

Seminar on Concurrent Audit

Advances Verification including NPA
Norms

Organised & Hosted by
WIRC of ICAI

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Advances

Balance Sheet Disclosure

Types of Advances

Commonly used terminologies

Appraisal

Documentation

Monitoring of Advances

IRAC Norms

Advances

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The Third Schedule of Banking Regulation Act, 1949 -
Schedule 9 of Form "A"

		Particulars	C.Y.	P.Y.
A	i	Bills Purchased and Discounted		
	ii	Cash credits, overdrafts and loans repayable in demand		
	iii	Term Loans		
		Total		
B	i	Secured by tangible assets		
	ii	Covered by Bank/Government Guarantees		
	iii	Unsecured		
		Total		

Advances

The Third Schedule of Banking Regulation Act, 1949 -
Schedule 9 of Form "A"

		Particulars	C.Y.	P.Y.
C.I		Advances in India		
	i	Priority Sector		
	ii	Public Sector		
	iii	Banks		
	iv	Others		
		Total		

Advances

The Third Schedule of Banking Regulation Act, 1949 -
Schedule 9 of Form "A"

		Particulars	C.Y.	P.Y.
C.II		Advances outside India		
	i	Due from banks		
	ii	Due from others		
	iii	(a) Bills purchased and discounted		
		(b) Syndicate Loans		
		(c) Others		
		Total		
		Total (C.I + C.II)		

Advances

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Types of Advances

Funded	Non-Funded
Term Loan	Bank Guarantees
Personal Loans	Letter of Credit
Gold Loans	Letter of Comfort
Advance against Securities	
Housing Loans	
Other Term Loans	
Working Capital Finances	
Cash Credit	
Overdraft	
WCTL / WCDL	

Advances

Balance Sheet Disclosure

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IRAC Norms

Commonly used terminologies

- Demand Loan
- Bills Purchased
- Bills Discounted
- Funded Credit Facilities
- Non-funded Credit Facilities
- Primary Security
- Collateral Security
- Personal Guarantee of borrower / guarantor
- Fixed Charged vis-à-vis floating charge
- Margin

Commonly used terminologies

Sole Banking

Consortium Arrangement

Multiple Banking

- Each lender has its own set of documentation

Loan Syndication

Inter bank Participation Certificates

Sharing of credit assets on ...

- *Risk-sharing basis*
- *Non-risk sharing basis*

Advances

Balance Sheet Disclosure

Types of Advances

Commonly used terminologies

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IRAC Norms

Advances - Appraisal

- Application Form
- Documents to be received with application
 - Financial Statements of borrower and guarantors
 - Financial Projections
 - Techno Economic Viability Study
 - Details of associate concerns
 - Primary and Collateral Security
 - Board / Other Resolutions
 - Valuation of Securities
 - Title Clearances
 - Requisite licenses & statutory returns / registrations

Advances - Appraisal

- Appraisal Process
 - KYC Compliance
 - MSME Registration Certificates
 - Compliance with RBI / Internal Exposure Norms
- Pre-disbursement Inspection

Advances - Appraisal

- Disbursement
 - Documentation
 - RoC Charge Creation
 - End-use (Invoices / Receipts)
 - Promoter's contribution
 - Insurance
 - Post-disbursement Inspection
- Monitoring
 - Exception Reports
 - Stock Audit
 - Branch Inspection
 - Renewal

Advances - Appraisal

- Check points for the auditor
 - Master Data in CBS (PSL Targets)
 - Accounts wherein renewal is pending
 - Short / Technical Review
 - Adhoc / TODs
 - Possibility of Ever-greening of Accounts
 - Whether appraised properly?
 - Waivers for conditions whether obtained from appropriate authorities?
 - Discretionary powers used for sanction – Whether within the delegated powers?

Advances - Appraisal

- Check points for the auditor
 - Whether adverse remarks of field officer are over-ruled by sanctioning authority?
 - Sanction letter and sanction note – Whether in sync with each other?
 - Any subsequent dilution of conditions – Whether sanctioned by competent authority?
 - Any possibility of account being restructured?
 - Adverse comments by auditors (Internal / Concurrent / Stock / Statutory): Whether cognition taken in appraisal?
 - Credit Rating – Internal / External vis-à-vis RoI

Advances - Appraisal

- Check points for the auditor
 - Financial Projections : Whether realistic and backed by adequate documentation?
 - Classification of Advance (Priority / Non-Priority, Sector, etc.)
 - Sanction Letter: Whether accepted by borrowers / guarantors?
 - Loan documentation: Legal Vetting
 - Valuation: More than two Valuators requirement
 - Original documents like share certificate, sale agreement, NoCs, Board Resolution, etc.
 - Applicability of State Stamp Duty

Advances - Appraisal

- Check points for the auditor
 - CIBIL report
 - Confidential Report (CR) from existing Bankers
 - Nayak Committee Recommendations
 - Assessment based on projected turnover
 - Working Capital Requirement to be @ 25% of Projections
 - 20-80 formula for own contribution – bank finance
 - Thus, 20% of Projected turnover = Working Capital Limits
 - Ensure no documents are executed blank / partially filled up
 - Charge Creation at RoC

Advances – Prudential Exposure Norms

Single Borrower / Group Borrower

Particulars	Remarks
Single borrower	15% of capital funds
Group borrower*	40% of capital funds

Capital Fund = Tier I + Tier II Capital

Special provisions for infrastructure

Additional 5% / 10% for single / group borrower limits

Advances – Prudential Exposure Norms

Group Borrower

- No specific definition for “Group Borrower”
- Guiding principle being commonality of management and effective control
- For PSUs, only single borrower exposure limit would be applicable

Advances – Prudential Exposure Norms

LCBD

- If LC issued by third bank, exposure would be on the said (LC issuing) bank
- If LC issued by same bank, exposure would be on the borrower

Advances – Prudential Exposure Norms

Exemptions

- Existing accounts under rehabilitation
- Food Credit
- Central Government Guaranteed Accounts
- Advance against own FDR
- Exposure to NABARD (excluding unrated non-SLR securities)

Advances – Prudential Exposure Norms

Industry-wise Exposure Norms

Particulars	Remarks
Sectorial limits	Banks to decide internal limits for each sector like textile, jute, tea, etc.
Real Estate	Should have internal guidelines
Leasing / Hire Purchase / Factoring Services	Exposure to each type of activity should not exceed 10% of total Advances

Advances – Prudential Exposure Norms

Real Estate Exposure

- Need to frame comprehensive prudential norms
- Policy should be approved by Board
- Need to ensure that borrower has obtained prior permissions from government / local government bodies wherever required
- Disbursement to be only after obtaining clearance from government authorities

Advances – Prudential Exposure Norms

Capital Market Exposure (CME)

- Direct investment in Equity, Convertible bonds / Debentures / Equity-Oriented MFs
- Advance against above mentioned securities (which are taken as primary security)
- Advance for investments in above mentioned securities
- Advances wherein primary security does not cover the exposure and collateral security is in the form of above-mentioned securities

Advances – Prudential Exposure Norms

Capital Market Exposure (CME)

- Secured / Unsecured advances including guarantees to stock-brokers / market makers
- Loan given to corporate for meeting promoter's contribution to equity of new companies in anticipation of raising resources
- Bridge loan given to companies against expected equity flow / issues
- Underwriting
- Financing stock-brokers for margin trading
- Exposure to VC Funds

Advances – Prudential Exposure Norms

Capital Market Exposure (CME)

Particulars	Remarks
Shareholding in companies directly / indirectly (as owner or by way of pledgee / mortgagee)	30% of paid-up capital of the company or 30% of its own capital, whichever is lower
Overall exposure to capital market in all forms <i>Solo as well as consolidated exposures</i>	40% of own net worth as at last March for all forms 20% of own net worth for <u>direct investments</u> in above mentioned securities and VCs

Advances – Prudential Exposure Norms

Definition of Net Worth

Inclusions	Exclusions
Paid up Capital	Accumulated Losses
Free Reserves	Revaluation Reserve A/C
Credit Balance of P & L	Debit Balance of P & L
Further infusion of capital subsequent to 31 st March can also be reckoned	Intangible Assets
	General or Specific Provision

Advances – Prudential Exposure Norms

How to calculate (Capital) Exposure?

Others	Fully drawn Term Loans
Limits or balance outstanding whichever is higher	Balance Outstanding provided that there is no scope for further draw down
Investments: Exposure to be calculated at Cost Price (irrespective of book value / market value)	

Advances – Prudential Exposure Norms

Financing of Equities

Particulars	Remarks
Advance against shares to individuals	Rs. 10 lakhs if held in physical form
	Rs. 20 lakhs if held in demat form
Financing for subscription to IPO i. Individuals ii. Others (Corporate)	Rs. 10 lakhs Prohibited
Financing employees (other than its own employees) for ESOPs	90% of purchase price or Rs. 20 lakhs, whichever is lower

Advances – Prudential Exposure Norms

Financing of Equities

Particulars	Remarks
Advance against shares to Other borrowers (other than individuals)	Prohibited for NBFC
	Cannot be accepted as primary security
	Can be accepted as collateral
	Should be accepted only in demat form
Bridge Loans	Permitted upto one year in anticipation of expected equity flow / issue

Advances – Prudential Exposure Norms

Financing of Equities

Particulars	Remarks
Advance against shares to Stock Brokers and Market Makers (including funding for Margin Trading)	To be decided on the basis of commercial judgment of the bank
	Prohibition for funding arbitrage operations in stock exchange
Margin on advance against shares / issue of guarantees	Uniform margin of 50%
Guarantees issued for capital market operations	Minimum 25% cash margin within overall 50% margin

Advances – Prudential Exposure Norms

Financing against MFs

Particulars	Remarks
Advance against units of Mutual Funds	Units must be listed or repurchase facility must be available
	Minimum lock-in period is completed
	Amount to be linked to NAV / Repurchase price / market Value whichever is less
Debt Oriented MFs	Margin to be decided by bank in Loan Policy
End-Use	Cannot be to subscribe to another scheme of MFs / purchase of shares / debentures / bonds

Advances – Prudential Exposure Norms

Advances - Restrictions

Particulars	Remarks
Advance against own shares	Prohibited
Loan to Directors of the Bank	Prohibited except for certain types of advances like i. Against FDR, LIP, Govt. Securities ii. Employee loans iii. With prior approval of RBI
Industries producing / consuming Ozone Depleting Substances (ODS)	Prohibited

Advances – Prudential Exposure Norms

Exposure to Unsecured Advances / Guarantees

Particulars	Remarks
Definition	Realisable value of security is less than 10% of the outstanding exposure ab-initio
	Security not to include Intangibles
Definition of Intangibles	Guarantees, Letter of Comforts, Rights, Licenses, authorisations, etc.
Exposure Norms	20% of outstanding Unsecured Guarantees plus total outstanding unsecured advances < 15% of Total Advances

Advances – Prudential Exposure Norms

Gold Loans – Non-agricultural loan against Gold Ornaments / Jewelry

- Maximum amount of exposure: Rs. 2 lakh
- Maximum Tenure of Loan: 12 months
- Bullet payment of interest permitted whereby interest levied monthly but due at the time of maturity
- LTV (Loan to Value) Ratio must be at least 75%
- Security Margin to be predefined
- Account can be NPA even before maturity if security margin not maintained
- Interest to be recognised on collection basis

Fair Practices Code for Lenders

Application and processing of loan

- Application form should be comprehensive
- Transparent disclosure of ...
 - Processing Fees / Charges & Refundable processing fees
 - Prepayment options and charges
 - Penalty for delayed payments
 - Penalty for non-compliances of terms and conditions
 - Conversion charges for switching between fixed and floating rates
- Must be displayed on website of bank
- Loan application to be disposed off within reasonable time
- Reasons for loan application rejection must be conveyed in writing

Fair Practices Code for Lenders

Loan appraisal and terms / conditions

- Proper assessment is mandatory
- Use of margin / security stipulation cannot be substituted to due diligence process
- All terms and conditions to be conveyed in writing to the borrower and his acknowledgement to be taken
- Copy of Loan agreement to all borrowers at the time of sanction / disbursement of loan to be given
- Change in Interest / Charges should be conveyed to borrower and should be applied prospectively
- Sufficient notice be given to borrowers
- In case of take-over of advance by other bank / Financial Institution, the consent / Objection to be conveyed within 21 days

Advances

Balance Sheet Disclosure

Types of Advances

Commonly used terminologies

Appraisal

Documentation

Monitoring of Advances

IRAC Norms

Advances - Documentation

- Loan Agreement / Hypothecation Agreement
- Deed of Guarantee
- Demand Promissory Note
- Continuing Security Bond (CC / OD)
- Acknowledgement of Debts
- Supplementary Deed (enhancement)
- Equitable Mortgage Deed
- General Lien and set-off
- Counter Guarantee (non-fund)

Advances - Documentation

- Mortgage
- Pledge
- Hypothecation
- Assignment
- Set off
- Lien

Advances – Documentation (Mortgage)

Particulars	Remarks
English Mortgage	Property is transferred to mortgagee with a condition that the same will be retransferred back provided loan is repaid before stipulated due date
Equitable Mortgage	Effected by delivery of original title deeds
Examples	Immovable Property

Advances – Documentation

(Pledge / Hypothecation / Assignment / Set off)

Particulars	Examples
Pledge The goods pledged are in possession of the bank	FDR, Gold, NSCs, Stock
Hypothecation Goods are not in possession but bank creates charge over the assets	Stock & book debts Vehicle, P & M
Assignment Only actionable claims are used for assignment	Life Insurance Policies
Set off Right to set off deposit account against Advances	Both should have same holder and rights

Advances – Documentation

(Pledge / Hypothecation / Assignment / Set off)

Type of Security	Remarks
Stock	Hypothecation or pledge
Gold Ornaments	Pledge
Bank's own FDRs	Pledge
Shares / Debentures / Bonds / NSCs / KVPs / IVPs / LIP	Pledge and assignment
Immovable Property	Mortgage

Advances – Documentation (Lien)

Particulars	Examples
General Lien	The right to retain goods / securities unless debt is squared off
Negative Lien	As undertaking given by borrower confirming that the goods / securities will not be hypothecated / pledged unless debt is squared off

Advances – Documentation Terminologies

Particulars	Remarks
Pari Passu	Equal rights
Inter se	Between or amongst themselves <i>(e.g.: Agreement of Consortium will be between the borrower and the lenders and between the lenders inter se)</i>
First Charge	Gives the lender the first call on any funds available from the sale of the property.
Second Charge	Gives lender right to receive remains after the first charge is exercised

Advances

Balance Sheet Disclosure

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Appraisal

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Monitoring of Advances

IRAC Norms

Advances - Monitoring

- Centralised Monitoring Department
- Usage of CAAT Tools
- Generation of Exceptional Reports
- Usage of Exceptional Reports
- Stock Audit / Unit Inspections

Advances

Balance Sheet Disclosure

Types of Advances

Commonly used terminologies

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IRAC Norms

Coverage

- Objective
- Identification of Account as NPA
- Exceptions / Clarifications
- Projects under Implementation
- Asset Classification and Provisioning
- Guidelines on Restructuring of Advances
- Prudential Framework for Resolution of Stressed Assets (RBI Circular dated 07.Jun.2019)
- Points to ponder

RBI Circulars Reference

- Master Circular dated April 01, 2022
(Earlier Master Circular dated October 01, 2021 on IRAC Norms & clarificatory circulars dated November 12, 2021 and February 15, 2022)
- Master Direction – RBI (Relief Measures by Banks in Areas affected by natural calamities) Directions, 2018 dated October 17, 2018

Objective

- The classification of assets of banks has to be done on the basis of objective criteria, which would ensure a uniform and consistent application of the norms.
- The provisioning should be made on the basis of the classification of assets based on the period for which the asset has remained non-performing and the availability of security and the realisable value thereof.

Asset Types

Standard Assets Performing Assets (PA)	Non-Performing Assets (NPAs)
Not Non-Performing	Ceases to generate income
Do not carry risk more than normal banking risk	Higher risk than normal banking risk
Exempted categories to retain status as PA	NPA as per various criteria defined

Criteria for NPA

Loans or Advance	<ul style="list-style-type: none">▪ Interest and/or installment remains overdue for a period of more than 90 days in respect of a term loan.▪ <i>Concession of para 2.1.3 – an account is classified as NPA only if interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter (Upto 31.Mar.2022)</i>
Exceptions	<ul style="list-style-type: none">▪ Loans with moratorium for payment of interest▪ Housing Loan or similar advance to staff

Criteria for NPA

Bills Purchased and discounted	Bill remains overdue for a Discounted period of more than 90 days.
Agricultural Advances	Interest or installment remains overdue for two crop seasons for short duration crop, one crop season for long duration crop.
	<i>*Definitions</i> <i>crop season – ‘period up to harvesting of crops raised’ as determined by SLBC</i> <i>Long duration crop – Crops wherein crop season is more than 12 months</i>

Criteria for NPA

Agricultural Advances	Banks have <u>discretion of rescheduling</u> the agricultural advances <u>in case of natural calamities</u> , which impair repaying capacity
Reference Circulars of Reserve Bank of India	FIDD.CO.Plan.BC.54/04.09.01/ 2014-15 dated April 23, 2015 FIDD.No.FSD.BC.52/ 05.10.001/2014-15 dated March 25, 2015 Master Direction dated July 01, 2016, July 03, 2017, October 17, 2018
FIDD.CO.Plan.BC.54/04.09.01/ 2014-15 dated April 23, 2015	Defines 'Farm Credit'

Criteria for NPA

FIDD.No.FSD.BC.52/ 05.10.001/2014-15
dated March 25, 2015

Guidelines for relief measures by banks in areas affected
by natural calamity

Natural
Calamity

12 types of natural calamities are defined

Institutional
framework

The Banks to have blueprint of action plan with adequate delegation of powers with discretionary powers granted to Divisional / Zonal Managers, to ensure assistance provided without loss of time.

Criteria for NPA

Guidelines for relief measures by banks in areas affected by natural calamity	
Meeting of SLBC / District Consultative Committee	<p><i>Immediate conveying of meeting by:</i></p> <p>If calamity covers entire state SLBC</p> <p>If small part of the state District Consultative Committee</p>
Declaration of natural calamity	<p>Domain of Sovereign (Central / State Government)</p> <p><u>Assessed Crop loss should be 33% or more</u></p>
Restructuring / rescheduling of existing loans	<p>Agricultural Loans</p> <ul style="list-style-type: none"> - Short Term - Long Term <p>Other Loans</p>

Criteria for NPA

Guidelines for relief measures by banks in areas affected by natural calamity

Short Term Agricultural Loans

Eligibility: Loan should not be overdue at the time of occurrence of natural calamity

<i>Crop Loss</i>	<i>Maximum repayment period extension (incl. of moratorium period)</i>
<i>33% to 50%</i>	<i>2 Years</i>
<i>50% or more</i>	<i>5 Years</i>

- Moratorium period – at least 1 year
- Principal and interest due in the year of natural calamity to be converted into Term Loan
- Additional collateral security not to be insisted upon

Criteria for NPA

Guidelines for relief measures by banks in areas affected by natural calamity

Long Term Agricultural Loans

Only Crop for that year is damaged and not the productive assets

- Reschedule installment during the year of natural calamity and extension of loan period by one year
- Willful defaulted installments not eligible for rescheduling
- Payment of interest may be postponed

Productive Assets are damaged (partially / totally)

Repayment period can be restructured provided generally it shouldn't exceed 5 years

Criteria for NPA

Guidelines for relief measures by banks in areas affected by natural calamity

Asset Classification	<ul style="list-style-type: none">- Restructured portion to be considered as current dues- Un-restructured portion to be governed by original terms and conditions- Additional finance to be treated as 'Standard Asset'- Second restructuring would not be considered as 'repeated restructuring'
Insurance Proceeds	To be adjusted against restructured loans wherein fresh loans are granted

Criteria for NPA

Derivative Transaction	Overdue receivables representing positive mark to market value of a derivative contract remaining unpaid for a period of 90 days from specified due date.
Liquidity facility	Remains outstanding for more than 90 days in respect of Securitisation transaction.
Credit Card dues	The minimum amount payable is not paid within 90 days from the next statement date. <i>The reporting to Credit Information Companies (CICs) & levying of penal charges only after 3 days from due date.</i>

Criteria for NPA

Cash Accounts	Credit	If the account is 'out of order'
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Conditions for out of order status

- Outstanding Balance remains continuously in excess of sanctioned limit / drawing power for more than 90 days
- No credit continuously for 90 days as on the date of Balance Sheet (for 90 days as on EoD w.e.f. 12.Nov.21)
- Credits in the account are not sufficient to cover interest debited during the same period

Criteria for NPA

What is 'Overdue'?

If an amount due to bank under any credit facility is not paid on the due date fixed by the bank.

Vital points w.r.t. IRAC Master Circular

Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

A] Appropriate internal systems for proper and timely identification of NPAs (Ref. Circular dated 14.Sep.2020 on automation of IRAC and provisioning process)

B] Credit card charges like penal charges, reporting to Credit Information Companies (CICs) only if credit card account remains 'past due' for more than three days

Vital points w.r.t. IRAC Master Circular

Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

C] Technical write-offs:

*Banks to extinguish all available means of recovery before writing off any account full or partially;
Need to disclose in FS.*

D] NPA Management – Requirement of Effective mechanism & Granular Data

E] Unrealised income represented by FITL:
Corresponding provision as 'Sundry Liabilities Account (Interest Capitalisation)

Vital points w.r.t. IRAC Master Circular

Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

F] Bank Loans for financing Promoters' Contribution: Permitted only to extend finance to 'specialized' entities (which are formed for taking over and turning around troubled entities)

G] Specification of due dates / Repayment date

H] Classification of SMA and NPA

Accounts to be flagged as a part of day-end process

Vital points w.r.t. IRAC Master Circular

Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances - Clarifications

I] Definition of 'out of order'

Changed criteria from 'quarter-end' to '(moving) 90 days'

J] NPA classification in case of interest payments

Para 2.1.3 concession removed and usual 90 days norms to apply

K] Upgradation of accounts classified as NPA

Only when 'entire arrears on interest and principal' are paid by borrower.

Clarity about 'partial recoveries' and 'subsequent recoveries'

Vital points w.r.t. IRAC Master Circular

Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances - Clarifications

L] Income recognition policy for loans with moratorium on payment of interest

Recognition of interest when moratorium of repayment of interest is granted

Sanctioned interest capitalization thus wont affect reversal of interest after NPA as its nature is considered as capital portion

M] Applicability of 'out of order' to all loan products offered as Overdraft including those not meant for business

Vital points w.r.t. IRAC Master Circular

Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances - Clarifications

N] Concept of 'previous 90 days' for determination of 'out of order' status to include the day on which EoD process is run

O] Loan can be upgraded only when entire arrears pertaining to all credit facilities are repaid

Criteria for NPA

Accounts with Temporary Deficiencies

Outstanding Balance in account based on the drawing power calculated from stock statements older than 3 months would be deemed as irregular & if such irregular drawing are permitted for a period of 90 days, account needs to be classified as NPA

Note: The leverage is applicable only for large borrowers

Non-renewal/ Non-regularisation of regular / adhoc limit within 180 days from the due date

Criteria for NPA

Exceptions / Clarifications

- Advances against term deposits, NSCs, IVPs, KVPs and Life Insurance Policies need not be treated as NPAs, till security cover is sufficient to cover outstanding balance.
- Income to be recognised subject to availability of margin

Advance against Gold Ornaments / Government Securities not exempt

Central Government guaranteed advance to be classified as NPA only if Government repudiates the guarantee when invoked.

Criteria for NPA

Exceptions / Clarifications

Classification Qua Borrower

All facilities granted to a borrower shall be treated as NPA & not only that facility which has become irregular

Exception

- (i) Credit facility to Primary Agricultural Credit Society (PACS) and Farmers Service Societies (FSS) under on lending arrangement;
- (ii) Bill Discounted against accepted LC

Criteria for NPA

Exceptions / Clarifications

Consortium Advances

- Member banks shall classify the accounts according to their own record of recovery.
- Bank needs to arrange to get their share of recovery or obtain an express consent from the Lead Bank otherwise the account in such deprived banks might be treated as NPA for non-servicing.

Criteria for NPA

Exceptions / Clarifications

Straightaway Classification (Potential threat of recovery)

- Erosion in Value Where realisable value of security is less than 50% of the value assessed (*by bank or value accepted in last RBI Inspection*), account to be straightaway classified as **Doubtful Asset..**
- Where realisable value (*as assessed by Bank / Valuator / RBI Inspector*) of security is less than 10% of outstanding balance, account to be straightaway classified as **Loss Asset.**

Criteria for NPA

Exceptions / Clarifications

Straightaway Classification (Potential threat of recovery)

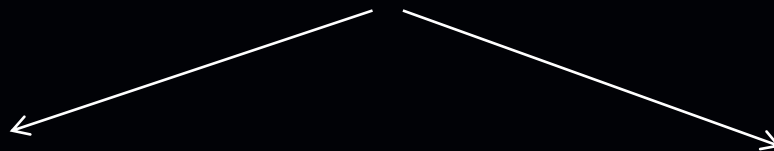
- Fraud
- 100% to be provided irrespective of security spread over 4 quarters commencing from the quarter in which fraud has been detected, provided the unprovided provision is debited to 'Other Reserves'
- If not reported to RBI within timeframe, 100% to be provided instantly

Criteria for NPA

Exceptions / Clarifications

Solitary or few credit entries recorded before Balance Sheet to regularise the account

Whether the account is having inherent weakness?



Yes

No

Mark the account as NPA

The bank to evidence the auditors about manner of regularisation of account

Criteria for NPA

Mandatory Valuation of Securities

Applicable only if balance in NPA is Rs. 5 crores & above

- Annual Stock Audit by external agencies
- Immovable Properties – Valuation to be carried out once in three years by approve valuer

Criteria for NPA

Vital aspects of Asset Classification / Upgradation

- Automation of IRAC and provisioning process in banks (RBI Circular dated 14.Sep.2020) w.e.f. 30.Jun.2021
- Upgradation of NPAs – Criteria
- Upgradation of NPAs
 - Partial Recoveries at cust-id level
 - Subsequent recoveries (after date of Balance Sheet)

Relief for MSME Borrowers

Date of Circular	Details of Circular	PA cut-off date
07.Feb.2018	One time restructuring of MSME Advances	31.Aug.2017
06.Jun.2018	Encouraged formalisation of MSME Sector	
01.Jan.2019	Scheme extended (31.Mar.2020)	01.Jan.2019
11.Feb.2020	Scheme extended (31.Dec.2020)	01.Jan.2020
06.Aug.2020	Scheme extended (31.Mar.2021)	01.Mar.2020
05.May.2021	Scheme extended (30.Sep.2021)	31.Mar.2021

Projects under Implementation

Essentials

Project loan means any term loan which has been extended for the purpose of setting up of an economic venture.

The bank needs to clearly spell out 'Date of Completion' (DC) and 'Date of Commencement of Commercial Operations' (DCCO).

Type of Project Loan:

1. Infrastructure Sector
2. Non-Infrastructure Sector

Projects under Implementation

When not considered as Restructuring?

If *change in repayment schedule* is caused due to increase in project outlay on account of increase in scope and size of the project & following conditions are fulfilled:

1. The increase in scope and size of the project takes place before commencement of commercial operations of the existing project;
2. The rise in cost excluding any cost-overrun in respect of the original project is 25% or more of the original outlay;
3. The bank re-assesses the viability of the project before approving the enhancement of scope and fixing a fresh DCCO;
4. On re-rating, (if already rated) the new rating is not below the previous rating by more than one notch.

Projects under Implementation

Deferment of DCCO

If deferent and consequential shift in repayment schedule is for equal or shorter duration, not considered as restructuring if:

Particulars	Infrastructure	Non-Infrastructure
Revised DCCO is within	Two years from original DCCO	One year from original DCCO
Revision due to Court Case	2 + 2 Years from original DCCO	1 + 1 Years from original DCCO
Revision due to any other reason	2 + 1 Years from original DCCO	

Projects under Implementation

Deferment of DCCO & Retention of Class – Conditions

1. Benefit of asset classification now available to CRE with extension by 1 year as per circular dated 07.Feb.2020
2. Application for restructuring (deferment of DCCO) is received upto to two years from date of original DCCO for Infrastructure and one year w.r.t. non-infrastructure
3. Account needs to be standard
4. If moratorium given for interest, income on accrual can be booked till two years from date of original DCCO for Infrastructure and one year w.r.t. non-infrastructure
5. Additional provision of 5% if extended beyond two years from date of original DCCO for Infrastructure and one year w.r.t. non-infrastructure

Projects under Implementation

Deferment of DCCO & Retention of Class – Conditions

6. Additional provision of sacrifice (diminishing in fair value) for standard assets is required to be made for extension of DCCO
7. In case of Infrastructure projects under implementation, appointed date is shifted due to inability of concession authority to comply requisite conditions, the loan need not be treated as 'restructuring' provided:
 - i. Project should be Public Private Partnership model
 - ii. Loan is not yet disbursed
 - iii. Revised date is documented by way of supplementary agreement
 - iv. Viability to be re-assessed and sanctioned

Projects under Implementation

Retention of Class – Change of Ownership (2+2+2)

Additional extension of DCCO permitted upto 2 years with retention of class subject to:

1. Project is stalled due to inadequacies of the promoters;
2. Change of ownership resulting in high probability of commencement of commercial operations;
3. New promoters need to have sufficient expertise
4. New promoters should own at least 51% of paid up equity
5. Viability of the project to be established
6. Intra-group company take over not eligible

Projects under Implementation

Retention of Class – Change of Ownership (2+2+2)

Additional extension of DCCO permitted upto 2 years with retention of class subject to:

7. Asset classification would be as of reference date (date on which preliminary binding agreement is executed)
8. Take over to be completed within 90 days
9. New promoters to demonstrate commitment by bringing in substantial portion of additional funds
10. Repayment schedule not to exceed beyond 85% of economic life
11. Facility available only once

Projects under Implementation

Retention of Class – Financing of Cost Over-runs

Standby Credit Facility:

1. Sanctioned at the time of initial financial closure
2. Purpose is to fund cost overruns, if required
3. To be disbursed only if cost overruns and not otherwise
4. Subsequent Standby Credit facility permitted if DCCO extended upto 2 / 1 year for infra and non-infra
5. Exemption from definition of restructuring provided:
 - i. Interest during construction due to delay can be funded
 - ii. Other cost overruns limited to 10% of original cost

Projects under Implementation

Retention of Class – Financing of Cost Over-runs

Standby Credit Facility:

5. Exemption from definition of restructuring provided:
 - iii. Debt / Equity Ratio need to be unchanged (promoters to infuse funds)
 - iv. Disbursement only after promoter's contribution
 - v. No other change in terms and conditions
 - vi. 10% cost-over run ceiling is excluding interest but including currency fluctuations

Income Recognition

For NPA accounts income should be recognised on realisation basis.

When an account becomes non-performing, unrealised interest / fees / commission of the previous periods should be reversed or provided.

Interest income on additional finance in NPA account should be recognised on cash basis.

In project loan, funding of interest in respect of NPA if recognised as income, should be fully provided.

If interest due is converted into (unlisted) equity or any other instrument, income recognised should be fully provided (if listed, income recognised to the extent of MV)

Income Recognition

Order of Recovery

Suggested though not mandatory

Unrealised Expenses

Unrealised Interest

Principal Outstanding

Clarification vide Master Circular - in the absence of clear agreement between the Bank and the Borrower, an appropriate policy to be followed in uniform and consistent manner.

Classification Norms

- **Standard Asset**

The account is not non-performing.

- **Sub-Standard Asset**

A sub-standard Asset is one which has remained NPA for a period of less than or equal to 12 months.

- **Loss Assets**

These are accounts, identified by the bank or internal or external auditors or by RBI Inspectors as wholly irrecoverable but the amount for which has not been written off.

Classification Norms

- Doubtful Asset - Three Categories

Category

Period

Doubtful - I

Up to One Year

Doubtful – II

One to Three Years

Doubtful - III

More than Three Years

Provisioning Norms

Primary Responsibility is of the Bank Management and Auditors

Standard Asset

▪Agricultural and SMEs Sectors	0.25%
▪Commercial Real Estate (CRE) Section	1.00%
▪CRE – Residential Housing Project	0.75%
▪Others	0.40%
▪Housing Loan during teaser rate period	2.00%

Provisioning Norms

Sub-standard Asset

- 15% of total outstanding
- 25% of total outstanding if loan is unsecured
- 20% of total outstanding if infrastructure loan provided its backed by escrow facility with first charge

Definition of Secured Loan:

If security is not less than 10% of exposure (funded & non-funded) ab initio

Provisioning Norms

Doubtful Assets:

<u>Period Provision</u>	<u>(Secured + Unsecured)</u>		
Up to 1 year	25%	+	100%
1 to 3 years	40%	+	100%
More than 3 years	100%	+	100%
Loss Asset	100% should be provided for		

**Intangible Security: Considered only if backed by legally enforceable and recoverable right over collection and rest of intangibles like rights, licenses, etc. are considered as 'Unsecured'*

Provisioning Norms

Provisioning for Country Risk

In respect of a country where its net funded exposure is $\geq 1\%$ of its total assets

Risk Category	ECGC Classification	Provision % age*
Insignificant	A1	0.25
Low	A2	0.25
Moderate	B1	5
High	B2	20
Very High	C1	25
Restricted	C2	100
Off-Credit	D	100

*Lower Provision @ 25% w.r.t. short term (180 d) exposures

Provisioning Norms

Provisions under Special Circumstances

Advances guaranteed by CGTMSE / CRGFTLIH / ECGC, Provision should be made only for balance in excess of the amount guaranteed by these corporations

CGTMSE: Credit Guarantee Fund Trust for Micro and Small Enterprises

CRGFTLIH: Credit Risk Guarantee Fund Trust for Low Income Housing

Take Out Finance

Transactions that involve prior commitments shall be governed by the circular DBOD.No.BP.BC.144/21.04.048-2000 dated February 29, 2000 on “Income Recognition, Asset Classification, Provisioning and other related matters and Capital Adequacy Standards – Takeout Finance”.

Other Aspects

Post Shipment Suppliers' Credit

Exim Bank has introduced Guarantee-cum-Refinance Scheme
(Guarantee to settle claim within period of 30 days)

Export Project Finance

The lending bank needs establish through documentary evidence that importer has cleared the dues in full in the bank abroad when its PA

Guidelines on Restructuring of Advances

Categories of Loan which can be restructured

Industrial Units

MSMEs

Industrial Units under
Rehabilitation

All other Advances

Guidelines on Restructuring of Advances

Eligibility

- Any account classified as standard, sub standard or doubtful.
- Restructuring cannot be done retrospectively and usual asset classification norms would continue to apply.
- Restructuring should be subject to customer agreeing to terms and conditions.
- Financial viability should be established.
- Borrowers indulging in frauds and malfeasance are ineligible.
- BIFR cases eligible for restructuring subject to approval from BIFR.

Guidelines on Restructuring of Advances

Stage at which restructuring can take place

Before Commencement of Commercial Production

After commencement of commercial production but
Asset is classified as NPA

After commencement of commercial production but
Asset is PA

Guidelines on Restructuring of Advances

Asset Classification Norms

Standard Asset to be reclassified as SSA

NPA will further slip to lower category as per pre-restructured repayment schedule

All accounts eligible for upgradation after satisfactory performance

Additional finance to be treated as Standard for one year

Guidelines on Restructuring of Advances

Satisfactory Performance

MSME with exposure less than Rs. 25 crores

No payment to remain overdrawn / overdue for period of more than 30 days , during one year from commencement of first payment

Others

No defaults during period from date of implementation of RP upto date of payment of at least 10% of outstanding principal debt

For exposures above Rs. 100 crores (Additional criteria)
Should be at least rated as investment grade (BBB- or better)

Guidelines on Restructuring of Advances

Provisioning Requirements

Normal provision
as per Asset
Classification

Provision for diminution in fair value,
recomputed at each Balance Sheet
date (Sacrifice)
(If loan exposure is less than 1 crore,
provision can be made @ 5%
notionally)

Part D – Annexes denotes the requirement of Sacrifice calculation
though methodology is not defined in Circular

Guidelines on Restructuring of Advances

Calculation of Sacrifice

Discounting Rate =
BPLR / Base Rate +
appropriate Term and
Credit Risk premium on
the date of restructuring
**applicable to borrower
category**

Apply Discounting Rate to future
Cash Inflows of principal and
interest and calculate NPV as
per original and revised
repayment schedules

Total provision not
to exceed 100%

Working Capital Finance
Tenure to be presumed at One Year
for calculation of Sacrifice

Early identification and reporting of stress

SMA Sub-category	<u>TL - Basis for classification</u> Principal / Interest or any other payment overdue partially or wholly for
SMA-0	1 to 30 days
SMA-1	31 to 60 days
SMA-2	61 to 90 days
SMA Sub-category	<u>CC / OD - Basis for classification</u> Outstanding Balance remains continuously in excess of the sanction limit / drawing power, whichever is lower for a period of
SMA-1	31 to 60 days
SMA-2	61 to 90 days

Early identification and reporting of stress

Reporting Requirements to CRILC (Central Repository of Information on Large Credits) Reporting

1. **Applicability: Coverage for Fund and Non-Fund based exposures above Rs. 5 crores excluding crop loans, Inter-Bank / SIDBI / EXIM / NHB / NABARD exposures**
2. **CRILC Main report – Monthly Basis**
3. **CRILC Weekly Reporting (Every Friday) – Defaults by all borrowers above Rs. 5 Crores of exposure**

Applicability of Prudential Framework for Resolution of Stressed Assets

(Ref.: RBI Circular dated June 07, 2019)

(Ref.: Para 9 of RBI Master Circular dated October 01, 2021)

Aggregate Exposure of Borrowers to the lenders	Reference Date
Rs. 2,000 crores and above	Date of these directions
Above Rs. 1,500 crores but below Rs. 2,000 crores	01.Jan.2020
Less than Rs. 1,500 crores	To be announced in due course

Circular dated June 07, 2019

Prudential Framework for Resolution of Stressed Assets

Applicability of guidelines & its purpose

1. Applicable with immediate effect
2. Providing framework for early recognition, reporting and time bound resolution of stressed assets
3. These directions are issued without prejudice to issuance of specific directions, from time to time, by the Reserve Bank to banks, in terms of the provisions of Section 35AA of the Banking Regulation Act, 1949, for initiation of insolvency proceedings against specific borrowers under the Insolvency and Bankruptcy Code, 2016 (IBC)

Circular dated June 07, 2019

Prudential Framework for Resolution of Stressed Assets

Framework

1. Early identification and reporting of stress
2. Implementation of resolution plan
3. Implementation of conditions for RP
4. Delayed implementation of Resolution Plan
5. Prudential Norms
 - a) Supervisory Review
 - b) Disclosures

Early identification and reporting of stress

SMA Sub-category	<u>TL - Basis for classification</u> Principal / Interest or any other payment overdue partially or wholly for
SMA-0	1 to 30 days
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SMA-1	31 to 60 days
SMA-2	61 to 90 days

Circular dated June 07, 2019

Reporting Requirements

1. CRILC Reporting for borrower accounts above Rs. 5 crores
2. CRILC Main report – Monthly Basis
3. CRILC Weekly Reporting (Every Friday) – Defaults by all borrowers above Rs. 5 Crores of exposure

Circular dated June 07, 2019

Implementation of Resolution Plan

1. All lenders must put Board Approved Policy
2. Expected that the lenders initiate the process of implementing Resolution Plan even before a default
3. Once default is reported, “Review Period” of 30 days, wherein lenders may decide on resolution strategy, may choose to initiate legal proceedings for insolvency or recovery.

Circular dated June 07, 2019

Implementation of Resolution Plan

4. If RP is to be implemented, all lenders to sign inter creditor agreement (ICA) during Review Period. Decision to be taken as agreed by lenders representing 75% by value of total outstanding credit facilities (FB+NFB) and 60% of lenders by number.
5. On or after the reference date, resolution plan must be implemented within 180 days from end of review period

Circular dated June 07, 2019

Aggregate Exposure of Borrowers to the lenders	Reference Date
Rs. 2,000 crores and above	Date of these directions
Above Rs. 1,500 crores but below Rs. 2,000 crores	01.Jan.2020
Less than Rs. 1,500 crores	To be announced in due course

Circular dated June 07, 2019

Implementation Conditions for Resolution Plan

1. 1 billion (100 Cr) and above exposure – Independent Credit Evaluation (ICE) of the residual debt by Credit Rating Agencies (CRAs) specifically authorised by RBI for this purpose.
2. 5 billion (500 Cr) and above exposure – Two such Independent Credit Evaluation (ICE) of the residual debt by Credit Rating Agencies (CRAs) specifically authorised by RBI for this purpose.
3. RP is implemented if following conditions are met.

Circular dated June 07, 2019

Conditions for Implementation of Resolution Plan

1. RP Not involving Restructuring / Change in Ownership shall be deemed to be implemented only if the borrower is not in default with any of the lenders as on 180th day from the end of Review Period
2. RP involving Restructuring / Change in Ownership shall be deemed to be implemented only if following conditions are met:
3. All related documentation, creation of security/charge / perfection of security are completed by the lenders

Circular dated June 07, 2019

Conditions for Implementation of Resolution Plan

4. New Capital Structure and changes in terms of conditions of the existing loans gets duly reflected in the books of the lenders and borrower
5. Borrower is not in default with any of the lenders.

Circular dated June 07, 2019

Delayed Implementation of Resolution Plan

Additional Provision Requirement

1. 180 days from end of review period – 20%
2. 365 days from end of commencement of review period:
15%

Overall provision should not exceed 100%

Circular dated June 07, 2019

Prudential Norms

Restructuring is an act in which a lender, for economic or legal reasons relating to the borrower's financial difficulty, grants concessions to the borrower.

Restructuring may involve modification of terms of the advances / securities, which would generally include, among others, alteration of payment period / payable amount / the amount of instalments / rate of interest; roll over of credit facilities; sanction of additional credit facility/ release of additional funds for an account in default to aid curing of default / enhancement of existing credit limits; compromise settlements where time for payment of settlement amount exceeds three months.

Circular dated June 07, 2019

Few examples of Financial Difficulty

1. A default or Borrowers credit facilities are NPA
2. Borrower not in default, but is probable that the borrower will default on any of its exposures in foreseeable future without the concession,
3. Borrowers outstanding securities have been delisted
4. Actual performance vs estimates, cash flows to be assessed insufficient to service all of its loans or debt securities
5. Borrowers existing exposures are categorised as exposures that have already evidenced difficulty in borrowers ability to repay in accordance with banks internal credit rating system

Circular dated June 07, 2019

Asset Classification

On restructuring account will be downgraded from Standard to Substandard. NPAs will remain in same category

Circular dated June 07, 2019

Asset Upgradation

Only when all the outstanding loan / facilities in the account demonstrate 'satisfactory performance' during the period from the date of implementation of RP up to the date by which at least 10% of the sum of outstanding principal debt as per RP and interest capitalisation sanctioned as a part of the restructuring, if any is repaid

(provided that account can not be upgraded before one year from the commencement of the first payment of interest or principal, whichever is later, on the credit facility with longest period of moratorium under the terms of RP)

Circular dated June 07, 2019

Asset Upgradation – Additional conditions

In case of aggregate exposure of Rs. 1 Billion and above

External credit rating of investment grade BBB- or better

In case of aggregate exposure of Rs. 5 Billion and above

Two such external credit ratings of investment grade BBB- or better

On failure to demonstrate satisfactory performance during monitoring period, asset classification upgrade is subjected to fresh restructuring / change of ownership framework as per IBC and additional provision of 15% for such accounts should be made at the end of review period.

Circular dated June 07, 2019

Provisioning Norms

Accounts restructured under the revised framework shall attract provisioning as per the asset classification category as laid out in the Master Circular on Prudential Norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances dated July 1, 2015, as amended from time to time

Master Direction on Transfer of Loan Exposures dated September 24, 2021

Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021

A] Directions to come into immediate effect replacing existing instructions

B] NBV: Funded outstanding in a loan exposure as reduced by specific provision made against such exposure

C] Chapter IV – Transfer of Stressed Loans
C: Transfer of loans to ARCs

Master Direction on Transfer of Loan Exposures dated September 24, 2021

Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021

Para 73: Stressed Loans which are in default for more than 60 days can be transferred

Stressed Loan: Loan exposure that is classified as NPA or SMA

Para 75: If stressed loan is transferred to ARC at price below NBV ... *permitted to use countercyclical or floating provisions*

Master Direction on Transfer of Loan Exposures dated September 24, 2021

Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021

Para 76: If stressed loan is transferred to ARC at price above NBV – reverse excess provision to PL only to the extent of cash received as initial consideration

Para 77: SRs / PTCs to be M2M periodically at NAV

Proviso to Para 77:

(i) Accounting at lower of NBV or NAV

Master Direction on Transfer of Loan Exposures dated September 24, 2021

Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021

Proviso to Para 77:

(ii) when the investment by a transferor in SRs backed by stressed loans transferred by it, is more than 10 percent of all SRs backed by its transferred loans and issued under that securitisation, the valuation of such SRs by the transferor will be additionally subject to a floor of face value of the SRs reduced by the provisioning rate as applicable to the underlying loans, had the loans continued in the books of the transferor.

Master Direction on Transfer of Loan Exposures dated September 24, 2021

Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021

Para 78: SRs/PTCs which are not redeemed as at the end of the resolution period (i.e., five years or eight years as the case may be) shall be treated as loss asset in books of the lenders and fully provided for.

Para 79: Valuation, classification and other norms applicable to Non-SLR instruments applicable

Points to Ponder

Divergences in NPA observed by RBI AFI

Verification Parameters in CBS vis-à-vis RBI Circular

Purity of Master Data in CBS

Reversal of un-serviced Interest of NPA

Availability of valuation of security for advances below 5 crores

Authenticity and regularity of stock statements

Date of NPA – current and prior year of newly identified NPAs

Unique Customer-id of borrower accounts

Accounts upgraded during the year

Regularisation of account subsequent to balance sheet date

Points to Ponder

Accounts other than Advances accounts including Sundries / Suspense Accounts

Accounts transferred to other branches – control over identification / classification of accounts

Income leakages identified and resulting in overdrawing of accounts

Recalculation of Drawing Power

Early Mortality Cases

Ever-greening of accounts

MOCs vis-à-vis Main Audit Report vis-à-vis LFAR



Thank you!

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