



Regulation – Objectives

- Regulation – Framing the rules of the game
- Supervision – Checking the compliance with the regulation
- Regulation & supervision aim to :
 - (i) safeguard the interest of depositors
 - (ii) oversee the implementation of the national socio – economic policies through the regulated entities in the IFS
 - (iii) adopt the international best practices
- Accordingly regulators try to ensure :
 - (i) solvency of the banking system
 - (ii) quality of assets
 - (iii) adequacy of liquidity
 - (iv) profitability
 - (v) competence of management



Indian Banking System – Evolution

- The evolution of the Indian banking system can be captured in four phases :
 - Foundation phase from 1950 to 1969
 - Expansionary phase from 1969 to 1985
 - Consolidation & Diversification phase from 1985 to 1991
 - Financial sector reforms phase from 1991 till date



FINANCIAL SECTOR REFORMS

PRUDENTIAL NORMS

1. IRAC
2. CRAR
3. EXPOSURE NORMS
4. INVESTMENTS - VALUATION



PURPOSE OF PRUDENTIAL NORMS

TO reflect the true financial position and health of the bank in its balance sheet

TO arrest the deterioration in the quality of its assets



Broadly IRAC stands for

- Income recognition- on the basis of record of recovery
- Classification of assets-on the basis of objective criterion-uniform and consistent application of norms
- Provision –on the basis of classification of assets into different categories



What is a Non performing Assets

- An asset, including a leased asset, becomes non performing when it ceases to generate income for the bank.
- Types of Assets : Term loan, Working capital and overdraft



EFFECTS OF NPAs

Reduced income

Erosion in current profit through provisioning

Less accretion to capital funds

Limit recycling of funds, AL mismatches

Higher cost of intermediation and adverse selection

Affect capacity to create good quality of assets



Classification of Assets as Non-Performing

- Earlier an asset was NPA based on the concept of '**Past Due**' for **30 days**.
- specific period was reduced as under:

31 March 1993	4 quarters
31 March 1994	3 quarters
31 March 1995	2 quarters
31 March 2001	No past due.

It is due date thereafter



What is 'Overdue'

Any amount due to the bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the bank.



Concept of overdue

- i) Interest and/or instalment of principal remain overdue* for a period of more than 90 days in respect of a Term Loan.
- (ii) The account remains 'Out of order' for a period of more than 90 days, in respect of an Overdraft/Cash Credit (OD/CC).
- iii) The bill remains overdue for a period of more than 90 days, in the case of bills purchased and discounted.



Concept of overdue

- iv. the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops,
- v. the instalment of principal or interest thereon remains overdue for one crop season for long duration crops,
- vi. the amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of guidelines on securitisation dated February 1, 2006.



What is an Out of Order A/c

- - the outstanding balance remains continuously in excess of the sanctioned limit/drawing power.
or
- there are no credits continuously for 90 days from 31.03.2004
or
- credits are not enough to cover the interest debited during the same period,



ASSET CLASSIFICATION

Standard Assets

Sub Standard Assets

Doubtful Assets

Loss Assets



Classification of Assets

- **Identification of assets as NPAs should be done on an ongoing basis**
- **Charging of interest at monthly rests**
- Any doubt in classification to be settled through internal channels within one month
- Provisions to be made at the end of each calendar quarter
- **Treatment of Accounts as NPAs** on basis of record of recovery
- **Treatment of NPAs – Borrower-wise and not Facility-wise**



Classification of Assets

Consortium : Each bank may classify according to its own record of recovery and other aspects

HL to Staff: interest need not be considered as overdue from the first quarter

Guaranteed by Central Govts: though overdue not treated as NPA; no recognition of income;

Guaranteed by State Govts: normal norms w.e.f. March 06



ASSET CLASSIFICATION

Sub Standard Assets

W.E.F 31/03/2005, the sub standard asset is one which has remained as NPA for a period not exceeding 12 months;

Where the terms of loan regarding interest and principal have been renegotiated/rescheduled after commencement of production is SubStandardAsset and remain so for 12 months;



ASSET CLASSIFICATION

Loss Assets:

An asset where loss has been identified by the bank or internal or external auditors or by the department or by RBI but has not been written off.

Asset which is uncollectable and of such little value



Guidelines for classification of assets

- Availability of security / net worth of borrower/ guarantor.
- Accounts with temporary deficiencies.
- Upgradation of loan accounts classified as NPAs.
- Accounts regularised near about the balance sheet date.
- Asset Classification to be borrower-wise and not facility-wise.
- Advances under consortium arrangements
- Accounts where there is erosion in the value of security/ frauds committed by borrowers.



Guidelines for classification of assets

Advances to PACS/FSS ceded to Commercial Banks

Advances against Term Deposits, NSCs, KVP/IVP, etc

Loans with moratorium for payment of interest

Agricultural advances

Government guaranteed advances



Asset Classification - NPA Norms for UCBs

- Tier I Banks:
- 180 days loan delinquency norm for loan (including gold loans and small loan upto Rs 1 lakh). This relaxation is upto March 31, 2009.

- Tier II Banks:
- 90 days loan delinquency norm for loan accounts including gold loans and small loans up to Rs. 1 lakh.



Asset Classification, w.e.f March 31, 2005

Tier I- banks	Tier II- banks
<p>The 12-month period for classification of a substandard asset in doubtful category will be effective from April 1, 2009</p>	<p>An asset is required to be classified as doubtful, if it has remained NPA for more than 12 months.</p>



Provisioning Norms

Tier I- banks	Tier II- banks
<p>(i) Standard Assets: 0.25 % for all type of standard advances.</p> <p>(ii) Sub standard- 10%</p>	<p>(i) Standard Asset: 0.40 per cent. For agricultural and SME sectors it is 0.25 per cent.</p> <p>ii) Sub standard- 10%</p>



Provisioning Norms

Tier I- banks	Tier II- banks
<p>(iii) Doubtful (up to one year): 100% of unsecured portion plus 20% of secured portion</p> <p>(iv) Doubtful (one to three years): 100% of unsecured portion plus 30% of secured portion</p> <p>(v) Doubtful for more than 3 years (D-III) : 100% of unsecured portion plus 50% of secured portion</p> <p>(vi) Loss: 100%.</p>	<p>(iii) Doubtful (up to one year): 100% of unsecured portion plus 20% of secured portion</p> <p>(iv) Doubtful (one to three years) : 100% of unsecured portion plus 30% of secured portion</p> <p>(v) Doubtful for more than 3 years (D-III) : 100% of unsecured portion plus 50% of secured portion</p> <p>(vi) Loss: 100%.</p>



Provisioning Norms for D-III assets, secured portion

W.e.f April 1, 2010

Tier II - W.e.f April 1, 2007

(i) outstanding stock of D-III assets as on March 31, 2010

-50 per cent

-60 per cent with effect from March 31, 2011

-75 per cent with effect from March 31, 2012

-100 per cent with effect from March 31, 2013

(i) outstanding stock of D – III assets as on March 31, 2007

-50 per cent

-60 per cent with effect from March 31, 2008

-75 per cent with effect from March 31, 2009

-100 per cent with effect from March 31, 2010



Provisioning Norms for D- III assets

Tier I -banks	Tier II -banks
<p>(ii) Advances classified as 'doubtful for more than three years' on or after April 1, 2010- 100 %.</p>	<p>(ii) Advances classified as 'doubtful for more than three years' on or after April 1, 2007- 100 %</p>



Position of Net Advances/Net NPAs

Sr.No.	Particulars	Current Year	Previous Year
1.	Gross Advances		
2.	Gross NPAs		
3.	Gross NPAs as % to Gross Advances		
4.	Deductions - Balance in interest suspense account/OIR* - DICGC/ECGC claims received and held pending adjustment - Part payment of NPA accounts received and kept in suspense account Total Deductions		



Prudential Guidelines on Restructuring of Advances

Asset classification norms

- (a) before commencement of commercial production / operation;
- (b) after commencement of commercial production / operation but before the asset has been classified as 'sub-standard';
- (c) after commencement of commercial production / operation and the asset has been classified as 'sub-standard' or 'doubtful'.



Prudential Guidelines on Restructuring of Advances

- 'standard assets' should be immediately re-classified as 'sub-standard assets' upon restructuring.
- The non performing assets, upon restructuring, would slip into further lower asset classification category as per extant asset classification norms with reference to the pre-restructuring repayment schedule.
- non-performing assets upon restructuring, would be eligible for up-gradation to the 'standard' category after observation of 'satisfactory performance' during the 'specified period'
- the asset classification of the restructured account would be governed as per the applicable prudential norms with reference to the ***pre-restructuring payment schedule***.



Restructured A/c-Income recognition norms

- Subject to other provisions interest income in respect of restructured accounts classified as 'standard assets' will be recognized on accrual basis and that in respect of the account classified as 'non performing assets' will be recognized on cash basis.



Restructured A/c- Provisioning norms

- Banks will hold provision against the restructured advances as per the existing provisioning norms.
- Provision for diminution in the fair value of restructured Advances
- Prudential Norms for Conversion of Unpaid Interest into 'Funded Interest Term Loan' (FITL)
- Asset classification norms



Restructured A/cs-Income recognition norms-

- (i) The income, if any, generated may be recognised on accrual basis, if FITL is classified as 'standard', and on cash basis in the cases where the same has been classified as a non-performing asset.
- (ii) The unrealised income represented by FITL should have a corresponding credit in an account styled as "Sundry Liabilities Account (Interest Capitalization)".
- (iii) Only on repayment in case of FITL, the amount received will be recognized in the P&L Account, while simultaneously reducing the balance in the "Sundry Liabilities Account (Interest Capitalisation)".



(e) Special Regulatory Treatment for Asset Classification

- As real estate sector has been extended special regulatory treatment i.e. commercial real estate exposures, which are restructured up to June 30, 2009.
- housing loans granted by banks would also be eligible for special regulatory treatment, if restructured.
- The special regulatory treatment has the following components :
 - (i) Incentive for quick implementation of the restructuring package.
 - (ii) Retention of the asset classification of the restructured account in the pre restructuring asset classification category



Restructured A/cs- Disclosures

- Banks should disclose in their published annual Balance Sheets, under 'Notes on Accounts', information relating to number and amount of advances restructured and the amount of diminution in the fair value of the restructured advances in Annex-VIII.



Agricultural Advances – natural calamities

UCBs on their own may decide to

- convert the short term production loan into a long term loan or reschedule the repayment period and
- sanction fresh short term loans
- these fresh loans will be governed by fresh term and conditions



Project financing:

Where moratorium is available for payment of interest, interest becomes due only after the moratorium or gestation period is over



Other advances:

Advances against term deposits, NSCs, IVPs, KVPs, Life policies need not be treated as NPAs, provided adequate margin is available

UCBs to fix monthly/quarterly instalments for repayment of gold loans for non agricultural purposes; such gold loans will be governed by IRAC norms

Gold loans for agricultural purposes, interest should be charged as per SC judgement at yearly intervals and payment should coincide with harvesting of crops; treated as NPAs if prescribed margin is not maintained

Investments also are subject to prudential IRAC norms



INCOME RECOGNITION

Income Recognition Policy

Reversal of income

Leased Assets

Appropriation of recovery in NPAs

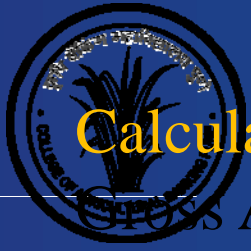
Interest Application

Computation of NPA levels



Recognition of Income on Investment

- **Recognition of Income on Investment Treated as NPAs**
- The investments are also subject to the prudential norms on income recognition. Banks should not book income on accrual basis in respect of any security irrespective of the category in which it is included, where the interest/principal is in arrears for more than 90 days .



Calculating Net NPAs:

Gross Advances and Gross NPAs less :-

- i) Balance in Interest Suspense Account
- ii) DICGC/ECGC claims received and held, pending adjustment
- iii) Part payment received and kept in suspense account
- iv) Total provisions held (excluding amount of technical write off and provision on standard assets)

For the purpose, the amount of gross advances should exclude the amount of Technical Write off but would include all outstanding loans and advances; including the advances for which refinance has been availed but excluding the amount of rediscounted bills. The level of gross and net NPAs will be arrived at in percentage terms by dividing the amount of gross and net NPAs by gross and net advances, computed as above, respectively.



Restructuring/ Rescheduling of Loans

- a. before commencement of commercial production;
- b. after commencement of commercial production but before the asset has been classified as sub standard,
- c. after commencement of commercial production and after the asset has been classified as sub standard.



Treatment of restructured standard accounts

Treatment of restructured substandard accounts

Upgradation of restructured accounts



INCOME RECOGNITION

Based on objective criteria and on record of recovery

Income not recognised on accrual basis but only when actually received; should not charge and take to income account interest on all NPAs

Interest on advances against TD, NSCs, IVPs, KVPs and life policies may be taken to income provided adequate margin is available

Fees and commissions earned as a result of renegotiation may be recognised over a period of time



INCOME RECOGNITION

Govt guaranteed advances: If overdue, interest should not be taken to income unless interest is realised

If any account becomes NPA as at the close of any year, interest accrued and credited in the corresponding previous year should be reversed or provided for if the same is not realised;

If interest becomes subject to non accrual, fees, commission and similar income should cease to accrue; if past dues are uncollected to be provided for



INTEREST APPLICATION

In case of NPAs, banks should show accrued interest separately or park in separate account so that interest receivable on such NPAs is computed and shown as such

Interest taken as income in respect of standard asset; if interest is not actually received, the account to be treated as NPA and income to be reversed



INTEREST APPLICATION

Guidelines for accounting of accrued interest:

NPAs: not to be debited to borrowal accounts; shown separately under “interest receivable account” and corresponding amount shown under “ Overdue Interest Reserve Account”

Performing Assets : to be debited to borrowal accounts and taken to income account; if the interest is not received before March 31 or account is treated as NPA later, equivalent amount to be reversed and credited to “OIR”

OIR not to be treated as “reserve” or “owned funds”



PROVISIONING NORMS

Std. Asset:

Tier I 0.25%

Tier II 0.40% but

Direct Agriculture and SME advances: 0.25% of the funded outstanding on portfolio basis

Provision for Std assets need not be netted from gross advances but to be shown as “contingent Provision against Std Assets” under “Other Funds and Reserves on Capital & Liabilities side)

Excess Provision can not be reversed

Full provision for retirement benefits



PROVISIONING NORMS

- Personal Loans, Capital Exposure &
- Real Estate Loans: 2.00%
- Residential HL (< Rs. 20 lakh): 1.00%
- All other loans: 0.40%

- SSA: General provision of 10% on total outstanding without any allowance for DICGC/ECGC cover and securities available



PROVISIONING NORMS

DA: 100% of the extent to which the advance is not covered by the realizable value of the security

Tier I bank

In regard to secured portion of Doubtful Assets

Upto 1 year 20%

Upto 3 years 30%

More than 3 years D III 50%

as on 31/03/07: 50%

As on 31/03/08: 60%

As on 31/03/09: 75%

As on 31/03/10: 100%



i. Funded Interest:

Income recognition in respect of the NPAs, regardless of whether these are or are not subjected to restructuring/ rescheduling/ renegotiation of terms of the loan agreement, should be done strictly on cash basis, only on realisation and not if the amount of interest overdue has been funded. If, however, the amount of funded interest is recognised as income, a provision for an equal amount should also be made simultaneously. In other words, any funding of interest in respect of NPAs, if recognised as income, should be fully provided for



DIVERGENCE IN ASSET CLASSIFICATION AND PROVISIONING



Thank you

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