

Pahal Financial Services Private Limited (Pahal)

Mumbai, India

Legal form: NBFC

January 2014

Code of Conduct (CoC) Assessment

Achievement	Maximum	Score achieved
Integrity, Governance and HR Strategy	30%	22.7%
Compliance with guidelines pertaining to clients	60%	49.0%
Effectiveness of client education efforts, and awareness	10%	7.7%
Overall CoC	100%	79.4%

Visit dates: 06-08 January 2014

M-CRIL

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Structure

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 - Governance
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Key for bullets:

- ✓ Positive
- Neutral
- Issue
- Description

Assessment tool and framework

Assessment Tool

- ▶ This assessment uses a scoring tool derived from the Unified Code of Conduct for member MFIs of Sa-Dhan and MFIN and the RBI guidelines and Fair Practices Code for NBFC MFIs.
- ▶ The tool not only covers the industry Code and the above-mentioned guidelines in letter but also delves deep into issues of adherence in spirit. The tool is arranged under three broad heads:
 - Integrity, Governance and HR Strategy
 - Compliance with guidelines pertaining to clients
 - Effectiveness of client education efforts and awareness

Methodology

- ▶ The assessment is based on a 3 day visit by an M-CRIL team of 2 analysts to the MFI's head office in Ahmedabad and to 4 branches across Gujarat. Multiple groups were visited in each branch. (Refer Slide No. 39 for detailed Methodology and Slide 41 for sampling plan details).

Perspective on the MFI

- ▶ Pahal's performance is good on various aspects of Code of Conduct. It has designed its loan products, policies and processes in line with RBI guidelines. It has made sincere efforts to integrate various aspects of CoC in its operational policies. However, there is a need to ensure reporting of CoC compliance status to board, improve grievance redressal mechanism and client privacy and design standardized training module which should include specific training to staff and clients on various aspects of CoC.

Level of cooperation with assessment team:

HO	HIGH	Branches	HIGH	Follow-up	HIGH
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...Assessment tool and framework

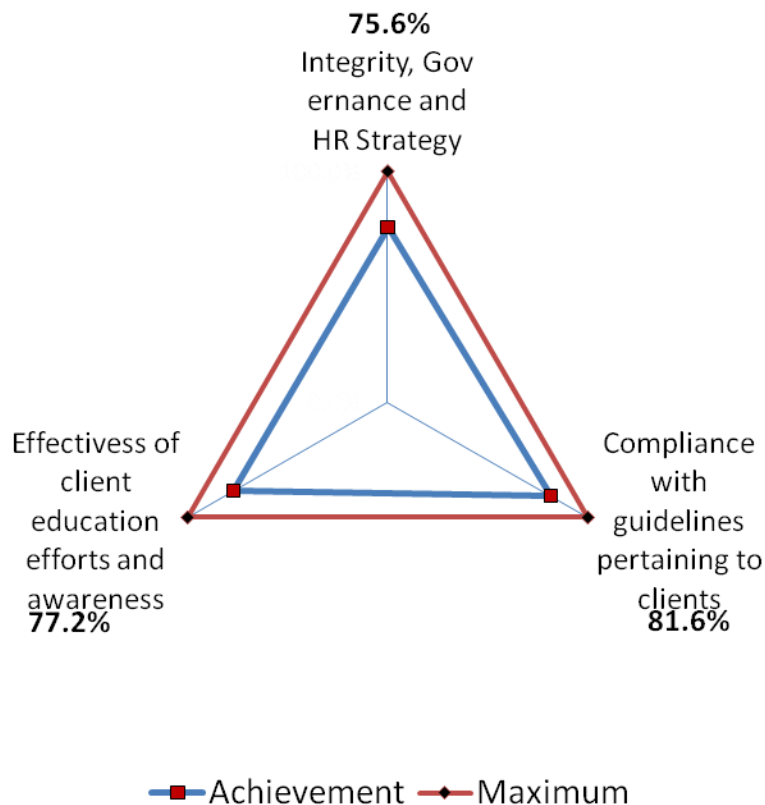
- ▶ The various aspects of the Unified Code of Conduct, RBI guidelines and the Fair Practices Code have been reclassified by M-CRIL under three broad heads (Integrity, Governance & HR Strategy, Effectiveness of Client Education Efforts and Awareness) and Compliance with Regulation Pertaining to Clients as per their logic and fit.
- ▶ Compliance with guidelines, being one of the most important aspects, has been given the maximum weight of 60%. Integrity, Governance and HR Strategy follows with 30% weight, and Efforts for Client Education, along with client awareness (as reflected through client interactions) is given a 10% overall weight.
- ▶ Level of internalisation of the codes of conduct by the MFI has been analysed for Approval, Documentation, Dissemination and Observance (ADDO) under each category, wherever applicable.
- ▶ Wherever relevant, more weight has been given to those policies adopted by the MFI and implemented in letter and spirit, compared to those which are well documented but not practiced.
- ▶ Field results have been included in each relevant section under the broad heads mentioned above. Field results have been given 40% weightage. Client Education section is assessed in terms of efforts as well as results i.e. levels of awareness about products, terms and conditions and policies of the MFI.

...Assessment tool and framework

The CoC Assessment tool was required to cover 8 points as per SIDBI's guidelines (shown on the right of the box below). This tool covers these by fitting them into broader parameters and capturing performance on them as well as other indicators in terms of Approval, Documentation, Dissemination and Observance.

Parameters and Indicators in M-CRIL tool		SIDBI requirements covered in this section
Integrity, Governance and HR Strategy	30%	
Integrity	10.0%	Integrating social values into operations
Governance	10.0%	
Human Resource Strategy	10.0%	
Compliance with regulations pertaining to clients	60%	Compliance status of MFI vis-à-vis latest RBI guidelines
Client Origination and targeting	9.0%	Client origination and targeting
Loan Appraisal Process	9.0%	Loan appraisal process
Loan product features and pricing	10.0%	Loan pricing and transparency
Transparency	10.0%	
Responsible lending	9.0%	Staff behaviour
Grievance mechanism	9.0%	Relationship management & grievance redressal mechanism
Privacy of client information	4.0%	Privacy of Client Information
Client Education Efforts and Field Results	10%	
Client Education (Efforts)	3%	
Client Awareness and other Results	7%	
Total	100%	

Code of Conduct performance



Rationale

- ✓ Pahal has achieved a reasonable score in Integrity & Governance for implementing key aspects of the CoC. Overall score can be improved by inducting a dedicated person to ensure compliance on CoC, submitting compliance report on the extent of compliance to board and improving its systems to ensure data entry on real time basis.
- ✓ Pahal has achieved a good score in regulatory compliance due to its adherence to RBI guidelines. The score can be further improved by tracking client income information in MIS, disseminating default-handling norms, displaying of rate of interest, obtaining client permission for sharing of information with CB and developing training module covering specific aspects of CoC
- ✓ Pahal has achieved a reasonable score in client education due to its efforts to educate clients through multiple interactions. However, client's awareness level was low especially on their rights and responsibilities as per CoC and privacy issues. Low level of awareness was also recorded on prepayment terms and conditions, processing fees and insurance charges.

Strengths

- ✓ Good governing structure - appropriate representation of independent directors on the Board. All the Board members are professionally qualified, with experience in banking, corporate and microfinance sectors
- ✓ Good efforts to educate clients about company products and policies and grievance redressal mechanism
- ✓ Good monitoring systems – direct involvement of promoter directors in monitoring and interactions with the clients
- ✓ Positive feedback from clients regarding staff behavior and product features

Issues

- ❑ Rural/urban classification is not done in the MIS
- ❑ Grievance redressal and CoC compliance reports are not submitted to the Board
- ❑ Does not have training manual and modules
- ❑ Scope to improve on client privacy issues by obtaining permission from clients for sharing their personal information with the credit bureaus
- ❑ Receipt for repayment of instalment need to be issued to group/clients to improve transparency
- ❑ Needs to make appropriate mechanism to ensure that collection details are entered in MIS on the same date
- ❑ No efforts to collect indebtedness related information from all sources - Field staff mostly relies on CB data
- ❑ Interest rate is not displayed in the branches and the interest rate on the website not updated
- ❑ Low level of clients awareness

Introduction and background

- ▶ Kelkar Leasing Company Private Ltd., an existing NBFC was acquired in February 2011 and renamed as Pahal Financial Services Private Limited.
- ▶ Pahal acquired the microfinance portfolio of Lok Vikas Nidhi, microfinance program of Vikas Centre for Development (VCD), a trust operating in the area of social development in Gujarat for 25 years.
- ▶ Pahal also acquired existing infrastructure of 14 branches of VCD across Gujarat with a total portfolio outstanding of Rs2.6 crores. As of December 2013, Pahal has its presence in 12 cities across Gujarat. It has reached out to 41,767 borrowers through a network of 23 branches.
- ▶ Pahal offers group loans to poor women in urban and rural areas for Income Generation, debt redemption and education. JLG loan ranges from Rs12,000 to Rs25,000 depending upon repayment capacity of the borrower.
- ▶ Pahal also offers individual loans ranging from Rs30,000 to Rs5,00,000, individual loan in excess of Rs50,000 are collateralized. Individual loans are mainly given for micro enterprises or for house repair.
- ▶ Pahal has a Board of five members consisting of three promoter cum executive directors; Daksha Niranjana Shah, Mr Kartik Shailesh Mehta and Purvi Jayendra Bhavsar and two independent directors. The Board members are well qualified and have good experience in microfinance, banking, development, government sector and corporate sector.
- ▶ Current promoters brought in the initial equity of Rs2 crores and received initial funding (term loans) from banks and financial institutions. During 2013-14, Pahal received financial assistance from SIDBI by way of Optionally Convertible Preference Shares (OCPS) worth Rs3 crores under Risk Capital Assistance scheme of SIDBI.

...Introduction and background

Vision

To reach out to 2,50,000 clients within first five years of operations

Mission

To provide sustainable services for financial inclusion in urban and rural areas

Main Performance Indicators*

	Mar-12	Mar-13	Dec-13
Active borrowers	18,340	36,094	41,767
Portfolio Outstanding (Rs.cr.)	12.89	30.13	41.68
Of which, Managed Portfolio	-	3.54	2.68
Number of states	1	1	1
Number of cities	12	12	12
Number of branches	14	20	23
Number of groups	3,874	7,297	8,503
Staff strength	58	103	129
PAR 60	0.23%	0.06%	0.23%
Total PAR inc write-off (Rs cr)	-	-	-
Yield on Portfolio	28.34%	26.99%	28.1%
Operating Self-Sufficiency	101.1%	106.3%	115.3%

*Note: As per the data provided by Pahal.

Microfinance policies

Branch Structure

- ▶ A branch typically has 5-6 Field Credit Officers (FCOs) who report to Branch Manger. FCOs are designated as Assistant Branch Manager (ABM) before promoting to BM level.
- ▶ FCOs are involved in group formation, disbursement and recovery of loans. They are also responsible for cash management and maintaining all required documentation at the branches.
- ▶ BMs supervise the activities of FCOs and are also involved in verifying the field level information reported by the FCOs. They are responsible for information flow to the Head Office and overall achievement of branch targets.

Village Selection

- ▶ To start operation in a particular village, Branch manager along with FCO conduct survey of that village and prepare a Village Information Sheet (in the prescribed format).
- ▶ The village is evaluated based on certain parameters like number of households, political and religious influence, economic activities (Agriculture or Micro Enterprises), repayment history of the borrowers in the area, existing infrastructure and accessibility and approach to the village.
- ▶ Similar exercise is done for evaluation of colonies/slums in urban area and preference is given to localities which are close to industrial clusters.

Group Formation

- ▶ Pahal targets low-income households in urban and rural areas.
- ▶ Interested women are informed about the loan terms and conditions and the KYC documents required to avail loans from Pahal.
- ▶ Those interested are invited to form groups of 4-7 persons, through self selection, and to elect a Leader.

Microfinance policies contd....

Loan Process

- ▶ Once a village is selected for operations, FCO holds an introductory meeting of interested women and briefs them about Pahal, its vision and mission, products and services, loan terms and conditions and KYC. FCO also does the reference check of women who express interest in availing loan from Pahal.
- ▶ After two days of first meeting, FCO revisits the village and facilitates group formation among interested women. A group consists of 4-7 women members.
- ▶ A visit to group member's house is conducted by FCO to collect the primary information about the household and economic activity and the same is verified by BM. If the BM is satisfied with the house verification and each applicant's household income and repayment capacity, a group is formed.
- ▶ Branch manager sends the primary information about the group members in an excel based format to HO for compulsory credit bureau (CB) check. HO sends the list of eligible clients as per CB report to branches.
- ▶ FCO provides 2 days Continuous Group Training (CGT) to eligible clients on a fixed date and venue. During CGT, applicants are briefed about the company, its loan products, processing fees and interest, joint liability norms, KYC documentation and grievance redressal mechanism. FCO also reads out the loan agreement during CGT.
- ▶ After successful completion of CGT, BM conducts a Group Recognition Test (GRT) where applicants are tested on their understanding of the terms and conditions for availing loan from Pahal, awareness about the products and joint liability etc.
- ▶ If the BM is satisfied with the performance, the group passes the GRT, after which the FCO fills the loan application form and collects the KYC documents (ID Proof, Voter ID, 3 photos and address proof). Each approved group is given an acknowledgement which is required to be produced to the branch at the time of disbursement.
- ▶ Loan application forms (with BM recommendations) along with GRT records are sent to HO for credit committee approval and incorporation of primary client information in MIS.

Microfinance policies contd....

Loan Process...contd

- ▶ Loans are approved by HO Credit Committee after considering the loan amount, purpose, business and household information, and repayment capacity.
- ▶ Decision for loan approval of groups is communicated to the branches through email, accordingly sanction letter is issued to each group by the respective branches.
- ▶ Loans are disbursed in cash at the branch office in front of all the group members and in the presence of the BM and the concerned FCO. The insurance premium amount and the processing fees are collected before making disbursement and receipt is given to all the members. During disbursement process, BM reads out the loan agreement and explains about group liability and loan terms and conditions.
- ▶ Collection of instalments takes place at the center meetings. Collection Demand sheet (CDS) for recovery is generated at the HO and sent to branches through courier. FCOs carry the CDS before going to the center meetings for collection. Loan card along with repayment schedule is issued to the members at the time of first instalment recovery.
- ▶ After collection, information about repayment collection is sent through email to the HO and a copy of the CDS is also sent through courier.
- ▶ In case, collection day falls on a national holiday, collection meeting would be scheduled for an earlier day immediately preceding the collection day.
- ▶ FCOs usually conduct the LUC at the time of first instalment collection.

Loan products

Product Name	Group loan	Individual Loan
Target Clients	Low income women	Micro Entrepreneurs
Loan size (Min-Max) in Rs	Rs12,000- 25,000	Rs30,000-5,00,000*
Term	Upto Rs15,000-12 months Above Rs15,000 – 24 months	3-12 months
Repayment frequency	Monthly	Monthly
Moratorium period	30 days	30 days
Processing fee(excl. Service tax)	1%	2%
Diminishing rate of interest % (p.a.)	28%	30%
Guarantee/Collateral	Joint liability	Collateral (Post-dated cheques/mortgage of property)
Penalty on overdues	None	None
Prepayment & foreclosure charge	None	None
Share in portfolio on 31 December 2013	97.02%	2.98%

* So far maximum amount of individual loan given is Rs2.5 Lakh only

Insurance

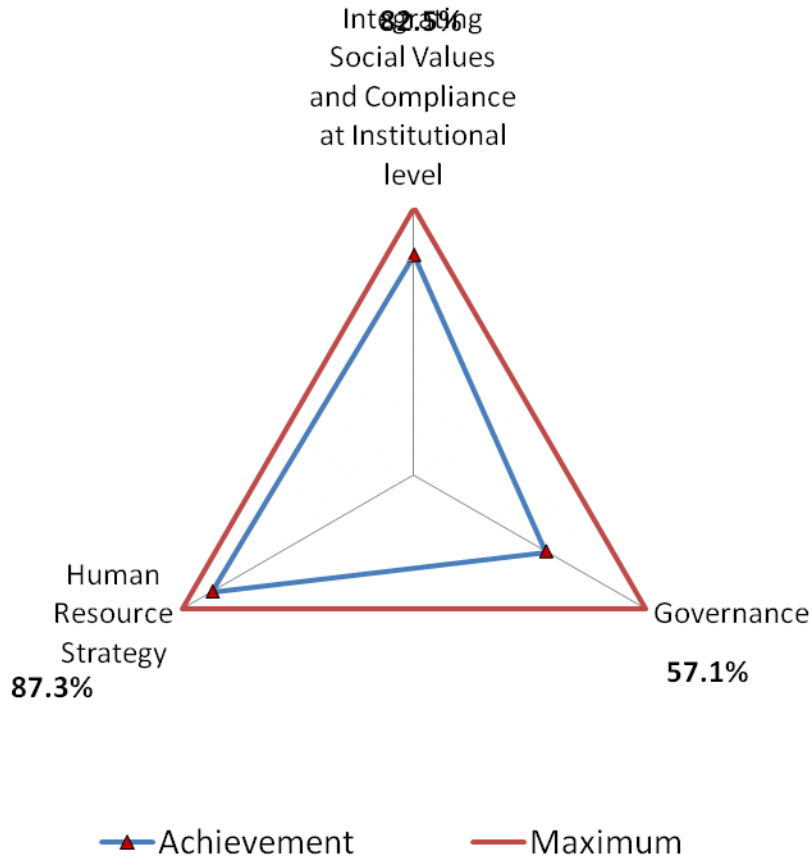
- ▶ Pahal has a tie-up with a third party insurance company for compulsory credit life insurance for each group borrower and their spouse.
- ▶ In the event of death, Pahal settles the outstanding loan amount and passes the remaining amount to the client's nominee.
- ▶ The clients/nominees have to produce death certificate and age proof document for the claim. In case of accidental death, postmortem report/ FIR is compulsory.

Insurance details:	
Date introduced	01 October 2011
Insurance company	Kotak Mahindra Old Mutual Life Insurance Limited
Coverage - who?	Clients and Spouse
Coverage - what?	Death of clients or spouse
Premium amount	Minimum Rs200, maximum Rs415
Tenure	12 to 24 months
Claim amount	For clients – disbursed loan amount For spouse – disbursed loan amount

Insurance Processing details (Apr-Dec'13)	
Total insurance accounts	83,534
Number of claims in the year	256
Number of payouts in the year	243
Number of rejected claims	0
% claims/accounts	0.31%
% payouts/claims	95%
Average time between claim & settlement	10 -15 days

Integrity, governance and strategy

Performance



Score obtained	Maximum
22.7%	30%

Levels of internalization

Levels of internalization	Approval	Documentation	Dissemination	Observance
Integrating Social Values and Compliance at Institutional level	Good	Moderate	Moderate	Good
Governance	Moderate	Weak	N.A	Good
Human Resource Strategy	Good	Good	Moderate	Moderate

...Integrity, governance and HR strategy

Integrating Social Values and Compliance at Institutional level	Compliance by Pahal
Not less than 85% of total assets of MFI	Pahal is compliant with the 85% qualifying assets criteria as per CA certificate issued for the quarter ending September 30, 2013.
Aggregate amount of loan extended for income generating activity is >70% of the total loans given	Pahal complies this criteria as more than 70% loans had been extended for income generating activities as per CA certificate for the quarter ending September 30, 2013.

Integrating Social Values at Institutional Level

- ✓ Pahal has incorporated the key principles of the Unified Code of Conduct (U-CoC), Fair Practices Code and RBI guidelines into its own Code of Conduct which is emphasized during one day class room training and also during supervisory visits.
- ✓ Both HO and branches have prominent displays of Pahal's CoC, product details, and grievance mechanism in the vernacular language. However at some branches old version of code of fair practices was displayed.
- ✓ Pahal has a good monitoring and internal control system to monitor all aspects of operations and adherence to RBI guidelines and Pahal's internal policies. Monitoring team also assesses staff behavior in dealing with clients and interacts with clients to understand client's issues and needs.
- ❑ Pahal is in the process of upgrading its systems to simplify the processes and achieve better control. As per the current practice, there is a one day delay in collection data entry in the system.
- ❑ HR manual does not include overdue collection policy and guidelines pertaining to employee interactions with the clients in the event of default. Field staff is aware of enforcing joint liability and visiting the house of defaulting borrowers.

...Integrity, governance and strategy

Integrating Social Values at Institutional Level

- ✓ Pahal achieved a margin within the 12% margin cap stipulated under RBI guidelines applicable until March 31, 2014 for all MFIs. As per the CA certificate, Pahal had a margin of 9.34% for the year ending March 31, 2013.
- ✓ Pahal's accounts are audited on yearly basis by a firm of qualified auditors (as per the standards issued by ICAI). Pahal displays its audited financial statements with full disclosures in public domain through its website and annual reports.
- Pahal does not have dedicated staff to ensure compliance with the code of conduct and RBI FPC guidelines. Aspects of COC are looked in to during quarterly visit of monitoring team.

...Integrity, governance and strategy

Governance

- ✓ Pahal has five professionally qualified persons who have expertise in banking, microfinance, corporate sector and government, on its Board.
- ✓ The 5 member board is composed of a Chairman who is an independent director, 3 executive cum promoter directors and an independent director (more than 1/3 of the board members are independent directors).
- ✓ The Board is actively involved in policy formulations and other important decisions. The meeting minutes show that the board discusses FPC guidelines and its implementation across the organization, compliance with statutory guidelines, policy on interest rate and product design.
- ❑ Pahal does not present a Code of Conduct compliance report to the board.
- ❑ Pahal has developed a grievance redressal mechanism and maintains a record of handling clients grievances, however, it does not analyse the types of issues and time taken for resolving the issues and no consolidated report is submitted to the board on grievance redressal.

...Integrity, governance and strategy

Human Resource Strategy

- Pahal recruits its field staff through advertisements placed in the local news papers or through employee referrals. Senior managers and promoters are closely involved in the recruitment process.
- ✓ Pahal makes a referral check through telephonic conversation from the candidate's previous employer at the time of selection. The BM visits the house and meets the family members of candidates who do not have prior work experience. In some of the cases a reference check is done with a college professor of the candidate. Pahal also responds to referral check request from other MFIs mainly over phone with in the stipulated time.
- ✓ Pahal seeks a copy of the resignation letter which has been duly accepted by the concerned organization before making an offer to a candidate. All new employees are required to submit the relieving letter to Pahal. All outgoing employees are issued a relieving letter except those who leave within 3 months of joining Pahal.
- ✓ A notice period of one month is served by all outgoing employees. This period is subject to review in case of any personal exigencies.
- ✓ All newly hired staff are given one day class room training on various aspects of operations including CGT, GRT and on some aspects of CoC. Pahal does not have any standardised training module or training manual.
- ✓ M-CRIL team during its visit observed that the field staff was aware about the internal code of fair practices developed by Pahal. Staff were aware of the guidelines for interactions with clients. In the event of overdues, field staff visits the defaulting borrower's house.
- Employees are incentivized on the number of borrowers and number of groups served by them. Client relationship is given a weightage of 15% during the half yearly appraisal. However, adherence to CoC guidelines are not incentivized.

...Integrity, governance and strategy

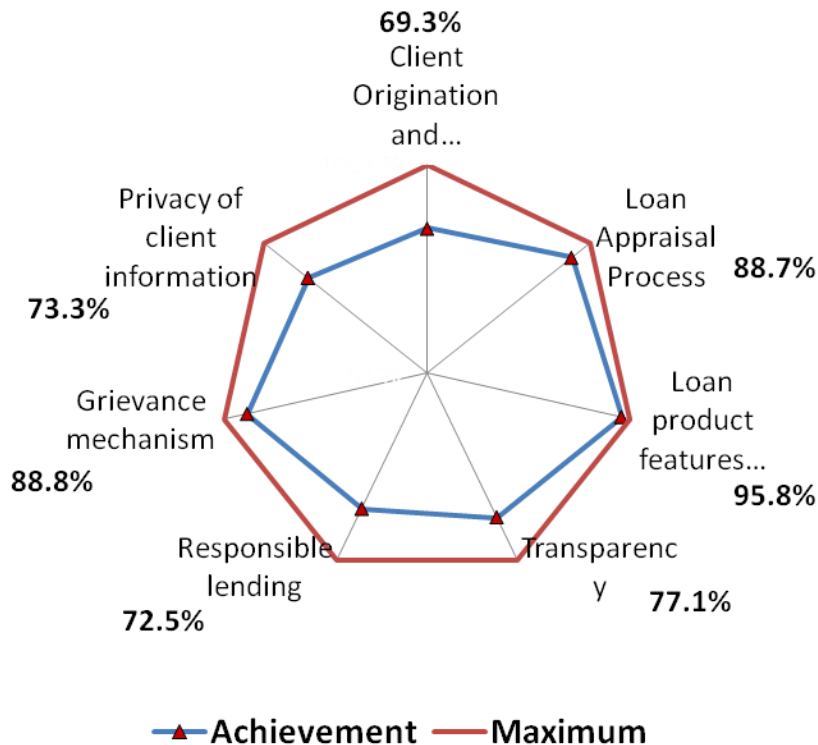
Human Resource Strategy

- Pahal may or may not assign the same operational area to new recruits (up to BM) as in most cases it deposes its staff near their home town.
- Pahal does not specify a penalty in cases of non-compliance of field staff with CoC but as per Pahal's Code of Fair Practices, disciplinary action can be taken against employees who violate the Code of Conduct.
- ✓ The MFI does not have a practice of making good the shortfalls in collection from its employees and its employee. Code of Conduct clearly specifies that this practice is unacceptable.
- ✓ Pahal uses only its own employees for the recovery of loans. No outsourced agents are engaged. In some cases senior management is also involved in recovery.
- ✓ Supervision and monitoring of compliance to CoC is part of internal control and monitoring mechanism. Monitoring team visits each branch on quarterly basis and monitors various aspects of CoC including staff behavior and grievance handling.

Compliance on Guidelines pertaining to Clients

Score obtained	Maximum
49.0%	60%

Performance



Levels of internalization

Levels of internalization	Approval	Documentation	Dissemination	Observance
Client Origination and targeting	Good	Moderate	Moderate	Moderate
Loan Appraisal Process	Good	Good	Good	Moderate
Loan product features and pricing	Good	Good	Good	Good
Transparency	Good	Moderate	Moderate	Moderate
Responsible lending	Moderate	Good	Moderate	Moderate
Grievance mechanism	Good	Moderate	Moderate	Good
Privacy of client information	Good	Moderate	Good	Moderate

Compliance with guidelines pertaining to clients

Client Origination and Targeting	Compliance by Pahal
Borrower's household income (HHI) does not exceed Rs 60,000 in rural areas and Rs 120,000 in non- rural areas	<ul style="list-style-type: none">✓ Pahal takes a self declaration from borrowers regarding their Household Income. Field staff also assesses client's household income and repayment capacity.❑ Rural/Urban classification is not done in MIS

Client Origination and targeting

- Pahal had 14 branches when it acquired the portfolio of the Vikas trust. It closed some of the branches and opened new ones to align its targeting and outreach.
- ✓ For opening of new branch, Pahal selects its operational area based on village surveys on occupation and cash flow of the potential clients, political/religious influence, accessibility and presence of competitors. In urban area it prefers to open a branch in or around industrial cluster to target the low income population working in that area.
- ✓ Loan application form captures details of client's household income, indebtedness information and repayment track record of previous loan.
- ✓ Pahal does not discriminate between its clients based on caste, religion or any such demographic characteristic.
- ✓ Requisite KYC documents (ID proof, address proof) with proper photo identification are taken from clients during appraisal. Voter ID is mandatory as it is used as the unique ID to track duplicate records.
- ✓ Clients are educated at various stages like introductory meeting, two days Continuous Group Training (CGT) and GRT. Pahal is in the process of launching a skill development program in partnership with Sadvichar Parivar, an NGO based at Ahmedabad.

Compliance with guidelines pertaining to clients

Loan Appraisal Process	Compliance by Pahal
<p>Total indebtedness of the borrower does not exceed Rs 50,000</p>	<ul style="list-style-type: none"> ✓ For indebtedness check of group loans, Pahal relies on compulsory Credit Bureau check and client declaration. ❑ Indebtedness information is not cross verified from group members/neighbors, although reference check from neighbours is done at the time of house verification
<p>The MFI ensures</p> <ul style="list-style-type: none"> ○ borrower does not have more than two NBFC-MFIs loans ○ borrower cannot be a member of more than one of its SHGs/JLGs ○ not lend to a single person as an individual & group borrower, simultaneously. ○ Involvement of more than one staff in loan sanctioning & disbursement 	<ul style="list-style-type: none"> ✓ A compulsory credit bureau check (in case of group loans) ensures that Pahal does not become the third lender to any individual. The loan application of clients who have two existing loans at the time of applying to Pahal, is rejected by the Credit Committee. ✓ The Individual and Group loan segments are entirely different and to ensure that clients do not borrow from different groups or branches, a de-dupe is done in the MIS using the voter ID card number (voter id card is mandatory for all clients of Pahal). ✓ All loans are approved by HO Credit committee comprising of any one of the directors, Operations Manager and branch manager of the respective branch. ✓ Disbursement takes place at the branch in the presence of BM and concerned FCO.

Compliance with guidelines pertaining to clients

Loan Appraisal Process	Compliance by Pahal
<p>Credit Bureau (CB)</p> <ul style="list-style-type: none">○ MFI is a member of at least one CB○ submits data regularly to the CB○ Checks with CB before sanctioning of loan○ In addition to CB checks, takes self certification from the borrowers	<ul style="list-style-type: none">✓ Data pertaining to group loans is submitted to both the Credit Bureaus – High Mark and Equifax. However, credit check is performed with Equifax only.✓ Credit bureau check is performed for all group loans and disbursements are made only to eligible clients.✓ Indebtedness information is captured in the loan application form which is duly signed by the borrower.○ During the visit most of the staff admitted to relying on CB data for information on indebtedness level of the clients.□ Also, it was observed that the field staff do not record loans taken from all sources other than MFIs, e.g. vehicle loans from banks.

Compliance with guidelines pertaining to clients

Product features	Compliance by Pahal
Loan size: does not exceed Rs 35,000 in 1st cycle and Rs 50,000 in subsequent cycles .	<ul style="list-style-type: none"> ✓ The loan size range for group loans in the first cycle is Rs12,000 -15,000 and in the subsequent cycles is Rs15,000-25,000, which is compliant with guidelines. ✓ Loan size for individual loan ranges between Rs30,000 to Rs5,00,000. Pahal claims that BM and loan approval committee at HO ensures that no individual loan exceeds Rs35,000 in the first cycle. Since these loans constitute only ~3% of the portfolio and do not come under the RBI guidelines, M-CRIL has not taken a view of it under this CoC assessment.
Tenure: not less than 24 months when loan amount >Rs 15,000	<ul style="list-style-type: none"> ✓ The tenure of the JLG loan product varies from 12 to 24 months. For loan size greater than Rs.15,000 the tenure is 24 months.
Repayment frequency: weekly/ fortnightly/ monthly at the choice of the borrower	<ul style="list-style-type: none"> ○ Client preference for monthly repayment is recorded in the loan application, though it appears to be more of a formality as the client awareness about the option for making weekly and fortnightly payments is extremely low.
Moratorium: is not less than the frequency of repayment (or min. one installment)	<ul style="list-style-type: none"> ✓ A moratorium period of at least 30 days is given to all clients.

Compliance with guidelines pertaining to clients

Pricing	Compliance by Pahal
Interest rate/pricing cap: <ul style="list-style-type: none"> Margin cap of 10% for large MFIs (with portfolio > Rs 100 crore), 12% for others Max. variance between the min. & max. interest rate does not exceed 4% 	<ul style="list-style-type: none"> ✓ Pahal is stipulated to maintain 12% margin cap as per RBI guidelines (for all MFIs applicable until March 31, 2014). As per the CA certificate dated Sept 20, 2013, Pahal has maintained a margin cap of 9.34% as on March 31, 2013. ✓ Pahal is charging 28% p.a. declining interest on group loans and maintains a variance of 4% between products (group and individual loans). ○ Interest rate on individual loans is 30% declining.
Pricing: only 3 components: (i) proc. fee (ii) interest (iii) insurance premium	<ul style="list-style-type: none"> ✓ Pahal does not take any fees other than the three components specified in RBI guidelines, therefore is fully compliant.
Processing fee: max 1% of loan	<ul style="list-style-type: none"> ✓ Compliant - Charges 1% of loan amount plus service tax. ○ Processing fees on individual loan is 2% plus service tax.
Insurance commission: as per IRDA norms	<ul style="list-style-type: none"> ✓ Pahal has a tie-up with Kotak Mahindra Old Mutual Life Insurance Limited for a compulsory term credit-linked life insurance for its borrowers and their spouse. Details of the product are on Slide 14. Only the premium amount is collected from customers and passed on to insurance company and no commission is collected from clients.
Other: <ul style="list-style-type: none"> No penalty for prepayment & delayed payments No collateral & security deposit 	<ul style="list-style-type: none"> ✓ Pahal does not charge penalty on prepayment & delayed payment for group/individual loans. ✓ Group loans are extended without collateral. ○ Collateral security in the form of post dated cheques/mortgage of property is taken for securing individual loans.

Compliance on Guidelines pertaining to Clients

Transparency	Compliance by Pahal
<p>Standard form of loan agreement: preferably in vernacular language</p>	<ul style="list-style-type: none"> ✓ The loan agreement and sanction letter was approved by the board on March 18, 2013. Both the documents are in vernacular language. Sanction letter contains details of the amount sanctioned, loan tenure, interest rate, processing fee, insurance premium and all the terms and conditions. ✓ Loan agreement includes all rights and responsibilities of members as part of the loan contract. It is signed by all group members, and a copy of the loan agreement is given to each member. ✓ Terms and conditions are read aloud and explained by the FCO before clients sign ✓ A Demand Promissory Note forms part of loan agreement and given to each client at the time of disbursement mentioning the amount disbursed to them as well as to the group.
<p>Loan card: reflecting of (i) EIR (ii) terms & conditions (iii) record all transactions;(iv) all entries in vernacular</p>	<ul style="list-style-type: none"> ✓ Passbooks are given to all borrowers on the day of first repayment. The loan passbook contains the APR and terms and conditions of the loan. ❑ The EIR (including insurance premium) is not shown, but APR (including interest and processing fee), declining and monthly interest are shown in loan documents. ❑ Pahal does not give its clients a receipt for repayment. The signature of the FCO in the loan passbook against the repayment amount in the amortization schedule is considered as the acknowledgement for repayment. ❑ Repayment schedule is printed in English.
<p>Display of the EIR in its offices & website</p>	<ul style="list-style-type: none"> ❑ The rate of interest charged by Pahal is not displayed in the branches. The rate of interest displayed on the website has not been updated.
<p>Member education: professional inputs to members in the formation groups</p>	<ul style="list-style-type: none"> ✓ Clients are educated on group responsibilities, loan terms and conditions and Pahal's eligibility criteria during group formation meeting, CGT/GRT and also at the time of disbursement.

Compliance on Guidelines pertaining to Clients

Transparency

- ✓ Pahal through Loan agreement communicates to the clients that their personal information would be kept confidential.
- ✓ Loan terms and conditions are verbally communicated to the client during group formation meetings, CGT/GRT and also before loan disbursement.
- ✓ Pahal does not take any collateral from the clients for group loans.
- Individual loan is secured by collateral either in the form of post dated cheques or mortgage of property.
- Receipt is given for loan processing fees and insurance premium but not for repayment of instalments.
- ✓ Pahal does not charge any fee for non-credit products/services like training. It does not collect any charges other than interest, processing fee (including service tax) and insurance premium. It declares the interest rate on reducing balance basis and processing charges in loan card and on sanction letter.

...Compliance with regulations

Responsible Lending	Compliance by Pahal
<p>Location for transactions and overdue recovery</p> <ul style="list-style-type: none">○ all transactions at a central location○ staff are allowed to make recovery at the place of residence or work if borrower fails to appear at central place on 2 or more successive occasions	<ul style="list-style-type: none">✓ Loans are disbursed at the branch office in the presence of BM as well as the FCO.✓ Repayment is collected by the FCO in a center meeting.✓ Recovery is never made by visiting clients' house at odd hours or on inappropriate occasions – staff were well aware of this during branch discussions.□ However, In the event of default, field staff visits the house of the client for recovery. They are not aware that they can visit the house of the client only if the borrower fails to appear in center meeting on 2 or more successive occasions.

Compliance with guidelines pertaining to clients

Responsible lending

- ✓ Pahal ensures one loan per person at a time by using a de-dupe mechanism which is in-built in its system. During the data entry of the physical forms if the voter ID of an already existing client is entered in the system, a pop-up will flash across the screen informing the data entry operator of a potential duplicate and further data entry of the form will not be possible.
- ✓ Pahal does not give individual loans to borrowers who are members of JLG/SHG or vice-versa. A thorough repayment capacity analysis is done before lending to an individual borrower. The details of the individual borrower are subject to both the CIBIL and the Equifax checks. The de-duplication tool of Pahal's system identifies any duplicate records, using the voter ID as unique ID.
- ✓ Collection of shortfalls are not made good from employees.
- ✓ No cases were reported by customers of any kind of misbehaviour or violation of ethics. Although HR manual does not specify this, field staff could recall the training received on dealing with clients.
- ✓ All loans are disbursed in the respective branches in the presence of the BM and the FCO. All the members of a group have to be present in the branch for disbursement. The monitoring team of Pahal conducts surprise visits to the branches in order to monitor the disbursement process.
- Pahal does not believe in restructuring its loans. In extreme cases a cooling off period may be given to the client.
- ✓ Loan utilization check is performed usually at the time of first collection for all clients.
- The promoters of Pahal are in regular touch with the clients and actively seek their feedback and suggestions during their visits to the field. However there was no evidence of incorporating client feedback in to product design and processes.
- Pahal does not have a board approved policy for dealing with each stage of default. Pahal's field staff enforce the joint liability in case of default and visit the house of residence of the defaulted borrower. Pahal doesn't have a board approved debt restructuring product/program.

Compliance on Guidelines pertaining to Clients

Grievance Mechanism

- ✓ Pahal has four levels of escalation for client grievances. The contact numbers of the concerned personnel are pasted on the notice boards of the branches.
- ✓ FCOs educate the clients on the grievance redressal process during the CGT/GRT and also at the time of disbursement. The grievance number is printed on all the loan passbooks.
 - Customer grievance calls are handled either by monitoring officer or by Ms Daksha Shah, promoter director, but there is no dedicated person to handle customer calls.
- ✓ Pahal maintains the log of borrowers' complaints and directs them to the concerned staff/branch. Action taken on the complaints is discussed with the concerned branch and is updated in the register.
 - A complaint and feedback register is placed in all the branches of Pahal. Every group has to write down its suggestions in the register post disbursement on any aspect of Pahal's policies and processes.
- Pahal does not have a formal mechanism to track the complaints till they are resolved.
- Calls received from clients are not analysed with regard to number of calls received, types of issues, resolution status and action taken and no consolidated report is submitted to the board on grievance redressal.
- It was observed that only 61% clients could rightly point out the helpline number in the passbook, indicating that client awareness about the facility needs to be improved.

Compliance with guidelines pertaining to clients

Privacy of client data

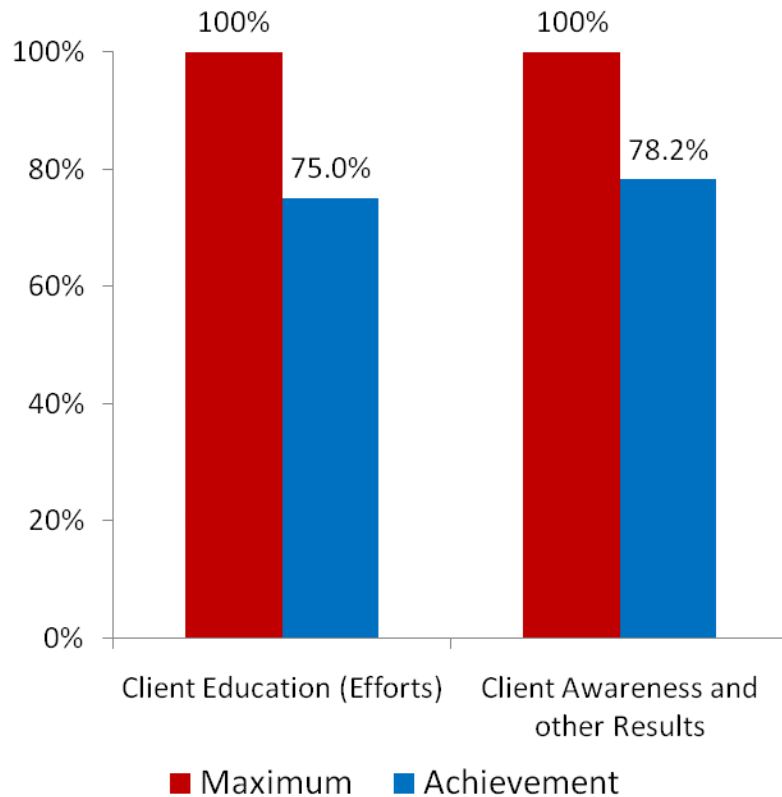
- ✓ Pahal has a centralized MIS department which ensures privacy and security of client data. All loan documents are couriered to the HO and stored safely.
- ✓ Adequate internal control has been built to access/enter the data at HO/branch level, using password protection and hierarchy-based data access levels.
- ✓ Information is shared with the High Mark and Equifax as per the RBI guidelines.
- ❑ Customers' written permission is not taken for sharing their personal data with the credit bureau (s).
- ❑ Around 56% clients interviewed were not aware about Pahal's privacy policy and such data sharing with Credit Bureau.

Monitoring & audit of compliance on guidelines pertaining to clients

- ✓ Monitoring team at HO visits each branch every quarter and makes surprise visits to center meetings, GRT and branches.
- ✓ Each branch is scored over 12 parameters covering various aspects of operations including, CGT, GRT, disbursement and collection process, book keeping and compliance on CoC and internal guidelines.
- ✓ Branch monitoring adequately covers aspects of multiple lending and over-indebtedness, client awareness, grievance redressal, client satisfaction and staff behavior.
- ✓ All the clients(100%) were regularly visited by BM or by supervisors other than BM. The promoters of Pahal are also actively involved in monitoring and interact with the clients often to understand their issues and needs.

Client education efforts & field results

Performance



Score obtained	Maximum
7.7%	10%

Levels of internalization

Parameter	Approval	Documentation	Dissemination	Observance
Client Education Efforts	Good	Moderate	Moderate	Good
Client Awareness	NA	NA	NA	Moderate

...Client education efforts & field results

Client Education

- ✓ Pahal educates the clients about loan products and loan terms and conditions at multiple stages (group formation meeting, CGT/GRT) to ensure that the borrowers make an informed decision before availing loans.
- ✓ Client education starts with the introductory meeting wherein potential clients are briefed about Pahal, its policies and products, lending methodology including group formation and joint liability, KYC document requirements, etc.
- ✓ Clients are educated on all terms and conditions including eligibility criteria, group liability, appraisal process and regulatory guidelines (including Credit bureau check, household income criteria and indebtedness criteria), product pricing, grievance redressal mechanism, during 2 days CGT.
- ✓ BM separately conducts a GRT during which each client's awareness level is tested and loans are approved and disbursed only after satisfactory awareness level of the group is established.
- ✓ The loan application of groups which score less than 60%, is rejected and a re-training is conducted.
- ✓ Client awareness is again checked at the time of disbursement in the branch office by the FCO. The loan agreement, which contains the rules and regulations of Pahal, loan terms and conditions, product features and customer grievance process is read out by the FCO during the CGT and also at the time of disbursement.
- ✓ The monitoring team of Pahal conducts surprise visits of branches on quarter basis to monitor the CGT, GRT and disbursement processes. The monitoring team checks and scores FCOs effort to educate clients about the products during the CGT, BMs effort on checking the awareness level of clients during the GRT and client awareness levels on the product features during the collection meetings respectively.
- ❑ Although most of the aspects of clients awareness are covered during group formation/CGT/GRT, specific training on CoC is not given to clients, thereby clients had very low understanding of their rights and responsibilities as per Code of Conduct and of privacy issues.

...Client education efforts & field results contd....

Client awareness and other results

- ✓ Awareness and recall of training received was high on most aspects. However clients could not recall training received on their rights and responsibilities as per code of conduct.
- ✓ A very high proportion of clients (>90%) were aware about the MFI details – its name and location; interest rate, loan amount, instalment amount and tenure etc.
- ✓ Awareness about grievance redressal system was high as 88% clients could point to the helpline number in loan passbook.
- ✓ 99% of the clients were aware about their responsibilities in a joint liability group. These had been communicated to the clients verbally during multiple interactions.
- ✓ Clients were happy with the product design and gave very good feedback about staff behaviour, citing zero instances of misbehaviour.
- ❑ A comparatively lower proportion of clients (49%) were aware about prepayment terms and conditions. Awareness on processing fees was also low as only 62% of the clients were aware about processing fees.
- ❑ Only 44% clients knew about privacy clause and sharing of their personal data with the credit bureau.
- ❑ Clients awareness on their rights and responsibilities was also low as only 48% clients could recall receiving training on CoC.
- Loan application has weekly/fortnightly/monthly repayment option but choice of repayment is monthly for all group loans by default. Although clients did not seem to had a problem with monthly repayments.

Annexes

Profile of the Board

Board member	Designation in the Board	Experience	Since
Pravin Kanubhai Laheri	Chairman cum independent Director	<ul style="list-style-type: none"> Former IAS officer retired as Chief Secretary, Government of Gujarat in 2005 Ex CMD of Sardar Sarovar Narmada Nigam Limited Currently, working as Director - Torrent Energy Limited, Ahmedabad Associated with many social development organisations 	02-05-2011
Daksha Niranjn Shah	Managing Director	<ul style="list-style-type: none"> One of the promoter directors of Pahal; a business graduate from IIM Ahmedabad and has over 20 years of experience in managing family business More than 11 years of experience as credit head with FWFB, having exposure to more than 80 microfinance institutions in India 	08-02-2011
Kartik Shailesh Mehta	Whole time Director	<ul style="list-style-type: none"> One of the promoter directors of Pahal; Kartik is a Chartered Accountant, a Cost Accountant and certified financial planner and has over 18 years of experience in banking and financial services industry in India. He was associated in developing retail microfinance business line at Development Credit Bank. At HDFC, he was involved in developing strategy for HDFC's initial expansion in to the state of Gujarat. During his stint with ICICI Bank he was associated with corporate agriculture finance and supply chain initiative of the bank. 	08/02/2011
Purvi Jayendra Bhavsar	Joint Managing Director	<ul style="list-style-type: none"> One of the promoter directors of Pahal; She has over 17 years of diverse experience in financial services and telecom sector. Worked in various functions including corporate finance, retail banking, channel management with Kotak Mahindra Bank, HDFC Bank and ICICI Bank. At ICICI Bank, she was heading the credit function for microfinance and also worked on BC model In her last stint with Vodafone group she was the Zonal head for Gujarat looking after the largest territory across India 	08/02/2011
Amal Dattkumar Dhru	Independent Director	<ul style="list-style-type: none"> Chartered accountant and management consultant (IIM-A Graduate) with over 30 years of practice. He has been a visiting faculty at IIM Ahmedabad and has also served as director of State Bank of Saurashtra and a public representative of SEBI for issue allotments. His professional experience ranges from designing accounting systems to investigations from financial structuring to mergers and acquisitions. 	16/02/2011

Shareholding Pattern

Sl. No.	Shareholder	Class of Equity	No. of Shares	Amount (Rs.)	% shareholding
1	Promoters, Family & Friends	Equity Shares	53,08,000	53,080,000	56.83%
2	SIDBI	Preference Shares	3,000,000	30,000,000	32.13%
3	Daksha Niranjn Shah	Equity Shares	366,666	3,666,660	3.93%
4	Kartik Shailesh Mehta	Equity Shares	366,666	3,666,680	3.93%
5	Purvi Jayendra Bhavsar	Equity Shares	299,666	2,966,660	3.18%
	TOTAL		9,338,000	93,380,000	100.00%

Methodology

- ▶ **Preliminary analysis of MFI's information, review of available reports and financial statements**
- ▶ **Visit to Head Office of MFI**
 - ❑ Discussions with the senior management (Operations, Human Resources, Internal Audit & Monitoring) to understand MFI's objectives, governance, market strategies, operations, products and services, integration of CoC in policies and procedures etc.
 - ❑ Collection and review of documents, manuals, Board minutes and associated documents to Code of Conduct.
- ▶ **Visit to branches – 4 branches in Gujarat**
 - ❑ Discussion with Branch Manager and all branch staff on different aspects of CoC, MFI's policies and procedures
 - ❑ Documentation review – client basic profile forms, loan application forms, internal audit reports, complaints register if any and CoC displays
- ▶ **Visit to centre meetings – FGD with minimum 2 groups per branch; due to mixed-group interaction, 8 FGDs were conducted with 82 clients from 21 groups**
 - ❑ Assess relationship between MFI staff and clients
 - ❑ Check for implementation of client protection principles
 - ❑ Spot check of passbooks, receipts, repayment cards, maintenance of documents
 - ❑ Feedback on products – suitability to client needs, application of terms & conditions
- ▶ **Data Analysis and Report writing**
- ▶ **Internal Review at M-CRIL**
- ▶ **Report draft sent to Pahal Financial Services Private Limited**

Sampling Plan

Sr. No	Branch	Region	Loan Cycle				Borrowers	Total Centres
			L1	L2	*L3	*L4		
1	Dehgam	Gujarat	20	-	-	-	20	2
2	Ahmedabad II	Gujarat	3	20	-	-	23	2
3	Mehsana	Gujarat	12	8	-	-	20	2
4	Kalol	Gujarat	4	8	1	6	19	2
Grand total							82	8

*Loans appearing in loan cycle 3 and 4 for Kalol branch pertains to the portfolio acquired from VCD.

Assessment tool: weight, scores and performance

Sections	No. of Indicators	Max Score	Weights	Performance
Integrity, Governance and HR Strategy	35	175	30%	22.7%
Integrating Social Values and Compliance at Institutional level	9	45	10%	8.3%
Governance	7	35	10%	5.7%
Human Resources Strategy	19	95	10%	8.7%
Compliance with regulations pertaining to clients	102	510	60%	49.0%
Client Origination and targeting	11	55	9%	6.2%
Loan Appraisal Process	7	35	9%	8.0%
Loan product features and pricing	24	120	10%	9.6%
Transparency	25	125	10%	7.7%
Responsible lending	19	95	9%	6.5%
Grievance mechanism	10	50	9%	8.0%
Privacy of client information	6	30	4%	2.9%
Client education and financial literacy	27	135	10%	7.7%
Client Education	4	20	3%	2.3%
Client Awareness	25	125	7%	5.5%
Overall	164	820	100%	79.4%

Abbreviations

ABM	Assistant Branch Manager	HR	Human Resources
APR	Annualized Percentage Rate	ICICI	Industrial Credit and Investment Corporation of India
ADDO	Approval Documentation Dissemination Observation	ICAI	Institute of Chartered Accountants of India
AM	Area Manager	IIM	Indian Institute of Management
BC	Banking Correspondent	JLG	Joint Liability Group
BM	Branch Manager	KYC	Know Your Customer
FCO	Field Credit Officer	MIS	Management Information System
MD	Managing Director	MD	Managing Director
CoC/		MFI	Micro Finance Institution
U-CoC	Code of Conduct/ Unified Code of Conduct	M-CRIL	Micro-Credit Ratings International Ltd
CA	Chartered Accountant	MIX	Microfinance Information eXchange
CB	Credit Bureau	MFIN	Microfinance Institutions Network
CDS	Collection Demand Sheet	NBFC	Non Banking Finance Company
CGT	Compulsory Group Test	NGO	Non-Governmental Organisation
EIR	Effective Interest Rate	OCPS	Optionally Convertible Preference Shares
EMI	Equated Monthly Installment	OSS	Operational Self Sufficiency
FPC	Fair Practices Code	PAR	Portfolio at Risk
FIR	First Information Report	Pahal	Pahal Financial Services Private Limited
FWWB	Friends of Women's World Banking	RBI	Reserve Bank of India
GRT	Group Recognition Test	SIDBI	Small Industries Development Bank of India
HO	Head Office	SEBI	Securities and Exchange Board of India
HHI	Household Income	VCD	Vikas Center for Development