

Significance of Lok Adalats in Resolving Debt Recovery Cases Instituted by Financial Institutions

Hanumanth A Satwik*

Abstract

The primary role of financial institutions is to get their corpus from the depositors and lend it to those who need it. Lending money is always coupled with the problem of defaults being committed by the borrowers. Further, growing NPAs are also a major concern for the banks, as it has a direct impact on the profitability of banks. The banks cannot afford defaults by the borrowers, as defaults may lead to the closure of banks. To avoid these scenarios, the banks resort to various techniques to recover loans. One of the methods to recover loan, being followed by the majority of the financial institutions, is filing suits before civil courts. Be it noted, considering the pendency of cases before the courts, delays in deciding those matters are bound to happen. In the meantime, the loan amount lent would get held up with the borrowers without being recovered. It is stated that, delay in disposing of suits filed for recovery of loans has serious effects on the banks and on the economy of the country. Here comes Lok Adalat as one of the Alternative Dispute Resolution Mechanisms (ADLR Mechanisms) to decide suits for recovery of loans effectively and speedily. Lok Adalat implies resolution of disputes by discussion, counseling, persuasion, and conciliation. Since Lok Adalat maintains the balance between the interests of the parties and since proceedings before Lok Adalat are speedier, it is an effective mode for resolving disputes concerning the recovery of loans.

Keywords: Lok Adalat, legal services, dispute resolution, pre-litigation, non-performing assets

* *PhD Research Scholar at School of Legal Studies, CMR University*

Introduction

The health of the bank and the economic prosperity of the country can be measured by the volume of Non-Performing Assets (NPAs). An increasing number of NPAs in banks is a great concern for the economic growth of the country. The volume of NPAs can be controlled only through a well-functioning recovery mechanism. In this background, the financial institutions should adopt a recovery method that is effective, efficient, and affordable. In this regard, Lok Adalats, as one of the Alternative Dispute Resolution Mechanisms, act as a coherent medium for the recovery of loans. Lok Adalat signifies resolution of disputes between the parties through conciliation, persuasion, and settlement. As per Sec. 2(d) of The Legal Services Authorities Act, 1987 (herein after referred as “the Act”) Lok Adalat means a Lok Adalat organised under Chapter VI of the Act. Earlier, in India, disputes were settled by a council of village elders, known as a *panchayat*. This was an accepted method of conflict resolution. Since Vedic times, India has been heralded as a pioneer in the achievement of the social goal of speedy and effective justice through informal but culminating resolution systems¹. ADR methods are not new to India and have been in existence in some form or the other in the days before the modern Justice delivery system was introduced by the colonial British rulers. The references about Lok Adalats can also be found in the works of Kautilya, Gautama, Brihaspati, and Yagnavalkya. In ancient times, Lok Adalats were known as Panchayats, Gram Sabhas, Kula Courts or Sreni Courts². The Lok Adalat movement was started in Gujarat during March 1982, and the first Lok Adalat was held at the village of Una in the Junagarh district. Soon Lok Adalat programme was adopted by the other states.

Resolving disputes through an adversarial mechanism is time-consuming. Financial institutions cannot afford delays in resolving disputes through the adversarial system, as the matters would involve large stakes, held up in the hands of one of the parties without being utilised. Since disposal of cases through Lok Adalats is expeditious and speedy, the financial institutions would benefit from this mode of dispute resolution mechanism. Thus, Lok Adalat as a method of dispute resolution helps the financial institutions to overcome delays. On this touchstone, highlighting the

¹ Law Commission of India, <https://cdnbbsr.s3waas.gov.in/s3ca0daec69b5adc880fb464895726dbdf/uploads/2022/08/2022081082-2.pdf> (last visited May 26, 2025).

² International Journal for Science and Innovations, <https://ijlsi.com/paper/a-brief-analysis-on-lok-adalats-in-contributing-legal-aid-and-speedy-justice/> (last visited Feb. 10, 2025).

importance of Lok Adalats, Hon'ble Supreme Court of India in its decision between Madhya Pradesh State Legal Services Authority V. Prateek Jain and Anr.³ held that the manifest objective of constitution of Lok Adalats is to have speedy resolution of the disputes through these Lok Adalats, with added advantage of cutting the cost of litigation and avoiding further appeals. The advent of the 1987 Act gave a statutory status to Lok Adalats, pursuant to the constitutional mandate in Article 39-A of the Constitution of India. Lok Adalats have been created to restore access to remedies and protections and alleviate the institutional burden of the millions of petty cases clogging the regular courts. These observations of the Hon'ble Court indicate the significant role being played by the Lok Adalats in resolving disputes.

As far as loan recovery matters pending before the courts are concerned, in the majority of cases, the fact that remains undisputed would be the borrowing of the loan from the bank. Thus, the only contesting question that lasts for consideration would be the rate of interest being charged by the financial institutions. In this regard, Lok Adalats provide an opportunity to the parties to mutually agree on the rate of interest chargeable on the loan and the method of its repayment. Thus seen, Lok Adalats offer an opportunity to the parties to interact with each other and come to mutually agreed solutions without resorting to formal court proceedings. In this background, Lok Adalats, through conciliation and persuasion, act as a medium to resolve loan recovery disputes effectively without giving a go bye to the interest of the parties.

Scope

Lok Adalats have been given statutory recognition by The Legal Services Authorities Act, 1987, which came into force on 09.11.1995. The Lok Adalats under the Act shall have jurisdiction to determine and arrive at a compromise or settlement between the parties in respect of cases pending before any court or any matter which falling within the jurisdiction of and is not brought before the court⁴. As such, both pending and the pre-litigation cases are amenable to the jurisdiction of the Lok Adalats. The Lok Adalats have no adjudicatory or judicial functions. Their functions relate purely to conciliation. A Lok Adalat determines a reference on the basis of compromise or settlement between the parties at its instance and puts its seal of conformity by making an award

³ Madhya Pradesh State Legal Services Authority V. Prateek Jain and Anr., (2014) 10 SCC 690.

⁴ The Legal Services Authorities Act, 1987, S.19(5), No.39, Acts of Parliament, 1987 (India).

in terms of the compromise or settlement. In their conciliatory role, the Lok Adalats are guided by the principles of justice, equity and fair play⁵.

In regard to reference of cases to Lok Adalats are concerned, the court can refer matters to Lok Adalat in the following circumstances.

- (a) the parties thereof agree; or
- (b) one of the parties thereof makes an application to the Court,
- (c) for referring the case to the Lok Adalat for settlement and if such court is *prima facie* satisfied that there are chances of such settlement; or
- (d) The court is satisfied that the matter is an appropriate one to be taken cognizance of by the Lok Adalat.

However, the court while *suo moto* referring a matter to Lok Adalat or when court refers a matter to Lok Adalat on the bases of an application of one of the parties, in either of the cases the court shall, before referring the matter to Lok Adalat, give reasonable opportunity of being heard to the parties. The above apart, on the bases of an application by any one of the parties, the authority conducting Lok Adalat, may *suo moto*, on giving reasonable opportunity of being heard to the parties, may refer the matter to Lok Adalat⁶. Further, with regard to matters relating to divorce are concerned, as per proviso to R.10(2) of The National Legal Services Authority (Lok Adalat) Regulations, 2009, such matters cannot be referred to Lok Adalat. Thus seen, barring few matters, the Act and 2009 regulations give wide range of subjects amenable to the jurisdiction of Lok Adalat.

Process of Lok Adalat

Hon'ble Supreme Court of India in its decision between Afcons Infrastructure Ltd. and Anr. V. Cherian Varkey Construction Pvt. Ltd and Ors.⁷ held that the courts should act on Sec.89 of CPC soon after the completion of pleadings and before framing of issues. Once the matter is referred to Lok Adalat, discussions on the subject matter would be held with the parties for arriving at a

⁵ State of Punjab and Anr. v. Jalour Singh and Ors., (2008) 2 SCC 660.

⁶ The Legal Services Authorities Act, 1987, S.20(2), No.39, Acts of Parliament, 1987 (India)

⁷ Afcons Infrastructure Limited and Anr. V. Cherian Varkey Construction Company Pvt. Ltd. And Ors., (2010) 8 SCC 24.

just settlement or compromise. Further, the Lok Adalat shall assist the parties in an independent and impartial manner in their attempt to reach amicable settlement of their disputes. In the process of Lok Adalat proceedings, members of Lok Adalat shall not pressurise or coerce any of the parties, to compromise or settle cases or matters, either directly or indirectly⁸. When it appears to the Lok Adalat that there exists an element of settlement which may be acceptable to the parties, the terms of a possible settlement may be formulated by the Lok Adalat and would be given to the parties for their observations. Further, any modifications suggested by the parties can be taken into consideration and terms of a possible settlement may be re-formulated by the Lok Adalat. If the parties reach a compromise or settlement of the dispute, the Lok Adalat may draw up or assist the parties in drawing up the compromise or settlement. Finally, an award will be drawn up in terms of settlement or compromise reached by the parties.

Further, in view of Sec.20 of the Act, every award of the Lok Adalat shall be deemed to be a decree of a civil court. As such, awards passed in Lok Adalats have the same sanctity as that of the decree passed by the civil courts and they are enforceable as decrees of civil courts. If no settlement is arrived at the Lok Adalat, the file referred would be returned to the concerned court to proceed with the matter from the stage which was reached before such reference was made to the Lok Adalat. Thus seen, the process of Lok Adalat is not cumbersome, and it is understandable also to a common man. The procedure followed in Lok Adalat being lucid and unambiguous, it is suitable to solve disputes relating to loan recovery.

Loan Recovery & Lok Adalat

The Lok Adalats as one of the modes of loan recovery, plays an important role in recovery of agricultural loans, educational loans, personal loans etc. Further RBI through its various circulars encouraged financial institutions to take advantage of Lok Adalats for compromise and settlement of the NPAs. In this direction, RBI has increased the monetary ceiling of the cases to be referred to the Lok Adalats to 20 lakhs⁹. Furthermore, with regard to scope of reference of matters to Lok Adalat is concerned all the matters relating to NPAs with respect to which accounts, suit has been instituted or not and which are in doubtful and loss category, with outstanding balance of Rs.5

⁸ The National Legal Services Authority (Lok Adalat) Regulations, R.13(2), Central Authority, 2009 (India).

⁹ Reserve Bank of India, https://rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=1813 (last visited May 26, 2025).

lakhs can be referred to Lok Adalat. However, the formula of settlement to be accepted is left to the discretion of the Board of Directors of each financial institution¹⁰.

The RBI vide its circular laid down the following guidelines to be followed by the financial institutions in relation to Lok Adalats¹¹;

- (a) The financial institution should sought for a decree from Lok Adalat for principal and interest claimed in the suit and after full payment of the decreed amount the banks shall issue discharge certificate to the borrower.
- (b) With regard to recovery of book dues, the banks concerned should frame flexible policies.
- (c) The repayment period should be fixed within one to three years.
- (d) The officer representing the financial institution before the Lok Adalat should have sufficient powers to accept the compromise worked out within the policy framework laid down by the Board of Directors of each financial institution.
- (e) The institutions should get in touch with State / District / Taluk level Legal Services Authorities for organising Lok Adalats. The banks / financial institutions should prescribe clear guidelines to their operating staff and monitor the progress regularly.
- (f) The banks should report the progress to the Central Office of the Department of Banking Operations and Development, and the financial institutions should report to the Central Office of the Department of Banking Supervision (Financial Institutions Division), Reserve Bank of India at quarterly intervals within one month from the quarters ending March, June, September and December, as per the format.
- (g) Reserve Bank of India would monitor the progress made by the institutions in effecting recovery under the scheme.

Thus, the guidelines above referred indicate that RBI through its circulars recognized Lok Adalats as one of the important dispute resolution mechanisms for matters relating to loan recovery.

Recovery of Loans at Pre-Litigation Stage

¹⁰ Reserve Bank of India, <https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=374&Mode=0> (last visited Feb.28, 2025).

¹¹ Reserve Bank of India, <https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=374&Mode=0> (last visited Feb.28, 2025).

‘Pre-Litigation matter’ means a dispute between the parties which is not filed before the court¹². A pre-litigation matter may be referred to the Lok Adalat by the concerned Legal Services Institution on the request of any of the parties after giving a reasonable opportunity of being heard to the other party. This is the stage wherein the dispute between the bank and the borrower has not yet reached the court. In pre-litigation cases any party may approach the legal services authority with a grievance. Once the party approaches the legal services authority concerned, it shall on securing the other party and on hearing both the parties may refer the matter to Lok Adalat. If a pre-litigation matter is not settled in Lok Adalat, the parties may be advised to resort to other Alternative Dispute Resolution (ADR) techniques or to approach a court of law and in appropriate cases they may be advised about the availability of legal aid. Thus seen, in pre-litigation cases the financial institutions have an opportunity to get their loan recovered from the borrower by getting their matter referred to Lok Adalat without even approaching the courts. This mode of loan recovery will help the banks to recover loan expeditiously and with no cost.

Benefits of Lok Adalat

As far as state of Karnataka is concerned, Lok Adalat was held on 14.09.2024. As per the statistics of Lok Adalat of Karnataka chapter, 139548 pre-litigation bank recovery cases were taken up for settlement and out of them 21599 matters were settled at Lok Adalat and the settled amount is Rs.894419088. Further, in the same Lok Adalat 5493 pending bank recovery cases were taken up for disposal and the number of matters that got settled were 1118 and the settled amount is Rs.749408915¹³. So also, in Maharashtra from April 2023 to February 2024, 2070050 pending cases and 1773592 pre-litigation cases were disposed in Lok Adalat¹⁴. Additionally, in Tamil Nadu from 01.11.1997 to 28.02.2024, 3267 bank suits were disposed in Lok Adalats and the settled amount is Rs.464,25,77,837.77/-¹⁵. These statistics themselves speak how Lok Adalat is conducive for recovery of debt by the banks and why people have faith in it. The importance of Lok Adalat

¹² The National Legal Services Authority (Lok Adalat) Regulations, R.2(ba), Central Authority, 2009 (India).

¹³ Karnataka State Legal Services Authority, <https://kslsa.kar.nic.in/pdfs/lok%20adalat/14.09.2024%20Statistics.pdf> (last visited Feb.27, 2025).

¹⁴ Maharashtra State Legal Services Authority, <https://cdnbbsr.s3waas.gov.in/s3d04863f100d59b3eb688a11f95b0ae60/uploads/2024/06/202406251019547226.pdf> (last visited Feb.8, 2025).

¹⁵ Tamil Nadu State Legal Services Authority, <https://www.tnlegalservices.tn.gov.in/pdfs/statistics/lokadalat.pdf> (last visited Feb.8, 2025).

was also highlighted in the discussions of Lok Sabha, wherein the Minister of State in the Ministry of Finance stated that Lok Adalats and Debts Recovery Tribunals (DRTs) are playing a significant role in disposal of recovery. During the financial years 2014-15 to 2016-17, as per RBI data, the aggregate amount recovered by Scheduled Commercial Banks through the Lok Adalat channel was Rs. 8,075 crore, and as per data reported by DRTs, 54,991 cases have been disposed of by DRTs¹⁶. The above apart, in the words of the Hon'ble Supreme Court of India following are the benefits of Lok Adalat¹⁷;

- (a) There is no Court fee and if Court fee is already paid the amount will be refunded if the dispute is settled at Lok Adalat according to the rules.
- (b) The basic features of Lok Adalat are the procedural flexibility and speedy trial of the disputes. There is no strict application of procedural laws like Civil Procedure Code and Evidence Act while assessing the claim by Lok Adalat.
- (c) The parties to the dispute can directly interact with the Judge through their Counsel which is not possible in regular Courts of law.
- (d) The award by the Lok Adalat is binding on the parties and it has the status of a decree of a Civil Court and it is non-appealable which does not cause the delay in the settlement of disputes finally.
- (e) In view of above facilities provided by the Legal Services Authorities Act, Lok Adalats have become boon to the financial institutions, as they can recover debt from the borrowers speedily and with no cost.

In view of above facilities provided by the Legal Services Authorities Act, Lok Adalats have become boon to the financial institutions, as they can recover debt from the borrowers speedily and with no cost.

Conclusion & Suggestions

It is seen that large number of loan recovery cases get settled before Lok Adalats, which are either pending suits referred from the courts or pre-litigation cases referred from the legal services

¹⁶ Digital Sansad, <https://sansad.in/getFile/loksabhaquestions/annex/14/AU4682.pdf?source=pqals> (last visited Feb.28, 2025).

¹⁷ P.T. Thomas v. Thomas Job, AIR 2005 SC 3575.

authorities concerned. However, there are also hindrances to the growth of Lok Adalats. One of the obstructions is the assurances given by the political parties during their election campaign. Be it stated, due to the assurances about loan waiver or rebates on loan given by the political parties in their election campaign, people who borrowed loans hardly come to settle the loan claim made by the banks, believing that the Government would waive off their loan. Be it stated, all the assurances given during election campaign would not become a reality. However, the people, especially the illiterate without understanding the intricacies of the assurances and believing the promises do not turn up to Lok Adalat to get their loan recovery disputes settled. Consequently, desired number of debt recovery cases will not get settled before Lok Adalats and as a result Lok Adalats would become unsuccessful. In this regard, it is necessary for the people to get clear information about the proposed loan waiver or loan rebates schemes of the political parties and possibility of it being implemented. So also, the banks are required to educate people on the assurance given by the political parties during their election campaign.

The above apart, it is seen that if loan recovery cases end up in compromise, that will have negative impact on the Cibil score and resultantly, banks would not come forward to lend money to the borrower for the next time. This is another cause for a smaller number of loan recovery matters getting settled before Lok Adalats. In this regard, it is necessary for the policy makers to look into this aspect and find a solution which would protect the interest of both financial institution and the borrowers.

Inspite of obstructions as elucidated above, Lok Adalats which consist of Judges and experienced lawyers as its members, are beneficial to the parties for resolving loan recovery matters speedily and with no cost. In this direction, it is necessary that the litigant public should be made aware about Lok Adalats and their benefits. This can be achieved through legal services authorities present at different levels, which can enlighten people about Lok Adalats through legal literacy programmes. Further, the litigants should be encouraged to settle their disputes through the medium of Lok Adalats. Besides, it is necessary for the courts to increase the number of references of debt recovery disputes to Lok Adalats. Furthermore, responsibility is cast on the lawyers, who are the officers of the court, to encourage their clients to settle their disputes through Lok Adalat, unmindful of loss of their brief. So also, it is the duty of the lawyers to make their clients aware about the benefits of Lok Adalat. Also, the litigant public should participate in the Lok Adalat

whole heartedly and disclose to the bench their grievances honestly, so as to enable the bench to persuade the parties to settle the matter. Thus, if all the stake holders put their combined efforts towards resolution of disputes through Lok Adalats, there will be better administration of justice, as the burden on the courts will come down and the courts can concentrate more on complicated cases involving serious questions of law and fact. So also, informed participation of litigants in Lok Adalats will help them to resolve their disputes effectively.