FINANCIAL REPORTING & COMPLIANCE

NPAs

WIRC OF ICAI

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Agenda

- Objectives
- Important Circulars
- Identification of Account as NPA
- Exceptions / Clarifications
- Projects under Implementation
- Asset Classification and Provisioning
- Restructuring of Advances (Erstwhile Guidelines)
- **Circular of February 12 2018**
- Some Practical Issues
- Ind AS 109 & Expected Credit Loss

Objectives

- 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.

RBI Circular Reference

- Master Circular dated 1st July 2015 on IRAC Norms. (Divided in three parts)
  - Part A – General Guidelines
  - Part B – Prudential Guidelines on Restructuring
  - Part C – Early recognition of financial distress
- Master Directions
- Relief for MSME Borrowers (07.Feb.2018)
- Resolution of Stressed Asset – Revised Framework – Circular dated February 12, 2018

Asset Type

- STANDARD ASSET / PERFORMING ASSET

  The account is not non-performing and does not carry more than the normal risk attached to the business.

- NON-PERFORMING ASSET (NPA)
  - The asset ceases to generate income for the bank.
  - Higher risk than normal risk attached to business.
  - Non performing as per various criteria for various types of loans.

Identification of Account as NPA

Loans or Advance	▪ Interest and/or installment remains overdue for a period of more than 90 days in respect of a term loan. ▪ **As per 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.**
Exceptions	▪ Loans with moratorium for payment of interest . ▪ Housing Loan or similar advance to staff.

Identification of Account as 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.
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 Account	If the minimum amount due is not paid fully within 90 days from the next statement date. The gap between two statements should not be more than a month.

Identification of Account as NPA …

- **Cash Credit / Overdrafts** $\Rightarrow$ Account remains 'out of order'

The account is treated as 'out of order' if :

- Outstanding Balance remains continuously in excess of sanctioned limit/drawing power (for how many days?) or
- No credit continuously for 90 days as on the date of Balance Sheet or
- Credits in the account are not sufficient to cover interest debited during the same period.

As per 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

Exceptions / Clarifications

Temporary deficiency

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

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.

Exceptions / Clarifications …

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

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

  Exception: Credit facility to Primary Agricultural Credit Society (PACS) and Farmers Service Societies (FSS) under on lending arrangement.

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.

Exceptions / Clarifications …

Solitary Credit Entry

- Care should be taken that a solitary or few credits in the account made at/near the balance sheet date extinguishing the overdue interest/principal is not the only criteria for classifying the asset as standard.

Exceptions / Clarifications…

Regularisation of Account

- Account need not be classified as NPA if account has been regularised by the date of Balance sheet by payment of overdue through genuine sources & not by sanction of additional facility or transfer of funds between accounts.

Relief for MSME Borrowers

- **Circular dated February 07, 2018**

Eligibility:

i) Borrower is classified as MSME under MSMED Act, 2006
ii) Registered under GST as on 31.Jan.2018
iii) Aggregate exposure (FB/NFB) upto Rs. 25 crores
iv) Account is standard as on 31.Aug.2017
v) Applicable only to TLs and not to CC/OD

Relief :

i) '<u>Overdues</u>' as on 01.Sep.17 to be paid not later than 180 days
ii) '<u>Dues</u>' between 01.Sep.17 & 31.Jan.18, to be paid not later than 180 days
iii) Additional provision of 5% against such accounts

Classification-Projects under Implementation

- 'Project Loan' would mean any term loan which has been extended for the purpose of setting up of an economic venture. Banks should fix a Date of Commencement of Commercial Operations (DCCO) for all project loans at the time of sanction of the loan / financial closure.
- For all projects financed by the FIs/ banks **after 28th May, 2002**, the date of completion of the project should be clearly spelt out at the time of financial closure of the project.
- **These asset classification norms would apply to the project loans before commencement of commercial operations.**

Classification - Projects under Implementation…

▪ Infrastructure Sector

- Classify as NPA any time before commencement of commercial operations, if it is 90 days overdue unless restructured and eligible to be classified as standard.

- Classify as NPA if its fails to commence commercial operations within two years from the original DCCO, **even if regular as per record of recovery** unless restructured and eligible to be classified as standard.

Classification - Projects under Implementation…

*If a project loan classified as standard is restructured any time during the period of two years from original DCCO, it can be retained as **standard,** if fresh DCCO is fixed within following limits*

- Court cases : another two years beyond the extended period of two years
- Other reason: another one year beyond the extended period of two years.

Classification - Projects under Implementation…

- ✓ **Other conditions:**
  - ➢ Application for restructuring should be received before the expiry of period of two years from original DCCO.
  - ➢ If there is a moratorium, bank should not recognise income beyond two years from original DCCO.
  - ➢ Bank should maintain necessary provision as long as these are standard assets.

Classification - Projects under Implementation…

- **Non Infrastructure Sector**
  - ✓Classify as NPA any time before commencement of commercial operations, if it is 90 days overdue unless restructured and eligible to be classified as standard.
  - ✓Classify as NPA if its fails to commence commercial operations within one year from the original DCCO, **even if regular as per record of recovery** unless restructured and eligible to be classified as standard.

Classification - Projects under Implementation…

- *If a project loan classified as standard is restructured any time during the period of* ***one year*** *from original DCCO, it can be retained as* ***standard,*** *if fresh DCCO is fixed within following limits*
- Another one year beyond the extended period of one year.

✓Other conditions:

- Application for restructuring should be received before the expiry of period of **one year** from original DCCO.
- If there is a moratorium, bank should not recognise income beyond **one year** from original DCCO.
- Bank should maintain necessary provision as long as these are standard assets.

Classification - Projects under Implementation…

In case of Infrastructure projects under implementation, where appointed date is shifted due to inability of the concession Authority to comply with the requisite conditions, change in DCCO need not be treated as 'restructurung' subject to following :

a) The Project is under ppp model awarded by public authority
b) The loan disbursement is yet to begin
c) The revised date of commencement of commercial operations is documented by way of a supplementary agreement between borrower and lender
d) Project viability has been reassessed and sanction from appropriate authority has been obtained at the time of supplementary agreement.

Classification - Projects under Implementation…

Other Issues:

- *All other aspects of restructuring of project loans before commencement of commercial operations would be governed by Part B of Master Circular*
- **Any change in the repayment schedule of a project loan due to increase in the project outlay would not be treated as restructuring if :**
  - ✓ The increase in scope and size of the project takes place before commencement of commercial operations of the existing project.
  - ✓ The rise in cost excluding any cost-overrun in respect of the original project is 25% or more of the original outlay.
  - ✓ The bank re-assesses the viability of the project before approving the enhancement of scope and fixing a fresh DCCO.
  - ✓ On re-rating, (if already rated) the new rating is not below the previous rating by more than one notch.

Income Recognition

- For NPA accounts income should be recognised on realisation basis.
- When an account becomes non-performing, unrealised interest 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 in respect of NPA is converted into equity or any other instrument, income recognised should be fully provided.

Income Recognition…

Adjustment of Recoveries - *Priority*

Unrealised Expenses

Unrealised Interest

Amount of 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

Exceptions / Clarifications …

Straightaway Classification

- ✓ Where realisable value of security is less than 50% of the value assessed, account to be straightaway classified as Doubtful Asset.
- ✓ Where realisable value of security is less than 10% of outstanding balance, account to be straightaway classified as Loss Asset.

Provisioning Norms

Standard Asset

- Direct advances to Agricultural and SME sector 0.25%
- Commercial Real Estate (CRE) -1%
- CRE Residential Housing Sector(RH) .75%
- Others .40%
- Housing Loans at teaser rates 2 % for one year then
- .40% when the rates are re set at higher rates.

Provisioning Norms…

Sub-standard Asset

- 15% of total outstanding
- 25% of total outstanding if loan is unsecured

✓ ***Unsecured exposure is defined as an exposure where the realizable value of the security as assessed by the bank/approved valuer / RBI inspecting officer is not more than 10% ab initio of the outstanding exposure***

Provisioning Norms…

- Project Loans restructured and other restructured loans with effect from 1st June 2013 (flow) 5.00%
- Stock of Project Loan classified as restructured as on 1st June 2013
- 31-3-14 3.5%
- 31-3-15 4.25%
- 31-3-16 5.00%

Provisioning Norms…

Doubtful Assets:

PeriodProvision	(Secured	+ Unsecured)
Up to 1 year	25%	+ 100%
1to 3 years	40%	+ 100%
More than 3 years	100%	+ 100%

Loss Asset:

100% should be provided for

Banks should have total provisioning coverage ratio of not less than 70% with reference to the gross NPA position in banks as on September 30 2010

Provisioning Norms …

Valuation of Securities

- ✓ In respect of NPAs with the balance of Rs. 5.00 crores & above, bank needs to formulate policy for annual stock audit by external agencies & in respect of immovable properties, valuation to be carried out once in 3 years by approved valuer.

Provisioning Norms …

Provision Under Special Circumstances

- Advance under rehabilitation programme approved by BIFR / Institutions, Provision should be continued to be made on existing facilities.

- Additional facilities no provision for a period of one year.

- In case of advances guaranteed by CGTSI / ECGC, Provision should be made only for balance in excess of the amount guaranteed by these corporations.

Guidelines on Restructuring of Advances (Accounts restructured prior to Feb 12,2018)

- ***Generally Banks have stopped restructuring since asset classification benefit have been withdrawn for all restructuring w.e.f 01/04/2015 (para 30.2 of the Master Circular)***

- Restructuring divided in following four categories:
    i. Industrial Units.

    ii. Industrial Units under CDR Mechanism

    iii. SMEs

    iv. 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.(***new appendix on viability parameters)***
  - ✓ Borrowers indulging in frauds and malfeasance are ineligible.
  - ✓ BIFR cases eligible for restructuring subject to approval from BIFR.

Guidelines on Restructuring of Advances…

- **Asset Classification Norms**
  - ✓ **Restructuring of accounts could take place in following stages:**
    - ∗ Before commencement of commercial production
    - ∗ After commencement of commercial production / operation but before the asset has been classified as ‘Sub Standard’.
    - ∗ After the commencement of commercial production / operation but after the asset has been classified as ‘Sub Standard’ or doubtful.

Guidelines on Restructuring of Advances…

▪ Asset Classification Norms (Cont'd)

- ✓ Standard Asset would get reclassified as sub standard and account which is already NPA would continue to have the same classification.

- ✓ Standard Account classified as NPA and NPA account retained in the same category on restructuring, should be upgraded only when all the outstanding in account perform satisfactorily during ***'specified period'***

- ✓ Additional finance would be treated as standard during specified period. However income should be recognized on cash basis if pre restructuring facilities were classified as NPA.

Guidelines on Restructuring of Advances…

- **Provisioning Norms**
  - ✓ Total provision required would be normal provision plus provision in lieu of diminution in fair value of advances.
  - ✓ Diminution in fair value would be required to be recomputed on each balance sheet date.
  - ✓ Banks have option of notionally computing the diminution in fair value and providing at 5% in case of all restructured accounts where the total dues to bank is less than one crore.

Key Terms relevant for Restructuring

- ✓ Viability parameters
- ✓ Specified period
- ✓ Repeated Restructuring

Framework for Revitalisation of Distressed Assets (Disconinued wef Feb 12 2018)

- Banks are required to identify incipient stress the account by creating three sub category under the Special Mention Account – SMA – 0, SMA – 1, SMA – 2.
- Banks to report SMA Accounts to Central Repository of Information on Large Credits of RBI.
- As soon as an account is reported as SMA 2, Banks have to form Joint Lender's Forum (JLF).

Framework for Revitalisation of Distressed Assets …

- JLF to decide Corrective Action Plan (CAP) which is required to be approved by 75% creditors in value and 50% of creditors in number
- CAP to include
  - **Rectification**
    - Obtain commitment of identifiable cash flows
    - No sacrifice / loss of lenders
    - Additional finance can be provided but no ever-greening of account

Framework for Revitalisation of Distressed Assets …

- **Restructuring**
  - ❑ Provided its prima facie viable and borrower is not willful defaulter
  - ❑ Quick implementation benefits available if the account if the approved package is implemented within 90 days
- **Recovery**
  - ❑ If first two options fail, due recovery process to be resorted

Framework for Revitalisation of Distressed Assets …

- JLF required to arrive at in agreement within 30 days from the reporting of SMA-2.
- Restructuring can either be referred to CDR or done independently by JLF.
- If aggregate exposure of Rs.500 crores above, TEV and Restructuring package will be subjected to evaluation by independent evaluation committee.

Framework for Revitalisation of Distressed Assets …

- While restructuring proposals is under consideration by the JLF/CDR, the usual asset classification norm would continue to apply.
- Accelerated provision in cases where banks fail to report SMS status of the accounts to CRILC.
- Banks would be required to identify directors whose name appear more than once in the list of wilful defaulters as also non cooperative borrowers.
- The provisioning for such cases will be at the rate of 5% if it is a standard account and accelerated provision.

Strategic Debt Restructuring (discontinued wef Feb 12 ,2018)

- This involves initiating of measures such as change of ownership in accounts which failed to achieve the projected viability milestones
- SDR involves measure of converting loan dues into equity shares of the borrower account
- **SDR includes following features:**
  - Initial restructure, JLF must incorporate as part of restructuring conditions to convert entire loan (including unpaid interest), or part thereof, into shares in the company subject to non fulfillment of ' critical conditions'
  - These conditions must be supported by necessary approvals and special resolutions from the borrower company as required and to the extent laws and regulations, to enable lenders to exercise the right
  - Would also be applicable to the accounts which have been restructured before the application of the scheme provided there are necessary enabling clauses in the agreement

Strategic Debt Restructuring

- Such decision should be approved by majority JLF members (minimum 75% by value of creditors and 60% creditors by number)
- Post collection JLF members should collectively hold at least 51% or more of the equity shares
- Share price for conversion as per the method prescribed in para 44 of the Circular
- Henceforth all Banks to include necessary covenants in all loan agreement to include SDR
- The JLF must approve the SDR conversion package within 90 days from the date of deciding to undertake SDR.
- The conversion of debt into equity should be completed within 90 days from the date of approval of SDR package .
- Overall time allowed is 210 days (Cir of Feb 25 2016)

Strategic Debt Restructuring

- Invoking of SDR will not be treated as restructuring
- Asset classification as on reference date to continue for 18 months Thereafter as per the extant IRAC norms
- The bank should consider appointing the suitable professional management to run the affairs of the company
- The lenders should divest their holdings to new promoters within stipulated time of 18 months
- Upon divesting to investor the account may be upgraded to standard, though the amount of provision will not be allowed to be reversed.
- Provision of 15 % would be required to be made in equal instalments over four quarters

Strategic Debt Restructuring

- The above benefit shall be available provided
  - The new promoter does not belong to or is associate of the original promoter group
  - The lenders should divest 26% of the shares of the company to the new promoters within the stipulated time line of 18 months and balance 25% gradually. (If the new promoter is NRI then he should own higher of 26% or applicable foreign investment limit)
- Acquisition of shares will be exempted from regulatory ceiling on Capital Market Exposure and will be assigned 150% risk weight for a period of 18 months
- The conversion though will result into bank holding more than 20 % the accounting standards applicable for such holdings will not be applied

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **Withdrawal of Extant Instructions :**
  1. Corporate Debt Restructuring (CDR) Schemes
  2. Strategic Debt Restructuring (SDR)
  3. Change of ownership outside SDR
  4. S4A
  5. JLF concept stands discontinued

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **Early Identification and Reporting of Stress:**
- Lenders shall identify incipient stress on ***default*** by classifying the stressed asset as special mention account (SMA)

SMA-0	1-30 days
SMA-1	31-60 days
SMA-2	61-90 days

- Lenders to:

❖ Report Central Repository of Information(CRILC) about SMA on all borrower having aggregate exposure of Rs. 5 cr and above on monthly basis from April 1 2018

❖ Report all borrowers in default on a weekly basis at the close of business on every Friday . First such report for the week ending Feb 23, 2018 .

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

Board approved policies for resolution of stressed assets including timelines for resolution:

- On default in borrower entity's account with any lender, all lenders to take steps to cure default by way of Resolution Plan (RP)
- *Resolution plan would involve :*

✓ Regularisation of account by way of overdues repayment

✓ Sale of exposure to other entities / investors

✓ Change in ownership

✓ Restructuring

Documentation of RP mandatory even if there is no change in terms and conditions

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- *RP Shall be deemed to be implemented if:*

1. Borrower is no more in default with any lender
2. If RP involves restructuring:
   a. Documentation must be completed by all lenders
   b. New capital structure / revised terms & conditions of existing loans to get reflected in books of all lenders and borrower
   c. If exposure is Rs. 100 crores and above

      Independent Credit Evaluation (ICE) by Credit Rating Agencies (CRAs) {2 CRAs for exposure above Rs. 500 crores) … rating should be RA4 or better

      (Annexure 2 of the Circular provides various ratings)

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

Timelines for reference to IBC:

- Timelines for implementation of RP for exposures above Rs. 2,000 crores

1. If default as on 01.Mar.2018(reference date), within 180 days from reference date
2. If default after reference date, then within 180 days from such default

If RP is not implemented as above, lenders to file insolvency application within 15 days from date of expiry of 180 days

If RP is implemented, the account should not be in default at any time during 'specified period', otherwise file insolvency application within 15 days from date of default

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **What is specified period ?**

1. Period from date of implementation of RP upto date by which at least 20% of outstanding principal debt as per RP and interest capitalized as per restructuring is repaid
2. Specified period cannot end before one year from commencement of first payment of interest / principal (whichever is later) on credit facility with longest period of moratorium under RP

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

Prudential Norms :

1. Upon restructuring Standard Assets to be classified as Sub Std Asset, thus, no retention of class benefit available
2. Upgradation only if satisfactory performance is demonstrated during specified period.
3. If exposure is above Rs.100 crores, credit rating should be BBB- or above at the end of specified period (Accounts above Rs. 500 crores, would require 2 ratings)
4. Additional Finance to be treated as Standard during specified period, provided the account performs satisfactorily

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- Prudential Norms (Cont'd)

In case of change of ownership:

1. Credit facilities may be continued / upgraded to standard after implementation of change of ownership under RP / IBC subject to following conditions:
   i. *Due Diligence by bank and compliance of section 29A of IBC*
   ii. *New promoter to acquire atleast 26% shares and should be the largest shareholder*
   iii. *New promoter to be in control of borrower entity*
   iv. *Conditions for implementation of RP as per this circular*
2. Continuation in standard category only if satisfactory performance is demonstrated during specified period

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **Sale and Lease back transactions**

To be treated as restructuring if …

1. *Seller is in financial difficulty*
2. *More than 50% revenue of buyer is from leased asset to seller*
3. *25% or more loan by buyer for purchase of asset are funded by lenders of seller*

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **Refinancing Exposure to Borrowers in different currency**
- To be treated as restructuring (if borrower is under financial difficulty) if foreign currency borrowings / export advances for repayment / refinancing of Rupee loans are obtained from:
- Lender who are part of Indian banking system
- With support of Indian banking system in the form of Guarantees / Standby Letter of Credit (SBLC) / LoC / LoU, etc.

Resolution of Stressed Assets – Revised Framework (Circular dt. Feb 12, 2018)

- **Non-applicability of guidelines**
- *Revival and rehabilitation of MSMEs continued to be guided by circular dated March 17, 2016 (having loan limits upto Rs. 25 crores)*
- *Restructuring of loans in the event of a natural calamity shall continue to be as per Master Directions dated July 03, 2017*

IRAC Norms- some Issues

- Divergence in NPA observed by RBI
- Verification of parameters set in the system for classification of account as NPA
- Non reversal of ***total*** interest in account classified as NPA
- Recognition of interest income in NPA A/cs
- Non availability of value of securities in case of NPA below Rs.5 Cr.
- Non submission of Stock Statement by small borrowers.

IRAC Norms- some Issues

- By virtue of reversal of interest, it is found that the account has become NPA in earlier year
- Carry forward of date of NPA
- Branch is located in rented premises and loan is given against this premises. Issue of recovery of interest and principal?
- Classification of accounts transferred from other branches
- NPA regularised after balance sheet date but before signing the accounts

IRAC Norms- some Issues

- Accounts upgraded during the year
- The Detailed Advances statement be tallied with GL, and individual accounts be checked for balances, security value, date of NPA, etc
- Income Leakage- Rate of Interest fed in system is incorrect, DP is wrongly calculated, penal interest not recovered on late submission of Stock statements and Financials etc
- Debit balance in nominal accounts be verified for provisioning
- MOCs be issued for correcting Asset classification, provisioning, income recognition
- Effect of MOCs passed in earlier year/quarter

- **NEW CREDIT IMPAIRED MODEL**

- **Credit loss provisioning approach has now moved from**

- Incurred Loss Model
- Expected Loss Mode

An ECL model will have three primary factors

Unbiased probability weighted amount	Evaluation of range of possible outcomes and consider risk of credit loss even if probability is very low
Present Value	Generally calculated using original EIR or an approximation as discount rate
Cash shortfall	Difference between contractual cash flow and an entity expect it to receive

Concepts while doing ECL model

Term	Description
Probability of default	Estimate of the likelihood of default over a given time horizon
Exposure at default	Estimate of an exposure at a future default date –expected changes in exposure after the reporting date, including repayment of principal and interest, and expected drawdowns on committed facilities
Loss Given Default	Estimate of the loss arising on default. It is based on the difference between contractual cash flows that are due and expected to receive including from collateral. It is generally referred as a percentage of exposure at default
Discount rate	Used to discount an expected loss to a present value at the reporting date using the effective interest rate at initial recognition

Particulars	Stage 1	Stage 2	Stage 3
Also referred as	Performing	Under performing	Non-performing
Credit quality	Not deteriorated significantly since its initial recognition	Deteriorated significantly since its initial recognition	Objective evidence of impairment
Credit risk	Low	Moderate to high	Very High
Recognize	12month ECL	Life time ECL	Life time ECL
ECL	Represents financial asset's life time ECL that are expected to arise from default events that are possible within 12 months	ECL that results from all possible default events over the expected life of an instrument.	
Interest	On gross basis	On gross basis	On net basis(gross carrying value minus loss allowance)
Low credit risk at reporting date	Assumed that risk has not increased significantly, hence apply 12 month ECL		

NEW CREDIT IMPAIRED MODEL

SIGNIFICANT INCREASE IN CREDIT RISK AS COMPARED TO ITS INITIAL RECOGNITION – INDICATORS

- Changes in general economic or market conditions, for example, adverse policy adoption by overseas companies which may affect IT services offered by Indian companies
- Significant changes in financial position or operating results of a borrower
- Changes in financial support from parent or group companies
- Expected or potential breaches of covenants
- Expected delay in payment

NEW CREDIT IMPAIRED MODEL

SIGNIFICANT INCREASE IN THE CREDIT RISK

- A rebuttable presumption that the credit risk of a financial asset has increased significantly since its initial recognition, where contractual payments are more than 30 days past due.
- It is a matter of debate and judgement that even after past due 30 days how can there be no significant increase in credit risk.

The reasonable and sufficient information can be reflected in a better way by doing an assessment of following -

- Past trends (history) and current situation correlation
- Getting adequate understanding by ensuring liquidity situation of a borrower
- Quick review of borrowers' business condition assessment such as sales, purchase, inventory situation
- Comfort from borrower's banker about its facilities and payment on other borrowings
- Analysis of recent events which may affect borrower's business adversely

Thank you!