

Arohan Financial Services Private Limited

Code of Conduct Assessment Report

September 29, 2016



ICRA Management Consulting Services Limited

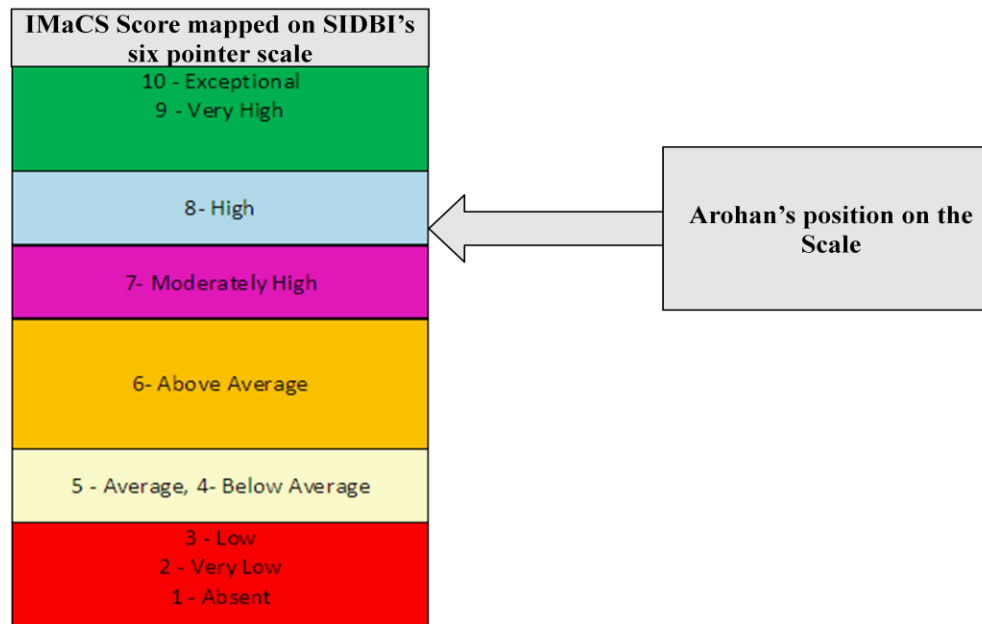
Assessment of Compliance with Code of Conduct Framework

OVERALL SCORE: 8

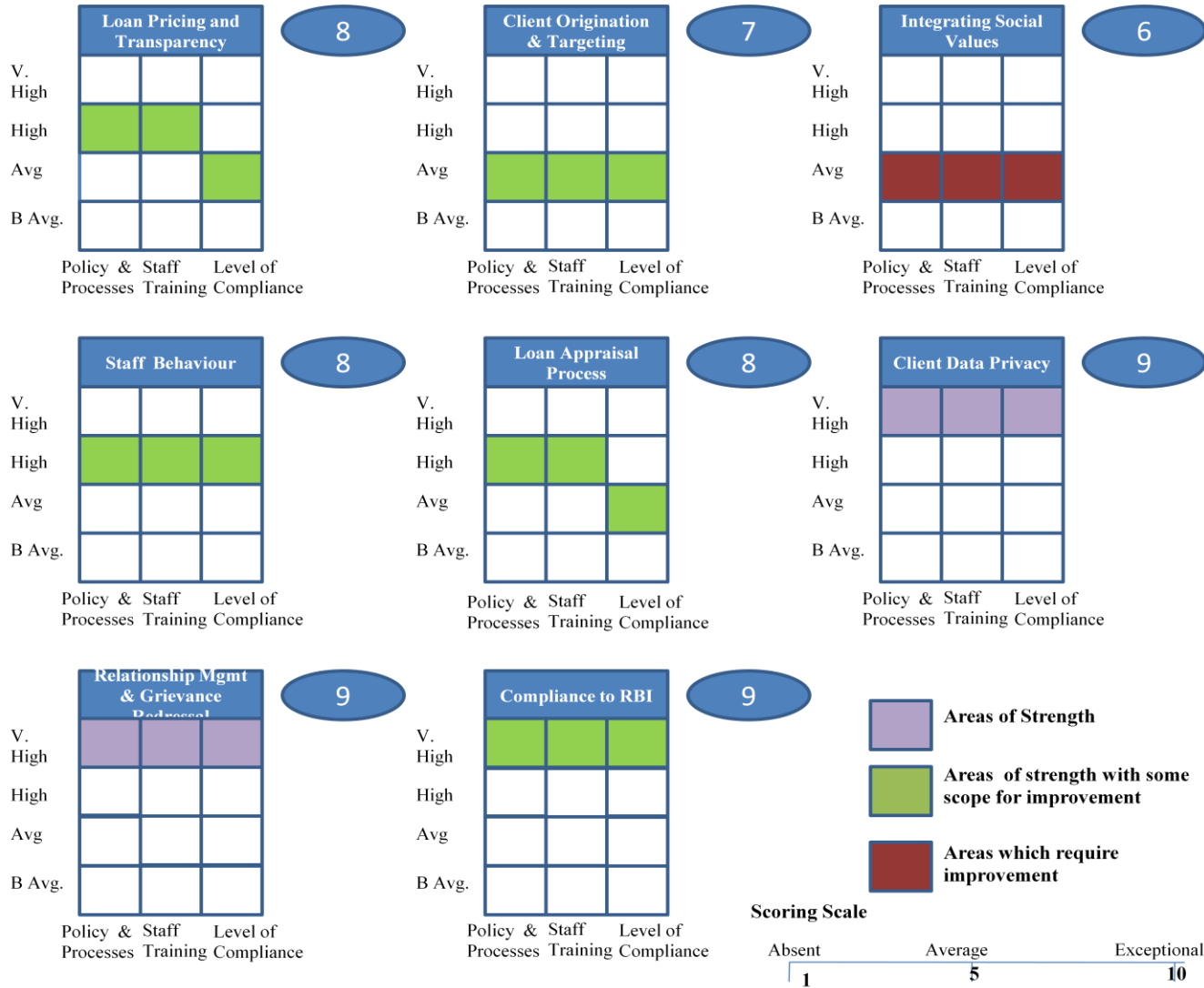
DEFINITION: HIGH LEVEL OF ADHERENCE

Arohan Financial Services Private Limited has satisfactorily articulated and documented detailed processes and policies adhering to several prescribed best practices for the MFI sector. The company has been successful in disseminating and ensuring compliance to its documented processes and policies at the ground level. There also remains a scope of improving certain policy areas related to implementing quantitative or score based poverty assessment framework, Incentive structure, Policy on penalties, and social performance management plan.

Mapping the IMaCS Score on Code of Conduct Assessment to SIDBI's Standardised Scale



Parameter-wise Code of Conduct Score



Company Background

Arohan Financial Services Pvt. Ltd. (Arohan) is a microfinance institution (MFI) set up in January 2006 as an NBFC. The entity started its operations in April 2006 in Kolkata, West Bengal. Since its inception, Arohan has raised capital from social investors (institutional and individuals). Till CY2009, Arohan's focus was to provide financial services to the urban and semi-urban poor. Since the beginning of CY2010, Arohan started lending to borrowers in rural areas as well. Arohan offers credit to economically backward women and men by offering varied products to suit their requirements. Its key focus is the group loan, for which it replicates the Grameen Bank model of lending. The company currently has operations in West Bengal, Bihar, Jharkhand, Odisha and Assam.

Executive Summary

- **Client Origination and Targeting**
 - Detailed manuals with adequate focus on area and borrower selection.
 - Staff incentives have 86% weightage for loan disbursements and 14% for compliance (branch audit grade).
- **Loan Pricing and Transparency**
 - Single, effective interest rate communicated along with insurance and processing fee.
 - No penalty for pre-closure of loan and no collateral or margin money taken.
- **Loan Appraisal Process**
 - Two KYC documents collected; however Credit Bureau (CB) checks reflect only 50% accounts seeded with both Voter ID (VID) and Aadhaar (UID).
 - Cash flow analysis appeared to be generic for the group with limited focus on the actual debt repayment capacity of the borrower.
- **Staff Behaviour**
 - Courteous behaviour of staff with clients.
 - Attrition rate of 29% during FY2016 which is comparable to industry benchmarks.
- **Privacy of Client Information**
 - MIS access based on separate logins, separate for each branch limiting access to borrower data.
 - Borrower data shared only with CBs.
- **Integrating Social Values into Operations**
 - Arohan tracks the seeding of financial products (other than loan eg. insurance).
 - Limited credit plus activities currently; however the company expects to improve the frequency and coverage of its social programmes.
- **Relationship Management and Grievance Redressal Mechanism**
 - Toll free number provided to all borrowers for registering complaints.
 - Grievance redressal mechanism has four levels of escalation along with timelines at each level.

- **Compliance Status of MFI vis-a-vis RBI Guidelines**

- Meets the guidelines on income eligibility, loan size, loan tenure, pricing cap, collateral, penalties and overall indebtedness.
- Scope for improvement in compliance with RBI guidelines on repayment frequency.

Areas of Strengths at Arohan

- **Well-defined Processes and Policies:**

- Arohan has captured its key processes and policies to a reasonable extent in its operations manual. It has also ensured fairly uniform dissemination and implementation of the processes and policies at the ground level. Although the operations manual is in English, a separate document for field staff laying out the operational processes in the vernacular language is maintained in each branch.
- Arohan has a well-defined area selection process and guidelines for borrower group formation. The company's lending decision takes into account a self-declaration from the borrowers that they have not borrowed from more than two MFIs and credit history records, with mandatory credit bureau check for all borrowers.
- The MFI conducts a two day Compulsory Group Training (CGT) followed by a Group Recognition Test (GRT) for new groups. The CGT process is documented well in the manual and covers all key aspects of lending including the joint liability concept, responsibilities and duties of group member, key loan terms and charges, product schemes and insurance details. All borrowers that we met with, reiterated that they have received multi-point communication from the MFI on key loans terms. The borrowers however could not recall the interest rates and other charges on the loans.
- The company has a loan restructuring policy for borrowers to address issues of genuine distress.

- **Strong Internal Audit:** The MFI has put in place a strong internal audit process with quarterly checks on key process parameters such as CGT, loan utilization checks (on sample basis), attendance, house verification, passbook updation, key centre registers and ledgers
- **Adequate Training Mechanism:** The company has a structured induction training programme for new joiners and also conducts periodic trainings for existing employees to keep them updated about policy changes. We observed a reasonably fair degree of understanding and compliance with the prescribed policies, procedures and values of the company by the staff at the ground level.
- **Structured Grievance Redressal Mechanism:** The company has put in place a fairly structured grievance redressal mechanism with a toll free number (operating during office hours only), along with the process, turnaround time and escalation matrix to address a grievance.
- **Strong Focus on Client Data Privacy:** The company gives utmost importance to maintaining privacy of client data and has a specific policy for that. Circumstances under which client data can be shared are also clearly mentioned. Additionally, Arohan has put in place checks to prevent unauthorized physical access to their offices.
- **Transparent Operations:** We observed that the MFI communicates a single, effective declining interest rate to its borrowers across all its written and oral communications, including its operations manuals, CGTs and borrower passbooks.

Areas that Require Improvement at Arohan

- **Quantitative Poverty Assessment Framework:** The MFI is yet to put in place a score based, quantitative poverty assessment framework that can enable it to choose households that meet its criteria of income threshold, occupation, living conditions, cattle ownership etc. Such a model would reduce subjectivity in the customer selection process.
- **Operational Lapses:** Even as the MFI has initiated all round measures to strengthen its internal processes, there remain few areas with scope for further improvement and strengthening. Along with strengthening its policies and processes, the MFI needs to encourage its branch employees to refer to its operations manuals regularly. At few areas in which operational lapses were observed:
 - EMI collected despite death of the spouse and even insurance claims submitted for a few (details given below) :

Branch name	Borrower Name	Reference number	Date of Death	Last EMI Collected
Kankarbagh	Manju Devi	1051/623143/3	January 14,2016	March 2016
Phulwarisharif	Lalita Devi	1051/501121/3	January 2016	August 2016
	Dharmshila Devi	Centre- 25563	July 2016	August 2016

The management has taken note of the same and directed branches to this practice.

- Discrepancies found between attendance marked in loan card and register. For the following borrowers the attendance was marked in the loan card but not in register:

Branch	Date	Borrower Name	Borrower Id
Ratu	July 4, 2016	Basanti Devi	1051/1276232/1
Namkum	May 5, 2016	Aarti Kumari	1051/553130/1
		Maalti Devi	1051/1423091/1
		Kavita Kumari	1051/1423079/1
		Sunita Tikrey	1051/553229/1
		Munni Devi	1051/1267796/1

- The centre leader (Daulti Devi) in centre-25563 of Phulwarisharif branch has not been changed in last 5 years. Arohan has now mandated change of centre meeting place every year with the centre leader being the owner of the house. This is expected to result in auto rotation of centre leaders.
- Incidences of non-receipt of insurance papers also came to light in some of the branches. Although the borrowers raised this issue with the CSRs (customer service representatives) and BHs (branch heads), a complaint was not raised through the centrally designated toll free number. Hence, Arohan's dissemination of the grievance escalation matrix has scope for improvement.

- **Scope for Improvement in Communication:**
 - Arohan has been moving to the centre responsibility in addition to group liability. However, there were instances of new groups being added in a centre earlier without the consent of existing groups as there was no joint liability. Hence, the borrowers in a few locations expressed reservations in moving to a centre responsibility mechanism.
 - Loans of Rs. 25,000 and above are individual in nature with no group guarantee mechanism. However, the borrowers have been communicated that these loans are also in a group mechanism and members are jointly liable to pay. Additionally, as per the management, the centre responsibility is only from a moral standpoint and the company does not expect the centre members to pay on behalf of the group member. However, the field staff and borrowers believe that the centre is liable to pay for any defaulting borrower. Hence, the communication to the borrowers could be improved.
- **Disbursement Linked Staff Incentives:** Incentive structure for the field staff comprises disbursement as a parameter, which could lead to aggressive underwriting. Additionally, incentive is also linked to branch audit grade which takes into account overdues. Hence, there is scope for the CSRs undertaking coercive methods of recovery.
- **Credit appraisal:**
 - The credit appraisal mechanism at Arohan could be strengthened further. The MFI collects information related to borrower household income and expenses. However, the cash flow analysis appeared to be generic for the applicants with limited focus on actual debt repayment capability of an individual borrower.
 - Although CB reports are generated centrally, they are not integrated with MIS. Also, the lending decision based on CB report is taken at the branch. Integration of reports with MIS would result in improved operational control and restrict overleveraging of borrowers. With mobile technology, Arohan has initiated CB checks on a real time and linking the same with MIS.
- **Compliance with RBI Guidelines:** Arohan could look to strengthen its compliance with RBI guidelines in terms of meeting the repayment frequency and loan usage criteria. For the accounts where LUC is carried out (20-25% of the cases for non plus loans), Arohan looks at the amount of funds used in non stated purpose, and insists on pre closure if diversion is more than 50% of the amount disbursed by Arohan.
- **Inadequate CSR Activities:** Arohan has undertaken computer literacy projects, skill building programmes and flood relief operations, the number of clients covered through the same are around 3000, which is less than 1% of the client base. Hence Arohan's credit plus activities are considerably lower when compared with its peer MFIs and has scope of improvement.

Key Operational Parameters

Key Financial Parameters	as on March 31, 2015	as on March 31, 2016
No. of Registered members	320848	553785
No. of Groups	61816	94991
Total Number of Branches	104	180
No of States	4	5
No. of Active Clients	320848	553785
No of Active Clients per Branch	3085	3077
Gross Loan Portfolio (Rs. crore)-Own	364.54	586.02
Gross Loan Portfolio (Rs. Crore)-Managed	18.78	81.54
Gross Loan Portfolio (Rs. crore)-Total	383.32	667.56
Growth in Total Portfolio size	19%	74%
Portfolio per Active Client	11947	12054
Increase in Portfolio per Active client	4%	1%
Portfolio per Branch	3.69	3.71

Credit Product Offerings

Product Name	Ticket Size (Rs.)	Purpose	Interest Rate Charged	Tenure	Processing Fees	Group Guarantee/ Individual Loan
Saral	10,000 to 20,000 (in multiples of 5,000)	Income Generation	24.99%	12 Months	1% + service tax (15%)	Group
Saral Plus	25,000 to 50,000 (in multiples of 5,000)			18 / 24 Months		Individual
Bazar	10,000 to 20,000 (in multiples of 5,000)			12 Months		Group
Bazar Plus	25,000 to 50,000			18 / 24 Months		Individual
Premium	50,000 to 2,00,000 (in multiples of 5,000)		26.99%	12 / 24 Months	3% (including insurance fee & service tax)	Individual

1. Client Origination and Targeting: Policy Articulation and Documentation

Policies	Best Practices		Arohans's Policies and Observations
Area Selection	Detailed process documented in the manual	High	<ul style="list-style-type: none"> Well documented coverage of village selection criteria and methodology in the policy manual A new area is selected by the area manager in consultation with the state head and HO
	Explicit policy of avoiding over-indebtedness in clients.	High	<ul style="list-style-type: none"> Customer details are verified with an RBI approved credit bureau and loans are sanctioned only to eligible borrowers Policy mandates that a member shouldn't have taken loan from more than one MFI. As per staff feedback, the selection process also ensures that the total borrowing does not exceed Rs. 60,000.
Borrower Selection	Guidelines for members to form groups well-articulated and groups to be formed by borrowers themselves	High	Prescribed norms in place for selection of members to form groups including income, age, and KYC.
	CGT process well documented with a strong focus on educating clients on the concept of joint liability	High	Detailed process to carry out CGT and GRT given in the manuals. The discussions for each training session are also documented. CGT for plus loans are conducted individually and not in a group.
	Quantitative or score-based poverty assessment framework defined	Moderate	The MFI collects information about the household income during group formation and the customers are required to fill customer information form with self declaration of their income and expenses. The MFI lends only to customers that fall within the income guideline specified by RBI. Arohan has developed a model to analyse the borrower data using the progress out of poverty index (PPI). It expects to be roll out the model across all the branches in the near future.
Policy on outsourced agents	Explicit policy of not using outsourced agents	High	The collections are made by the MFI's staff only. No instance of outsourced agents being used came to IMACS's notice.
	Strong internal audits and checks	High	Quarterly audits are carried out by an independent internal audit team. A detailed audit checklist with focus on operational policies and risk indicators is used.
	Annual rotation of centre leaders	High	The field staff mentioned the need to rotate centre leaders

Policies	Best Practices	Arohans's Policies and Observations	
			every year. The leaders were rotated annually in most of the centres visited by IMaCs. Further, Arohan has mandated rotation of centre meeting place annually and the owner of the house where centre meets becomes the default centre leader.
Policy on incentive structure	Incentive structure not linked to disbursements and recovery.	Low	The company's policy incentivises the staff members for number of loans disbursed during a month (with a maximum payout of Rs. 3000). Further, the incentive structure is also dependent upon audit scores, which takes into account the overdue position at the branch.
	Incentive structure to be linked to borrower retention and process compliance	Moderate	Incentive structure for field staff gives 86% weight to loan disbursements 14% to branch audit grade.

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none"> • New recruits undergo a class room training at regional office for three days, followed by five days on the job training at field with BH/CSR, and again three days final class room training. A test is conducted at the regional office before the final selection. • Regular training sessions are held by the area manager or regional trainer. Refresher training is also provided to existing employees as per need and when a request is raised by the area manager. • Employees were largely aware and updated about the changes in processes and policies. • Each branch has a hard copy of the operations manual but in a non-vernacular language. However, a working document with processes relevant to the field staff is available in the vernacular as well, in each branch. The field staff largely followed the policies. • CSRs were found to be reasonably articulate with the MFI's policies related to origination, targeting, group formation, conducting CGTs and GRTs. Most of the staff members have been provided training and instructions to follow the policies prescribed in the manuals. 	<ul style="list-style-type: none"> • In branches in Jharkhand and Bihar, although induction training was conducted for all staff members, refresher trainings were not conducted regularly. • As per borrower feedback, CGT for new borrowers (joining in an existing group) is for 60 minutes 30 minutes each on two days). However for repeat borrowers, the training is for one day only. GRT is conducted by the branch head and the borrowers are counselled individually. • Members further confirmed that they were apprised of product features, rates and fees, repayment schedule and JLG concept. No discrepancy in the information provided in the CGT vis-a-vis the actual transactions was noticed. • Collection is done at the centre meetings whereas the disbursement is mandatorily done at the branch which provides a direct connect to the borrowers with the company's branch heads. • Most centres reported that the centre leaders were rotated periodically. In some cases, the same leader was appointed for subsequent years voluntarily by the members. • The company has stressed on the need to maintain strong portfolio quality (with minimum over dues) which could lead to coercive methods of recovery by the CSRs. • Arohan is in the process of capturing borrower wise PPI data in the system to better analyse and understand the improvement in borrower's life on account of Arohan's loans.

2. Loan Pricing and Transparency : Policy Articulation and Documentation

Policies	Best Practices	Arohans's Policies and Observations	
Board's policy and involvement in pricing	Loan pricing policy specified and fixed by board	High	The pricing decisions are approved by the Board.
	ROE and margin caps specified	High	Current regulations play an important role while setting the loan pricing.
	Documentation of CGT process with CGT manuals printed in vernacular	High	The CGT and GRT process is documented. Although the operations manual at the branches is in English, the branches maintain a separate document covering salient operational features in the vernacular language.
Client coaching and communication	Structured training program with coverage of JLG, effective interest rates and other terms	High	The process of conducting CGT and GRT is fairly well documented and includes sessions on joint liability, effective interest rates and other terms to the group members.
	Refresher training programs and regular coaching of clients	Moderate	The operations manual encourages the CSR to hold discussions with borrowers on key product features and regulations. However, the same is not being practiced, with the focus of the centre meetings limited to collections. Going forward, training modules would be displayed on the mobile devices used for collection in the field and hence refresher trainings are expected to improve.
	Multi-point communication of effective interest rates, processing fees, and pre-payment terms to clients	High	Loan terms and the concept of group guarantee are conveyed to the clients at the time of group formation, during CGT and are also printed on the loan cards.
Transparency in disclosure of loan terms	All terms and conditions mentioned in the pass books. Pass-books updated on a regular basis	High	All terms and conditions were found in the pass-books. Collections are updated in the pass-books on a regular basis.
	Clear communication of effective interest rates without any mention of flat rates	High	Arohan quotes a single, effective rate of interest to its clients.
	Pass-books contain information in vernacular language	High	Most of the information in the loan pass-books is in the vernacular. However, the insurance information, dates and numbers are in English.
	No collateral or margin money accepted	High	No collateral security or margin money is taken from the borrowers for the micro finance loan.

Policies	Best Practices	Arohans's Policies and Observations	
	No hidden costs related to distribution of third party financial products	High	Fees and charges related to third party products (TPP) are communicated upfront.
	No prepayment penalty	High	The company gives an option to borrowers for pre-closure of loan.

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none"> Most staff members are adequately trained and understand the importance of transparent communication with respect to interest rates and other fees. Customers acknowledge the multi-point disclosure of loan terms by the MFI staff at the time of group formation, CGT and GRT. TPPs are sold at least one day after the loan disbursement. This is to delink loan disbursements/ sanction with TPP and hence instil confidence among borrowers to reject a TPP. CSRs were also aware of the importance of selling only products useful to the borrowers. Arohan undertakes outbound calls to identify instances of force selling – of both micro finance loans or third party products. 	<ul style="list-style-type: none"> Group guarantees are not applicable on plus loans. However, the communication to borrowers was not adequate as evidenced by the enforcement of group guarantee mechanism for plus customers, in some centres. Arohan is currently moving towards a centre responsibility concept in addition to group liability. As per management, although the centre members are not financially liable for other group members, the understanding among members is of centre being financial liability. In some centres, members consent was not taken before shifting to centre responsibility. CSRs follow most centre meeting rules as prescribed in the manuals. However, CSRs do not undertake discussions on product, policies and regulations. As most borrowers could not recollect the interest rates, grievance redressal mechanism and insurance norms, regular discussions would be helpful. All loan cards and pass-books contained information in vernacular language and were up to date. The amortization schedule of the loan is also pre-printed. Effective rate of interest, processing fee are mentioned in the loan pass book and loan card.

3. Loan Appraisal Process: Policy Articulation and Documentation

Policies	Best Practices		Arohans's Policies and Observations
Loan Appraisal Process	Detailed lending process in manuals	High	Complete coverage of the lending process in the operations manual
	KYC policy	High	Minimum two KYCs are required to be taken from each borrower with VID being mandatory. UID is preferred as a second KYC document, however is linked to state level penetration. There is adequate focus on adhering to KYC policy and mandatory guideline for borrower's identity card before a lending decision.
	Formal credit appraisal framework with credit scoring or Income to Installment Ratio	Moderate	Staff members assess the borrower's income and other liabilities before recommending a loan. However, the cash flow analysis appeared to be generic for the group, without a focus on the individual borrower.
Checks on over-indebtedness of clients	Declaration on total borrowings of the member's household in the application form	High	Loan application form captures the details of other borrowings. Total indebtedness is also checked from the CB.
	CB checks	High	Compulsory CB checks for all new and repeat loan applications, routed centrally through the head office.
	Mandatory house visits and reference checks of borrowers	High	Policy covers a detailed housing survey verification process and mandatory house visit before the group formation.
Credit Risk Management	Process to ensure adequate attendance in client meetings	High	Policy lays down the importance of attendance during centre meetings to maintain discipline and low over dues. Members were informed that subsequent loans would not be sanctioned in case of attendance lower than 80-85%.
	Strong MIS to track customer credit history with the company, IIRs, attendance, loan purpose etc. Factors considered for future loan eligibility	High	The MIS is robust and captures borrower level data. Borrower's basic data (name, address, KYC.) along with loan purpose, repayments, outstanding amount, and loan cycle can be generated from the MIS.
	Centralised credit centres for conducting credit checks in addition to field checks	High	CB checks are carried out centrally, and field officers also discuss repayment track record with other borrowers in the locality.
Loan Utilization Checks	Loan utilisation declaration in the application form	High	Sufficient coverage in the loan form.

Policies	Best Practices	Arohans's Policies and Observations	
	Policy on 100% LUC checks and implications of non compliance specified	Moderate	Policy mandates 100% LUC for plus loans and at least one borrower per JLG which generally comprises 4-5 members.
	Strong audits on LUCs	High	The audit department interacts with borrowers and checks for LUC compliance on a sample basis.

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none"> CSRs understand the company's loan appraisal process adequately. Any change in the process is regularly updated in manuals/circulars and disseminated through the BHs/ DMs. The staff takes VID (mandatory) and one more KYC (Aadhaar/ration card/electricity bill) for each of its borrowers. The audit team conducts regular audits including a complete check of the loan appraisal process, centre meetings, attendance and LUCs and adherence to the operations manual. 	<ul style="list-style-type: none"> CB checks are done centrally from the regional office and the reports are shared with the branches where the credit decisions are taken. The CB report is currently not integrated with the MIS, and hence could result in operational lapses during loan sanction. Documentation related to filling of application form, KYC, CGTs and GRTs were complied with. We observed uniformity in loan processes across the centres visited. Clients confirmed that the BHs and CSRs visited the members houses both before and post disbursement (including for LUC). If the LUC is not satisfactory, the borrowers are closely tracked and no further loan is extended in future to the borrower. Discrepancies were noticed in the attendance recorded in the collection sheet and the attendance register. The registers were not maintained properly at a few centres, with entries for a few months missing completely. Based on data submitted to CBs for incremental disbursements, Aadhaar penetration level was at ~50% for Arohan (~80% if adjusted for North East). However for overall borrower base, the Aadhaar penetration was at 5%, indicating a scope of improvement.

4. Staff Behaviour: Policy Articulation and Documentation

Policies	Best Practices	Arohans's Policies and Observations	
Focus on client as reflected in company's values and policies	Mission and Vision reflects the company's social mission	High	Mission: "Arohan's mission is to empower the under-served by offering a range of financial services, in a manner sustainable for all stakeholders" Vision: "Arohan's vision is to be among the top 3 Financial Inclusion players in the East, North East and Central Low Income States, serving over 10 lakh customers across 10 states, and being in the top 10 preferred places to work"
Staff communication to clients	Standard code of behaviour towards the clients captured in the manuals	High	Staff members must abide by the company's code of conduct including client handling. Detailed code of conduct document is maintained at the branches.
	Clear penalties prescribed for breach of behaviour specified in the manuals	High	Specific matrix defines the penalties depending on the deviation/ breach of rules. Staff members indicated that breach of code could result in even termination of employment.
	Keeping staff attrition rate under check to ensure better and continuous compliance with guidelines	Moderate	Attrition rate in the company was reported at 29% during FY2016, which is comparable with industry benchmarks.
Policies for partial collection centres	Recovery policy for partial collection centres is client friendly	High	The MFI has a joint liability approach for loans upto Rs. 25,000, at the group level. If one member defaults or is unable to pay, others in the group are required to contribute on her behalf. In case of a delay or default, the staff informs the BH who counsels the group to pay. Arohan is moving towards the centre responsibility concept in addition to group liability.
	Rules and timings for visit to clients house for recovery are specified and captured in manuals	High	CSRs are advised to interact with clients during centre meetings and restrict visiting a member's house or place of work only in certain exceptional cases (overdue clients).
	Restructuring policy for genuinely distressed borrowers	High	Arohan's restructuring policy prescribes relief for borrowers in distress situations; however we did not come across any borrower requiring loan restructuring.

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none">• The CSR training programme has adequate focus on compliance with the code of conduct.• In case of non-payment by a member or group, the staff informs the branch head who along with area manager further discusses with and counsels the members.• CSR incentives are not directly linked to recovery of arrears. However, the branch audit grade has weightage for overdue accounts which impacts the payouts for the CSR.	<ul style="list-style-type: none">• Most CSRs were observed to be courteous and polite during all centre meetings, greeted the client members and explained all required details to the customers.• Most customers acknowledged that CSRs are courteous and polite in their interactions and they are comfortable approaching them for loans, queries and/or difficulties.• There were no complaints of visits at odd times to client residences.• However, in a couple of branches instances of enforcing centre guarantees came to our notice for plus loans (which are individual in nature).

5. Privacy of Client Data: Policy Articulation, Documentation, Dissemination and Observed Compliance

Best Practices	Arohan's Policies and Observations	
Policy on maintaining client data privacy	High	Arohan's fair practice code restricts sharing client data.
Policy prescribing conditions for sharing client data	High	Information can be shared under the following three circumstances: <ul style="list-style-type: none"> • If it as a customary practice among all financial institutions (such as sharing data with CB), • Disclosure required by law, • The stakeholder has agreed to and/or permits disclosure of the information.
Penalties for breach of client data privacy specified	High	Penalties specified for various level of breach or violation of policy. CSRs further indicated that breach of privacy could lead to disciplinary action and even termination of employment.
Adequate storage of client documents with limited access	High	Arohan maintains the physical records of client data in its regional offices. These documents are stored with care which prevents unauthorized access. The company shares borrower details only with CBs.
MIS rights limited and access rights defined	High	MIS access rights are login based, limited and defined based on the role/position of employees

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none"> • The staff were aware that client data should not be shared • Client documents are maintained at the RO, thus restricting access to field staff 	<ul style="list-style-type: none"> • No instance of breach of confidential data of the clients found during our branch visits

6. Integrating Social Values into Operations: Policy Articulation, Documentation, Dissemination and Observed Compliance

Best Practices	Policies and Observations	
Social Vision, Mission and Core Values	High	The company's mission and vision implicitly reflect the entity's focus on empowering the under-served through access to a range of financial services
Corporate Social Responsibility Program	Low	Arohan has undertaken a computer literacy projects and flood relief operations in specific pockets of its operations. Skill building programmes are also being carried out. However the client coverage remain low at less than 1% of Arohan's total borrower base.
Social performance targets monitoring and reporting	High	Monthly report is submitted to the Board highlighting seeding of non-microfinance loans.

Level of Dissemination	Level of Observed Compliance
<ul style="list-style-type: none"> Staff members were not fully aware of the company's vision and mission. However, the staff members were aware of the company's focus on improving non-loan product penetration among clients. 	<ul style="list-style-type: none"> During our centre visits, we found little communication on the social mission and objectives to the borrowers. No instance of force selling of third party products came to light. Arohan aims to improve the frequency and coverage of the social programmes.

7. Grievance Redressal Mechanism and Client Relationship Management : Policy Articulation and Documentation

Best Practices	Arohan's Policies and Observations	
Grievance Redressal Policy and Process – Involvement of board and top management	High	The MFI has put in place a Grievance management and redressal mechanism to resolve any issue that the borrower faces. It also presents a summary of complaints received and resolution offered in its board meetings as well.
Multi-point Grievance Redressal Mechanism Toll free , 24-hour phone number for registering grievances Phone numbers of branch head and centre managers noted on centre registers Complaint boxes at branches Clients visit branches during the loan tenure	High	A toll free number is provided to clients and dedicated for client complaints and grievance redressal. The number is operational during office hours. Discussions indicate that complaints are generally resolved within three days by the BH. The phone numbers of BH and CSR are mentioned on the register and borrowers are aware of the same. Clients visit the branch office for disbursements and hence, have access to branches.
Specific timeframe for complaints resolution and responsibilities prescribed and documented	High	The grievance redressal mechanism has four levels of escalation along with timelines at each level.
Penalty action specified for certain breaches and customer complaints	High	Policy defines penalties for various levels of breaches/ deviations. Complaints are also tracked by the internal audit team and the board. Deviations could lead to disciplinary and / or other actions including termination of employment.
Level of Dissemination	Level of Observed Compliance	
<ul style="list-style-type: none"> The staff at the centres visited were aware of the grievance redressal mechanism and understand that any complaint/query received has to be addressed at the earliest possible Officers were found to be responsive to the requirements of client members. During our visit, we found CSRs to be actively engaged in resolving queries from borrower and discussing with the BH as needed. Regular audits and surprise visits are made to ensure that staff officers adhere to the processes and systems 	<ul style="list-style-type: none"> Most members (>90%) at the branches visited were found to be comfortable with approaching any staff member of the MFI for query resolution. Most borrowers were aware of the CSR or BH's number and the toll free number on the loan card. However, the borrowers generally do not escalate issues through toll free number and choose to follow-up with only the CSR/ BHs. The borrowers could be encouraged to raise complaints through the central toll free number. 	

8. Compliance with RBI Guidelines for MFIs

Conditions	RBI Policy Announcement	Arohan's Policy	Compliance
Income limits for eligible borrowers	Rural: Rs 100,000 Non Rural: Rs 1,60,000	Rural: Rs 1,00,000 Non Rural: Rs 1,60,000	The company assesses client income, conducts physical checks of the residences and also takes self-declaration of income from the borrowers.
Loan Size (maximum)	First Cycle: Rs. 60,000 Later: Rs. 100,000	Currently the maximum first cycle loan size is Rs. 20,000 and overall maximum loan size is Rs. 50,000.	Satisfactory. All client groups and individuals were found to be within the limits. Higher loans are provided under individual loans.
Borrower Indebtedness	Limited to Rs 1,00,000	Arohan captures the total loans availed by a borrower in the customer information form. The company also checks with the CB before any loan disbursement.	Client credit history is verified with the CB and also with other informal sources.
Tenure	24 months for amounts in excess of Rs 30,000	For loan products of more than Rs 30,000, the minimum specified loan tenure is 24 months	Compliant.
Loan Used criterion	Minimum 50% of MFI portfolio for income generation	If the usage of loan proceeds in non stated purpose is lower than 50%, the CSRs have to highlight the same.	LUC needs to be carried out on a sample basis and not for entire customer set.
Repayment Frequency	Weekly, fortnightly or monthly at the choice of the borrower	Monthly repayment	The company offers only monthly repayment loans to its clients. The same is communicated to the clients at the time of group formation.
Pricing Cap	Interest rate at 2.75 times the average base rate announced for	Lending rate at 24.99% (except Premium which is at 26.99%)	Arohan fixes the interest rates in compliance with regulations.

Conditions	RBI Policy Announcement	Arohan's Policy	Compliance
	MFIs by RBI Margin Cap at 10% for large MFIs (Assets of more than Rs 100 crore) and 12% for small MFIs. Processing fee of 1% (not included in interest cap or margin cap)	Processing fee of 1% of the loan amount.	
Collateral & group mechanisms	No collateral	Microfinance loans are extended without collateral.	Borrowers confirmed that no collateral or deposits were demanded from them.
Various penalties related to delayed payment	No delayed payment and prepayment penalties and no security deposits	Policy mentions no penalty to be levied on delayed payments or pre-closure. No deposits are also accepted by Arohan.	Borrowers were not aware of the charges. However, no instance of security deposit being demanded by Arohan came to IMAC's notice during client interaction.

The company meets the RBI guidelines (for NBFC-MFIs) on income eligibility, loan size, loan tenure, pricing caps, pre-payment penalties, collateral and overall indebtedness. Arohan would however require to improve its compliance with RBI guidelines in terms of meeting the loan usage criteria and repayment frequency. For the accounts where LUC is carried out, Arohan looks at the amount of funds used in non stated purpose, and insists on pre closure if diversion is more than 50% of the amount disbursed by Arohan.

Annexure I: Overall Score Calculation

Code of Conduct Parameters	Board Policy and Documented Processes	Staff Training and Efforts to disseminate	Level of Observed Compliance	Overall Score
Client Origination and Targeting	Moderately High	Moderately High	Moderately High	7
Loan Pricing and Transparency	High	High	Moderately High	8
Loan Appraisal Process	High	High	Moderately High	8
Staff Behaviour	High	High	High	8
Privacy of Client Information	Very High	Very High	Very High	9
Integrating Social Values into Operations	Above Average	Above Average	Above Average	6
Relationship Management and Grievance Redressal Mechanism	Very High	Very High	Very High	9
Compliance Status of MFI vis-a-vis RBI Guidelines	Very High	Very High	Very High	9
Overall Score				8.0

Annexure II: Code of Conduct Assessment Framework

Objective: To assess the extent of adherence to the common Code of Conduct for MFIs. The eight primary parameters that reflect the common Code of Conduct Assessment practices are:

- Client Origination and Targeting,
- Loan Pricing and Transparency,
- Loan Appraisal Process,
- CB Check
- Staff Behaviour,
- Privacy of Client Information,
- Integrating Social Values into Operations,
- Relationship Management and Grievance Redressal Mechanism, and
- Compliance Status of MFI vis-a-vis RBI guidelines

Evaluation of the 8 parameters done on three levels:

- Adequacy/robustness of company's documented policies, processes and systems addressing the key parameters
- Training and orientation of MFIs staff to the organisational policies and processes and efforts to disseminate relevant information to the customers
- Level of compliance to the prescribed policies and processes as prescribed for the key parameters

Assessment exercise process involved:

- Evaluation of key documents of the MFI (annual reports, board meeting agenda, HR Policies, operating manual, training manuals, internal audit reports, portfolio audit reports)
- Discussion with senior management
- Discussion with branch heads and field officers
- Discussion with other market participants (lenders, associations)
- Key limitation: Absence of interaction with a defaulting member

Annexure II: Details of Branches visited for exercise and number of clients interviewed

S No.	Branch Name	State Name	Number of centres interacted with	Number of clients interviewed
1	Namkum	Jharkhand	2	28
2	Hatia	Jharkhand	2	22
3	Ratu	Jharkhand	2	21
4	Kankarbagh	Bihar	2	23
5	Phulwari Sharif	Bihar	2	20
6	Danapur	Bihar	2	22
7	Rajarhat	West Bengal	1	24
8	Behala	West Bengal	2	33
9	Jodhpurpark	West Bengal	2	25
10	Beliaghata	West Bengal	2	29
11	Shyambazar	West Bengal	2	34
12	Maniktala	West Bengal	2	20

Annexure III: Description of Code of Conduct Parameters

1. **Client Origination and Targeting:** Client Origination and Targeting is the beginning point of effective micro-finance operations as it ensures that finance is extended to the deserving and genuine clients for making improvements to their livelihood. We conducted an assessment of the board's policy and implementation on selection of geography, poverty assessment of target clientele, formation of client members group, excluding risk of over-leveraging and ensuring that appropriate products reach the target clientele.
2. **Loan Pricing and Transparency:** Exorbitant interest rates and lack of transparency in disclosing the effective cost of loans to the clients can lead to a threat of excessive debt burden for the client. We evaluated the policy decision taken by the board to limit excessive margins and ensure complete transparency in disclosure and communication to make clients understand the all-inclusive cost of the loans with respect to declining interest rates, processing fees, insurance charges, collateral deposits and pre-payment penalties.
3. **Loan Appraisal Process:** A robust loan appraisal process is essential to ensure that the client borrow within their repayment capacity, do not get over-leveraged and potentially cause stress to themselves and their group members. The company's policies on conducting verification on client's household income and repayment capacity, field verification to collaborate the information provided in the forms, checks to ascertain the existing leverage of the clients with credit bureaus and other sources and a mechanism to deploy loan utilisation checks are the key parameters to be assessed and evaluated.
4. **Staff Behaviour:** Another critical parameter is staff's conduct towards clients. It is extremely critical that the field officers and other staff of the MFI treat the customers with respect and humility so as to create an environment where the clients are at ease with sharing their concerns and suggestions. Further, in the past, coercive recovery mechanism of MFI staff have been an issue of concern. The assessment will focus on MFIs prescribed policies on granting grace period for repayment, norms for staff behaviour towards clients, execution of Joint Liability Group program, visit to client's houses and use of physical pressure/threats for recovery.
5. **Privacy of Client Information:** The Company should have a board level policy to ensure the privacy of individual client's data related to demographics, income, sex, race, age, education, home ownership etc and also define explicit access rights to the client information with restrictions on usage of the information by unauthorised parties that can cause potential stress to the clients.
6. **Integrating social values into operations:** MFIs even though profit making, are built on a social premise of serving the deprived sections of the society which do not have access to other formal means of finance. The focus of MFIs to build their operations on this social premise as reflected in its vision, mission and endeavours to making contributions to improving the availability of livelihood opportunities and skills/capabilities of clients to leverage on these opportunities has to be evaluated and given due weightage.
7. **Relationship management and grievance redressal mechanism:** MFIs approach towards clients should be to focus on developing long term relationship with the clients and provide them a positive environment which fosters open communication of clients concerns,

suggestions and grievances to the MFI staff. There should be a formal grievance redressal system which ensures that an effective feedback channel is made available to clients, with clear roles, responsibilities and timelines prescribed for effective and quick resolution of the complaints.

8. **Compliance status of MFI vis-a-vis RBI guidelines:** RBI has issued guidelines to provide boundaries to MFIs operations in terms of defining the qualifying assets of MFIs to be treated as priority sector lending from banks, interest rate caps, margin caps, repayment options offered to clients, collateral and purpose of the taking the loans. All MFIs have to necessarily adhere to RBI guidelines to be able to qualify under priority sector lending from banks and are critical in ensuring compliance to a model code of conduct.