

Legislation for the relief of
Indebtedness

by . Prof. C.N. Vakil

LEGISLATION FOR THE RELIEF OF INDEBTEDNESS.¹

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In different provinces legislation has been passed in recent years and in some provinces some measures are under consideration with a view to afford relief to those who are heavily indebted. An attempt is made in this paper to analyse briefly the principal remedies recently adopted in most of the provinces. We are too near the event yet to be able to study the effects of this legislation, though an attempt will be made to examine the general possibilities of the same.

The legislation may be broadly classified as under :—

- (1) Control of money lending.
- (2) Scaling down of old debts.
- (3) Liquidation of old debts.
- (4) Restrictions on the transfer of land.
- (5) Other measures.

I. *Control of Money lending.*

The principal features of this measure are :—

- (a) Definition of a moneylender.
- (b) Registration or licensing of moneylenders.
- (c) Regulation of accounts.
- (d) Regulation of interest.

(a) *Definition of a moneylender.*

In Bengal, Assam and Bihar the definition of a moneylender is broad, inasmuch as, according to the legislation passed in these provinces, the moneylender is a person who advances loans.

In Bombay and the C. P. the definition of a moneylender read along with that of a loan excludes the registered banks, co-operative societies and the government. In these two provinces therefore, institutions which are already subject to legislative control and are properly organised are not further controlled by the new legislation regarding indebtedness. The object in all provinces obviously is to

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regulate private moneylending which has not been organised and which by its very nature causes various difficulties. It is possible that the broader definition of the other provinces mentioned above may be amended in due course.

Along with the definition of a moneylender the question arises whether all the advances in money and kind should be treated as loans. Whereas the legislation in most provinces is not clear on the point, the Madras Act excludes "an advance made by any person not having for its primary object the lending of money, if such loan is advanced in the regular course of business." This attempt to distinguish between different types of loans with a view to bring under control usurious loans as compared with ordinary loans which arise from modern business transactions is useful. In the light of the experience in Madras, the other provinces may in due course have an object lesson to amend their legislation in this connection.

(b) *Registration or licensing of moneylenders.*

The registration of moneylenders is compulsory in Bihar and the C. P. only. The registration fee in Bihar is Rs. 25 the certificate of registration being valid for five years. In the C. P. the fee is Rs. 18, the certificate of registration being valid for four years. The Bombay Bill provides for the licensing of moneylenders. The annual license duty varies according to the capital employed by the moneylender, being Re. 1. when the capital does not exceed Rs. 2000, rising to Rs. 1000 when it exceeds Rs. 10 lakhs. If a moneylender does not possess a license, he is not allowed to seek the assistance of the courts in enforcing his claims, and has to pay a fine for default.

The proposed Bombay arrangements for licensing moneylenders will in the first instance bring some income to the government, and at the same time machinery will be provided by which we shall have information, which will enable us to classify moneylenders according to their capacity. It may also be the beginning of a step which may make it possible to link certain classes of moneylenders with the Reserve Bank under certain conditions. It appears that for the purpose of the legislation regarding the relief of indebtedness the registration or licensing of moneylenders is an essential step. It is to be hoped that the other provinces will adopt similar measures in due course.

(c) *Regulation of accounts.*

According to the legislation, moneylenders are required to maintain proper accounts. The moneylender is under an obligation

(1) to maintain regularly a detailed account in respect of every loan advanced and every transaction made ;

(2) to furnish in a prescribed form a statement of accounts signed by himself or his agent showing the outstanding amount of principal and interest, and the amount and debt of every payment received from the debtor.¹ The debtor to whom such a statement is submitted is not bound to acknowledge or deny its correctness, and his failure to protest is not by itself an admission of the correctness of the statement ;

(3) To pass receipts for payments. In Bihar receipts have to be given also for articles pawned with their description.

Provision has been made in the legislation for adequate penalty in cases where the provisions relating to the keeping of proper accounts are contravened by a moneylender. The penalty takes the form of a fine or imprisonment, or deduction of interest due from the debtor or compensation to the debtor in some other form and so on.

(d) *Regulation of interest.*

The rates of interest which can be charged are also laid down in the different provinces which may be summarised as under :

Rates of Interest prescribed by law.

| Provinces. | Secured, | | Unsecured. | |
|---------------|------------------|----------------------|------------------|----------------------|
| | Simple interest. | Compound interest. | Simple interest. | Compound interest. |
| Madras | 6½ | ... | 6½ | ... |
| Bombay | 9 | prohibited | 12 | prohibited |
| Bengal | 15 | 10 | 25 | 10 |
| Punjab | 12 | 9 | 18 | 14 |
| Bihar | 9 | prohibited | 12 | prohibited |
| C. P. | 7 | 5 with yearly rests. | 10 | 5 with yearly rests. |
| Assam | 12½ | prohibited | 18½ | prohibited |

In the U. P. the rates of interest are regulated with reference to the amount of the loan, the rates being lower as the amount is larger. These new rates apply to transactions made after the U. P. Agriculturists' Relief Act of 1934 came into force. So far as the loans incurred before the Act came into force are concerned the govern-

1. This has to be submitted on demand in Bengal, Madras and Assam ; once in six months in the Punjab, and annually in the rest.

ment notifies the rates of interest allowed from time to time. The following tables indicate the rates thus laid down.

Rates of Interest on new loans since 1934 in the U. P.

| Amount | Secured | | Unsecured. | |
|---------------------------|---------|----------|------------|----------|
| | Simple | Compound | Simple | Compound |
| Rs. 500 and under | 5½ | 3 | 10½ | 7½ |
| Rs. 501 to 5,000 | 4½ | 2½ | 8 | 6 |
| Rs. 5001 to 20,000 | 3½ | 2 | 6½ | 4½ |
| Over Rs. 20,000 | 2½ | 1½ | 5 | 3½ |

Rates of interest allowed for old loans for the period 1-4-1930 to date in the U. P.

| Amount | Secured | | Unsecured. | |
|----------------------------|---------|----------|------------|----------|
| | Simple | Compound | Simple | Compound |
| Rs. 500 and under | 9½ | 7 | 13½ | 10 |
| Rs. 501 to 5,000 | 8½ | 6½ | 12 | 9 |
| Rs. 5001 to 20,000 | 7½ | 6 | 10½ | 8 |
| Rs. 20,000 and over | 6½ | 5½ | 9 | 7 |

Except in the U. P. which makes a specific provision for rates to be applied to old debts transacted before the Act came into force, in other provinces the rates which have been laid down apply to transactions made after the particular Act came into force. The Bombay rate is still not in operation because it is still in the form of a bill. In Bihar the courts are empowered to reopen old transactions to relieve the debtor of all liability in respect of any interest in excess of the maximum rates as laid down above in a suit in respect of a loan advanced before the commencement of the Act.

A provision closely allied to the regulation of interest rates which is common to most of the provinces is the application of the rule of Damdupat. This rule means that no court shall decree on account of arrears of interest a sum greater than the principal of the loan given after the commencement of the Act. In Assam, the Punjab and Bihar this rule applies also to loans advanced before the recent legislation was passed. In Bengal and the C. P. this rule does not apply to loans advanced before the legislation was passed if the court is

satisfied that the moneylender had reasonable grounds for not enforcing his claims earlier. In the U. P. the rule of Damdupat does not apply. It has been laid down however, that when the aggregate of interest realised or accrued on loans advanced after the commencement of the Act becomes equal to the principal, the rate of interest allowed is one notified by the local government as the prevailing rate at simple interest on secured loans and at 2% above that for unsecured loans.

In spite of the reduction, the rates are fairly high in some cases, looking to the prevailing rate at which money can be had in the cities. Besides, the disparity of rates from province to province is remarkable. These tendencies show the absence of a well-organised money-market in the country and also the limited sphere in which the Reserve Bank has to function.

II. *Scaling down of old debts.*

Two different methods have been tried for the scaling down of debts, voluntary and compulsory. The compulsory method is of recent origin adopted by some of the Congress Governments in a few provinces. The voluntary method which has been in vogue in some provinces in the last few years involves the establishment of Debt Conciliation Boards. Such legislation existed in Assam, the Punjab, Bengal, C. P. and Madras. The Debt Conciliation Boards have a statutory existence and have certain powers of civil courts, such as, to compel the attendance of persons, and the production of documents, and power to receive evidence. The registration of the agreement of amicable settlement has the force of a decree of Court. The creditor is not compelled to give up his claims, but if he refuses a fair and reasonable offer, the Board may disallow the cost in any subsequent proceeding pertaining to the same and any interest in excess of 6% from the date of the certificate of the Board. Besides, if a creditor who has been asked to submit his claim fails to do so, his claim is treated as duly discharged and if he does not produce any document, it becomes inadmissible thereafter. Provision has been made by which the benefit of this legislation be confined mainly to agriculturists of an average status. So far as the position of creditors *inter se* is concerned, in the Punjab an amicable settlement can be effected between a debtor and any of his creditors, but a certificate can only be granted if the creditors to whom not less than 40% of the total debt is due have come to a settlement. In the C. P. a certificate can be granted if creditors owing 40% or more of a debtor's debt come to an amicable settlement.

The compulsory scaling down of debt is the chief feature of the Madras Agriculturists' Relief Act recently passed. For this purpose,

an agriculturist is defined as a person who has a saleable interest in any agricultural or horticultural land in the province. The method of scaling down of debts as laid down by the law is not affected by any other law, custom or agreement to the contrary. In case of old debts incurred before 1st October, 1932, (1) all interest outstanding on 1st October 1937 shall be deemed to have been discharged and only the principal will be payable, or (2) if the payment on account of principal or interest or both is twice the amount of the original principal, the whole of the amount shall be deemed to have been discharged, and if the payment is less than double the principal, only the balance shall be paid. In the case of debts contracted after 1st October 1932 the amount of the whole transaction shall be made up at 5% simple interest on the original loan, and the balance after deducting all payments shall only be payable. The rates of interest on debts so scaled down shall be 6½%, the rate which shall also be payable on new loans hereafter incurred.

In the C. P. new legislation has been proposed by which the former voluntary method of scaling down debt will be replaced by the compulsory method. Provision has been made to establish debt relief courts whose duty it will be to reduce interest and principal in accordance with the scales laid down. The jurisdiction of the courts can be invoked by debtors only. The rates of interest laid down for this purpose are—4½% compound interest with yearly rests; 6% simple interest on secured debt and 9% simple interest on unsecured debt. The scale of reduction of debts is laid down as under; if the debt was incurred before 31st December 1925, 30%; if the debt was incurred after 1st January 1926 but before 1st October 1929, 20%; if the debt was incurred after 1st October 1929 but before 31st December 1930, 15%. It may be pointed out that these percentages were fixed with reference to the estimated fall in the value of land.

Though the method both in Madras and C. P. is compulsory there are differences in details. The Madras method is apparently simple and is expected to work on the basis of a formula laid down by law. Litigation will be necessary only if the parties do not agree in the application of the law to their case. In the C. P. the scaling down of the debt itself is subject to a legal arrangement which will therefore be more thorough, but at the same time will involve more trouble and delay to the parties concerned.

Similar legislation for scaling down debts does not exist in other Provinces. This does not mean that the problem is not acute in those provinces. It may mean that the vested interests are stronger or that the Government is not yet strong enough to face the opposition that such measures will arouse.

III. Liquidation of old debts.

Once the amount of the debt is settled either on the voluntary or the compulsory method, the next question is that of liquidating the same. In fact the very object of scaling down the debt is to enable the debtor to pay it off in reasonable time. It is obvious that if the creditors are able to obtain cash the scaling down of the debt will certainly be easier, but unfortunately the debtors are not always in a position to pay cash even at the reduced figure.

The Land Mortgage Bank can play a useful part in this connection. Such a Bank may lend money for a long period on adequate security. It may either pay down the reduced debt immediately or pay the instalments to the creditor.

In order that the Land Mortgage Banks are able to do this work successfully there should be on the one hand a large number of such banks spread over throughout the country with adequate State support. Though the step taken in some provinces to organise Land Mortgage Banks is in the right direction, their number and their resources and consequently their work is still of a limited character compared with the magnitude of the task facing them.

The following table shows the number of Land Mortgage Banks in different provinces by the end of 1936-37.

| PROVINCES. | CENTRAL. | PRIMARY. | TOTAL. |
|------------------|----------|----------|--------|
| Madras | 1 | 93 | 94 |
| Bombay | 1 | 13 | 14 |
| Bengal (1935-36) | — | 5 | 5 |
| U. P. | — | 5 | 5 |
| Punjab | — | 12 | 12 |
| Bihar | — | — | — |
| C. P. | — | 12 | 12 |
| Assam | — | — | — |
| N. W. F. P. | — | — | — |
| Orissa | — | — | — |
| Sind | — | — | — |

Under the able guidance of the Late Sir Ramchandra Rao, the Madras Presidency has been far ahead of others in the matter of banking institutions of this type. There are primary land mortgage banks in every district except in Malabar and South Kanara where legal difficulties came in the way. The Government increased the amount of debentures guaranteed as to principal and interest to 150 lakhs and the amount advanced during 1936-37 was 141 lakhs. The rate of interest charged to the ultimate borrower was 2 per cent higher

than the borrowing rate of the Central Bank which was 3 per cent during the same year.

IV. *Restrictions on the Transfer of Land.*

Attempts have been made in the past to prevent land being transferred to the ownership of non-agriculturists on account of the indebtedness of agriculturists. The Punjab Land Alienation Act of 1900, which also applies to the N. W. Frontier Province, and which has been amended several times, the Bundelkhand Land Alienation Act of 1903 and the C. P. Land Alienation Act of 1916 are illustrations.

Under the Punjab Act certain ancestral cultivating clans are notified. The C. P. Act is limited in its application to aboriginal tribes only. Under these Acts, alienation of land is allowed only in those cases where the alienor is not a member of the agricultural tribe, or where both the parties belong to the same tribe or to a tribe in the same group. In all other cases, the sanction of the Deputy Commissioner is required. Any sale in contravention of the Act is valid and takes the form of usufructuary mortgage.

It has been further laid down that usufructuary conditional mortgages and leases are not allowed for a period exceeding twenty years. By a recent amendment of the Punjab Act, it has been laid down that this limit cannot be extended in any case by any device. Another amendment of this Act provides that no land belonging to a member of an agricultural tribe shall in execution of a decree or order of any civil or revenue court be leased or farmed for a period exceeding 20 years.

Witnesses from the Punjab before the Royal Commission on Agriculture were of the opinion that this legislation was successful in its main object, namely, to prevent the transfer of agricultural land from cultivating to non-cultivating clans.

With the exception of recent amendments to the Punjab Act referred to above, no steps have been taken to revise the existing legislation or to extend it to other parts or to other classes of agriculturists. This does not mean that the problem does not exist elsewhere, though there may be differences in degree.

V. *Other Measures.*

(a) Some protection to the agricultural debtor is provided in the Civil Procedure Code by which his implements, cattle and seed grain required to earn his livelihood are not liable to attachment and sale.

(b) The C. P. Debtors' Protection Act and the Bombay Money-lenders' Bill provide for the protection of debtors from molestation and intimidation by the creditors for the recovery of debts.

(c) The Insolvency Law affords relief to debtors under certain conditions. But its provisions have been found unsuitable to agricultural debtors. The Royal Commission on Agriculture recommended a Rural Insolvency Act. Some of the difficulties in this connection have been removed in the Punjab by reducing the amount for which an insolvency petition can be made. In Bengal however under the Agricultural Debtors' Act of 1935, the Conciliation Boards are empowered to declare a debtor insolvent when his debt is so high as cannot be repaid within 20 years. In settling the debt the dwelling house and one-third of the land held by the insolvent debtor in his direct possession exclusive of the land occupied by his dwelling house, with a minimum of one acre of land is exempt from sale in satisfaction of his debt.

Conclusions.

This brief summary of the attempts made in different provinces for the relief of indebtedness shows that the authorities are now fully conscious of the gravity of the situation and are anxious to take some steps. Though fundamentally the problem in each province is substantially the same the difference in the methods adopted reveal the differences in the local situation in each province as well as to some extent the outlook of the Government of the day.

Restriction of Credit.

One thing which stands out most clearly is the fact that steps of this nature are likely to restrict credit. The agriculturist cannot do without credit because of the nature of his profession, and if these measures come in the way of his future work they will defeat the purpose for which they have been made. To some extent restriction of credit may also be a boon to the agriculturist inasmuch as it is well known that a large part of his debt has been hitherto for unproductive purposes. If the agriculturist realises out of sheer necessity the need for not going into debt for unproductive purposes some good will have been done. For productive purposes the conditions in future are likely to be difficult, but the agriculturist may reasonably hope to obtain credit particularly if he has a security to offer. This is so mainly because the moneylender even under the new restrictions would like to see his money properly employed, if possible. A tendency for capital to migrate from rural to urban areas has been observed and this may have been partly due to this legislation. But the avenues

of profitable employment of capital in urban areas are not many at present. In the absence of any such alternative therefore, the money-lender may be compelled to continue his business even though under certain restrictions.

The need for a comprehensive approach.

The relief of indebtedness in one form or another, may not be desirable unless it is simultaneously accompanied by other steps. The object of this relief obviously is to put the agriculturist on his legs, to start him on a new career, to enable him to do his work more cheerfully, to assure him a fair return on his labour and to create an interest in life for him. But these things require other efforts in the absence of which the agriculturist may once again relapse into a state of indebtedness. Compulsory consolidation of holdings, prevention of fragmentation of holdings, co-operative farming, co-operative marketing along with other improvements in rural life should go hand in hand with measures of relief of indebtedness.

Unless a comprehensive approach to the problem of rural economic life is made, and several aspects attacked simultaneously and vigorously, success may not be realised. The standard of life in our villages has become so low, that it is difficult to create an impetus for self-help, if the various forces working against improvement are not checked at a time. If we want to see that our efforts in one direction are not negated by evils in other directions, we must beware in time. In view of the neglect of generations, we are face to face with a problem which is both desperate and baffling. But it is exactly because of these reasons that the remedies shall have to be heroic and courageous on the one hand and comprehensive and thoroughgoing on the other.

Suggestions.

If a complete scheme of rural development can be launched so that all the essential reforms can be carried out without delay, and adequate self-help on the part of the agriculturist be thus guaranteed, one may go to the length of suggesting that (1) those debtors for whom it is impossible to pay their debts within reasonable time should be allowed the facilities of a Rural Insolvency Law; and (2) in the case of others, the State should take over the responsibility for the reduced debts, and allow the agriculturist to have a fresh lease of life. This can be done by the State issuing bonds to the creditors, paying the interest on the same, through the machinery of the Land Mortgage Banks. The lands of the debtors would be mortgaged to

the Banks as representing the State, the instalments to the Bank being spread over a number of years.

Before launching any such scheme inquiries will have to be instituted to ascertain the position of debtors. There will be some debtors in each province who can with a certain amount of ease pay their debts in full. There will be another class of debtors who would be in a position to pay only if the debts are scaled down to a reasonable figure. And perhaps the largest number of debtors will be those whose cases are desperate, and who are not in a position to pay at all, and therefore must be brought under the operation of a Rural Insolvency Law. Though some attempt was made by the Provincial Banking Enquiry Committees to make estimates of indebtedness in different provinces, these were not sufficiently detailed, and they were made from a different point of view. Besides, these estimates have become out of date by now. If the benefits of any such scheme as outlined above are to be properly availed of, such systematic inquiries are an essential preliminary, which no provincial government seems to have thought of hitherto. In fact there is a want of confidence in such inquiries among some of the responsible ministers now in power. Perhaps experience alone will make them realise the value of such scientific inquiries, or when alone sound legislation can be based and successfully carried out. Hasty steps may lead to undesirable consequences which should be avoided when we are dealing with large masses of people. The co-operation of Universities and Economists in such inquiries if properly organised would be invaluable. Whereas the Bureaucratic Government in the past systematically avoided Economists and their studies in this country, the Responsible Governments now in power may find it both easy and cheap to institute such inquiries through the medium of the Economics Departments of the Universities.

In addition to this, simultaneous arrangements will have to be made for providing adequate credit facilities through co-operative banks for the current needs of the agriculturist. Conditions will have to be laid down*to see that the facilities thus provided are used to proper advantage and not for unproductive expenditure. In other words, the agriculturist will have to be taught to behave in a responsible fashion in his own interest, if the benefits suggested here are to do him any permanent good. This is as it should be, because unless such safeguards are provided the temptation to treat these benefits as windfalls and therefore to run once again into debt will be overpowering.

It is obvious therefore, that the working out in greater detail of a scheme of this nature will require a large organisation and ex-

penditure on behalf of the State. But the Provincial Governments who are determined with one voice to improve the lot of the agriculturist must be bold enough to face such expenditure and undertake such organisation. It should be realised fully that the problem of the Indian farmer has become so acute, that it cannot be solved by piecemeal legislation of a half-hearted nature though undertaken with the best of intentions. What is required is radical measures of a comprehensive nature put into effect with a determined effort without undue delay.