borrowers came to ICRA's notice during the field visit. The same has been documented in the operational manual as well. Interviewed branch managers were aware regarding the guidelines.
- Annapurna undertakes review of its margin regularly. It gets the prevailing base rates of five largest banks from RBI. The company also gets compliance with RBI pricing guidelines certified by an independent CA agency on a quarterly basis.
- Any changes in its interest rate are documented through formal circulars and the same were found in each of the branches visited.
- Review of latest loan files revealed that the loans had been disbursed at the latest rate of interest.
- The internal audit report tracks whether all clients receive the necessary loans documents and the same was reviewed by the board in the past year.
- The branch staff had received training from a senior staff regarding the documents to be provided to clients.
- Clients are provided with loan cards which includes all the terms and conditions of the loan. However, the copy of loan agreement is kept at the head office.
- Clients receive sanction letters stating terms and conditions of the loan.
- The company's code of conduct compliance report for the year 2015 is available in the public domain.
- The financial statements and annual report for 2015- 2016 is available on the company's website.

1. Transparency

Weaknesses

- The loan card does not provide the complete repayment schedule including number of instalments with interest and principal separately mentioned. There is a common register for the group where the combined repayment schedule of all the clients is mentioned. Also, in the loan card, a manual entry is done for each payment done broken down in interest and principal.
- While Annapurna has developed acknowledgement and acceptance formats for clients, interactions with borrowers revealed that they did not get a written acknowledgement when they apply for a loan.
- Annapurna does not have a system of documenting why a loan has not been sanctioned against an accepted loan application.

2. Client Protection

Strengths

- During the last one year, Annapurna's board has discussed the performance of the company on the following:
 - proportion of qualifying loan assets to total assets
 - loan sizes of qualifying loan assets
 - loan tenure of qualifying loans
 - loan purpose of qualifying loans
 - income of borrowers
 - KYC norms
- The norms regarding loan size, loan tenure and loan end use, borrower income criteria and turnaround times have been documented in operating manuals or the circulars. Additionally, AMPL's operational manual designs the loan tenure, size, etc in such a manner that it complies with RBI guidelines.
- Internal audit report keeps track of the following parameters and their compliance with RBI directions:
 - loan sizes of qualifying loan assets
 - loan purpose of qualifying loans
 - income of borrowers
 - KYC status of clients
- No instances of the following were observed during client visits:
 - Loan size or tenure being in non-compliance with RBI directions.
 - Clients being deliberately made to pre-pay.
 - Offering any un-approved product/service.
 - A party other than the MFI staff or client (and her family member), was involved in filling up her loan application.
 - A borrower made to pay for a service or product as a precondition for loan.
 - Annapurna charging clients additionally for insurance, apart from premium payable.
 - Clients had to make payment to informal agents or bribes.
 - Unauthorised sharing of client data by Annapurna.
- During discussions with borrowers, loan utilisation was found to be in line with RBI's directions. Most of the loans were taken for income generation purpose.
- Not a single case was found during interview with clients and review of loan records, where a client had to make the first repayment on her loan before seven days had passed on a weekly repayment product or 14 days had passed on fortnightly repayment product or a month had passed on a monthly repayment product.
- There was consistency in repayment observed and repayment as per the loan contract among the client sample.
- Annapurna has a clear policy regarding documents to be collected for identity and address proof. The company requires borrowers to have either Aadhar Card or Voter ID as a primary KYC document. The copy of KYC collected from clients will need to be verified with original documents. ICRA did not come across a single instance where a loan classified as qualifying microfinance loan, identity proof (verified with original declaration) had not been obtained.
- Borrowers were satisfied with the monthly repayment frequency of loans.
- ~90% of the borrowers interviewed revealed that they had been disbursed loans within specified time limits.
- Annapurna has a policy stating that any non-credit product offered will be voluntary for the client and would not be a precondition for loans and the same has been documented. Branch staff interviewed was found to be aware of the policy regarding the same.
- Annapurna provides insurance to its clients through IRDA approved agency. Review of insurance claims settled by the MFI revealed that all of the sample claims had been settled within a period of 90 days.
- In the past year, Annapurna board had assessed its credit appraisal guidelines with respect to credit risk of the company.
- Before entering a particular state or district, Annapurna performs state, district and village surveys where micro credit saturation profile of the area is analysed. The saturation profile of the areas the where it operates was reviewed by the board in the past one year.

Strengths

- The operational staff revealed that they had been trained on how to assess repayment capacity of borrowers as mentioned in credit manual which includes housing surveys and cash flow analysis done on the loan form.
- Around 94% of branch managers were aware of the RBI's directions regarding loan size and income level of borrower.
- Around 89% of branch managers were aware of the RBI's directions regarding loan tenures.
- Most of the borrowers interacted with were found to be in compliance with respect to economic status and the income mentioned in the application forms was in compliance with the norms.
- Annapurna's loan application form captures borrower's household income, expenses and indebtedness. While all the loan forms verified by us had a cash flow analysis, it was generic in nature and not stringent. Further, in some branches, the income and expenditure data in the hand held devices was wrongly entered.
- Annapurna's branch visited had records that state the most recent loan appraisal criteria of the MFI.
- In the sample of clients interviewed the income, expense and indebtedness levels broadly matched with the stated levels in the loan form.
- In the past year, Annapurna's board has reviewed its performance with respect to indebtedness of borrowers.
- Annapurna's incentive policy specifies an upper limit for incentives related to monthly client enrolment targets. The maximum a field officer gets for enrolling clients is Rs 3,500 per month for adding 120 clients. The Branch Manager gets 30% incentive of the total incentive given to all the field officers in his branch.
- Annapurna does not have an incentive policy stating an upper limit for incentives related to number of clients managed.
- Annapurna has documented guidelines regarding credit bureau checks to be performed on loan applications to check indebtedness of the client.
- Around 96% of the clients interviewed had borrowing from two or fewer lenders, including loans taken from the BC channel.
- Interviewed Branch Staff have been given training or orientation on RBI's guidelines regarding maximum indebtedness of clients.
- Interviewed Branch Staff are aware of process to be followed in case credit bureau reports are found to be inaccurate.
- Internal audit keep track of indebtedness of borrowers and whether compliance with RBI's directions is being met.
- The maximum loan given by Annapurna under SHG loans does not exceed Rs 60,000. ICRA did not come across any instance where the total loan to a borrower exceeded Rs 60,000.
- The operational manual specifies guidelines for the following which is approved by the board.
 - Informing the clients regarding the product and services of the MFI, particularly the interest rates and other costs
 - Conducting client meetings
 - Collecting repayments
 - Recovering overdue loans
- The operational staff confirmed that they have received training on the following:
 - Conducting client meetings
 - Collecting repayments
 - Recovering overdue loans
- Borrowers reported that MFI staff arrives on time for client meetings and staff conduct is professional.
- Discussions with clients revealed that they did not find the process of making repayments inconvenient or risky.
- Internal audit report has been reviewed by the board, regarding non occurrence or otherwise of the following:
 - Abusive language or threats
 - Visiting borrowers at odd hours
 - Forcible entry into dwelling and forced seizure of property without the legal orders
- The operational manual clearly present guidelines to prevent the following:
 - Abusive language or threats
 - Visiting borrowers at odd hours

Strengths

- Forcible entry into dwelling and forced seizure of property without the legal orders
- The MFI staff confirmed that they had received training regarding the policy of not visiting borrowers at odd hours and not to forcibly enter into dwelling and seize client property without the legal orders.
- Interviews with borrowers revealed that the staff did not indulge in the following:
 - Abusive language or threats
 - Visiting borrowers at odd hours
 - Forcible entry into dwelling and forced seizure of property without the legal orders.
- Annapurna designs its products in a way which that the loan tenures are compliant with RBI guidelines and the products are approved by the Board.
- There is proof that Annapurna has initiated action against staff members against whom complaint regarding unacceptable behaviour has been received.
- The total compensation of field staff (BM, AM, LO) remains the same whether the repayment rate attributed to the staff is 98% or 100%. The incentive depends on monthly client enrolment but there is no incentive for number of client managed.
- Internal audit report has been reviewed by the MFI's Board, regarding appropriate vouching or by MFI staff. The staff confirmed that they had been trained on the same.
- All clients revealed that they receive accurate receipts for all transaction.
- Annapurna has documented guidelines regarding credit bureau checks to be performed on loan applications to check indebtedness of the client. There are documented guidelines regarding maximum indebtedness which includes loans that a borrower may have taken from banks through BCs or otherwise. Annapurna as a policy does not lend as a third lender and the total indebtedness of the borrower does not exceed Rs. 60,000.
- Annapurna has issued a clearance circular on overriding/not using credit bureau reports if they are inaccurate. Discussions with branch managers revealed that incase borrowers approach the MFI stating that they have foreclosed a particular loan and the bureau report is not reflecting the right status, in those cases NOC is taken from the old lender. However such instances are minimal.
- Annapurna has a board approved policy of recovering delinquent loans. The operational manual presents guidelines on dealing with delinquent clients, for different stages of default.
- Interviews with staff members revealed they were aware of the process to be followed with delinquent clients.
- Review of Board minutes reveals that action initiated against delinquent clients was discussed. The reasons of delinquency are shared with Board during Risk Committee meeting and Board gives their inputs when necessary.
- Interviews with employees reveal that they never had to make good any shortfalls in collection from their own money.
- MFI has a policy on maintaining the privacy and security of client's data.
- The MFI takes backup of digital data on a weekly basis.
- The operational manual does not present how client data is to be stored by the MFI. However the same is incorporated in privacy policy.
- The staff members were aware of the importance of keeping client data confidential and the manuals also state that the data collected would be for purposes specified.
- Internal audit guidelines require internal audit checks to be performed on whether client data has been stored with adequate security.

2. Client Protection

Weaknesses

- Annapurna's board don't review its performance on its turnaround times for loan sanction and disbursement. However, the loan agreement states that recommendation/ rejection will be intimated within twenty one working days from the date of application.
- Annapurna does not lend as a 3rd MFI and extends a maximum loan of Rs.60,000 under SHG model. However, in some cases ICRA noticed that indebtedness of borrower was more than that stipulated by RBI. Also, in 2QFY17 internal audit it was observed that 66 cases or 0.07% of the disbursed members were having over-indebtedness more than the stated guideline. At the time of lending, Annapurna was not the third lender, and the indebtedness was under prescribed norms.
- The Board has not reviewed any exceptions that the MFI may have made on credit bureau reports in the previous quarter.
- Annapurna does not perform verification tests through additional credit bureau checks on clients after loan disbursement.
- The credit manual does not link the loan sizes and duration with the assessment of the repayment capacity.
- Internal audit checklist includes indicators on whether credit bureau check has been done not more than 15 days prior to disbursement. Loan files reviewed also indicated that credit bureau checks have been made not more than 15 days prior to disbursement in all cases. However, the internal audit report of 2QFY17 states that there were 451 (0.45%) groups where member's KYC id was not resent for CB check after 15 days. There is no stated mechanism for credit bureau check which automatically restricts the disbursement post 15 days of CB check. However, Annapurna stated that there were few instances where company withdrew cash for disbursement but the process was delayed due to client's inconvenience to visit branches for disbursement.
- There is a documented HR policy that shortfall in collections like miscalculation of funds during collection will make the employee liable for disciplinary action such as penalty, termination. However, Annapurna stated that this is a precautionary measure only and any disciplinary action or punishment is given only after repeated occurrence of such event and proper investigation.
- Annapurna's board has not reviewed progress made by the company in collecting Aadhaar of clients in the past year.
- For second and subsequent cycle loans, clients may be identified through their Voter ID or UIDAI (Aadhaar) numbers for the purpose of credit bureau reports. However, Aadhaar number is not mandatory as of yet for second cycle loans CB check. As a company policy, the benchmark for minimum Aadhaar requirement is state level Aadhaar penetration (published by MFIN) plus 5%.
- Client awareness of the fact that their data can only be shared for authorized purposes was only 46% of the clients interviewed. However, permission had been obtained for the same from each borrower in the loan agreement.

3. Governance

Strengths

- Annapurna has a Fit and Proper policy which states that the members inducted should be of good and sound reputation. All the members of the existing board of the MFI have good and sound reputation and are qualified to provide direction to the MFI.
- The board meets at least once every quarter and the minutes of the meetings are maintained by the MFI.
- The policies and procedure of the MFI and any subsequent changes to the same are approved by the board. The meeting agenda contains the key operational and financial information of the MFI.
- The audited financials disclose the compensation of key managerial personnel which consists of CEO compensation.
- Annapurna has a board approved policy for restructuring loans of borrowers facing repayment stress. ~92% of the branch staff interviewed were aware of the same.
- MFI has never restructured loans of clients facing repayment stress in the past.
- Annapurna has constituted an audit committee of the board with an independent director as chairperson.
- The audit committee has met four times over the past year. Minutes of the audit committee have been maintained.
- Annapurna has a dedicated internal audit team. The internal audit head directly reports to the Board committee.
- The audit committee of the Board has reviewed whether the scope of Internal Audit is adequate.
- The audit committee of the Board has reviewed that the Internal Audit team has adequate staff strength during the previous one year. The Audit team discloses its staff strength to the Board. Any planning about change in staff strength is done with the HR department.
- The Internal audit team conducts branch audits every quarterly. However, ~83% of the branches visited had action taken report based on the last audit report.
- There were no adverse observations in the Auditor's Report for the year 2015-2016 regarding accounting standards followed by the MFI.

Weaknesses

- The Board chair person is an executive (Chairman cum Managing Director) of the company and not an Independent Chairperson.
- Annapurna does not have a written policy regarding that 1/3rd of the board members are independent persons.
- Annapurna's board consists of 10 directors of which 3 are independent.
- Staff satisfaction related to compensation and incentive is not covered by internal audit.
- Annapurna does not have structured compliance report on code of conduct parameters which is presented to the board on a regular basis.

4. Recruitment

Strengths

- The board has reviewed the recruitment policies or resource planning policy during board meeting held in September'16. The recruitment process is documented in the HR manuals.
- Reference check for new joinees is conducted including from previous employer.
- The MFI has a documented system of reference checks on all its new employees. There is documentary evidence to show that MFI has performed reference checks.
- The MFI has a policy of providing sufficient notice to employees whose employment is being terminated. The notice period for field officer to Branch manager is 1 month while for Area Manager and above is 2 months.
- There is documentary evidence to suggest that MFI has honoured the notice period for all employees who have left it.
- Submission of relieving letter from the previous employer is mandatory for new joinees.
- There is documentary evidence that the MFI has provided relieving letter to all employees who have given adequate notice before quitting.
- The MFI has a documented policy that when it recruits staff from another MFI, the said staff will not be assigned to the same area he/she was serving at the previous employer for a period of one year. Interview with employees of the MFI does not provide any evidence contrary to the above.

Weaknesses

- The MFI does not have a defined and documented process for responding to reference check requests. However, there is a documentary evidence to suggest that the MFI responded to reference check requests.

5. Client Education

Strengths

- Annapurna has a documented CGT process which states that all borrowers should be informed about the products, terms and conditions, and responsibilities.
- The staff members were trained by senior branch staff on the various processes to be followed including CGT and the disclosures to be made to the borrowers.
- Borrowers confirmed receiving detailed trainings (compulsory group training) on the product and organisation policy. The borrower's further confirmed that no payment has been made for these trainings.
- Proportion of clients aware of each of the terms and conditions is as follows:
 - Annualized Interest rate - ~90%
 - Processing fees - ~90%
 - Insurance claim settlement process - ~95%
 - Insurance charges - ~92%
- Internal audit checklist includes assessment of clients' awareness and understanding on aspects like interest rates and other charges, products, choices and responsibilities.

6. Feedback & Grievance Redressal

Strengths

- Annapurna's GRM policy has details of the grievance redressal and includes time frames for grievance resolution as well as escalation mechanism. Annapurna has provided a complaint box at all the branches. Additionally, the central number (toll number) is provided with every loan card for registration of complaints by borrowers.
- The members of staff confirmed receiving training from seniors on the grievance redressal mechanism.
- The Group Nurturing of the SHGs is a 3 day process which includes training on the mechanism of Grievance Redressal Mechanism established by Industry associations.
- During borrower's visits, we noticed that almost all the clients were aware of the MFI name and branch location.
- In its loan agreement the MFI makes a declaration that it is responsible for the behaviour of its staff.
- Grievance redressal mechanism established by industry associations is notified in the passbook.
- Annapurna provides the number of the client grievance redressal/feedback official to all its clients in loan cards/passbooks etc.
- Grievance redressal system set up by the MFI is displayed by 89% of its branches visited.
- In 89% of the branches visited, the MFI displays that it is responsible for the actions of its staff and that the clients will be treated fairly despite grievance being lodged.
- Around 88% of the clients were aware of the grievance redressal mechanism.
- There was a positive response when a surprise call was made on the toll free number provided.
- Annapurna has a system for recording complaints diligently and ~89% of the branches visited maintain action taken reports on the complaints received from clients.
- Nature and status of resolution of complaints forms a part of the internal audit report and the same had been presented to the board in the past year.

Weaknesses

- There was no documentary proof that Annapurna has provided acknowledgement to clients and acted upon grievances in a time bound manner and as mandated in its policies.
- Annapurna has designated a grievance redressal officer; however the same is not a dedicated resource.
- In all the branches visited, the contact number and address of SRO nodal official (as applicable), had not been displayed in a manner that made it clear that a client could approach the official in case she is dissatisfied with the way her grievance has been handled.
- The borrowers confirmed that the central toll number was explained to them during the loan disbursement however some of the borrowers (~28%) were aware of the process to be followed in case of any grievance except reaching out to the field officer and branch manager.
- Clients were not aware of the existence of Grievance redressal mechanism of the Industry Associations. However, the management has sent circulars presenting the MFI grievance redressal number to all branches to be displayed.

7. Data Sharing

Strengths

- Annapurna is a member of all four credit bureaus and reports data to each of them on a weekly and monthly basis.
- Both the operational and financial performance numbers for FY2016 are available on the company's website.
- Annapurna has provided data when called for by the RBI or MFIN.

Annexure: Methodologies

Microfinance Grading Methodology

<http://www.icra.in/Files/Articles/mfi%20grading%20methology%20note%20for%20upload.pdf>

COCA Methodology

The Code of Conduct Assessment (COCA) tool was developed as a response to the need expressed in a meeting of stakeholders in Indian microfinance by the Small Industries Development Bank of India (SIDBI) and the World Bank in December 2009. The code of conduct dimensions were identified by reviewing the various norms for ethical finance. These included RBI's fair practices guidelines for Non Banking Financial Companies, industry code of conduct (Sadhan-MFIN) and Smart Campaign's Client Protection Principles (CPP).

In 2016, need was felt to harmonize COCA to the most recent industry code of conduct and to standardize COCA tools of different rating/assessment agencies. This grading is based on the harmonized COCA tool. In the harmonized COCA tool, the dimensions were classified in three categories – highest order, higher order and building blocks. This grading is based on the harmonized COCA tool.

Highest Order	
Sensitive Indicators	
Higher Order	
Integrity & Ethical Behavior	
Building Blocks	
Governance	Client Protection, Recruitment
Transparency	Feedback/Grievance Redressal
Client Education	Data Sharing

Chart: COCA Indicators Framework

Number of indicators in each category is presented below

Higher Order Indicators	Number of Indicators
Integrity and Ethical Behaviour	32
Sensitive indicators	27
Building Blocks	Number of Indicators
Transparency	40
Client Protection	123
Governance	30
Recruitment	13
Client Education	14
Feedback & Grievance Redressal	25
Data Sharing	6
Total	251

Methodology

This is regarding the Code of Conduct Assessment (COCA) exercise to be conducted by us. The COCA exercise is spread over 15-30 days. The first day is spent at the head office. The assessment team visits the branches over the next three to fifteen days, after

which we take around five days to share our draft report. Depending upon the size and the operational area of the MFI, up-to fifteen branches and 300 clients are sampled for primary survey.

Sampling guidelines

The following is taken as the guideline to determine the sample size for a COCA exercise.

MFI Size	No. of branches to be visited	No. of borrowers to be visited
Small MFI (Less than 8 branches)	All branches	15 clients per branch covering minimum two centers.
Small / Mid size MFI (up to 2,50,000 borrowers)	8 – 10 branches (geographically distributed)	60-120 clients (15 clients per branch covering minimum two centers).
Large MFI (>2,50,000 borrowers)	12 – 15 branches (geographically distributed)	240-300 clients (20 clients per branch covering minimum two centers).
Large MFIs (Loan portfolio outstanding of Rs500 crore or more, irrespective of the number of borrowers)	18 – 20 branches (geographically distributed)	360-400 clients (20 clients per branch covering minimum two centers).

The selection of branches can be done using a criteria based approach.

Step 1- High stress branches: Violations of the code of conduct are most likely to occur in areas where an MFI’s loan portfolio is experiencing stress. Hence, it is suggested that branches which have shown portfolio quality problem should be included in the sample. The maximum number of branches selected using this criteria should be 40% of the total branches that need to be sampled.

Step 2: After identifying branches based on step 1, a list of districts along with the number of branches, distance of the branches from their District Office, and the number of clients, may be prepared. We can then select districts to identify the remaining branches that need to be sampled. The districts may be selected following a methodology that gives a higher probability of selection to those districts that have higher proportion of MFI clients. In other words, the probability of selection of a district should be close to the proportion of clients that the MFI has in that district. The sampling of the district should be done without replacement. In this approach it is possible that a particular district may appear more than once in the sample. Finally, branches should be selected from the districts chosen. We may choose as many branches from a district as the number of times it appears in the sample.

Thus, we may choose one or more branch per district. This selection may be based on the following rules:

1. The branch should have been in operation for atleast six months

2. Adequate representation (around 30% of total branches sampled) should be given to branches that are at least 30 km (or farthest) away from the nearest district office.

Selection of Clients in the Sample

In the sampled branches, two cluster of clients should be selected. These clusters could be JLG-centers or large client groups or village etc. In each of these clusters, around 10 clients should be interviewed. This will give us a sample of around 20 clients in each branch. Further, in each branch four interviews with clients (2 in each cluster) should be made at a location of the clients preference.

Code of Conduct Assessment exercise requires:

1. Review of policy documents and manuals at the head office. These are reviewed in order to assess the policy as well as documentation regarding important aspects of the code of conduct.
2. Discussions with key staff members and the senior management at the head office, particularly the senior operational management team as well as the human resources team. These discussions focus on key issues of the code of conduct identified after the review of documents.
3. Sampling of branches. The assessment team samples branches for review. The branches are chosen across different states in case the MFI operates in more than one state.
4. Discussions with the branch staff at the branch office. Discussions with branch managers and the field staff is carried out to assess their understanding of the key code of conduct principles.
5. Sampling of respondents in the selected branches. A sampling is performed on the MFI's clients by the assessment team to draw respondents.
6. Interview with the clients. Information from the clients is collected primarily during the group meetings. Some clients are also met at a location of their preference. Additionally telephonic interviews are held with some clients.
7. Review of loan files. This review focuses on loan appraisal performed before disbursing loans as well as the documents collected from the clients.

As part of this assessment, we visited eighteen branches of the MFI. The details of the branches visited are provided below.

Sr No	Branch	State	No of clients interviewed
1	Balipatna	Odisha	20
2	Khurda	Odisha	16
3	Dhenkanal	Odisha	18
4	Choudaar	Odisha	23
5	Begunia	Odisha	19
6	Tangi	Odisha	17
7	Salepur	Odisha	23

Sr No	Branch	State	No of clients interviewed
8	Barang	Odisha	25
9	Shirdi	Maharashtra	20
10	Sangamner	Maharashtra	23
11	Jalgaon	Maharashtra	21
12	Pachora	Maharashtra	21
13	Dhule	Maharashtra	25
14	Chalisgaon	Maharashtra	20
15	Satana	Maharashtra	20
16	Manmad	Maharashtra	24
17	Mohua	Bihar	25
18	Bidupur	Bihar	16
Total			376