Updating the courseware for CAIIB Main subjects--- ABM--- Credit Management

Chapter 26 Overview of Credit Management

(1) Priority Sector Lending- Targets and Classification

RBI makes changes in the targets and classification of priority sector lending as and when the changing social/economic conditions demand so. The latest position is given in the **Master Circular DCBR.BPD.(PCB).MC.No:11/09.09.001/2015-16 dated July 1, 2015.** The salient features are as under:

No loan related and ad-hoc service charges/inspection charges should be levied on priority sector loans up to Rs. 25,000. In the case of eligible priority sector loans to SHGs/ JLGs, this limit will be applicable per member and not to the group as a whole.

The target is mentioned as a percentage of Adjusted Net Bank Credit (ANBC) (total loans and advance minus bills rediscounted with RBI and other Financial Institutions plus investments made after August 30, 2007 in non-SLR bonds under HTM category) or Credit Equivalent Amount of Off-Balance Sheet Exposure (OBE), whichever is higher as on March 31 of the previous year.

The overall target is 40% for domestic banks and foreign banks. Foreign banks with less than 20 branches have to achieve this in a phased manner within 2020..Foreign banks with 20 branches and above have to achieve the Total Priority Sector Target within a maximum period of five years starting from April 1, 2013 and ending on March 31, 2018.

There are sub-targets, within the overall target, for Agriculture (18%), Micro-enterprises (7.5 %) (7% by March 2016 and 7.5% by March 2017) and Weaker sections (10%).

Detailed description of activities eligible to be classified as priority sector are given in the above mentioned circular. Some of such activities/loans are given below.

Loans to individuals for educational purposes for studies in India including vocational courses up to Rs. 10 lakh will be considered as eligible for priority sector.

Bank loans up to a limit of Rs.5 crore per borrower for building social infrastructure for activities namely schools, health care facilities, drinking water facilities and sanitation facilities including construction/ refurbishment of household toilets and household level water improvements in Tier II to Tier VI centers and bank credit to Micro Finance Institutions (MFIs) extended for on-

lending to individuals and also to members of SHGs/JLGs for water and sanitation facilities, will be eligible for categorization as priority sector under 'Social Infrastructure', subject to certain conditions.

The following are also eligible to be considered for priority sector:

i. Bank loans up to a limit of Rs. 15 crore to borrowers for purposes like solar based power generators, biomass based power generators, wind mills, micro-hydel plants and for non-conventional energy based public utilities *viz.* street lighting systems, and remote village electrification. For individual households, the loan limit will be Rs. 10 lakh per borrower.

ii. Loans not exceeding Rs. 50,000/- per borrower provided directly by banks to individuals and their SHG/JLG, provided the individual borrower's household annual income in rural areas does not exceed Rs.100,000/- and for non-rural areas it does not exceed Rs. 1,60,000/-.

iii. Loans to distressed persons [other than farmers included under III (1.1) A (v)] not exceeding Rs. 100,000/- per borrower to prepay their debt to non-institutional lenders.

iv. Loans sanctioned to State Sponsored Organizations for Scheduled Castes/ Scheduled Tribes for the specific purpose of purchase and supply of inputs and/or the marketing of the outputs of the beneficiaries of these organizations.

Overdraft in PMJDY accounts: Overdrafts extended by banks upto Rs. 5,000/- in Pradhan Mantri Jan-Dhan Yojana (PMJDY) accounts will be eligible for classification under priority sector advances ('others' category) as also weaker sections, provided the borrower's household annual income does not exceed Rs. 60,000/- for rural areas and Rs.1,20,000/- for non-rural areas.

(2) Streamlining flow of credit to Micro and Small Enterprises (MSEs)

(Details in RBI circular dated August 27, 2015)

Micro and small units are more prone to facing financial difficulties during their Life Cycle than large enterprises / corporates when the business conditions turn adverse. Absence of timely support at such a juncture could lead to the unit turning sick and many a times irreversibly. Accordingly, banks have been advised to put in place Board approved policy on lending to MSEs, adopting an appropriate system of timely and adequate credit delivery to borrowers in the MSE segment within the broad prudential regulations of Reserve Bank of India. Banks are also advised to ensure that their lending policies for MSEs are streamlined and made flexible in order

to empower the officials concerned to take quick decisions on credit delivery to MSEs. .On August 27, 2015, RBI advised the banks to review their lending policies and mayadopt the following measures so as to facilitate timely and adequate availability of credit to viable MSE borrowers especiallywhen they are in need of fundsduring unforeseen circumstances.

i) Standby Credit Facility – Banks are allowed, at the time of sanction of project loans, to sanction a 'standby credit facility' to fund unforeseen project cost overruns, if needed. Such 'standby credit facilities' are sanctioned at the time of initial financial closure; but disbursed only when there is a cost overrun. At the time of credit assessment of borrowers / project, such cost overruns are also taken into account while determining viability and repayment ability of the borrower. Banks may, as part of their lending policy to MSEs, consider a similar approach of providing a 'standby credit facility', while funding capital expenditure, to fund unforeseen increases in capital expenditure. Further, at the discretion of banks, such 'standby credit facility' may also be sanctioned to fund periodic capital expenditure. The objective of such 'standby credit facility' would be, among others, to extend credit speedily so that the capital asset creation is not delayed and commercial production can commence at the earliest.

ii) Working Capital Limits –Banks may also incorporate, in their lending policy to MSEs, a policy for fixing a separate additional limit, at the time of sanction / renewal of working capital limits, specifically for meeting the temporary rise in working capital requirements arising mainly due to unforeseen / seasonal increase in demand for products produced by them. Such limits may be released primarily, where there is sufficient evidence of increase in the demand for products produced by MSEs. Banks may also sanction ad-hoc limits subject to the extant prudential norms, to be regularized not later than three months from the date of sanction.

iii) Review of Regular Working Capital Limits –Banks review working capital limits at least once in a year based on audited financial statements. However, audited financial statements of MSE units would ordinarily be available with a time lag, post-closing of the financial year. In such cases and where banks are convinced that changes in the demand pattern of MSE borrowers require a mid-term review, they may do so. Such mid-term reviews may be based on an assessment of sales performance of the MSEs since last review without waiting for audited financial statements. However, such mid-term reviews shall be revalidated during the subsequent regular review based on audited financial statements.

iv) Timelines for Credit Decisions – Timely credit is critical to the growth of a healthy MSE sector. Towards this Reserve Bank has issued several guidelines. On May 9, 2013, banks were advised to put in place a structured monitoring mechanism for holistic monitoring of all credit related matters, pertaining to MSE Sector. Banks were also advised to have a Credit Proposal Tracking System (CPTS) with a view to closely track the applications and ensure speedy disposal. Further, 'Guidelines on Fair Practices Code for Lenders', advised that the time frame within which loan applications up to Rs.2 lakh will be disposed of should be indicated at the time of acceptance of loan applications. Banks were also advised that they should clearly delineate the procedure for disposal of loan proposals, with appropriate timelines, and institute a suitable monitoring mechanism for reviewing applications pending beyond the specified period, without any compromise on due diligence requirements. Banks are also required to make suitable disclosures on the timelines for conveying credit decisions through their websites, notice-boards, product literature, etc. RBI has now advised the banks that the above systems should be put in place with regard to credit facilities (regular, additional / ad-hoc credit facilities and restructuring of accounts, if considered viable) for MSE borrowers.

(3) Common guidelines / instructions for lending to MSME sector (Details in Master Circular dated July 1, 2015)

1 Issue of Acknowledgement of Loan Applications to MSME borrowers

Banks have been advised to mandatorily acknowledge all loan applications, submitted manually or online, by their MSME borrowers and ensure that a running serial number is recorded on the application form as well as on the acknowledgement receipt. Banks are further encouraged to start Central Registration of loan applications. The same technology may be used for online submission of loan applications as also for online tracking of loan applications.

2 Collateral

Banks are mandated not to accept collateral security in the case of loans up to Rs.10 lakh extended to units in the MSE sector. Banks are also advised to extend collateral-free loans up to Rs. 10 lakh to all units financed under the Prime Minister Employment Generation Programme (PMEGP) administered by KVIC.

Banks may, on the basis of good track record and financial position of the MSE units, increase the limit to dispense with the collateral requirement for loans up to Rs.25 lakh (with the approval of the appropriate authority).

Banks are advised to strongly encourage their branch level functionaries to avail of the Credit Guarantee Scheme cover, including making performance in this regard a criterion in the evaluation of their field staff.

3 Composite loan

A composite loan limit of Rs.1 crore can be sanctioned by banks to enable the MSE entrepreneurs to avail of their working capital and term loan requirement through Single Window.

4 Specialised MSME branches

Public sector banks have been advised to open at least one specialised branch in each district. Further, banks have been permitted to categorise their general banking branches having 60% or more of their advances to MSME sector as specialized MSME branches in order to encourage them to open more specialised MSME branches for providing better service to this sector as a whole. As per the policy package announced by the Government of India for stepping up credit to MSME sector, the public sector banks will ensure specialized MSME branches in identified clusters/centers with preponderance of small enterprises to enable the entrepreneurs to have easy access to the bank credit and to equip bank personnel to develop requisite expertise. The existing specialised SSI branches, if any, may also be redesignated as MSME branches. Though their core competence will be utilized for extending finance and other services to MSME sector, they will have operational flexibility to extend finance/render other services to other sectors/borrowers.

5 Delayed Payments

Under the Amendment Act, 1998 of Interest on Delayed Payment to Small Scale and Ancillary Industrial Undertakings, penal provisions have been incorporated to take care of delayed payments to MSME units. After the enactment of the Micro, Small and Medium Enterprises Development (MSMED), Act 2006, the existing provisions of the Interest on Delayed Payment Act, 1998 to Small Scale and Ancillary Industrial Undertakings, have been strengthened as under:

(i) The buyer has to make payment to the supplier on or before the date agreed upon between him and the supplier in writing or, in case of no agreement, before the appointed day. The period agreed upon between the supplier and the buyer shall not exceed forty five days from the date of acceptance or the day of deemed acceptance.

(ii) In case the buyer fails to make payment of the amount to the supplier, he shall be liable to pay compound interest with monthly rests to the supplier on the amount from the appointed day or, on the date agreed on, at three times of the Bank Rate notified by Reserve Bank.

(iii) For any goods supplied or services rendered by the supplier, the buyer shall be liable to pay the interest as advised at (ii) above.

(iv) In case of dispute with regard to any amount due, a reference shall be made to the Micro and Small Enterprises Facilitation Council, constituted by the respective State Government.

Further, banks have been advised to fix sub-limits within the overall working capital limits to the large borrowers specifically for meeting the payment obligation in respect of purchases from MSMEs.

6 Revised Guidelines for Rehabilitation of Sick Micro and Small Enterprises

In view of the recommendations of Working Group on rehabilitation of potentially viable sick units (Chairman: Dr. K. C. Chakrabarty), regarding changing the definition of sickness and the procedure for assessing the viability of sick MSE units, a Committee was set up by the Ministry of MSME to look into the issue. Based on the recommendation of the Committee, revised guidelines for rehabilitation of sick units in the MSE sector have been issued vide RBI circular dated November 1, 2012.

The objective of the revised guidelines is to hasten the process of identification of a unit as sick, early detection of incipient sickness, and to lay down a procedure to be adopted by banks before declaring a unit as unviable.

As per the new guidelines, a Micro or Small Enterprise (as defined in the MSMED Act 2006) may be said to have become Sick, if (a) any of the borrowal account of the enterprise remains NPA for three months or more OR (b) there is erosion in the net worth due to accumulated losses to the extent of 50% of its net worth during the previous accounting year.

The revised guidelines also provide the procedures to be adopted by the banks before declaring any unit as unviable. Banks have been advised that the decision on viability of the unit should be taken at the earliest but not later than 3 months of becoming sick under any circumstances and

the rehabilitation package should be fully implemented within six months from the date the unit is declared as 'potentially viable' / 'viable'.

7 Micro and Small Enterprises Sector – Financial Literacy and consultancy support

Keeping in view the high extent of financial exclusion in the MSME sector, it is imperative for banks that the excluded units are brought within the fold of the formal banking sector. The lack of financial literacy, operational skills, including accounting and finance, business planning etc. represent formidable challenge for MSE borrowers underscoring the need for facilitation by banks in these critical financial areas. Moreover, MSE enterprises are further handicapped in this regard by absence of scale and size. To effectively and decisively address these handicaps, Scheduled commercial banks have been advised vide RBI circular dated August 1, 2012, that the banks could either separately set up special cells at their branches, or vertically integrate this function in the Financial Literacy Centers (FLCs) set up by them, as per their comparative advantage. The bank staff should also be trained through customised training programs to meet the specific needs of the sector.

8 Structured Mechanism for monitoring the credit growth to the MSE sector

In view of the concerns emerging from the deceleration in credit growth to the MSE sector, an Indian Banking Association (IBA)-led Sub-Committee (Chairman: Shri K.R. Kamath) was set up to suggest a structured mechanism to be put in place by banks to monitor the entire gamut of credit related issues pertaining to the sector. Based on the recommendations of the Committee, banks have been advised to:

- strengthen their existing systems of monitoring credit growth to the sector and put in place a system-driven comprehensive performance management information system (MIS) at every supervisory level (branch, region, zone, head office) which should be critically evaluated on a regular basis;
- put in place a system of e-tracking of MSE loan applications and monitor the loan application disposal process in banks, giving branch-wise, region-wise, zone-wise and State-wise positions. The position in this regard is to be displayed by banks on their websites; and
- monitor timely rehabilitation of sick MSE units. The progress in rehabilitation of sick MSE units is to be made available on the website of banks.

Detailed guidelines have been issued to the scheduled commercial banks vide RBI circular dated May 9, 2013.

9 Revised General Credit Card (GCC) Scheme

In order to enhance the coverage of GCC Scheme to ensure greater credit linkage for all productive activities within the overall Priority Sector guidelines and to capture all credit extended by banks to individuals for non-farm entrepreneurial activity, the GCC guidelines have been revised on December 2, 2013.

10 State Level Inter Institutional Committee (SLIIC)

In order to deal with the problems of co-ordination for rehabilitation of sick micro and small units, State Level Inter-Institutional Committees were set up in the States. However, the matter of continuation or otherwise, of the SLIIC Forum has been left to the individual States / Union Territory. The meetings of these Committees are convened by Regional Offices of RBI and presided over by the Secretary, Industry of the concerned State Government. It provides a useful forum for adequate interfacing between the State Government Officials and State Level Institutions on the one side and the term lending institutions and banks on the other. It closely monitors timely sanction of working capital to units which have been provided term loans by SFCs, implementation of special schemes such as Margin Money Scheme of State Government and reviews general problems faced by industries and sickness in MSE sector based on the data furnished by banks. Among others, the representatives of the local state level MSE associations are invited to the meetings of SLIIC which are held quarterly. A sub-committee of SLIIC looks into the problems of individual sick MSE unit and submits its recommendations to the forum of SLIIC for consideration.

11 Empowered Committee on MSMEs

Empowered Committees on MSMEs have been constituted under the Chairmanship of the Regional Directors with the representatives of SLBC Convenor, senior level officers from two banks having predominant share in MSME financing in the state, representative of SIDBI Regional Office, the Director of Industries of the State Government, one or two senior level representatives from the MSME Associations in the state, and a senior level officer from SFC/SIDC as members. The Committee will meet periodically and review the progress in MSME financing as also rehabilitation of sick Micro, Small and Medium units. It will also

coordinate with other banks/financial institutions and the state government in removing bottlenecks, if any, to ensure smooth flow of credit to the sector. The committees may decide the need to have similar committees at cluster/district levels.

12 Debt Restructuring Mechanisms for MSMEs

(i) Prudential Guidelines on SME Debt Restructuring by banks have been advised to l banks by RBI vide circular dated August 27,2006, read with circular dated May 30, 2013 and DBOD Mail Box clarification dated June 6, 2013 and March 30, 2015 and the subsequent guidelines on Restructuring of Advances by banks issued from time to time.

(ii) In the light of the recommendations of the Working Group on Rehabilitation of Sick MSEs (Chairman: Dr. K.C. Chakrabarty), banks were advised vide RBI circular dated May 4, 2009 to:

(a) put in place loan policies governing extension of credit facilities, Restructuring/Rehabilitation policy for revival of potentially viable sick units/enterprises and non- discretionary One Time Settlement scheme for recovery of non-performing loans for the MSE sector, with the approval of the Board of Directors and

(b) implement recommendations with regard to timely and adequate flow of credit to the MSE sector.

(iii) Banks have been advised to give wide publicity to the One Time settlement scheme implemented by them, by placing it on the bank's website and through other possible modes of dissemination. They may allow reasonable time to the borrowers to submit the application and also make payment of the dues in order to extend the benefits of the scheme to eligible borrowers.

13 Cluster Approach

All SLBC Convenor banks have been advised to incorporate in their Annual Credit Plans, the credit requirement in the clusters identified by the Ministry of Micro, Small and Medium Enterprises, Government of India.

(i) As per Ganguly Committee recommendations (September 4, 2004), banks have been advised that a full-service approach to cater to the diverse needs of the SSI sector (now MSE sector) may be achieved through extending banking services to recognized MSE clusters by adopting a 4-C approach namely, Customer focus, Cost control, Cross sell and Contain risk. A cluster based approach to lending may be more beneficial:

(a) in dealing with well-defined and recognized groups;
(b) availability of appropriate information for risk assessment and
(c) monitoring by the lending institutions.

Clusters may be identified based on factors such as trade record, competitiveness and growth prospects and/or other cluster specific data.

14 Scheme of Small Enterprises Financial Centers (SEFCs):

A scheme for strategic alliance between branches of banks and SIDBI located in clusters, named as "Small Enterprises Financial Centers" has been formulated.

15 Credit Linked Capital Subsidy Scheme (CLSS)

Government of India, Ministry of Micro, Small and Medium Enterprises has conveyed their approval for continuation of the Credit Linked Capital Subsidy Scheme (CLSS) for Technology Upgradation of Micro and Small Enterprises from X Plan to XI Plan (2007-12) subject to the following terms and conditions:

(i) Ceiling on the loan under the scheme is Rs.1 crore.

(ii) The rate of subsidy is 15% for all units of micro and small enterprises up to loan ceiling at Sr. No. (i) above.

(iii) Calculation of admissible subsidy will be done with reference to the purchase price of plant and machinery instead of term loan disbursed to the beneficiary unit.

(iv) SIDBI and NABARD will continue to be implementing agencies of the scheme.

16 Banking Codes and Standard Board of India (BCSBI)

The Banking Codes and Standard Board of India (BCSBI) has formulated a Code of Bank's Commitment to Micro and Small Enterprises. This is a voluntary Code, which sets minimum standards of banking practices for banks to follow when they are dealing with Micro and Small Enterprises (MSEs) as defined in the Micro Small and Medium Enterprises Development (MSMED) Act, 2006. It provides protection to MSE and explains how banks are expected to deal with MSE for their day to-day operations and in times of financial difficulty. The Code does not replace or supersede regulatory or supervisory instructions issued by the Reserve Bank of India (RBI) and banks will comply with such instructions /directions issued by the RBI from time to time.

(4) Interest Rates on Advances

In order to improve the efficiency of monetary policy transmission, the Reserve Bank, through its circular dated December 17, 2015, has decided that banks shall follow the following guidelines for pricing their advances:

a) Internal Benchmark

i. All rupee loans sanctioned and credit limits renewed w.e.f. April 1, 2016 will be priced with reference to the **Marginal Cost of Funds based Lending Rate (MCLR)** which will be the internal benchmark for such purposes.

ii. The MCLR will comprise of:

a. Marginal cost of funds;
b. Negative carry on account of CRR;
c. Operating costs;
d. Tenor premium.

a. Marginal Cost of funds: The marginal cost of funds will comprise of Marginal cost of borrowings and return on networth. RBI has given the detailed methodology for computing marginal cost of funds in its circular.

b. Negative Carry on CRR: Negative carry on the mandatory CRR which arises due to return on CRR balances being nil, will be calculated as under:

Required CRR x (marginal cost) / (1- CRR)

The marginal cost of funds arrived at (a) above will be used for arriving at negative carry on CRR.

c. Operating Costs

All operating costs associated with providing the loan product including cost of raising funds will be included under this head. It should be ensured that the costs of providing those services which are separately recovered by way of service charges do not form part of this component.

d. Tenor premium

These costs arise from loan commitments with longer tenor. The change in tenor premium should not be borrower specific or loan class specific. In other words, the tenor premium will be uniform for all types of loans for a given residual tenor.

iii. Since MCLR will be a tenor linked benchmark, banks shall arrive at the MCLR of a particular maturity by adding the corresponding tenor premium to the sum of Marginal cost of funds, Negative carry on account of CRR and Operating costs.

iv. Accordingly, banks shall publish the internal benchmark for the following maturities:

a. overnight MCLR,
b. one-month MCLR,
c. three-month MCLR,
d. six month MCLR,
e. One year MCLR.

In addition to the above, banks have the option of publishing MCLR of any other longer maturity.

b) Spread

i. Banks should have a Board approved policy delineating the components of spread charged to a customer. The policy shall include principles:

a. To determine the quantum of each component of spread.
b. To determine the range of spread for a given category of borrower / type of loan.
c. To delegate powers in respect of loan pricing.

ii. For the sake of uniformity in these components, all banks shall adopt the following broad components of spread:

a. Business strategy

The component will be arrived at taking into consideration the business strategy, market competition, embedded options in the loan product, market liquidity of the loan etc.

b. Credit risk premium

The credit risk premium charged to the customer representing the default risk arising from loan sanctioned should be arrived at based on an appropriate credit risk rating/scoring model and after taking into consideration customer relationship, expected losses, collaterals, etc.

iii. The spread charged to an existing borrower should not be increased except on account of deterioration in the credit risk profile of the customer. Any such decision regarding change in spread on account of change in credit risk profile should be supported by a full-fledged risk profile review of the customer.

iv. The stipulation contained in sub-paragraph (iii) above is, however, not applicable to loans under consortium / multiple banking arrangements.

c) Interest Rates on Loans

i. Actual lending rates will be determined by adding the components of spread to the MCLR. Accordingly, there will be no lending below the MCLR of a particular maturity for all loans linked to that benchmark

ii. The reference benchmark rate used for pricing the loans should form part of the terms of the loan contract.

d) Exemptions from MCLR

i. Loans covered by schemes specially formulated by Government of India wherein banks have to charge interest rates as per the scheme, are exempted from being linked to MCLR as the benchmark for determining interest rate.

ii. Working Capital Term Loan (WCTL), Funded Interest Term Loan (FITL), etc. granted as part of the rectification/restructuring package, are exempted from being linked to MCLR as the benchmark for determining interest rate.

iii. Loans granted under various refinance schemes formulated by Government of India or any Government Undertakings wherein banks charge interest at the rates prescribed under the schemes to the extent refinance is available are exempted from being linked to MCLR as the benchmark for determining interest rate. Interest rate charged on the part not covered under refinance should adhere to the MCLR guidelines.

iv. The following categories of loans can be priced **without** being linked to MCLR as the benchmark for determining interest rate:

(a) Advances to banks' depositors against their own deposits.

(b) Advances to banks' own employees including retired employees.

(c) Advances granted to the Chief Executive Officer / Whole Time Directors.

(d) Loans linked to a market determined external benchmark.

(e) Fixed rate loans granted by banks. However, in case of hybrid loans where the interest rates are partly fixed and partly floating, interest rate on the floating portion should adhere to the MCLR guidelines.

e) Review of MCLR

i. Banks shall review and publish their **Marginal Cost of Funds based Lending Rate (MCLR)** of different maturities every month on a pre-announced date with the approval of the Board or any other committee to which powers have been delegated.

ii. However, banks which do not have adequate systems to carry out the review of MCLR on a monthly basis, may review their rates once a quarter on a pre-announced date for the first one year i.e. upto March 31, 2017. Thereafter, such banks should adopt the monthly review of MCLR as mentioned in (i) above.

f) Reset of interest rates

i. Banks may specify interest reset dates on their floating rate loans. Banks will have the option to offer loans with reset dates linked either to the date of sanction of the loan/credit limits or to the date of review of MCLR.

ii. The Marginal Cost of Funds based Lending Rate (MCLR) prevailing on the day the loan is sanctioned will be applicable till the next reset date, irrespective of the changes in the benchmark during the interim.

iii. The periodicity of reset shall be one year or lower. The exact periodicity of reset shall form part of the terms of the loan contract.

g) Treatment of interest rates linked to Base Rate charged to existing borrowers

i. Existing loans and credit limits linked to the Base Rate may continue till repayment or renewal, as the case may be.

ii. Banks will continue to review and publish Base Rate as hitherto.

iii. Existing borrowers will also have the option to move to the Marginal Cost of Funds based Lending Rate (MCLR) linked loan at mutually acceptable terms. However, this should not be treated as a foreclosure of existing facility.

(5) Foreign Currency Convertible Bonds (FCCBs) and Foreign Currency Exchangeable Bonds (FCEBs)

FCCBs are foreign currency denominated instruments which should be issued in accordance with the Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993 as amended from time to time. FCEBs should be issued in accordance with the Issue of Foreign Currency Exchangeable Bonds Scheme, 2008. The principal and interest in respect of these bonds are payable in foreign currency and these are

convertible into ordinary shares of the issuing company or the offered company, as the case may be, in any manner, either in whole, or in part, on the basis of any equity related warrants attached to debt instruments. An Indian company, which is not eligible to raise funds from the Indian securities market, including a company which has been restrained from accessing the securities market by the Securities and Exchange Board of India (SEBI) shall not be eligible to issue FCCBs/FCEBs. In addition to various provisions listed below, FCCBs and FCEBs should also conform to applicable Regulations of Foreign Exchange Management

(6) External Commercial Borrowings (ECB)

ECBs are borrowings raised by permitted resident entities from recognised non-resident entities. Borrowings raised under the ECB framework can have one of the following forms:

i. Bank loans;
ii. Securitized instruments (e.g. floating rate notes and fixed rate bonds, non-convertible, optionally convertible or partially convertible preference shares / debentures);
iii. Buyers' credit;
iv. Suppliers' credit;
v. Foreign Currency Convertible Bonds (FCCBs);
vi. Financial Lease; and
vii. Foreign Currency Exchangeable Bonds (FCEBs)

While the first six forms of borrowing can be availed of both under the automatic and approval routes, FCEBs can be issued only under the approval route.

Individual Limits

The individual limits of ECB that can be raised by eligible entities under the automatic route per financial year for all the three tracks are set out as under:

a. Up to USD 750 million or equivalent for the companies in infrastructure and manufacturing sectors;
b. Up to USD 200 million or equivalent for companies in software development sector;
c. Up to USD 100 million or equivalent for entities engaged in micro finance activities; and
d. Up to 500 million or equivalent for remaining entities.

Minimum Average Maturity (MAM) Period

The minimum average maturity is 3 years for ECB up to USD 50 million or its equivalent and 5 years for ECB beyond USD 50 million or its equivalent. For certain category of companies, it is 10 years irrespective of the amount.

Revised Framework on ECB is detailed in RBI Notification Dt March 30,2016. Which may be read with any further Notifications from time to time.

(7) Issuance of Rupee denominated bonds overseas

In order to facilitate Rupee denominated borrowing from overseas, RBI has put in place a framework for issuance of Rupee denominated bonds overseas within the overarching ECB policy. The broad contours of the framework are as follows:

i. **Eligible borrowers:** Any corporate or body corporate as well as Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs).
ii. **Recognised investors:** Any investor from a Financial Action Task Force (FATF) compliant jurisdiction.
iii. **Maturity:** Minimum maturity period of 5 years.
iv. **All-in-cost:** All in cost should be commensurate with prevailing market conditions.
v. **Amount:** As per extant ECB policy.
vi. **End-uses:** No end-use restrictions except for a negative list.

(8) Restrictions under Section 20 of the Banking Regulation Act, 1949 – Loans to Directors

(Details in RBI circular dated September 16, 2015)

Section 20 of Banking Regulation Act, 1949 (B.R. Act, 1949) prohibits banks from granting any loan or advance to any of its Directors. However, the following loans/advances granted to the Chief Executive Officer / Whole Time Directors are not considered as 'loans and advances':

i. Loan for purchasing of car
ii. Loan for purchasing of personal computer
iii. Loan for purchasing of furniture
iv. Loan for constructing/acquiring a house for personal use
v. Festival advance

vi. Credit limit under credit card facility

The above mentioned loans and advances required banks to approach RBI for prior approval, except in case of loans granted to a Director who was an employee of the bank immediately prior to his/her appointment as a Director. In order to streamline the existing processes and to obviate the need to approach RBI on case-to-case basis, RBI has now decided that in exercise of the powers vested with RBI under Section 35B of the B.R. Act, 1949, commercial banks can grant loans and advances to the Chief Executive Officer/ Whole Time Directors, without seeking prior approval of RBI, subject to the following conditions:

a) The loans and advances shall form part of the compensation /remuneration policy approved by the Board of Directors or any committee of the Board to which powers have been delegated or the Appointments Committee, as the case may be.

b) The guidelines on Base Rate will not be applicable on the interest charged on such loans. However, the interest rate charged on such loans cannot be lower than the rate charged on loans to the bank's own employees.

3. The terms and conditions of the loans granted to the Chief Executive Officer / Whole Time Directors which are currently outstanding may, at the banks' discretion, be reviewed in the light of the above guidelines in order to address transition issues.

4. Banks should note that in view of the prohibition under Section 20 of the BR Act, 1949, apart from the types of loans mentioned in paragraph 1 of this circular, no other loan can be sanctioned to Directors.

(9) Finance to non-constituent borrowers

As per circular dated 7/1/16, RBI has relaxed the guidelines for not extending any non-fund based facilities to non-constituents borrowers of the banks. The restriction was imposed to prevent frauds, diversion of funds etc. in case bank sanctions "one-off" transaction facilities without assessment of credit needs of the borrowers on well-established credit norms. The above restriction has led to the problems faced by those customers, who require Non-Fund based facilities like Letter of Credits (LCs), Bank Guarantees, but do not avail of any Fund based facility from any bank. Now the Scheduled Commercial Banks can grant non-fund based facilities including Partial Credit Enhancement (PCE) to those customers, who do not avail any fund based facility from any bank in India, subject to the conditions of formulating a

comprehensive Board approved loan policy for grant of non-fund based facility to such borrowers, verification of customer credentials, credit appraisal and due-diligence, compliance with KYC norms, submission of credit information to CICs, and adherence to the exposure norms as prescribed by RBI from time to time.

.Banks are, however, prohibited from negotiating unrestricted LCs of non-constituents, as hitherto. In cases where negotiation of bills drawn under LC is restricted to a particular bank and the beneficiary of the LC is not a constituent of that bank, the bank shall have the option to negotiate such LCs, subject to the condition that the proceeds are remitted to the regular banker of the beneficiary.

(10) Fair Practices Code- Disclosing all information relating to processing fees / charges

With a view to bringing in fairness and transparency, banks are advised by RBI that they must transparently disclose to the borrower all information about fees/charges payable for processing the loan application, the amount of fees refundable if loan amount is not sanctioned/disbursed, pre-payment options and charges, if any, penalty for delayed repayments if any, conversion charges for switching loan from fixed to floating rates or vice versa, existence of any interest reset clause and any other matter which affects the interest of the borrower. Such information should also be displayed in the website of the banks, if any, for all categories of loan products. In other words, banks must disclose **'all in cost' inclusive of all such charges involved in processing/sanction of loan application in a transparent manner** to enable the customer to compare the rates/charges with other sources of finance. It should also be ensured that such charges / fees are non-discriminatory.

(11) Transfer of Borrowal Accounts from One Bank to Another (Details in RBI circular dated May 10, 2012)

In view of complaints that critical information on the health of the borrowal accounts being taken over is not being shared by the transferor bank with the transferee bank, resulting in inadequate due diligence at the time of taking over of accounts, RBI has advised the banks as under:

a) Banks should put in place a Board approved policy with regard to take-over of accounts from another bank. The policy may include norms relating to the nature of the accounts that may be taken over, authority levels for sanction of takeover, reporting of takeover to higher authorities,

monitoring mechanism of taken over accounts, credit audit of taken over accounts, examination of staff accountability especially in case of quick mortality of such cases after takeover, periodic review of taken over accounts at Board /Board Committee level, Top Management level, etc.

b) In addition, before taking over an account, the transferee bank should obtain necessary credit information from the transferor bank as per the format prescribed in circular dated December 8, 2008, on "Lending under Consortium Arrangement/Multiple Banking Arrangements".. This would enable the transferee bank to be fully aware of the irregularities, if any, existing in the borrower's account(s) with the transferor bank. The transferor bank, on receipt of a request from the transferee bank, should share necessary credit information as per the prescribed format at the earliest.

(12) Framework for dealing with loan frauds (Details in RBI circular dated May 7, 2015)

In the context of increasing incidence of frauds in general and in loan portfolios in particular, objective of this framework is to direct the focus of banks on the aspects relating to prevention, early detection, prompt reporting to the RBI (for system level aggregation, monitoring & dissemination) and the investigative agencies (for instituting criminal proceedings against the fraudulent borrowers) and timely initiation of the staff accountability proceedings (for determining negligence or connivance, if any) while ensuring that the normal conduct of business of the banks and their risk taking ability is not adversely impacted and no new and onerous responsibilities are placed on the banks. In order to achieve this objective, the framework also seeks to stipulate time lines with the action incumbent on a bank. The time lines / stage wise actions in the loan life-cycle are expected to compress the total time taken by a bank to identify a fraud and aid more effective action by the law enforcement agencies. The early detection of Fraud and the necessary corrective action are important to reduce the quantum of loss which the continuance of the Fraud may entail.

Early Warning Signals (EWS) and Red Flagged Accounts (RFA): The concept of a Red Flagged Account (RFA) has been introduced in the framework as an important step in fraud risk control. A RFA is one where a suspicion of fraudulent activity is thrown up by the presence of one or more Early Warning Signals (EWS). These signals in a loan account should immediately put the bank on alert regarding a weakness or wrong doing which may ultimately turn out to be

fraudulent. A bank cannot afford to ignore such EWS but must instead use them as a trigger to launch a detailed investigation into a RFA. An illustrative list of some EWS is given, for the guidance of banks, in the above referred circular which also deals with various other aspects like staff accountability, role of auditors, filing complaint with enforcement agencies, etc.

Chapter 27 Analysis of financial statements

(1) Legal position regarding Financial Statements

The Companies Act 2013 has prescribed the formats of both Balance Sheet and Profit & Loss account. Earlier, format of only the balance sheet was prescribed. The Companies Act 2013 mentions the following in respect of financial statements.

(1) The financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III:

Provided that the items contained in such financial statements shall be in accordance with the accounting standards:

Provided further that nothing contained in this sub-section shall apply to any insurance or banking company or any company engaged in the generation or supply of electricity, or to any other class of company for which a form of financial statement has been specified in or the Act governing such class of company:

Without prejudice to sub-section (*1*), where the financial statements of a company do not comply with the accounting standards referred to in sub-section (*1*), the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.

Format of balance sheet

Name of the Company…………………….

Balance Sheet as at ………………………

(Rupees in…………)

Particulars	Note	Figures as at the	Figures as at the

	No.	end of current reporting period	end of the previous reporting period
1	2	3	4
I. EQUITY AND LIABILITIES			
(1) **Shareholders' funds**			
(*a*) Share capital			
(*b*) Reserves and surplus			
(*c*) Money received against share warrants			
(2) **Share application money pending allotment**			
(3) **Non-current liabilities**			
(*a*) Long-term borrowings			
(*b*) Deferred tax liabilities (Net)			
(*c*) Other Long term liabilities			
(*d*) Long-term provisions			
(4) **Current liabilities**			
(*a*) Short-term borrowings			
(*b*) Trade payables			
(*c*) Other current liabilities			
(*d*) Short-term provisions			
TOTAL			
II. ASSETS			
Non-current assets			
(1) (*a*) Fixed assets			
(*i*) Tangible assets			
(*ii*) Intangible assets			
(*iii*) Capital work-in-progress			
(*iv*) Intangible assets under development			
(*b*) Non-current investments			

(*c*) Deferred tax assets (net)

(*d*) Long-term loans and advances

(*e*) Other non-current assets

(2) **Current assets**

(*a*) Current investments

(*b*) Inventories

(*c*) Trade receivables

(*d*) Cash and cash equivalents

(*e*) Short-term loans and advances

(*f*) Other current assets

TOTAL

Format of statement of profit and loss

Name of the Company……………………….

Profit and loss statement for the year ended ………………………

(Rupees in…………)

	Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
	1	2	3	4
I	Revenue from operations		xxx	xxx
II	Other income		xxx	xxx
III	Total Revenue (I + II)		xxx	xxx
IV	Expenses: Cost of materials consumed		Xxx Xxx	Xxx Xxx

	Purchases of Stock-in-Trade Changes in inventories of finished goods work-in-progress and Stock-in-Trade Employee benefits expense Finance costs Depreciation and amortization expense Other expenses Total expenses		Xxx xxx	Xxx Xxx
V	Profit before exceptional and extraordinary items and tax (III - IV)		xxx	xxx
VI	Exceptional items		xxx	xxx
VII	Profit before extraordinary items and tax (V - VI)		xxx	xxx
VIII	Extraordinary items		xxx	xxx
IX	Profit before tax (VII-VIII)		xxx	xxx
X	Tax expense: (1) Current tax (2) Deferred tax		 Xxx Xxx	 Xxx Xxx

XI	Profit (Loss) for the period from continuing operations (VII-VIII)		xxx	xxx
XII	Profit/(loss) from discontinuing operations		xxx	xxx
XIII	Tax expense of discontinuing operations		xxx	xxx
XIV	Profit/(loss) from Discontinuing operations (after tax) (XII-XIII)		xxx	xxx
XV	Profit (Loss) for the period (XI + XIV)		xxx	xxx
XVI	Earnings per equity share: (1) Basic (2) Diluted		 Xxx xxx	 Xxx xxx

Chapter 28 Working capital finance

(1) Guidelines for Issue of Commercial Paper (Details in RBI Master Circular dated July 1, 2015)

1. Introduction

Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note. CP, as a privately placed instrument, was introduced in India in 1990 with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors. Subsequently, primary dealers (PDs) and all-India financial institutions (FIs) were also permitted to issue CP to enable them to meet their short-term funding requirements.

2. Eligibility for Issue of CP:

a. Companies, PDs and FIs are permitted to raise short term resources through CP.

b. A company would be eligible to issue CP provided:

i. the tangible net worth of the company, as per the latest audited balance sheet, is not less than Rs.4 crore;
ii. the company has been sanctioned working capital limit by bank/s or FIs; and
iii. the borrowal account of the company is classified as a Standard Asset by the financing bank/institution.

3. Issue of CP – Credit enhancement, limits, etc.

a. CP shall be issued as a ‘stand-alone’ product. Further, it would not be obligatory in any manner on the part of the banks and FIs to provide stand-by facility to the issuers of CP.
b. Banks and FIs may, based on their commercial judgement, subject to the prudential norms as applicable to them, with the specific approval of their respective Boards, choose to provide stand-by assistance/credit, back-stop facility etc. by way of credit enhancement for a CP issue.
c. Non-bank entities (including corporates) may provide unconditional and irrevocable guarantee for credit enhancement for CP issue provided:
   i. the issuer fulfils the eligibility criteria prescribed for issuance of CP;
   ii. the guarantor has a credit rating at least one notch higher than the issuer given by an approved CRA; and
   iii. the offer document for CP properly discloses the net worth of the guarantor company, the names of the companies to which the guarantor has issued similar guarantees, the extent of the guarantees offered by the guarantor company, and the conditions under which the guarantee will be invoked.
d. The aggregate amount of CP that can be issued by an issuer shall at all times be within the limit as approved by its Board of Directors or the quantum indicated by the CRA for the specified rating, whichever is lower.
e. Banks and FIs shall have the flexibility to fix working capital limits, duly taking into account the resource pattern of company’s financing, including CP.
f. An issue of CP by an FI shall be within the overall umbrella limit prescribed in the Master Circular on Resource Raising Norms for FIs, issued by the Department of Banking Regulation, Reserve Bank of India, as prescribed/ updated from time-to-time.
g. The total amount of CP proposed to be issued should be raised within a period of two weeks from the date on which the issuer opens the issue for subscription. CP may be issued on a single

date or in parts on different dates provided that in the latter case, each CP shall have the same maturity date.

h. Every issue of CP, and every renewal of a CP, shall be treated as a fresh issue.

4. Eligibility for Investment in CP

a. Individuals, banks, other corporate bodies (registered or incorporated in India) and unincorporated bodies, Non-Resident Indians and Foreign Institutional Investors (FIIs) shall be eligible to invest in CP.

b. FIIs shall be eligible to invest in CPs subject to (i) such conditions as may be set for them by Securities Exchange Board of India (SEBI) and (ii) compliance with the provisions of the Foreign Exchange Management Act, 1999, the Foreign Exchange (Deposit) Regulations, 2000 and the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, as amended from time to time.

5. Form of the Instrument, mode of issuance and redemption

5.1 Form

a. CP shall be issued in the form of a promissory note and held in physical form or in a dematerialised form through any of the depositories approved by and registered with SEBI, provided that all RBI regulated entities can deal in and hold CP only in dematerialised form through such depositories.

b. Fresh investments by all RBI-regulated entities shall be only in dematerialised form.

c. CP shall be issued in denominations of Rs. 5 lakh and multiples thereof. The amount invested by a single investor should not be less than Rs. 5 lakh (face value).

d. CP shall be issued at a discount to face value as may be determined by the issuer.

e. No issuer shall have the issue of CP underwritten or co-accepted.

f. Options (call/put) are not permitted on CP.

5.2 Tenor

a. CP shall be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue.

b. The maturity date of the CP shall not go beyond the date up to which the credit rating of the issuer is valid.

5.3. Procedure for Issuance

a. Every issuer must appoint an IPA for issuance of CP.

b. The issuer should disclose to the potential investors, its latest financial position as per the standard market practice.
c. After the exchange of confirmation of the deal between the investor and the issuer, the issuer shall arrange for crediting the CP to the Demat account of the investor with the depository through the IPA.
d. The issuer shall give to the investor a copy of IPA certificate to the effect that the issuer has a valid agreement with the IPA and documents are in order.

5.4 Rating Requirement

Eligible participants/issuers shall obtain credit rating for issuance of CP from any one of the SEBI registered CRAs. The minimum credit rating shall be 'A3' as per rating symbol and definition prescribed by SEBI. The issuers shall ensure at the time of issuance of the CP that the rating so obtained is current and has not fallen due for review.

5.5 Investment / Redemption

a. The investor in CP (primary subscriber) shall pay the discounted value of the CP to the account of the issuer through the IPA.
b. The investor holding the CP in physical form shall, on maturity, present the instrument for payment to the issuer through the IPA.
c. The holder of a CP in dematerialised form shall get the CP redeemed and receive payment through the IPA.

5.6 Documentation Procedures

a. Standardised procedures and documentation for CPs are prescribed in consultation with Fixed Income Money Market and Derivatives Association of India (FIMMDA) in consonance with international best practices.
b. Issuers /IPAs shall follow the operational guidelines issued by FIMMDA, from time to time, with the approval of RBI.

6. Trading and Settlement of CP

a. All OTC trades in CP shall be reported within 15 minutes of the trade to the reporting platform of Clearcorp Dealing System (India) Ltd.(CDSIL).
b. OTC trades in CP shall be settled through the clearing house of the National Stock Exchange (NSE), i.e., the National Securities Clearing Corporation Limited (NSCCL), the clearing house of the Bombay Stock Exchange (BSE), i.e., Indian Clearing Corporation Limited (ICCL), and the

clearing house of the MCX-Stock Exchange, i.e., MCX-SX Clearing Corporation Limited (CCL), as per the norms specified by NSCCL, ICCL and CCL from time to time.

c. The settlement cycle for OTC trades in CP shall either be T+0 or T+1.

7. Buyback of CP

a. Issuers may buyback the CP, issued by them to the investors, before maturity.
b. Buyback of CP shall be through the secondary market and at prevailing market price.
c. The CP shall not be bought back before a minimum period of 7 days from the date of issue.
d. Issuer shall intimate the IPA of the buyback undertaken.
e. Buyback of CPs should be undertaken after taking approval from the Board of Directors.

8. Duties and Obligations

The duties and obligations of the Issuer, IPA and CRA are set out in the RBI circular, referred above.

<u>(2) Bank Finance to Factoring Companies</u>

Banks can extend financial assistance to support the factoring business of Factoring Companies complying with certain criteria, which, inter-alia, include:

i. They derive at least 50 per cent of their income from factoring activity.
ii. The receivables purchased / financed, irrespective of whether on 'with recourse' or 'without recourse' basis, form at least 50 per cent of the assets of the Factoring Company.

<u>(3) Provision of Factoring Services by Banks</u>

In order to ensure that the bank offering factoring services has enough margin to cover any deficiencies in the payment of the related invoice, RBI had earlier stipulated that the pre-payment amount offered by banks for the receivables acquired under factoring should not exceed 80% of the invoice value. On a review, RBI has advised that banks offering factoring services may decide percentage of the invoice to be paid upfront based on their own assessment of the credit worthiness of the assignor/ buyer, due diligence carried out by them and other commercial considerations.

(4) Export factoring on non-recourse basis (RBI circular dated July 16, 2015)

In order to facilitate exports, Authorised Dealer Category – I (AD Category –I) banks had been permitted to provide 'export factoring' services to exporters on 'with recourse' basis by entering into arrangements with overseas institutions for this purpose, without prior approval from the Reserve Bank of India, subject to compliance with guidelines issued by the Department of Banking Regulation in this regard.

Taking into account the recommendation made by the Technical Committee on Facilities and Services to the Exporters (Chairman: Shri G. Padmanabhan), RBI has decided to permit AD banks to factor the export receivables on a non-recourse basis, so as to enable the exporters to improve their cash flow and meet their working capital requirements subject to conditions as under:

a. AD banks may take their own business decision to enter into export factoring arrangement on non-recourse basis. They should ensure that their client is not over financed. Accordingly, they may determine the working capital requirement of their clients taking into account the value of the invoices purchased for factoring. The invoices purchased should represent genuine trade invoices.
b. In case the export financing has not been done by the Export Factor, the Export Factor may pass on the net value to the financing bank/ Institution after realising the export proceeds.
c. AD bank, being the Export Factor, should have an arrangement with the Import Factor for credit evaluation & collection of payment.
d. Notation should be made on the invoice that importer has to make payment to the Import Factor.
e. After factoring, the Export Factor may close the export bills and report the same in the Export Data Processing and Monitoring System (EDPMS) of the Reserve Bank of India.
f. In case of single factor, not involving Import Factor overseas, the Export Factor may obtain credit evaluation details from the correspondent bank abroad.
g. KYC and due diligence on the exporter shall be ensured by the Export Factor.

(5) Rupee (INR) Denominated trade credit (Details in RBI circular dated September 10, 2015)

Importers often raise trade credit (buyers' credit / suppliers' credit) from overseas supplier, bank and financial institution for import of capital and non-capital goods into India. With a view to providing greater flexibility for structuring of trade credit arrangements, RBI has decided that the resident importer can raise trade credit in Rupees (INR) within the following framework after entering into a loan agreement with the overseas lender:

i. Trade credit can be raised for import of all items (except gold) permissible under the extant Foreign Trade Policy
ii. Trade credit period for import of non-capital goods can be upto one year from the date of shipment or upto the operating cycle whichever is lower
iii. Trade credit period for import of capital goods can be upto five years from the date of shipment
iv. No roll-over / extension can be permitted by the AD Category - I bank beyond the permissible period
v. AD Category - I banks can permit trade credit upto USD 20 mn equivalent per import transaction
vi. AD Category - I banks are permitted to give guarantee, Letter of Undertaking or Letter of Comfort in respect of trade credit for a maximum period of three years from the date of shipment
vii. The all-in-cost of such Rupee (INR) denominated trade credit should be commensurate with prevailing market conditions
viii. All other guidelines for trade credit will be applicable for such Rupee (INR) denominated trade credits

Overseas lenders of Rupee (INR) denominated trade credits will be eligible to hedge their exposure in Rupees through permitted derivative products in the on-shore market with an AD Category - I bank in India.

(6) Guarantees on behalf of Share and Stock Brokers/ Commodity Brokers

Banks may issue guarantees on behalf of share and stock brokers in favour of stock exchanges in lieu of security deposit to the extent it is acceptable in the form of bank guarantee as laid down by stock exchanges. Banks may also issue guarantees in lieu of margin requirements as per stock exchange regulations. Banks have been advised that they should obtain a minimum margin of 50 percent while issuing such guarantees. A minimum cash margin of 25 per cent (within the above margin of 50 per cent) should be maintained in respect of such guarantees issued by banks. The above minimum margin of 50 percent and minimum cash margin requirement of 25 percent

(within the margin of 50 percent) will also apply to guarantees issued by banks on behalf of commodity brokers in favour of the national level commodity exchanges, viz., National Commodity & Derivatives Exchange (NCDEX), Multi Commodity Exchange of India Limited (MCX) and National Multi-Commodity Exchange of India Limited (NMCEIL), in lieu of margin requirements as per the commodity exchange regulations. Banks should assess the requirement of each applicant and observe usual and necessary safeguards including the exposure ceilings.

(7) Irrevocable Payment Commitments (IPCs)

Banks issuing Irrevocable Payment Commitment (IPCs) to various Stock Exchange on behalf of Mutual Funds and FIIs are advised to adopt the following risk mitigation measures:

Only those custodian banks would be permitted to issue IPCs who have a clause in the Agreement with their clients which gives them an inalienable right over the securities to be received as payout in any settlement. However, in cases where transactions are pre-funded i.e. there are clear INR funds in the customer's account and, in case of FX deals, the bank's nostro account has been credited before the issuance of the IPC by custodian banks, the requirement of the clause of inalienable right over the security to be received as payout in the agreement with the clients will not be insisted upon.

Issue of Irrevocable Payment Commitments (IPCs).forms part of Capital Market Exposure CME) of the banks and instructions for its calculation are contained in Master Circular dated July 1, 2015.

(8) Working Capital Finance to Information Technology and Software Industry

Following the recommendations of the "National Task Force on Information Technology and Software development", Reserve Bank has framed guidelines for extending working capital to the said industry. Banks are however free to modify the guidelines based on their own experience without reference to the Reserve Bank of India to achieve the purpose of the guidelines in letter and spirit. The salient features of these guidelines are set forth below:

i. Banks may consider sanction of working capital limits based on the track record of the promoters' group affiliation, composition of the management team and their work experience as well as the infrastructure.

ii. In the case of the borrowers with working capital limits of up to Rs 2 crore, assessment may be made at 20 percent of the projected turnover. However, in other cases, the banks may consider assessment of MPBF on the basis of the monthly cash budget system. For the borrowers enjoying working capital limits of Rs 10 crore and above from the banking system the guidelines regarding the loan system would be applicable.

iii. Banks can stipulate reasonable amount as promoters' contribution towards margin.

iv. Banks may obtain collateral security wherever available. First/ second charge on current assets, if available, may be obtained.

v. The rate of interest as prescribed for general category of borrowers may be levied. Concessional rate of interest as applicable to pre-shipment/post-shipment credit may be levied.

vi. Banks may evolve tailor-made follow up system for such advances. The banks could obtain quarterly statements of cash flows to monitor the operations. In case the sanction was not made on the basis of the cash budgets, they can devise a reporting system, as they deem fit.

Chapter 29 Term loans

(1) Partial Credit Enhancement (PCE) to Corporate Bonds

The credit needs of the infrastructure sector in India are huge. As the Indian corporate bond market is at a nascent stage of development, there is excessive pressure on the banking system to fund the credit needs for project development, including the infrastructure sector. Due to greater asset-liability mismatch in infrastructure and project financing, banks are exposed to liquidity risk. The insurance and provident/pension funds, whose liabilities are long term, may be better suited to finance such projects.

With a view to encouraging corporates to avail of bond financing, RBI has decided to allow banks to provide PCE to bonds issued by corporates /special purpose vehicles (SPVs) for funding all types of projects, subject to certain guidelines. To begin with, banks are allowed to offer PCE only in the form of a non-funded irrevocable contingent line of credit. The objective behind allowing banks to extend PCE is to enhance the credit rating of the bonds issued so as to enable corporates to access the funds from the bond market on better terms. Some of the RBI guidelines for this facility are as under; (details available in RBI circular dated September 24, 2015)

i. The aggregate PCE provided by all banks for a given bond issue shall be limited to 20 per cent of the bond issue size.

ii. The PCE facility shall be provided at the time of the bond issue and will be irrevocable.

iii. Banks may offer PCE only in respect of bonds whose pre-enhanced rating is **BBB minus or better**.

iv. Banks cannot provide PCE by way of guarantee.

v. Banks providing PCE to bonds issued by a corporate/SPV will not be eligible to invest in those bonds. They can, however, provide other need based credit facilities (funded and/or non-funded) to the corporate/SPV.

vi. The contingent facility may, at the discretion of the PCE providing bank, be made available as a revolving facility.

vii .In the event of the project failure / bankruptcy, in terms of repayment priority, the PCE must rank below the claims of the enhanced bond holders.

viii. PCE facilities to the extent drawn should be treated as an advance in the balance sheet. Undrawn facilities would be an off-balance sheet item and reported under 'Contingent Liability – Others'.

ix. Banks should ensure that the project assets, created out of the bond issue for which PCE has been provided by them, and the cash flows from the project are ring fenced through an escrow account mechanism administered under a bond trustee arrangement. The manner in which security interest in the project assets would be shared by the lenders to the project, bond holders and banks providing the PCE and the manner in which the project cash flows would be shared for servicing loans, if any, and the bonds and PCE, should be decided and agreed upon before the issue of bonds and should be properly documented.

x. The project should have a robust and viable financial structure even before the credit enhancement is taken into account. Nevertheless, while providing PCE, banks should exercise necessary due diligence and risk appraisal, including making their own internal credit analysis/rating and should not entirely rely on the ratings of external agencies. Banks should strengthen their internal rating systems which should also include building up of a system of regular (quarterly or half-yearly) tracking of the financial position of the issuer with a view to ensuring continuous monitoring of the rating migration of the issuers/issues.

xi. Banks must honour the full PCE commitment made ab-initio in respect of a bond issue irrespective of the asset classification of the concerned borrower's credit facilities.

(2) Bank Loans for Financing Promoters' Contribution

As per earlier RBI guidelines, the promoters' contribution towards the equity capital of a company should come from their own resources and banks should not normally grant advances to take up shares of other companies. These guidelines have since been revised and the banks can extend finance to 'specialized' entities established for acquisition of troubled companies subject to the general guidelines applicable to advances against shares/debentures/bonds. The lenders should, however, assess the risks associated with such financing and ensure that these entities are adequately capitalized, and debt equity ratio for such entity is not more than 3:1. A 'specialized' entity will be a body corporate exclusively set up for the purpose of taking over and turning around troubled companies and promoted by individuals or/and institutional promoters (including Government) having professional expertise in turning around 'troubled companies' and eligible to make investments in the industry/segment to which the target asset belonged.

(3) Guidelines for Financing Infrastructure Projects

a) The definition of 'infrastructure lending' has been revised as below:

A credit facility extended by lenders (i.e. banks and select All India Term-Lending and Refinancing Institutions) to a borrower for exposure in the following infrastructure sub-sectors will qualify as 'infrastructure lending':

Category	Infrastructure sub-sectors	
Transport	i	Roads and bridges
	ii	Ports[1]
	iii	Inland Waterways
	iv	Airport
	v	Railway Track, tunnels, viaducts, bridges[2]
	vi	Urban Public Transport (except rolling stock in case of urban road transport)
Energy	i	Electricity Generation
	ii	Electricity Transmission
	iii	Electricity Distribution
	iv	Oil pipelines
	v	Oil / Gas / Liquefied Natural Gas (LNG) storage

		facility[3]
	vi	Gas pipelines[4]
Water & Sanitation	i	Solid Waste Management
	ii	Water supply pipelines
	iii	Water treatment plants
	iv	Sewage collection, treatment and disposal system
	v	Irrigation (dams, channels, embankments etc)
	vi	Storm Water Drainage System
	vii	Slurry Pipelines
Communication	i	Telecommunication (Fixed network)[5]
	ii	Telecommunication towers
	iii	Telecommunication & Telecom Services
Social and Commercial Infrastructure	i	Education Institutions (capital stock)
	ii	Hospitals (capital stock)[6]
	iii	Three-star or higher category classified hotels located outside cities with population of more than 1 million
	iv	Common infrastructure for industrial parks, SEZ, tourism facilities and agriculture markets
	v	Fertilizer (Capital investment)
	vi	Post-harvest storage infrastructure for agriculture and horticultural produce including cold storage
	vii	Terminal markets
	viii	Soil-testing laboratories
	ix	Cold Chain[7]
	x	Hotels with project cost[8] of more than Rs.200 crores each in any place in India and of any star rating;
	xi	Convention Centers with project cost[8] of more than Rs.300 crore each.
1. Includes Capital Dredging		
2. Includes supporting terminal infrastructure such as loading / unloading		

terminals, stations and buildings
3. Includes strategic storage of crude oil
4. Includes city gas distribution network
5. Includes optic fiber / cable networks which provide broadband / internet
6. Includes Medical Colleges, Para Medical Training Institutes and Diagnostics Centers
7. Includes cold room facility for farm level pre-cooling, for preservation or storage of agriculture and allied produce, marine products and meat.
8. Applicable with prospective effect from November 25, 2013 i.e. the date of issue of circular by RBI in this regard and available for eligible projects for a period of three years; Eligible costs exclude cost of land and lease charges but include interest during construction.

b) Refinancing of Project Loans

In terms of RBI guidelines, a restructured account is one where the bank, for economic or legal reasons relating to the borrower's financial difficulty, grants to the borrower concessions that the bank would not otherwise consider. Restructuring would normally involve modification of terms of the advances/securities, which would generally include, among others, alteration of repayment period/repayable amount/ the amount of installments/rate of interest (due to reasons other than competitive reasons*)*. Thus, any change in repayment schedule of a loan will render it as restructured account. However, if the banks refinance any existing infrastructure and other project loans by way of take-out financing, even without a pre-determined agreement with other banks / FIs, and fix a longer repayment period, the same would not be considered as restructuring if the following conditions are satisfied:

a. Such loans should be 'standard' in the books of the existing banks, and should have not been restructured in the past.

b. Such loans should be substantially taken over (more than 50% of the outstanding loan by value) from the existing financing banks/Financial institutions.

c. The repayment period should be fixed by taking into account the life cycle of the project and cash flows from the project.

c) Flexible Structuring of Long Term Project Loans to Infrastructure and Core Industries (Loans sanctioned after July 15, 2014)

1 Reserve Bank's instructions do not come in the way of banks' structuring long term projects insofar as the prudential and regulatory framework is meticulously observed. However, as banks have certain misgivings that refinancing of long term projects loans may be construed as restructuring, and the estimated cash flows (balance debt in the form of bullet payment) at the end of each refinancing period may not be allowed to be counted in the appropriate buckets for the purpose of ALM, the RBI has clarified that it would not have any objection to banks' financing of long term projects in infrastructure and core industries sector having the following features:

i. The fundamental viability of the project would be established on the basis of all requisite financial and non-financial parameters, especially the acceptable level of interest coverage ratio (EBIDTA / Interest payout), indicating capacity to service the loan and ability to repay over the tenor of the loan;

ii. Allowing longer tenor amortisation of the loan (Amortisation Schedule), say 25 years (within the useful life / concession period of the project) with periodic refinancing (Refinancing Debt Facility) of balance debt, the tenor of which could be fixed at the time of each refinancing, within the overall amortisation period;

iii. This would mean that the bank, while assessing the viability of the project, would be allowed to accept the project as a viable project where the average debt service coverage ratio (DSCR) and other financial and non-financial parameters are acceptable over a longer amortisation period of say 25 years (Amortisation Schedule), but provide funding (Initial Debt Facility) for only, say, 5 years with refinancing of balance debt being allowed by existing or new banks (Refinancing Debt Facility) or even through bonds; and

iv. The refinancing (Refinancing Debt Facility) after each of these 5 years would be of the reduced amounts determined as per the Original Amortisation Schedule.

2 The banks' financing of project loans, with the features mentioned in paragraph 1 above will, however, be subject to the following conditions:

i. Only term loans to infrastructure projects, as defined under the 'Harmonised Master List of Infrastructure' of RBI, and projects in core industries sector, included in the Index of Eight Core Industries (base: 2004-05) published by the Ministry of Commerce and Industry, Government of India, (viz., coal, crude oil, natural gas, petroleum refinery products, fertilisers, steel (Alloy + Non Alloy), cement and electricity - some of these sectors such as fertilisers, electricity

generation, distribution and transmission, etc. are also included in the Harmonised Master List of Infrastructure sub-sectors) - will qualify for such refinancing;

ii. At the time of initial appraisal of such projects, banks may fix an amortisation schedule (Original Amortisation Schedule) while ensuring that the cash flows from such projects and all necessary financial and non-financial parameters are robust even under stress scenarios;

iii. The tenor of the Amortisation Schedule should not be more than 80% (leaving a tail of 20%) of the initial concession period in case of infrastructure projects under public private partnership (PPP) model; or 80% of the initial economic life envisaged at the time of project appraisal for determining the user charges / tariff in case of non-PPP infrastructure projects; or 80% of the initial economic life envisaged at the time of project appraisal by Lenders Independent Engineer in the case of other core industries projects;

iv. The bank offering the Initial Debt Facility may sanction the loan for a medium term, say 5 to 7 years. This is to take care of initial construction period and also cover the period at least up to the date of **commencement of commercial operations (DCCO**) and revenue ramp up. The repayment(s) at the end of this period (equal in present value to the remaining residual payments corresponding to the Original Amortisation Schedule) could be structured as a bullet repayment, with the intent specified up front that it will be refinanced. That repayment may be taken up by the same lender or a set of new lenders, or combination of both, or by issue of corporate bond, as Refinancing Debt Facility, and such refinancing may repeat till the end of the Amortisation Schedule;

v. The repayment schedules of Initial Debt Facility should normally correspond to the Original Amortisation Schedule, unless there is an extension of DCCO. In that case, mere extension of DCCO would not be considered as restructuring subject to certain conditions, if the revised DCCO falls within the period of two years and one year from the original DCCO for infrastructure and non-infrastructure projects respectively. In such cases the consequential shift in repayment schedule by equal or shorter duration (including the start date and end date of revised repayment schedule) than the extension of DCCO would also not be considered as restructuring provided all other terms and conditions of the loan remain unchanged or are enhanced to compensate for the delay and the entire project debt amortisation is scheduled within 85% of the initial economic life of the project as prescribed in paragraph 2 (iii) above;

vi. The Amortisation Schedule of a project loan may be modified once during the course of the loan (after DCCO) based on the actual performance of the project in comparison to the assumptions made during the financial closure without being treated as 'restructuring' provided:

a) The loan is a standard loan as on the date of change of Amortisation Schedule;

b) Net present value of the loan remains the same before and after the change in Amortisation Schedule; and

c) The entire outstanding debt amortisation is scheduled within 85% of the economic life of the project as prescribed in paragraph 2 (iii) above;

vii. If the Initial Debt Facility or Refinancing Debt Facility becomes NPA at any stage, further refinancing should stop and the bank which holds the loan when it becomes NPA, would be required to recognise the loan as such and make necessary provisions as required under the extant regulations. Once the account comes out of NPA status, it will be eligible for refinancing in terms of these instructions;

viii. Banks may determine the pricing of the loans at each stage of sanction of the Initial Debt Facility or Refinancing Debt Facility, commensurate with the risk at each phase of the loan, and such pricing should not be below the Base Rate of the bank;

ix. Banks should secure their interest by way of proper documentation and security creation, etc;

x. Banks will be initially allowed to count the cash flows from periodic amortisations of loans as also the bullet repayment of the outstanding debt at the end of each refinancing period for their asset-liability management; however, with experience gained, banks will be required in due course to conduct behavioural studies of cash flows in such amortisation of loans and plot them accordingly in ALM statements;

xi. Banks should recognise from a risk management perspective that there will be a probability that the loan will not be refinanced by other banks, and should take this into account when estimating liquidity needs as well as stress scenarios. Further, unless the part or full refinancing by other banks is clearly identified, the cash flows from such refinancing should not be taken into account for computing liquidity ratios. Similarly, once committed, the refinancing bank should take into account such cash flows for computing their liquidity ratios; and

xii. Banks should have a Board approved policy for such financing.

3. The above structure is applicable to new loans to infrastructure projects and core industries projects sanctioned after July 15, 2014. Further, the instructions on 'take-out finance' (circular

dated February 29, 2000) and ‘transfer of borrowal accounts’ (circular dated May 10, 2012) cease to be applicable on any loan to infrastructure and core industries projects sanctioned under these instructions.

d) Flexible Structuring of Long Term Project Loans to Infrastructure and Core Industries (Loans sanctioned before July 15, 2014)

1 Banks may also flexibly structure the existing project loans (sanctioned before July 15, 2014) to infrastructure projects and core industries projects with the option to periodically refinance the same as per the norms given below:

i. Only term loans to projects, in which the aggregate exposure of all institutional lenders exceeds Rs.500 crore, in the infrastructure sector (as defined under the Harmonised Master List of Infrastructure of RBI) and in the core industries sector (included in the Index of Eight Core Industries (base: 2004-05) published by the Ministry of Commerce and Industry, Government of India) will qualify for such flexible structuring and refinancing;

ii. Banks may fix a Fresh Loan Amortisation Schedule for the existing project loans once during the life time of the project, after the date of commencement of commercial operations (DCCO), based on the reassessment of the project cash flows, without this being treated as ‘restructuring’ provided:

a) The loan is a standard loan as on the date of change of loan amortisation schedule;

b) Net present value of the loan remains same before and after the change in loan amortisation schedule;

c) The Fresh Loan Amortisation Schedule should be within 85 per cent (leaving a tail of 15 per cent) of the initial concession period in case of infrastructure projects under public private partnership (PPP) model; or 85 per cent of the initial economic life envisaged at the time of project appraisal for determining the user charges / tariff in case of non-PPP infrastructure projects; or 85 per cent of the initial economic life envisaged at the time of project appraisal by Lenders Independent Engineer in the case of other core industries projects; and

d) The viability of the project is reassessed by the bank and vetted by the Independent Evaluation Committee constituted under the aegis of the Framework for Revitalising Distressed Assets in the Economy dated January 30, 2014 and communicated to the banks by Indian Banks Association vide its circular No. C&I/CIR/2013-14/9307 dated April 29, 2014.

iii. If a project loan is classified as 'restructured standard' asset as on the date of fixing the Fresh Loan Amortisation Schedule as per para (ii) above, while the current exercise of fixing the Fresh Loan Amortisation Schedule may not be treated as an event of 'repeated restructuring', the loan should continue to be classified as 'restructured standard' asset. Upgradation of such assets would be governed by the extant prudential guidelines on restructuring of accounts taking into account the Fresh Loan Amortisation Schedule;

iv. Any subsequent changes to the above mentioned Fresh Loan Amortisation Schedule will be governed by the extant restructuring norms;

v. Banks may refinance the project term loan periodically (say 5 to 7 years) after the project has commenced commercial operations. The repayment(s) at the end of each refinancing period (equal in value to the remaining residual payments corresponding to the Fresh Loan Amortisation Schedule) could be structured as a bullet repayment, with the intent specified up front that it will be refinanced. The refinance may be taken up by the same lender or a set of new lenders, or combination of both, or by issue of corporate bond, as refinancing debt facility, and such refinancing may repeat till the end of the Fresh Loan Amortisation Schedule. The proviso regarding net present value as at paragraph (ii) would not be applicable at the time of periodic refinancing of the project term loan;

vi. If the project term loan or refinancing debt facility becomes a non-performing asset (NPA) at any stage, further refinancing should stop and the bank which holds the loan when it becomes NPA would be required to recognise the loan as such and make necessary provisions as required under the extant regulations. Once the account comes out of NPA status, it will be eligible for refinancing in terms of these instructions;

vii. Banks may determine the pricing of the loans at each stage of the project term loan or refinancing debt facility, commensurate with the risk at each phase of the loan, and such pricing should not be below the Base Rate of the bank;

viii. Banks should secure their interest by way of proper documentation and security creation, etc;

ix. Banks will be initially allowed to count the cash flows from periodic amortisations of loans as also the bullet repayment of the outstanding debt at the end of each refinancing period for their asset-liability management; however, with experience gained, banks will be required in due

course to conduct behavioural studies of cash flows in such amortisation of loans and plot them accordingly in ALM statements;

x. Banks should recognise from a risk management perspective that there will be a probability that the loan will not be refinanced by other banks, and should take this into account when estimating liquidity needs as well as stress scenarios; and

xi. Banks should have a Board approved policy for such financing.

2. Banks may also provide longer loan amortisation as per the above framework of flexible structuring of project loans to existing project loans to infrastructure and core industries projects which are classified as 'non-performing assets'. However, such an exercise would be treated as 'restructuring' and the assets would continue to be treated as 'non-performing asset'. Such accounts may be upgraded only when all the outstanding loan/facilities in the account perform satisfactorily during the 'specified period' (as defined in the extant prudential guidelines on restructuring of accounts), i.e. principal and interest on all facilities in the account are serviced as per terms of payment during that period. However, periodic refinance facility would be permitted only when the account is classified as 'standard' as prescribed in the para (vi) above.

3 The exercise of flexible structuring and refinancing should be carried out only after DCCO. Further, RBI instructions on 'take-out finance', 'transfer of borrowal accounts', 'refinancing of project loans by way of partial takeover' and 'restrictions on the repayment period of the restructured advance' ' will cease to be applicable on any loan to infrastructure and core industries projects refinanced under the ambit of these instructions.

The guidelines in b) and c) above, are also applicable to external commercial borrowings (ECBs) availed for funding projects in infrastructure and core industries sectors, subject to regulations issued under the Foreign Exchange Management Act, 1999.

e) Financing of Cost Overruns for Projects under Implementation

1 Internationally, project finance lenders sanction a 'standby credit facility' to fund cost overruns if needed. Such 'standby credit facilities' are sanctioned at the time of initial financial closure; but disbursed only when there is a cost overrun. At the time of credit assessment of borrowers/project, such cost overruns are also taken into account while determining the project Debt Equity Ratio, Debt Service Coverage Ratio, Fixed Asset Coverage Ratio etc. Such 'standby

credit facilities' rank pari passu with base project loans and their repayment schedule is also the same as that of the base project loans.

2 Accordingly, in cases where banks have specifically sanctioned a 'standby facility' at the time of initial financial closure to fund cost overruns, they may fund cost overruns as per the agreed terms and conditions.

3. Where the initial financial closure does not envisage such financing of cost overruns, based on the representations from banks, it has been decided to allow banks to fund cost overruns, which may arise on account of extension of DCCO upto two years and one year from the original DCCO stipulated at the time of financial closure for infrastructure projects and non-infrastructure projects respectively, without treating the loans as 'restructured asset' subject to the following conditions:

i) Banks may fund additional 'Interest During Construction', which may arise on account of delay in completion of a project;

ii) Other cost overruns (excluding Interest During Construction) up to a maximum of 10% of the original project cost;

iii) The Debt Equity Ratio as agreed at the time of initial financial closure should remain unchanged subsequent to funding cost overruns or improve in favour of the lenders and the revised Debt Service Coverage Ratio should be acceptable to the lenders;

iv) Disbursement of funds for cost overruns should start only after the Sponsors/Promoters bring in their share of funding of the cost overruns; and

i) All other terms and conditions of the loan should remain unchanged or enhanced in favour of the lenders.

4 The ceiling of 10 per cent of the original project cost prescribed in paragraph 3 (ii) above is applicable to financing of all other cost overruns (excluding interest during construction), including cost overruns on account of fluctuations in the value of Indian Rupee against other currencies, arising out of extension of date of commencement of commercial operations.

Chapter 30 Credit Delivery

Lending under Consortium Arrangement / Multiple Banking Arrangements

Banks are required to strengthen their information back-up about the borrowers enjoying credit facilities from multiple banks by obtaining declaration from the borrowers about the credit facilities already enjoyed by them from other banks. Banks are also required to exchange information about the conduct of borrowers' accounts with other banks in the specified format at least at quarterly intervals. RBI further advised banks under Consortium Arrangement / Multiple Banking Arrangements that the information exchange should also, inter alia, cover information relating to borrowers' derivative transactions and unhedged foreign currency exposures. In terms of circular dated November 21, 2012, , banks are advised to strictly adhere to the instructions regarding sharing of information relating to credit, derivatives and unhedged foreign currency exposures among themselves and put in place an effective mechanism for information sharing by end-December 2012. Any sanction of fresh loans / ad hoc loans / renewal of loans to new / existing borrowers with effect from January 1, 2013 should be done only after obtaining / sharing necessary information. Non-adherence to the above instructions by banks would be viewed seriously by the Reserve Bank and they would be liable to action, including imposition of penalty, wherever considered appropriate.

Chapter 31 Credit control and monitoring

(1) Formation of Central Repository of Information on Large Credits (CRILC) (Details in RBI circulars dated February 13, 2014 and May 22, 2014)

The RBI has set up a Central Repository of Information on Large Credits (CRILC) to collect, store, and disseminate credit data to lenders. The banks are required to report credit information, including classification of an account as SMA to CRILC on all their borrowers having aggregate fund-based and non-fund based exposure of Rs.50 million and above with them. However, Crop loans are exempted from such reporting, but, banks should continue to report their other agriculture loans in terms of the above instruction. Banks need not report their interbank exposures to CRILC including exposures to NABARD, SIDBI, EXIM Bank and NHB.

RBI Guidelines require banks to also report outstanding current account balance of their customers (debit or credit) of ` 10 million and above. In this context, RBI has clarified that for the purpose of reporting in the Return, banks should report outstanding Current Account balance of any client whose name appears in the PAN Master of the Return, irrespective of the fact whether the client has availed any exposure (fund based and or non-fund based) or not from the bank.

RBI has reiterated that all banks should take utmost care about data accuracy and integrity while submitting the data on large credit to RBI, failing which penal action, as per provisions of the Banking Regulation Act, 1949 could be invoked.

Applicability in Certain Cases

1. It is clarified that banks must report their Cash Credit (CC) and Overdraft (OD) accounts, including overdraft arising out of devolved LCs/invoked guarantees to CRILC as SMA 2 when these are 'out of order' for more than 60 days. Similarly, bills purchased or discounted (other than those backed by LCs issued by banks) and derivative exposures with receivables representing positive mark to market value remaining overdue for more than 60 days should be reported to CRILC as SMA-2.

2 Banks should continue to report the credit information and SMA status to CRILC on loans including loans extended by their overseas branches. However, formation of JLF will not be mandatory in cases of offshore borrowers which do not have any presence in India, either by way of a subsidiary, parent or a group entity. Further, the inclusion of offshore lenders as part of JLF shall not be mandatory.

3 Under CRILC-Main (Quarterly submission) return, banks are required to report their total investment exposure to the borrower being reported. It is clarified that formation of JLF will not be mandatory on reporting of investment portfolio as SMA, except in cases of bonds/debentures acquired on private placement basis or due to conversion of debt under restructuring of advances.

(2) Membership of Credit Information Companies (CICs)

Presently, four CICs, viz. Credit Information Bureau (India) Limited, Equifax Credit Information Services Private Limited, Experian Credit Information Company of India Private Limited and CRIF High Mark Credit Information Services Private Limited have been granted Certificate of Registration by RBI. In terms of Section 15 of the Credit Information Companies (Regulation) Act, 2005 (CICRA), every Credit Institution shall become member of at least one CIC. Further, Section 17 of CICRA stipulates that a CIC may seek and obtain credit information from its members (Credit Institution / CIC) only. As a result, when a Specified User, as defined in CICRA and Credit Information Companies Regulations, 2006, obtains credit information on a particular borrower/client from a CIC, it gets only such information that has been provided to the CIC by its members. This does not include credit history related to those non-member Credit Institutions with which the borrower/client has/had a current or a past exposure. To overcome this problem of incomplete/inaccurate credit information, **on January 15, 2015, RBI has directed that all Credit Institutions (CIs) shall become members of all CICs** and submit data (including historical data) to them. Further, CICs and CIs shall keep the credit information collected/maintained by them, updated regularly on a monthly basis or at such shorter intervals as may be mutually agreed upon between the CI and the CIC in terms of Regulation 10 (a) (i) and (ii) of the Credit Information Companies Regulations, 2006.

As a consequence of above, one-time membership fee charged by the CICs, for CIs to become their members, shall not exceed Rs.10, 000 each. The annual fees charged by the CICs to CIs shall not exceed Rs.5000 each.

(3) End Use of Funds – Monitoring (Details in RBI circular dated January 14, 2011)

Effective monitoring of the end use of funds lent is of critical importance in safeguarding a bank's interest. Further, this also acts as a deterrent for borrowers to misuse the credit facilities sanctioned, and in the process, helps build a healthy credit culture in the Indian banking system. On an assessment of the practices in vogue at certain banks for ensuring the end use of funds by RBI. It was revealed that the expected level of due diligence had not been exercised in some cases facilitating diversion of funds by the borrowers. The shortcomings, amongst others, included, crediting of term loan disbursements to the current/cash credit accounts of borrowers and utilisation thereof for day-to-day operations, as also, **exclusive** reliance on Chartered

Accountants' certification both in regard to infusion of promoters' contribution and deployment of banks' funds.

In the context of the above, RBI has advised that the efficacy of the existing machinery for post-sanction supervision and follow-up of advances should be evaluated and made robust, wherever considered necessary, by each bank. **Illustratively,** the systems and procedures may broadly include the following:

i. meaningful scrutiny of the periodical progress reports and operating/financial statements of the borrowers;
ii. regular visits to the assisted units and inspection of securities charged/ hypothecated to the banks;
iii. periodical scrutiny of the books of accounts of the borrowers;
iv. introduction of stock audits depending upon the extent of exposure;
v. obtention of certificates from the borrowers that the funds have been utilised for the purposes approved and in case of incorrect certification, initiation of prompt action as may be warranted, which may include withdrawal of the facilities sanctioned and legal recourse as well. In case a specific certification regarding diversion/siphoning of funds is desired from the auditors of the borrowers, a separate mandate may be awarded to them and appropriate covenants incorporated in the loan agreements; and
vi. examination of all aspects of diversion of funds during internal audit/ inspection of the branches and at the time of periodical reviews.

(4) Legal Audit of title documents in respect of large value loan accounts (RBI circular dated June 7, 2013)

RBI had issued a circular on June 30, 2011, requiring banks to put in place a system wherein the concurrent auditors were required to look into and report, inter alia, on the genuineness of the title documents especially for large value loans.

2. On a review, RBI has decided that the banks should also subject the title deeds and other documents in respect of all credit exposures of Rs. 5 crore and above to periodic legal audit and

re-verification of title deeds with relevant authorities as part of regular audit exercise till the loan stands fully repaid.

3. The banks should furnish a review note to its Board/ Audit Committee of the Board at quarterly intervals on an ongoing basis giving therein the information in respect of such legal audits which should cover aspects, inter alia, like number of loan accounts due for legal audit for the quarter, how many accounts covered, list of deficiencies observed by the auditors, steps taken to rectify the deficiencies, number of accounts in which the rectification could not take place, course of action to safeguard the interest of bank in such cases, action taken on issues pending from earlier quarters.

Chapter 32 Risk Management and credit rating

(1) Individual Housing Loans

The Loan to Value (LTV) ratios and risk weights for individual housing loans have been revised by RBI on October 8,2015, as under:

Category of loan	LTV ratio (%)	Risk Weight (%)
Upto Rs. 30 lakh	≤ 80	35
	> 80 and ≤ 90	50
Above Rs. 30 lakh and upto Rs. 75 lakh	≤ 75	35

(2) RBI Guidelines on Credit Default Swaps for Corporate Bonds (Details in RBI circular dated May 25, 2011)

1. Objective; The objective of introducing Credit Default Swaps (CDS) on corporate bonds is to provide market participants a tool to transfer and manage credit risk in an effective manner through redistribution of risk. CDS as a risk management product offers the participants the opportunity to hive off credit risk and also to assume credit risk which otherwise may not be possible. Since CDS have benefits like enhancing investment and borrowing opportunities and reducing transaction costs while allowing risk-transfers, such products would increase investors' interest in corporate bonds and would be beneficial to the development of the corporate bond market in India.

2. CDS for Indian Markets – Product Design

2.1 Eligible Participants – Participants in the CDS market are classified as under:

• Users: Entities permitted to buy credit protection (buy CDS contracts) only to hedge their underlying credit risk on corporate bonds. Such entities are not permitted to hold credit protection without having eligible underlying as a hedged item. Users are also not permitted to sell protection and are not permitted to hold short positions in the CDS contracts. However, they are permitted to exit their bought CDS positions by unwinding them with the original counterparty or by assigning them in favour of buyer of the underlying bond.

• Market-makers: Entities permitted to quote both buy and/or sell CDS spreads. They would be permitted to buy protection without having the underlying bond.

2.1.1 The eligible entities under market-makers and users categories would be as under: Market-makers* Commercial Banks, standalone Primary Dealers (PDs), Non-Banking Financial Companies (NBFCs) having sound financials and good track record in providing credit facilities and any other institution specifically permitted by the Reserve Bank. Users Commercial Banks, PDs, NBFCs, Mutual Funds, Insurance Companies, Housing Finance Companies, Provident Funds, Listed Corporates, Foreign Institutional Investors (FIIs) and any other institution specifically permitted by the Reserve Bank.

*Insurance companies and Mutual Funds would be permitted as market-makers subject to their having strong financials and risk management capabilities as prescribed by their respective regulators (IRDA and SEBI) and as and when permitted by the respective regulatory authorities.

2.1.2 All CDS trades shall have an RBI regulated entity at least on one side of the transaction.

2.2 Eligibility norms for market-makers

2.2.1 Commercial banks who intend to act as market-makers shall fulfill the following criteria: a) Minimum CRAR of 11 per cent with core CRAR (Tier I) of at least 7 per cent; b) Net NPAs of less than 3 per cent. Banks should submit their Board approved policy and the date of commencement of CDS trading as market-makers to RBI.

2.2.2 NBFCs having sound financial strength, good track record and involved in providing credit facilities may be allowed to act as market-makers, subject to complying with the following criteria: a) Minimum Net Owned Funds of Rs. 500 crore; b) Minimum CRAR of 15 per cent; c) Net NPAs of less than 3 per cent; and d) Have robust risk management systems in place to deal with various risks. NBFCs shall only participate in CDS market as users. As users, they would be permitted to buy credit protection only to hedge their credit risk on corporate bonds they hold. They are not permitted to sell protection and hence not permitted to enter into short positions in

the CDS contracts. However, they are permitted to exit their bought CDS positions by unwinding them with the original counterparty or by assigning them in favour of buyer of the underlying bond.

2.2.3 PDs intending to act as market-makers shall fulfil the following criteria: a) Minimum Net Owned Funds of Rs. 500 crore; b) Minimum CRAR of 15 per cent; and c) Have robust risk management systems in place to deal with various risks.

2.2.4 In case a market-maker fails to meet one or more of the eligibility criteria subsequent to commencing the CDS transactions, it would not be eligible to sell new protection. As regards existing contracts, such protection sellers would meet all their obligations as per the contract.

2.2.5 The list of eligible market-makers will be available on RBI website.

2.3 Reference entity

The reference entity in a CDS contract, against whose default the protection is bought and sold, shall be a single legal resident entity [the term resident will be as defined in Section 2(v) of Foreign Exchange Management Act, 1999] and the direct obligor for the reference asset/obligation and the deliverable asset/obligation.

2.4 Reference obligation (eligible underlying for CDS) - eligibility criteria (i) CDS will be allowed only on listed corporate bonds as reference obligations. (ii) However, CDS can also be written on unlisted but rated bonds of infrastructure companies. Besides, unlisted/unrated bonds issued by the SPVs set up by infrastructure companies are also eligible as reference obligation. In the case of banks, the net credit exposure on account of such CDS should be within the limit of 10% of investment portfolio prescribed for unlisted/unrated bonds as per extant guidelines issued by RBI. (iii) NBFCs and PDs shall adhere to the extant regulatory guidelines prescribed in respect of credit exposure limits for investment in unlisted/unrated bonds. (iv) The reference obligations are required to be in dematerialised form only. (v) The reference obligation of a specific obligor covered by the CDS contract should be specified a priori in the contract and reviewed periodically for better risk management. (vi) Protection sellers should ensure not to sell protection on reference entities/obligations on which there are regulatory restrictions on assuming exposures in the cash market such as, the restriction against banks holding unrated bonds, single/group exposure limits and any other restriction imposed by the regulators from time to time.

2.5 Requirement of the underlying in CDS

2.5.1 The users cannot buy CDS for amounts higher than the face value of corporate bonds held by them and for periods longer than the tenor of corporate bonds held by them.

2.5.2 Holding CDS Protection by users without having an underlying: Since the users are envisaged to use the CDS only for hedging their credit risks, assumed due to their investment in corporate bonds, they shall not, at any point of time, maintain naked CDS protection i.e. CDS purchase position without having an eligible underlying.

2.6 Exiting CDS transactions by users

2.6.1 Users cannot exit their bought positions by entering into an offsetting sale contract. They can exit their bought position by either unwinding the contract with the original counterparty or, in the event of sale of the underlying bond, by assigning (novating) the CDS protection, to the purchaser of the underlying bond (the "transferee") subject to consent of the original protection seller (the "remaining party"). After assigning the contract, the original buyer of protection (the "transferor") will end his involvement in the transaction and credit risk will continue to lie with the original protection seller.

2.6.2 In case of sale of the underlying, every effort should be made to unwind the CDS position immediately on sale of the underlying. The users would be given a maximum grace period of ten business days from the date of sale of the underlying bond to unwind the CDS position.

2.6.3 In the case of unwinding of the CDS contract, the original counterparty (protection seller) is required to ensure that the protection buyer has the underlying at the time of unwinding. The protection seller may also ensure that the transaction is done at a transparent market price and this must be subject to rigorous audit discipline.

2.7 CDS transactions between related parties; CDS transactions are not permitted to be entered into either between related parties or where the reference entity is a related party to either of the contracting parties. Related parties for the purpose of these guidelines will be as defined in 'Accounting Standard 18 – Related Party Disclosures'. In the case of foreign banks operating in India, the term 'related parties' shall include an entity which is a related party of the foreign bank, its parent, or group entity.

2.8 Other Requirements The single-name CDS on corporate bonds should also satisfy the following requirements: (i) the user (except FIIs) and market-maker shall be resident entities; (ii) the identity of the parties responsible for determining whether a credit event has occurred must

be clearly defined a priori in the documentation; 5 (iii) the reference asset/obligation and the deliverable asset/obligation shall be to a resident and denominated in Indian Rupees; (iv) the CDS contract shall be denominated and settled in Indian Rupees; (v) Obligations such as asset-backed securities/mortgage-backed securities, convertible bonds and bonds with call/put options shall not be permitted as reference and deliverable obligations; (vi) CDS cannot be written on interest receivables; (vii) CDS shall not be written on securities with original maturity up to one year e.g., Commercial Papers (CPs), Certificate of Deposits (CDs) and Non-Convertible Debentures (NCDs) with original maturity up to one year; (viii) the CDS contract must represent a direct claim on the protection seller; (ix) the CDS contract must be irrevocable; there must be no clause in the contract that would allow the protection seller to unilaterally cancel the contract. However, if protection buyer defaults under the terms of contract, protection seller can cancel/revoke the contract; (x) the CDS contract should not have any clause that may prevent the protection seller from making the credit event payment in a timely manner, after occurrence of the credit event and completion of necessary formalities in terms of the contract; (xi) the protection seller shall have no recourse to the protection buyer for credit-event losses; (xii) dealing in any structured financial product with CDS as one of the components shall not be permitted; and (xiii) dealing in any derivative product where the CDS itself is an underlying shall not be permissible.

2.9 Documentation Fixed Income Money Market and Derivatives Association of India (FIMMDA) shall devise a Master Agreement for Indian CDS. There would be two sets of documentation: one set covering transactions between user and market-maker and the other set covering transactions between two market-makers. While drafting documents, it would be absolutely necessary for the participating institutions to ensure that transactions are intra vires and legal risks are reduced to the maximum possible extent.

2.10 Standardisation of the CDS Contract; The CDS contracts shall be standardized. The standardisation of CDS contracts shall be achieved in terms of coupon, coupon payment dates, etc. as put in place by FIMMDA in consultation with the market participants.

2.11 Credit Events

2.11.1 The credit events specified in the CDS contract may cover: Bankruptcy, Failure to pay, Repudiation/moratorium, Obligation acceleration, Obligation default, Restructuring approved under Board for Industrial and Financial Reconstruction (BIFR) and Corporate Debt

Restructuring (CDR) mechanism and corporate bond restructuring. The contracting parties to a CDS may include all or any of the approved credit events. Further, the definition of various credit events should be clearly defined in the bilateral Master Agreement prepared by FIMMDA.

2.11.2 Succession event: Participants may adhere to the provisions given in the Master Agreement for CDS prepared by FIMMDA.

2.11.3 Determination Committee: The Determination Committee (DC) shall be formed by the market participants and FIMMDA. The DC shall be based in India and shall deliberate and resolve CDS related issues such as Credit Events, CDS Auctions, Succession Events, Substitute Reference Obligations, etc. The decisions of the Committee would be binding on CDS market participants. In order to provide adequate representation to users, at least 25 per cent of the members should be drawn from the users.

2.12 Settlement methodologies

2.12.1 The parties to the CDS transaction shall determine upfront, the procedure and method of settlement (cash/physical/auction) to be followed in the event of occurrence of a credit event and document the same in the CDS documentation.

2.12.2 For transactions involving users, physical settlement is mandatory. For other transactions, market-makers can opt for any of the three settlement methods (physical, cash and auction), provided the CDS documentation envisages such settlement. While the physical settlement would require the protection buyer to transfer any of the deliverable obligations against the receipt of its full notional / face value, in cash settlement, the protection seller would pay to the protection buyer an amount equivalent to the loss resulting from the credit event of the reference entity.

2.12.3 Auction Settlement: Auction settlement may be conducted in those cases as deemed fit by the DC. Auction specific terms (e.g. auction date, time, market quotation amount, deliverable obligations, etc.) will be set by the DC on a case by case basis. If parties do not select Auction Settlement, they will need to bilaterally settle their trades in accordance with the Settlement Method (unless otherwise freshly negotiated between the parties).

2.13 Accounting The accounting norms applicable to CDS contracts shall be on the lines indicated in the 'Accounting Standard AS-30 – Financial Instruments: Recognition and Measurement', 'AS- 31, Financial Instruments: Presentation' and 'AS-32 on Disclosures' as approved by the Institute of Chartered Accountants of India (ICAI). As the accounting standards

on derivatives are still evolving, market participants, with the approval of their respective boards, shall adopt appropriate norms for accounting of CDS transactions which are in compliance with the Indian accounting standards and approved by the regulators from time to time.

The RBI circular also gives details regarding pricing/Valuation methodologies and Risk Management architecture for CDS.

(3) Credit Risk Management

In addition to the guidelines contained in 'Risk Management Systems in Banks' and 'Guidance Notes on Management of Credit Risk and Market Risk'. RBI has advised the banks the following:

1. Lenders should carry out their independent and objective credit appraisal in all cases and must not depend on credit appraisal reports prepared by outside consultants, especially the in-house consultants of the borrowing entity.

2. Banks/lenders should carry out sensitivity tests/scenario analysis, especially for infrastructure projects, which should inter alia include project delays and cost overruns. This will aid in taking a view on viability of the project at the time of deciding Corrective Action Plan (CAP) under SDR (Strategic Debt Restructuring)

3 Lenders should ascertain the source and quality of equity capital brought in by the promoters /shareholders. Multiple leveraging, especially, in infrastructure projects, is a matter of concern as it effectively camouflages the financial ratios such as Debt/Equity ratio, leading to adverse selection of the borrowers. Therefore, lenders should ensure at the time of credit appraisal that debt of the parent company is not infused as equity capital of the subsidiary/SPV.

4 Ministry of Corporate Affairs had introduced the concept of a Director Identification Number (DIN) with the insertion of Sections 266A to 266G of Companies (Amendment) Act, 2006. Further, in terms of paragraph 5.4 of our Master Circular on Wilful Defaulters dated July 1, 2013, in order to ensure that directors are correctly identified and in no case, persons whose names appear to be similar to the names of directors appearing in the list of wilful defaulters, are wrongfully denied credit facilities on such grounds, banks/FIs have been advised to include the Director Identification Number (DIN) as one of the fields in the data submitted by them to Reserve Bank of India/Credit Information Companies.

5. It is reiterated that while carrying out the credit appraisal, banks should verify as to whether the names of any of the directors of the companies appear in the list of defaulters/ wilful defaulters by way of reference to DIN/PAN etc. Further, in case of any doubt arising on account of identical names, banks should use independent sources for confirmation of the identity of directors rather than seeking declaration from the borrowing company.

6. In the context of Wilful Defaulters, RBI guidelines state that, "with a view to monitoring the end-use of funds, if the lenders desire a specific certification from the borrowers' auditors regarding diversion / siphoning of funds by the borrower, the lender should award a separate mandate to the auditors for the purpose. To facilitate such certification by the auditors the banks and FIs will also need to ensure that appropriate covenants in the loan agreements are incorporated to enable award of such a mandate by the lenders to the borrowers / auditors".

7. In addition to the above, banks are advised that with a view to ensuring proper end-use of funds and preventing diversion/siphoning of funds by the borrowers, lenders could consider engaging their own auditors for such specific certification purpose without relying on certification given by borrower's auditors. However, this cannot substitute bank's basic minimum own diligence in the matter.

8. **Registration of security with CERSAI**: Currently security registration, especially registration of mortgages, is done at district level and Central Registry of Securitisation Asset Reconstruction and Security Interest of India (CERSAI) is generally used to register equitable mortgages. The Government mandate to register all types of mortgages with CERSAI will have to be strictly followed by banks. In this connection, instructions contained in RBI circular dated April 21, 2011, on 'Setting up of Central Electronic Registry under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002' should be followed, i.e. transactions relating to securitization and reconstruction of financial assets and those relating to mortgage by deposit of title deeds to secure any loan or advances granted by banks and financial institutions, as defined under the SARFAESI Act, are to be registered in the Central Registry.

9. Board Oversight: The Board of Directors of banks should take all necessary steps to arrest the deteriorating asset quality in their books and should focus on improving the credit risk management system. Early recognition of problems in asset quality and resolution envisaged in these guidelines requires the lenders to be proactive and make use of CRILC as soon as it

becomes functional. Boards of banks should put in place a policy for timely submission of credit information to CRILC and accessing information therefrom, prompt formation of Joint Lenders' Forums (JLFs)[3], monitoring the progress of JLFs and adoption of Corrective Action Plans (CAPs)[4], etc. There should be a periodical review, say on a half yearly basis, of the above policy. The boards of banks should put in place a system for proper and timely classification of borrowers as wilful defaulters or/and non-cooperative borrowers. Further, Boards of banks should periodically review the accounts classified as such, say on a half yearly basis.

Chapter 33 Rehabilitation and recovery

(1) Non-Cooperative Borrowers (Details in RBI circular dated December 22, 2014)

The definition of a Non-Cooperative Borrower is as under:

"A non-cooperative borrower is one who does not engage constructively with his lender by defaulting in timely repayment of dues while having ability to pay, thwarting lenders' efforts for recovery of their dues by not providing necessary information sought, denying access to assets financed / collateral securities, obstructing sale of securities, etc. In effect, a non-cooperative borrower is a defaulter who deliberately stone walls legitimate efforts of the lenders to recover their dues."

Banks/FIs should take the following measures in classifying/declassifying a borrower as non-cooperative borrower and reporting information on such borrowers to Central Repository of Information on Large Credits (CRILC):

a. The cut off limit for classifying borrowers as non-cooperative would be those borrowers having aggregate fund-based and non-fund based facilities of Rs.50 million from the concerned bank/FI. A non-cooperative borrower in case of a company will include, besides the company, its promoters and directors (excluding independent directors and directors nominated by the Government and the lending institutions). In case of business enterprises (other than companies), non-cooperative borrowers would include persons who are in-charge and responsible for the management of the affairs of the business enterprise.

b. It would be imperative on the part of the banks / FIs to put in place a transparent mechanism for classifying borrowers as non-cooperative. A solitary or isolated instance should not be the basis for such classification. The decision to classify the borrower as non-cooperative borrower should

be entrusted to a Committee of higher functionaries headed by an Executive Director and consisting of two other senior officers of the rank of General Managers/ Deputy General Managers as decided by the Board of the concerned bank/FI.

c. If the Committee concludes that the borrower is non-cooperative, it shall issue a Show Cause Notice to the concerned borrower (and the promoter/whole-time directors in case of companies) and call for his submission and after considering his submission issue an order recording the borrower to be non-cooperative and the reasons for the same. An opportunity should be given to the borrower for a personal hearing if the Committee feels such an opportunity is necessary.
d. The order of the Committee should be reviewed by another Committee headed by the Chairman / CEO and MD and consisting, in addition, of two independent directors of the Bank/FI and the order shall become final only after it is confirmed by the said Review Committee.
e. Banks/FIs will be required to report information on their non-cooperative borrowers to CRILC within 21 days from the close of the relevant quarter.
f. Boards of banks/FIs should review on a half-yearly basis the status of non-cooperative borrowers for deciding whether their names can be declassified as evidenced by their return to credit discipline and cooperative dealings. Removal of names from the list of non-cooperative borrowers should be separately reported under CRILC with adequate reasoning/rationale for such removal.
g. If any particular entity as mentioned in (a) above is reported as non-cooperative, any fresh exposure to such a borrower will by implication entail greater risk necessitating higher provisioning. Banks/FIs will therefore be required to make higher provisioning as applicable to substandard assets in respect of new loans sanctioned to such borrowers as also new loans sanctioned to any other company that has on its board of directors any of the whole time directors/promoters of a non-cooperative borrowing company or any firm in which such a non-cooperative borrower is in charge of management of the affairs. However, for the purpose of asset classification and income recognition, the new loans would be treated as standard assets. It is reiterated that as the CRILC data is collected under the provisions of the RBI Act, non-adherence to reporting instructions attracts penal provisions under the Act.

(2) Provisioning pertaining to Credit Card Accounts

In order to bring in greater credit discipline as also to provide operational flexibility to credit card issuers, RBI has decided that, with effect from July 16,2015, 'past due' status of a credit card account for the purpose of asset classification would be reckoned from the payment due date mentioned in the monthly credit card statement. Consequently, in case of banks, a credit card account will be treated as non-performing asset if the minimum amount due, as mentioned in the statement, is not paid fully within 90 days from the payment due date mentioned in the statement. However, banks shall report a credit card account as 'past due' to credit information companies (CICs) or levy penal charges, viz. late payment charges, etc., if any, only when a credit card account remains 'past due' for more than three days. The number of 'days past due' and late payment charges shall, however, be computed from the payment due date mentioned in the credit card statement.

(3) Framework for Revitalising Distressed Assets in the Economy

(3 a) Strategic Debt Restructuring

(Details in RBI circulars dated February 26, 2014, October 21, 2014, June 8, 2015, September 24, 2015 and February 25, 2016)

1. Formation of Joint Lenders' Forum

Before a loan account turns into a NPA, banks are required to identify incipient stress in the account by creating three sub-categories under the Special Mention Account (SMA[1]) category as given below:

SMA Sub-categories	Basis for classification
SMA-0	Principal or interest payment not overdue for more than 30 days but account showing signs of incipient stress*
SMA-1	Principal or interest payment overdue between 31-60 days
SMA-2	Principal or interest payment overdue between 61-90 days

*Illustrative list of signs of stress for categorising an account as SMA-0:

1. Delay of 90 days or more in (a) submission of stock statement / other stipulated operating control statements or (b) credit monitoring or financial statements or (c) non-renewal of facilities based on audited financials.
2. Actual sales / operating profits falling short of projections accepted for loan sanction by 40% or more; or a single event of non-cooperation / prevention from conduct of stock audits by banks; or reduction of Drawing Power (DP) by 20% or more after a stock audit; or evidence of diversion of funds for unapproved purpose; or drop in internal risk rating by 2 or more notches in a single review.
3. Return of 3 or more cheques (or electronic debit instructions) issued by borrowers in 30 days on grounds of non-availability of balance/DP in the account or return of 3 or more bills / cheques discounted or sent under collection by the borrower.
4. Devolvement of Deferred Payment Guarantee (DPG) instalments or Letters of Credit (LCs) or invocation of Bank Guarantees (BGs) and its non-payment within 30 days.
5. Third request for extension of time either for creation or perfection of securities as against time specified in original sanction terms or for compliance with any other terms and conditions of sanction.
6. Increase in frequency of overdrafts in current accounts.
7. The borrower reporting stress in the business and financials.
8. Promoter(s) pledging/selling their shares in the borrower company due to financial stress.

Banks are advised that as soon as an account is reported by any of the lenders to CRILC as SMA-2, they should mandatorily form a committee to be called Joint Lenders' Forum (JLF) if the aggregate exposure (AE) [fund based and non-fund based taken together] of lenders in that account is Rs 1000 million and above (Banks are permitted to report their SMA-2 accounts and JLF formations on a weekly basis at the close of business on every Friday. If Friday happens to be a holiday, they will report the same on the preceding working day of the week). Lenders also have the option of forming a JLF even when the AE in an account is less than Rs.1000 million and/or when the account is reported as SMA-0 or SMA-1. Formation of JLF will not be mandatory in cases of offshore borrowers which do not have any presence in India, either by way of a subsidiary, parent or a group entity. Further, the inclusion of offshore lenders as part of JLF shall not be mandatory. Formation of JLF will also not be mandatory on reporting of investment

portfolio as SMA, except in cases of bonds/debentures acquired on private placement basis or due to conversion of debt under restructuring of advances.

While the existing Consortium Arrangement for consortium accounts will serve as JLF, with the Consortium Leader as convener, for accounts under Multiple Banking Arrangements (MBA), the lender with the highest AE will convene JLF at the earliest and facilitate exchange of credit information on the account. In case, there are multiple consortium of lenders for a borrower (e.g. separate consortium for working capital and term loans), the lender with the highest AE will convene the JLF.

It is possible that a borrower may request the lender/s, with substantiated grounds, for formation of a JLF on account of imminent stress. When such a request is received by a lender, the account should be reported to CRILC as SMA-0, and the lenders should also form the JLF immediately if the AE is Rs. 1000 million and above. Presently, JLF formation is optional in other cases of SMA-0 reporting.

All the lenders should formulate and sign an Agreement (which may be called JLF agreement) incorporating the broad rules for the functioning of the JLF. The Indian Banks' Association (IBA) would prepare a Master JLF agreement and operational guidelines for JLF which could be adopted by all lenders. The JLF should explore the possibility of the borrower setting right the irregularities/weaknesses in the account. The JLF may invite representatives of the Central/State Government/Project authorities/Local authorities, if they have a role in the implementation of the project financed.

While JLF formation and subsequent corrective actions will be mandatory in accounts having AE of Rs.1000 million and above, in other cases also, the lenders will have to monitor the asset quality closely and take corrective action for effective resolution as deemed appropriate.

2. Joint Lenders' Forum Empowered Group (JLF – EG)

It was represented to RBI that sometimes Boards of the banks find it difficult to approve the decisions taken by JLF as the JLFs do not have senior level representations from the participating lenders. Therefore, RBI has advised, through its circular dated September 24, 2015, that the banks are expected to depute sufficiently empowered senior level officials for deliberations and decisions in the meetings of JLF. RBI has also decided that JLF will finalise the CAP and the same will be placed before an Empowered Group (EG) of lenders, which will

be tasked to approve the rectification/restructuring packages under CAPs. **RBI has modified this on February 25, 2016, and has advised that approval of JLF-EG is mandatory only in cases of rectification with additional finance and cases of restructuring under a CAP.**

The JLF-EG shall have the following composition:

a. The top two banks in the system, in terms of advances, namely SBI and ICICI Bank, will continue to be permanent members of JLF EG, irrespective of whether or not they are lenders in the particular JLF.

b. If SBI and ICICI Bank are the lenders in a JLF, the JLF-EG would consist of these two banks, the three lenders (other than ICICI Bank and SBI) having largest exposures to the borrower and the two largest banks in terms of advances (as per list on RBI website) which do not have any exposure to the borrower.

c. If either of SBI or ICICI bank is a lender, the JLF-EG would consist of these two banks, the four lenders (other than ICICI Bank and SBI) having largest exposures to the borrower and the next largest bank in terms of advances which does not have any exposure to the borrower.

d. If neither SBI nor ICICI Bank are the lenders in a JLF, then the JLF-EG would consist of these two banks and the five lenders having largest exposures to the borrower.

e. All the JLF-EG members would have equal voting rights irrespective of size of exposure to the borrower.

The JLF convening bank will convene the JLF-EG and provide the secretarial support to it.

3. Corrective Action Plan (CAP) by JLF

3.1 The JLF may explore various options to resolve the stress in the account. The intention is not to encourage a particular resolution option, e.g. restructuring or recovery, but to arrive at an early and feasible solution to preserve the economic value of the underlying assets as well as the lenders' loans. The options under Corrective Action Plan (CAP) by the JLF would generally include:

(a) Rectification - Obtaining a specific commitment from the borrower to regularise the account so that the account comes out of SMA status or does not slip into the NPA category. The commitment should be supported with identifiable cash flows within the required time period and without involving any loss or sacrifice on the part of the existing lenders. If the existing promoters are not in a position to bring in additional money or take any measures to regularise the account, the possibility of getting some other equity/strategic investors to the company may

be explored by the JLF in consultation with the borrower. These measures are intended to turn-around the entity/company without any change in terms and conditions of the loan. The JLF may also consider providing need based additional finance to the borrower, if considered necessary, as part of the rectification process. However, it should be strictly ensured that additional financing is not provided with a view to ever-greening the account.

(b) Restructuring - Consider the possibility of restructuring the account if it is prima facie viable and the borrower is not a wilful defaulter, i.e., there is no diversion of funds, fraud or malfeasance, etc. At this stage, commitment from promoters for extending their personal guarantees along with their net worth statement supported by copies of legal titles to assets may be obtained along with a declaration that they would not undertake any transaction that would alienate assets without the permission of the JLF. Any deviation from the commitment by the borrowers affecting the security/recoverability of the loans may be treated as a valid factor for initiating recovery process. For this action to be sustainable, the lenders in the JLF may sign an Inter Creditor Agreement (ICA) and also require the borrower to sign the Debtor Creditor Agreement (DCA) which would provide the legal basis for any restructuring process. The formats used by the Corporate Debt Restructuring (CDR) mechanism for ICA and DCA could be considered, if necessary with appropriate changes. Further, a 'stand still'[2] clause could be stipulated in the DCA to enable a smooth process of restructuring. The 'stand-still' clause does not mean that the borrower is precluded from making payments to the lenders. The ICA may also stipulate that both secured and unsecured creditors need to agree to the final resolution.

(c) Recovery - Once the first two options at (a) and (b) above are seen as not feasible, due recovery process may be resorted to. The JLF may decide the best recovery process to be followed, among the various legal and other recovery options available, with a view to optimising the efforts and results.

3.2 The decisions, **agreed upon by a minimum of 75% of creditors by value and 50% of creditors by number** in the JLF, would be considered as the basis for proceeding with the restructuring of the account, and will be binding on all lenders under the terms of the ICA. However, if the JLF decides to proceed with recovery, the minimum criteria for binding decision, if any, under any relevant laws/Acts, would be applicable.

3.3 The JLF is required to arrive at an agreement on the option to be adopted for CAP within **45 days** from (i) the date of an account being reported as SMA-2 by one or more lender, or (ii)

receipt of request from the borrower to form a JLF, with substantiated grounds, if it senses imminent stress. The JLF should sign off the detailed final CAP within the next 30 days from the date of arriving at such an agreement.

3.4 If the JLF decides on options 3.1 (a) or (b), but the account fails to perform as per the agreed terms under option (a) or (b), the JLF should initiate recovery under option 3.1 (c).

4. Restructuring Process

4.1 If the JLF decides restructuring of the account as CAP, it will have the option of either referring the account to CDR Cell after a decision to restructure is taken under para 3.1 as indicated above or restructure the same independent of the CDR mechanism.

4.2 Restructuring by JLF

4.2.1 If the JLF decides to restructure an account independent of the CDR mechanism, the JLF should carry out the detailed Techno-Economic Viability (TEV) study, and if found viable, finalise the restructuring package within 30 days from the date of signing off the final CAP as mentioned in paragraph 3.3 above.

4.2.2 For accounts with AE of less than Rs.5000 million, the above-mentioned restructuring package should be approved by the JLF and conveyed by the lenders to the borrower within the next 15 days for implementation.

4.2.3 For accounts with AE of Rs.5000 million and above, the above-mentioned TEV study and restructuring package will have to be subjected to an evaluation by an Independent Evaluation Committee (IEC) of experts fulfilling certain eligibility conditions. The IEC will look into the viability aspects after ensuring that the terms of restructuring are fair to the lenders. The IEC will be required to give their recommendation in these cases to the JLF within a period of **45 days**. Thereafter, considering the views of IEC if the JLF decides to go ahead with the restructuring, the restructuring package including all terms and conditions as mutually agreed upon between the lenders and borrower, would have to be approved by all the lenders and communicated to the borrower within next 15 days for implementation.

4.2.4 Asset Classification benefit as applicable under the extant guidelines will accrue to such restructured accounts as if they were restructured under CDR mechanism. For this purpose, the asset classification of the account as on the date of formation of JLF will be taken into account.

4.2.5 The above-mentioned time limits are maximum permitted time periods and the JLF should try to arrive at a restructuring package as soon as possible in cases of simple restructuring.

4.2.6 Restructuring cases will be taken up by the JLF only in respect of assets reported as Standard, SMA or Sub-Standard by one or more lenders of the JLF. While generally no account classified as doubtful should be considered by the JLF for restructuring, in cases where a small portion of debt is doubtful i.e. the account is standard/sub-standard in the books of at least 90% of creditors (by value), the account may then be considered under JLF for restructuring. **In partial modification of the above, RBI advised on September 24, 2015, that a JLF may decide on restructuring of an account classified as 'doubtful' in the books of one or more lenders, similar to the restructuring of SMA2 and sub-standard assets, if the account has been assessed as viable under the TEV and the JLF-EG concurs with the assessment and approves the proposal.**

4.2.7 Wilful defaulters will normally not be eligible for restructuring. However, the JLF may review the reasons for classification of the borrower as a wilful defaulter and satisfy itself that the borrower is in a position to rectify the wilful default. The decision to restructure such cases should however also have the approvals of the board/s of individual bank/s within the JLF who have classified the borrower as wilful defaulter. **In cases of fraud/malfeasance, where the existing promoters are replaced by new promoters and the borrower company is totally delinked from such erstwhile promoters/management, banks and JLF may take a view on restructuring of such accounts based on their viability, without prejudice to the continuance of criminal action against the erstwhile promoters/management**

4.2.8 The viability of the account should be determined by the JLF based on acceptable viability benchmarks determined by them. Illustratively, the parameters may include the Debt Equity Ratio, Debt Service Coverage Ratio, Liquidity/Current Ratio and the amount of provision required in lieu of the diminution in the fair value of the restructured advance, etc.

4.3 Restructuring Referred by the JLF to the CDR Cell

4.3.1 If the JLF decides to refer the account to CDR Cell after a decision to restructure is taken under para 3.1, the following procedure may be followed.

4.3.2 As the preliminary viability of account has already been decided by the JLF, CDR Cell should directly prepare the Techno-Economic Viability (TEV) study and restructuring plan in consultation with JLF within 30 days from the date of reference to it by the JLF.

4.3.3 For accounts with AE of less than Rs.5000 million, the above-mentioned restructuring package should be submitted to CDR Empowered Group (EG) for approval. Under extant

instructions, CDR EG can approve or suggest modifications but ensure that a final decision is taken within a total period of 90 days, which can be extended up to a maximum of 180 days from the date of reference to CDR Cell. However, the cases referred to CDR Cell by JLF will have to be finally decided by the CDR EG within the next 30 days. If approved by CDR EG, the restructuring package should be approved by all lenders and conveyed to the borrower within the next 30 days for implementation.

4.3.4 For accounts with AE of Rs.5000 million and above, the TEV study and restructuring package, prepared by CDR Cell, will have to be subjected to an evaluation by an Independent Evaluation Committee (IEC) of experts. The IEC will look into the viability aspects after ensuring that the terms of restructuring are fair to the lenders. The IEC will be required to give their recommendation in these aspects to the CDR Cell under advice to JLF within a period of **45 days**. Thereafter, considering the views of IEC if the JLF decides to go ahead with the restructuring, the same should be communicated to CDR Cell and CDR Cell should submit the restructuring package to CDR EG within a total period of 7 days from receiving the views of IEC. Thereafter, CDR EG should decide on the approval/modification/rejection within the next 30 days. If approved by CDR EG, the restructuring package should be approved by all lenders and conveyed to the borrower within the next 30 days for implementation.

5. Other Issues/Conditions Relating to Restructuring by JLF/CDR Cell

5.1 Both under JLF and CDR mechanism, the restructuring package should also stipulate the timeline during which certain viability milestones (e.g. improvement in certain financial ratios after a period of time, say, 6 months or 1 year and so on) would be achieved. The JLF must periodically review the account for achievement/non-achievement of milestones and should consider initiating suitable measures including recovery measures as deemed appropriate. With a view to ensuring more stake of promoters in reviving stressed accounts and provide banks with enhanced capabilities to initiate change of ownership in accounts which fail to achieve the projected viability milestones, banks may, at their discretion, undertake a **'Strategic Debt Restructuring (SDR)'** by converting loan dues to equity shares. In addition to conversion of debt into equity under SDR, banks may also convert their debt into equity at the time of restructuring of credit facilities under the extant restructuring guidelines. In cases of failure of rectification or restructuring as a CAP as decided by JLF, JLF will have the option to initiate **Strategic Debt Restructuring (SDR)** to effect change of management of the borrower

company. **(Guidelines for conversion of loans into equity, change of ownership/management, asset classification benefits and regulatory exemptions, are given in RBI circulars dated June 8, 2015 and February 25, 2016)**

SDR framework will also be available to Asset Reconstruction Company (ARC), if it is a member of the JLF undertaking SDR of a borrower company.

5.2 Restructuring whether under JLF or CDR is to be completed within the specified time periods. The JLF and CDR Cell should optimally utilise the specified time periods so that the aggregate time limit is not breached under any mode of restructuring. If the JLF/CDR takes a shorter time for an activity as against the prescribed limit, then it can have the discretion to utilise the saved time for other activities provided the aggregate time limit is not breached.

5.3 The general principle of restructuring should be that the shareholders bear the first loss rather than the debt holders. With this principle in view and also to ensure more 'skin in the game' of promoters, JLF/CDR may consider the following options when a loan is restructured:

- Possibility of transferring equity of the company by promoters to the lenders to compensate for their sacrifices;
- Promoters infusing more equity into their companies;
- Transfer of the promoters' holdings to a security trustee or an escrow arrangement till turnaround of company. This will enable a change in management control, should lenders favour it.
- It has been observed that in many cases of restructuring of accounts, borrower companies are not able to come out of stress due to operational/ managerial inefficiencies despite substantial sacrifices made by the lending banks. In such cases, change of ownership will be a preferred option. So, the Joint Lenders' Forum (JLF) should actively consider such change in ownership under the above Framework

(**Note: The Strategic Debt Restructuring (SDR) has been introduced with a view to ensuring more stake of promoters in reviving stressed accounts and providing banks with enhanced capabilities to initiate change of ownership, where necessary, in accounts which fail to achieve the agreed critical conditions and viability milestones. Therefore, banks should consider using SDR only in cases where change in ownership is likely to improve the economic value of the loan asset and the prospects of recovery of their dues. The trigger for SDR must be non-achievement of viability milestones and /or non-adherence to 'critical conditions' linked to the option of invoking SDR, as stipulated in restructuring agreement,**

and SDR cannot be triggered for any other reason. Banks should include necessary covenants in all loan agreements, including restructuring, supported by necessary approvals/authorisations (including special resolution by the shareholders) from the borrower company, as required under extant laws/regulations, to enable invocation of SDR in applicable cases'. Further, as JLF has the option to initiate SDR to effect change of management of the borrower company in cases of failure of rectification or restructuring as a CAP as decided by JLF, necessary covenants should also be part of rectification arrangement.)

5.4 In case a borrower has undertaken diversification or expansion of the activities which has resulted in the stress on the core-business of the group, a clause for sale of non-core assets or other assets may be stipulated as a condition for restructuring the account, if under the TEV study the account is likely to become viable on hiving-off of non-core activities and other assets.

5.5 For restructuring of dues in respect of listed companies, lenders may be ab-initio compensated for their loss/sacrifice (diminution in fair value of account in net present value terms) by way of issuance of equities of the company upfront, subject to the extant regulations and statutory requirements. In such cases, the restructuring agreement shall not incorporate any right of recompense clause. However, if the lenders' sacrifice is not fully compensated by way of issuance of equities, the right of recompense clause may be incorporated to the extent of shortfall. For unlisted companies, the JLF will have option of either getting equities issued or incorporate suitable 'right to recompense' clause.

5.6 If acquisition of equity shares, as indicated in paragraph 5.5 above, results in exceeding the extant regulatory Capital Market Exposure (CME) limit, the same will not be considered as a breach of regulatory limit. However, this will require reporting to RBI and disclosure by banks in the Notes to Accounts in Annual Financial Statements.

5.7 In order to distinguish the differential security interest available to secured lenders, partially secured lenders and unsecured lenders, the JLF/CDR could consider various options like:

- Prior agreement in the ICA among the above classes of lenders regarding repayments, say, as per an agreed waterfall mechanism;
- A structured agreement stipulating priority of secured creditors;
- Appropriation of repayment proceeds among secured, partially secured and unsecured lenders in certain pre-agreed proportion.

The above is only an illustrative list and the JLF may decide on a mutually agreed option. It also needs to be emphasised that while one bank may have a better security interest when it comes to one borrower, the case may be vice versa in the case of another borrower. So, it would be beneficial if lenders appreciate the concerns of fellow lenders and arrive at a mutually agreed option with a view to preserving the economic value of assets. Once an option is agreed upon, the bank having the largest exposure may take the lead in ensuring distribution according to agreed terms once the restructuring package is implemented.

5.8 As regards prudential norms and operational details, RBI's guidelines on CDR Mechanism, including OTS, will be applicable to the extent that they are not inconsistent with these guidelines.

6. Prudential Norms on Asset Classification and Provisioning

6.1 While a restructuring proposal is under consideration by the JLF/CDR, the usual asset classification norm would continue to apply. The process of re-classification of an asset should not stop merely because restructuring proposal is under consideration by the JLF/CDR.

6.2 **As an incentive for quick implementation of a restructuring package, the special asset classification benefit was provided in the scheme. However, this has been withdrawn for all restructurings, with effect from April 1, 2015, with the exception of provisions related to changes in Date of Commencement of Commercial Operations (DCCO) in respect of infrastructure and non-infrastructure project loans.**

6.3 As a measure to ensure adherence to the proposals made in these guidelines as also to impose disincentives on borrowers for not maintaining credit discipline, accelerated provisioning norms (as detailed in paragraph 7 below) has been introduced.

7. Accelerated Provisioning

7.1 In cases where banks fail to report SMA status of the accounts to CRILC or resort to methods with the intent to conceal the actual status of the accounts or evergreen the account, banks will be subjected to accelerated provisioning for these accounts and/or other supervisory actions as deemed appropriate by RBI. The current provisioning requirement and the revised accelerated provisioning in respect of such non performing accounts are as given in RBI circulars dated February 26, 2014 and September 24, 2015. **(In this connection, banks have represented to RBI that in many cases JLF is not formed due to lead bank of the consortium/bank with**

the largest AE under the multiple banking arrangements, not convening the JLF and not taking initiatives in the matter. Accordingly, RBI has decided that if an account is reported by any of the lenders to CRILC as SMA 2 and the JLF is not immediately formed or CAP is not decided within the prescribed time limit due to above reasons, then the accelerated provisioning will be applicable only on the bank having responsibility to convene JLF and not on all the lenders in consortium/multiple banking arrangement. In other cases, accelerated provisioning will be applicable on all banks in the consortium/multiple banking arrangement. Banks are also advised that in case the lead bank of the consortium/bank with the largest AE under the multiple banking arrangement fails to convene JLF within 15 days of reporting SMA-2 status, the bank with second largest AE shall convene the JLF within the next 15 days, and have the same responsibilities and disincentives as applicable to the lead bank/bank with largest AE).

7.2 Further, any of the lenders who have agreed to the restructuring decision under the CAP by JLF and is a signatory to the ICA and DCA, but changes their stance later on, or delays/refuses to implement the package, will also be subjected to accelerated provisioning requirement as indicated at para 7.1 above, on their exposure to this borrower i.e., if it is classified as an NPA. If the account is standard in those lenders' books, the provisioning requirement would be 5%. Further, any such backtracking by a lender might attract negative supervisory view during Supervisory Review and Evaluation Process.

7.3 Presently, asset classification is based on record of recovery at individual banks and provisioning is based on asset classification status at the level of each bank. However, if lenders fail to convene the JLF or fail to agree upon a common CAP within the stipulated time frame, the account will be subjected to accelerated provisioning as indicated at para 7.1 above, if it is classified as an NPA. If the account is standard in those lenders' books, the provisioning requirement would be 5%.

7.4 If an escrow maintaining bank under JLF/CDR mechanism does not appropriate proceeds of repayment by the borrower among the lenders as per agreed terms resulting into down gradation of asset classification of the account in books of other lenders, the account with the escrow maintaining bank will attract the asset classification which is lowest among the lending member

banks, and corresponding provisioning requirement. **(On a review, RBI has decided that in such cases, account in the books of the escrow maintaining bank will not only attract the asset classification which is lowest among the lending member banks but will also be subjected to corresponding accelerated provision instead of normal provision. Further, such accelerated provision will be applicable for a period of one year from the effective date of provisioning or till rectification of the error, whichever is later.)**

8. Wilful Defaulters and Non-Cooperative Borrowers

The following additional prudential measures will be applicable:

(a) The provisioning in respect of existing loans/exposures of banks to companies having director/s (other than nominee directors of government/financial institutions brought on board at the time of distress), whose name/s appear more than once in the list of wilful defaulters, will be 5% in cases of standard accounts; if such account is classified as NPA, it will attract accelerated provisioning as indicated at para 7.1 above. This is a prudential measure since the expected losses on exposures to such borrowers are likely to be higher. No additional facilities should be granted by any bank/FI to the listed wilful defaulters.

(b) If any particular entity is reported as non-cooperative, any fresh exposure to such a borrower will by implication entail greater risk necessitating higher provisioning. Banks/FIs will therefore be required to make higher provisioning as applicable to substandard assets in respect of new loans sanctioned to such borrowers as also new loans sanctioned to any other company that has on its board of directors any of the whole time directors/promoters of a non-cooperative borrowing company or any firm in which such a non-cooperative borrower is in charge of management of the affairs. However, for the purpose of asset classification and income recognition, the new loans would be treated as standard assets.

9. Dissemination of Information

9.1 At present, the list of Suit filed accounts of Wilful Defaulters (Rs.2.5 million and above) is submitted by banks to the Credit Information Companies (CICs) of which they are member(s), who display the same on their respective websites as and when received. The list of non-suit filed accounts of Wilful Defaulters (Rs.2.5 million and above) is confidential and is disseminated by RBI among banks and FIs only for their own use. In order to make the current system of banks/FIs reporting names of suit filed accounts and non-suit filed accounts of Wilful Defaulters and its availability to the banks by CICs/RBI as current as possible, banks are advised to forward

data on wilful defaulters to the CICs/Reserve Bank at the earliest but not later than a month from the reporting date and they must use/ furnish the detailed information as per the format prescribed.

9.2 In case any falsification of accounts on the part of the borrowers is observed by the banks / FIs, and if it is observed that the auditors were negligent or deficient in conducting the audit, banks should lodge a formal complaint against the auditors of the borrowers with the Institute of Chartered Accountants of India (ICAI) to enable the ICAI to examine and fix accountability of the auditors. RBI reiterates these instructions for strict compliance. Pending disciplinary action by ICAI, the complaints may also be forwarded to the RBI (Department of Banking Supervision, Central Office) and IBA for records. IBA would circulate the names of the CA firms against whom many complaints have been received amongst all banks who should consider this aspect before assigning any work to them. RBI would also share such information with other financial sector regulators/Ministry of Corporate Affairs (MCA)/Comptroller and Auditor General (CAG).

9.3 Further, banks may seek explanation from advocates who wrongly certify as to clear legal titles in respect of assets or valuers who overstate the security value, by negligence or connivance, and if no reply/satisfactory clarification is received from them within one month, they may report their names to IBA. The IBA may circulate the names of such advocates/valuers among its members for consideration before availing of their services in future. The IBA would create a central registry for this purpose.

10. Disagreement on restructuring as CAP and Exit Option

Dissenting lenders who do not want to participate in the rectification or restructuring of the account as CAP, which may or may not involve additional financing, will have an option to exit their exposure completely by selling their exposure to a new or existing lender(s) within the prescribed timeline for implementation of the agreed CAP. The **exiting lender will not have the option to continue with their existing exposure and simultaneously not agreeing for rectification or restructuring as CAP**. The new lender to whom the exiting lender sells its stake may not be required to commit any additional finance, if the agreed CAP involves additional finance. In such cases, if the new lender chooses to not to participate in additional finance, the share of additional finance, pertaining to the exiting lender, will be met by the existing lenders on a pro-rata basis. If the dissenting lender is not able to exit by arranging a

buyer within the above prescribed time, it has to necessarily adhere to the agreed CAP and provide additional finance, if the CAP so envisages.

.**If restructuring has been decided as the CAP, then banks will not be permitted to sell such assets to SCs/RCs, without arranging their share of additional finance to be provided by a new or existing creditor.**

As undue delays by banks in communicating their decision on CAP defeats the very purpose of this framework for initiating prompt corrective measures in cases of stressed accounts, RBI has decided to put in place an incentive structure for banks to communicate their decision on the agreed CAP in a time bound manner. Details of this are given in RBI circular dated February 25, 2015, which also mentions that the additional funding provided under restructuring/rectification as part of the CAP, will have priority in repayment over repayment of existing debts. Therefore, instalments of the additional funding which fall due for repayment will have priority over the repayment obligations of the existing debt. Necessary conditions shall accordingly be incorporated in the JLF agreement.

(4) Change in Ownership of Borrowing Entities (Outside Strategic Debt Restructuring Scheme) (RBI circulars dated September 25, 2015 and February, 25, 2016)

In order to enhance banks' ability to bring in a change in ownership of borrowing entities which are under stress primarily due to operational/ managerial inefficiencies despite substantial sacrifices made by the lending banks, RBI has decided to allow banks to upgrade the credit facilities extended to borrowing entities whose ownership has been changed outside SDR, to 'Standard' category upon such change in ownership, subject to the following guidelines:

(i) Change in ownership may be by way of sale by the lenders, to a new promoter, of shares acquired by invocation of pledge or by conversion of debt of the borrower into equity outside SDR, or bringing in a new promoter by issue of fresh shares by the borrowing entity or acquisition of the borrowing entity by another entity. However, the exemptions from SEBI regulations, permitted under SDR guidelines, will not be available;

(ii) On such change in ownership of the borrowing entities, credit facilities of the concerned borrowing entities may be upgraded as ‘Standard’. However, the quantum of provision held by the bank against the said account as on the date of change in ownership of the borrowing entities shall not be reversed except as permitted at (v) below;

(iii) The upgrade in the asset classification is subject to the following conditions:

a. The ‘new promoter’ should not be a person/entity/subsidiary/associate etc. (domestic as well as overseas), from/belonging to the existing promoter/promoter group. Banks should exercise the necessary due diligence in this regard and clearly establish that the acquirer does not belong to the existing promoter group; and
b. The new promoter should have acquired at least 51 per cent of the paid up equity capital of the borrower company. If the new promoter is a non-resident, and in sectors where the ceiling on foreign investment is less than 51 per cent, the new promoter should own at least 26 per cent of the paid up equity capital or up to applicable foreign investment limit, whichever is higher, provided banks are satisfied that with this equity stake the new non-resident promoter controls the management of the company.

(iv) At the time of takeover of the borrowing entity by a ‘new promoter’, banks may refinance the existing debt of the borrowing entities, considering the changed risk profile, without treating the exercise as ‘restructuring’ subject to banks making provisions for any diminution in fair value of the existing debt on account of the refinance;

(v) Banks may reverse the provision held against the said account only when all the outstanding loan/facilities of the borrowing entities perform satisfactorily during the ‘specified period’ (as defined in the extant norms on restructuring of advances), i.e., principal and interest on all facilities in the account are serviced as per terms of payment during that period;

(vi) In case satisfactory performance during the specified period is not evidenced, the asset classification of the restructured account would be governed by the extant asset classification norms with reference to the repayment schedule that existed before the change in ownership as envisaged at (ii) above and assuming that upgrade in asset classification had not been given. However, in cases where the bank exits the account completely, i.e. no longer has any exposure to the borrower, the provision may be reversed/absorbed as on the date of exit.

(vii) Personal guarantees/commitments obtained from existing promoters should also cover losses incurred by lenders. Therefore, banks should devise an appropriate mechanism as per the

bank's board approved policy towards invocation/release of personal guarantees and this should be based on the principle of reasonable satisfaction of lenders' claims. This could include pledge of the existing promoters' share in favour of the lenders if not already done. In any case, personal guarantees should be released only after transfer of ownership and/or management control to the new promoters.

(5) Sale of Financial Assets to Securitisation Company (SC)/Reconstruction Company (RC) (RBI circulars dated February 26, 2014 and February 25, 2016)

As per existing guidelines, a financial asset may be sold to the SC/RC by any bank/FI where the asset is:

i) A NPA, including a non-performing bond/debenture, and
ii) A Standard Asset where:
(a) the asset is under consortium/multiple banking arrangements,
(b) at least 75% by value of the asset is classified as non-performing asset in the books of other banks / FIs, and
(c) at least 75% (by value) of the banks/FIs who are under the consortium/ multiple banking arrangements agree to the sale of the asset to SC / RC.

RBI has advised that In addition to the above, henceforth a financial asset may be sold to the SC/RC by any bank/FI where the financial asset is reported as SMA-2 by the bank/FI to Central Repository for Information on Large Credit (CRILC). **However, if restructuring has been decided as the CAP, then banks will not be permitted to sell such assets to SCs/RCs, without arranging their share of additional finance to be provided by a new or existing creditor.**

RBI has also advised that banks using auction process for sale of NPAs to SCs/RCs should be more transparent, including disclosure of the Reserve Price, specifying clauses for non-acceptance of bids, etc. Banks shall disclose the Reserve Price at the time of inviting bids/expression of interest from the SCs/RCs. If a bid received is above the Reserve Price and a minimum of 50 per cent of sale proceeds is in cash, and also fulfils the other conditions specified in the Offer Document, acceptance of that bid would be mandatory. Banks shall provide

adequate time and due facilitation to SCs/RCs to conduct due diligence on financial assets offered for sale. Banks shall provide not less than 2 weeks for submission of bids from the time of inviting bids/expression of interest from SCs/RCs.

(6) Purchase/Sale of Non-Performing Financial Assets to Other Banks

As per the existing guidelines, a non-performing asset in the books of a bank shall be eligible for sale to other banks only if it has remained a non-performing asset for at least two years in the books of the selling bank. Also, a non-performing financial asset should be held by the purchasing bank in its books at least for a period of 15 months before it is sold to other banks

In partial modification to the above, RBI has advised that banks will be permitted to sell their NPAs to other banks/FIs/NBFCs (excluding SCs/RCs) without any initial holding period. However, the non-performing financial asset should be held by the purchasing bank in its books at least for a period of 12 months before it is sold to other banks/financial institutions/NBFCs (excluding SCs/RCs). The extant prudential norms on asset classification of such assets in the books of purchasing banks/FIs/NBFCs will remain unchanged.