Prudential Norms on Income Recognition, Asset Classification and Provisioning Pertaining to Advances

DBOD No. BP. BC. 1 / 21.04.048 / 2002- 2003

4 July 2002

Chief Executives of all Scheduled Commercial Banks
(excluding RRBs and LABs)

Dear Sir,

Please refer to the Master Circular No. DBOD. BP. BC. 20/ 21.04.048/ 2001- 2002 dated 30 August 2001 consolidating instructions/ guidelines issued to banks till 30 June 2001 on matters relating to prudential norms on income recognition, asset classification and provisioning pertaining to advances. The Master Circular has been suitably updated by incorporating instructions issued upto 30 June 2002 and has also been placed on the RBI web-site (http://www.rbi.org.in).

This Master Circular is a compilation of all the instructions contained in the circulars issued by RBI on the above subject, which are operational as on the date of this circular.

Yours faithfully,

(M. R. Srinivasan)
Chief General Manager-in-Charge
Encls : As above

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1. GENERAL

1.1 In line with the international practices and as per the recommendations made by the Committee on the Financial System (Chairman Shri M. Narasimham), the Reserve Bank of India has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks so as to move towards greater consistency and transparency in the published accounts.

1.2 The policy of income recognition should be objective and based on record of recovery rather than on any subjective considerations. Likewise, the classification of assets of banks has to be done on the basis of objective criteria which would ensure a uniform and consistent application of the norms. Also, the provisioning should be made on the basis of the classification of assets based on the period for which the asset has remained non-performing and the availability of security and the realisable value thereof.

1.3 With the introduction of prudential norms, the Health Code-based system for classification of advances has ceased to be a subject of supervisory interest. As such, all related reporting requirements, etc. under the Health Code system also cease to be a supervisory requirement. Banks may, however, continue the system at their discretion as a management information tool.

2. DEFINITIONS

2.1 Non-performing assets

2.1.1 An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A 'non-performing asset' (NPA) was defined as a credit facility in respect of which the interest and/ or instalment of principal has remained 'past due' for a specified period of time. The specified period was reduced in a phased manner as under:

Year ending March 31	Specified period
1993	four quarters
1994	three quarters
1995 onwards	two quarters

2.1.2 An amount due under any credit facility is treated as "past due" when it has not been paid within 30 days from the due date. Due to the improvements in the payment and settlement systems, recovery climate, upgradation of technology in the banking system, etc., it was decided to dispense with 'past due' concept, with effect from March 31, 2001. Accordingly, as from that date, a Non-performing Asset (NPA) shall be an advance where

i) interest and/or instalment of principal remain overdue for a period of more than 180 days in respect of a Term Loan,

ii) the account remains ‘out of order’ for a period of more than 180 days, in respect of an Overdraft/Cash Credit (OD/CC),

iii) the bill remains overdue for a period of more than 180 days in the case of bills purchased and discounted,

iv) interest and/or instalment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purposes, and

v) any amount to be received remains overdue for a period of more than 180 days in respect of other accounts.

2.1.3 With a view to moving towards international best practices and to ensure greater transparency, it has been decided to adopt the ‘90 days’ overdue’ norm for identification of NPAs, from the year ending March 31, 2004. Accordingly, with effect from March 31, 2004, a non-performing asset (NPA) shall be a loan or an advance where;

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,

vi) interest and/or instalment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purposes, and

v) any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

As a facilitating measure for smooth transition to 90 days norm, banks have been advised to move over to charging of interest at monthly rests, by April 1, 2002. However, the date of classification of an advance as NPA should not be changed on account of charging of interest at monthly rests. Banks should, therefore, continue to classify an account as NPA only if the interest charged during any quarter is not serviced fully within 180 days from the end of the quarter with effect from April 1, 2002 and 90 days from the end of the quarter with effect from March 31, 2004.

2.2 'Out of Order' status

An account should be treated as **'out of order'** if the outstanding balance remains continuously in excess of the sanctioned limit/drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit/drawing power, but there are no credits continuously for six months as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as **'out of order'**.

2.3 ‘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.

3. INCOME RECOGNITION

3.1 Income recognition - Policy

3.1.1 The policy of income recognition has to be objective and based on the record of recovery. Internationally income from non-performing assets (NPA) is not recognised on accrual basis but is booked as income only when it is actually received. Therefore, the banks should not charge and take to income account interest on any NPA.

3.1.2 However, interest on advances against term deposits, NSCs, IVPs, KVPs and Life policies may be taken to income account on the due date, provided adequate margin is available in the accounts.

3.1.3 Fees and commissions earned by the banks as a result of re-negotiations or rescheduling of outstanding debts should be recognised on an accrual basis over the period of time covered by the re-negotiated or rescheduled extension of credit.

3.1.4 If Government guaranteed advances become NPA, the interest on such advances should **not** be taken to income account unless the interest has been realised.

3.2 Reversal of income

3.2.1 If any advance, including bills purchased and discounted, becomes NPA as at the close of any year, interest accrued and credited to income account in the corresponding previous year, should be reversed or provided for if the same is not realised. **This will apply to Government guaranteed accounts also**.

3.2.2 In respect of NPAs, fees, commission and similar income that have accrued should cease to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.

3.2.3 Leased Assets

i)The net lease rentals (finance charge) on the leased asset accrued and credited to income account before the asset became non-performing, and remaining unrealised, should be reversed or provided for in the current accounting period.

ii)The term 'net lease rentals' would mean the amount of finance charge taken to the credit of Profit & Loss Account and would be worked out as gross lease rentals adjusted by amount of statutory depreciation and lease equalisation account.

iii) As per the **'Guidance Note on Accounting for Leases'** issued by the Council of the Institute of Chartered Accountants of India (ICAI), a separate Lease Equalisation Account should be opened by the banks with a corresponding debit or credit to Lease Adjustment Account, as the case may be. Further, Lease Equalisation Account should be transferred every year to the Profit & Loss Account and disclosed separately as a deduction from/addition to gross value of lease rentals shown under the head 'Gross Income'.

3.3 Appropriation of recovery in NPAs

3.3.1 Interest realised on NPAs may be taken to income account provided the credits in the accounts towards interest are not out of fresh/ additional credit facilities sanctioned to the borrower concerned.

3.3.2 In the absence of a clear agreement between the bank and the borrower for the purpose of appropriation of recoveries in NPAs (i.e. towards principal or interest due), banks should adopt an accounting principle and exercise the right of appropriation of recoveries in a uniform and consistent manner.

3.4 Interest Application

There is no objection to the banks using their own discretion in debiting interest to an NPA account taking the same to Interest Suspense Account or maintaining only a record of such interest in proforma accounts.

3.5 Reporting of NPAs

3.5.1 Banks are required to furnish a Report on NPAs as on 31st March each year after completion of audit. The NPAs would relate to the banks' global portfolio, including the advances at the foreign branches. The Report should be furnished as per the prescribed format given in the Annexure I.

3.5.2 While reporting NPA figures to RBI, the amount held in interest suspense account, should be shown as a deduction from gross NPAs as well as gross advances while arriving at the net NPAs. Banks which do not maintain Interest Suspense account for parking interest due on non-performing advance accounts, may furnish the amount of interest receivable on NPAs as a foot note to the Report.

3.5.3 Whenever NPAs are reported to RBI, the amount of technical write off, if any, should be reduced from the outstanding gross advances and gross NPAs to eliminate any distortion in the quantum of NPAs being reported.

4.ASSET CLASSIFICATION

4.1 Categories of NPAs

Banks are required to classify non-performing assets further into the following three categories based on the period for which the asset has remained non-performing and the realisability of the dues:

a) Sub-standard Assets

b) Doubtful Assets

c) Loss Assets

4.1.1 Sub-standard Assets

A sub-standard asset was one, which was classified as NPA for a period not exceeding two years. With effect from 31 March 2001, a sub-standard asset is one, which has remained **NPA for a period less than or equal to 18 months**. In such cases, the current net worth of the borrower/ guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the banks in full. In other words, such an asset will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected**.**

4.1.2 Doubtful Assets

A doubtful asset was one, which remained NPA for a period exceeding two years. With effect from 31 March 2001, an asset is to be classified as doubtful, if it has remained **NPA for a period exceeding 18 months**. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full, – on the basis of currently known facts, conditions and values – highly questionable and improbable.

With effect from March 31, 2005, an asset would be classified as doubtful if it remained in the sub-standard category for 12 months.

4.1.3 Loss Assets

A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

4.2 Guidelines for classification of assets

4.2.1 Broadly speaking, classification of assets into above categories should be done taking into account the degree of well-defined credit weaknesses and the extent of dependence on collateral security for realisation of dues.

4.2.2 Banks should establish appropriate internal systems to eliminate the tendency to delay or postpone the identification of NPAs, especially in respect of high value accounts. The banks may fix a minimum cut off point to decide what would constitute a high value account depending upon their respective business levels. The cut off point should be valid for the entire accounting year. Responsibility and validation levels for ensuring proper asset classification may be fixed by the banks. The system should ensure that doubts in asset classification due to any reason are settled through specified internal channels within one month from the date on which the account would have been classified as NPA as per extant guidelines.

4.2.3 **Accounts with temporary deficiencies**

(i) The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as non-availability of adequate drawing power based on the latest available stock statement, balance outstanding exceeding the limit temporarily, non-submission of stock statements and non-renewal of the limits on the due date, etc. In the matter of classification of accounts with such deficiencies banks may follow the following guidelines:

a) Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However, considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular. A working capital borrowal account will become NPA if such irregular drawings are permitted in the account for a continuous period of 180 days even though the unit may be working or the borrower's financial position is satisfactory.

b) Regular and ad hoc credit limits need to be reviewed/ regularised not later than three months from the due date/date of ad hoc sanction. In case of constraints such as non-availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is already on and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the regular/ ad hoc credit limits have not been reviewed/ renewed within 180 days from the due date/ date of ad hoc sanction will be treated as NPA.

4.2.4 **Accounts regularised near about the balance sheet date**

The asset classification of borrowal accounts where a solitary or a few credits are recorded before the balance sheet date should be handled with care and without scope for subjectivity. Where the account indicates inherent weakness on the basis of the data available, the account should be deemed as a NPA. In other genuine cases, the banks must furnish satisfactory evidence to the Statutory Auditors/Inspecting Officers about the manner of regularisation of the account to eliminate doubts on their performing status.

4.2.5 Asset Classification to be borrower-wise and not facility-wise

i) It is difficult to envisage a situation when only one facility to a borrower becomes a problem credit and not others. Therefore, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility or part thereof which has become irregular.

ii)If the debits arising out of devolvement of letters of credit or invoked guarantees are parked in a separate account, the balance outstanding in that account also should be treated as a part of the borrower's principal operating account for the purpose of application of prudential norms on income recognition, asset classification and provisioning.

4.2.6 **Advances under consortium arrangements**

Asset classification of accounts under consortium should be based on the **record of recovery of the individual member banks** and other aspects having a bearing on the recoverability of the advances**.** Where the remittances by the borrower under consortium lending arrangements are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account will be treated as not serviced in the books of the other member banks and therefore, be treated as NPA. The banks participating in the consortium should, therefore, arrange to get their share of recovery transferred from the lead bank or get an express consent from the lead bank for the transfer of their share of recovery, to ensure proper asset classification in their respective books.

4.2.7 Accounts where there is erosion in the value of security

i) A NPA need not go through the various stages of classification in cases of serious credit impairment and such assets should be straightaway classified as doubtful or loss asset as appropriate. Erosion in the value of security can be reckoned as significant when the realisable value of the security is less than 50 per cent of the value assessed by the bank or accepted by RBI at the time of last inspection, as the case may be. Such NPAs may be straightaway classified under doubtful category and provisioning should be made as applicable to doubtful assets.

ii) If the realisable value of the security, as assessed by the bank/ approved valuers/ RBI is less than 10 per cent of the outstanding in the borrowal accounts, the existence of security should be ignored and the asset should be straightaway classified as loss asset. It may be either written off or fully provided for by the bank.

4.2.8 Advances to PACS/FSS ceded to Commercial Banks

In respect of agricultural advances as well as advances for other purposes granted by banks to ceded PACS/ FSS under the on-lending system, only that particular credit facility granted to PACS/ FSS which is in default for a period of two harvest seasons (not exceeding two half years)/two quarters, as the case may be, after it has become due will be classified as NPA and not all the credit facilities sanctioned to a PACS/ FSS. The other direct loans & advances, if any, granted by the bank to the member borrower of a PACS/ FSS outside the on-lending arrangement will become NPA even if one of the credit facilities granted to the same borrower becomes NPA.

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

Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and life policies need not be treated as NPAs. Advances against gold ornaments, government securities and all other securities are not covered by this exemption.

4.2.10 Loans with moratorium for payment of interest

i) In the case of bank finance given for industrial projects or for agricultural plantations etc. where moratorium is available for payment of interest, payment of interest becomes 'due' only after the moratorium or gestation period is over. Therefore, such amounts of interest do not become overdue and hence NPA, with reference to the date of debit of interest. They become overdue after due date for payment of interest, if uncollected.

ii) In the case of housing loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such loans/advances should be classified as NPA only when there is a default in repayment of instalment of principal or payment of interest on the respective due dates

4.2.11 Agricultural advances

i) In respect of advances granted for agricultural purpose where interest and/or instalment of principal remains unpaid after it has become past due for two harvest seasons but for a period not exceeding two half-years, such an advance should be treated as NPA. The above norms should be made applicable to all direct agricultural advances as listed at items 1.1, 1.1.2 (i) to (vii), 1.1.2 (viii)(a)(1) and 1.1.2 (viii)(b)(1) of Master Circular on lending to priority sector No. RPCD. PLAN. BC. 12/04.09.01/ 2001- 2002 dated 1 August 2001. An extract of the list of these items is furnished in the Annexure II. In respect of agricultural loans, other than those specified above, identification of NPAs would be done on the same basis as non agricultural advances which, at present, is the 180 days delinquency norm.

ii) Where natural calamities impair the repaying capacity of agricultural borrowers, banks may decide on their own as a relief measure - conversion of the short-term production loan into a term loan or re-schedulement of the repayment period; and the sanctioning of fresh short-term loan, subject to various guidelines contained in RBI circulars RPCD.No.PLFS.BC.128/05.04.02/97-98 dated 20.06.98 and RPCD.No.PLFS.BC.9/05.01.04/98-99 dated 21.07.98.

iii) In such cases of conversion or re-schedulement, the term loan as well as fresh short-term loan may be treated as current dues and need not be classified as NPA. The asset classification of these loans would thereafter be governed by the revised terms & conditions and would be treated as NPA if interest and/or instalment of principal remains unpaid, for two harvest seasons but for a period not exceeding two half years.

4.2.12 **Government guaranteed advances**

The credit facilities backed by guarantee of the Central Government though overdue may be treated as NPA only when the Government repudiates its guarantee when invoked. This exemption from classification of Government guaranteed advances as NPA is not for the purpose of recognition of income. With effect from 1st April 2000, advances sanctioned against State Government guarantees should be classified as NPA in the normal course, if the guarantee is invoked and remains in default for more than two quarters. With effect from March 31, 2001 the period of default is revised as more than 180 days.

4.2.13 Restructuring/ Rescheduling of Loans

i) A standard asset where the terms of the loan agreement regarding interest and principal have been renegotiated or rescheduled after commencement of production should be classified as sub-standard and should remain in such category for at least one year of satisfactory performance under the renegotiated or rescheduled terms. In the case of sub-standard and doubtful assets also, rescheduling does not entitle a bank to upgrade the quality of advance automatically unless there is satisfactory performance under the rescheduled / renegotiated terms. Following representations from banks that the foregoing stipulations deter the banks from **restructuring of standard and sub-standard loan** assets even though the modification of terms might not jeopardise the assurance of repayment of dues from the borrower, the norms relating to restructuring of standard and sub-standard assets were reviewed in March 2001. In the context of restructuring of the accounts, the following stages at which the restructuring / rescheduling / renegotiation of the terms of loan agreement could take place, can be identified:

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.

In each of the foregoing three stages, the rescheduling, etc., of principal and/or of interest could take place, with or without sacrifice, as part of the restructuring package evolved.

ii) <u>Treatment of Restructured Standard Accounts</u>

a) A rescheduling of the instalments of **principal alone**, at any of the aforesaid first two stages would not cause a standard asset to be classified in the sub standard category provided the loan/credit facility is fully secured.

b) A rescheduling of **interest element** at any of the foregoing first two stages would not cause an asset to be downgraded to sub standard category subject to the condition that the amount of sacrifice, if any, in the element of interest, **measured in present value terms**, is either written off or provision is made to the extent of the sacrifice involved. For the purpose, the future interest due as per the original loan agreement in respect of an account should be discounted to the present value at a rate appropriate to the risk category of the borrower (i.e., current PLR+ the appropriate credit risk premium for the borrower-category) and compared with the present value of the dues expected to be received under the restructuring package, discounted on the same basis.

c)n case there is a sacrifice involved in the amount of interest in present value terms, as at (b) above, the amount of sacrifice should either be **written off or provision made** to the extent of the sacrifice involved.

iii) <u>Treatment of restructured sub-standard accounts</u>

a) A rescheduling of the instalments of principal alone, would render a sub-standard asset eligible to be **continued** in the sub-standard category for the specified period, **provided** the loan/credit facility is **fully secured**.

b) A rescheduling of interest element would render a sub-standard asset eligible to be **continued** to be classified in **sub standard** category for the specified period subject to the condition that the amount of sacrifice, if any, in the element of interest, **measured in present value terms**, is either written off or provision is made to the extent of the sacrifice involved. For the purpose, the future interest due as per the original loan agreement in respect of an account should be discounted to the present value at a rate appropriate to the risk category of the borrower (i.e., current PLR + the appropriate credit risk premium for the borrower-category) and compared with the present value of the dues expected to be received under the restructuring package, discounted on the same basis.

c)In case there is a sacrifice involved in the amount of interest in present value terms, as at (b) above, the amount of sacrifice should either be written off or provision made to the extent of the sacrifice involved. Even in cases where the sacrifice is by way of write off of the **past** interest dues, the asset should continue to be treated as sub-standard.

(iv) Upgradation of restructured accounts

The sub-standard accounts which have been subjected to restructuring etc., whether in respect of principal instalment or interest amount, by whatever modality, would be eligible to be upgraded to the standard category only after the specified period i.e., a period of one year after the date when first payment of interest or of principal, whichever is earlier, falls due, subject to satisfactory performance during the period. The amount of provision made earlier, net of the amount provided for the sacrifice in the interest amount in present value terms as aforesaid, could also be reversed after the one year period. During this one year period, the sub-standard asset will not deteriorate in its classification if satisfactory performance of the account is demonstrated during the period. In case, however, the satisfactory performance during the one year period is not evidenced, the asset classification of the restructured account would be governed as per the applicable prudential norms with reference to the pre-restructuring payment schedule.

(v) General

(a) These instructions would be applicable to all type of credit facilities including working capital limits, extended to industrial units, provided they are fully covered by tangible securities.

(b) As trading involves only buying and selling of commodities and the problems associated with manufacturing units such as bottleneck in commercial production, time and cost escalation etc. are not applicable to them, these guidelines should not be applied to restructuring/ rescheduling of credit facilities extended to traders.

(c) While assessing the extent of security cover available to the credit facilities, which are being restructured/ rescheduled, collateral security would also be reckoned, provided such collateral is a tangible security properly charged to the bank and is not in the intangible form like guarantee etc. of the promoter/ others.

4.2.14 Corporate Debt Restructuring

Background

(i) Inspite of their best efforts and intentions, sometimes corporates find themselves in financial difficulty because of factors beyond their control and also due to certain internal reasons. For the revival of the corporates as well as for the safety of the money lent by the banks and FIs, timely support through restructuring in genuine cases is called for. However, delay in agreement amongst different lending institutions often comes in the way of such endeavours.

(ii) Based on the experience in other countries like the U.K., Thailand, Korea, etc. of putting in place institutional mechanism for restructuring of corporate debt and need for a similar mechanism in India, a Corporate Debt Restructuring System has been evolved, as under :

Objective

(i) The objective of the Corporate Debt Restructuring (CDR) framework is to ensure timely and transparent mechanism for restructuring of the corporate debts of **viable entities facing problems, outside the purview of BIFR, DRT and other legal proceedings, for the benefit of all concerned.** In particular, the framework will aim at preserving viable corporates that are affected by certain internal and external factors and minimize the losses to the creditors and other stakeholders through an orderly and coordinated restructuring programme.

Structure

(ii) CDR system in the country will have a three tier structure :

(A) CDR Standing Forum
(B) CDR Empowered Group
(C) CDR Cell

(A) CDR Standing Forum :

a) The CDR Standing Forum would be the representative general body of all financial institutions and banks participating in CDR system. All financial institutions and banks should participate in the system in their own interest. CDR Standing Forum will be a self empowered body, which will lay down policies and guidelines, guide and monitor the progress of corporate debt restructuring.

The Forum will also provide an official platform for both the creditors and borrowers (by consultation) to amicably and collectively evolve policies and guidelines for working out debt restructuring plans in the interests of all concerned.

The CDR Standing Forum shall comprise Chairman & Managing Director, Industrial Development Bank of India; Managing Director, Industrial Credit & Investment Corporation of India Limited; Chairman, State Bank of India; Chairman, Indian Banks Association and Executive Director, Reserve Bank of India as well as Chairmen and Managing Directors of all banks and financial institutions participating as permanent members in the system. The Forum will elect its Chairman for a period of one year and the principle of rotation will be followed in the subsequent years. However, the Forum may decide to have a Working Chairman as a whole-time officer to guide and carry out the decisions of the CDR Standing Forum.

b) A CDR Core Group will be carved out of the CDR Standing Forum to assist the Standing Forum in convening the meetings and taking decisions relating to policy, on behalf of the Standing Forum. The Core Group will consist of Chief Executives of IDBI, ICICI, SBI, Bank of Baroda, Bank of India, Punjab National Bank, Indian Banks Association and a representative of Reserve Bank of India.

The CDR Standing Forum shall meet at least once every six months and would review and monitor the progress of corporate debt restructuring system. The Forum would also lay down the policies and guidelines to be followed by the CDR Empowered Group and CDR Cell for debt restructuring and would ensure their smooth functioning and adherence to the prescribed time schedules for debt restructuring. It can also review any individual decisions of the CDR Empowered Group and CDR Cell.

c) The CDR Standing Forum, the CDR Empowered Group and CDR Cell (described in following paragraphs) shall be housed in IDBI. The administrative and other costs shall be shared by all financial institutions and banks. The sharing pattern shall be as determined by the Standing Forum.

(B) CDR Empowered Group and CDR Cell

a) The individual cases of corporate debt restructuring shall be decided by the CDR Empowered Group, consisting of ED level representatives of IDBI, ICICI Limited and SBI as standing members, in addition to ED level representatives of financial institutions and banks who have an exposure to the concerned company. In order to make the CDR Empowered Group effective and broad based and operate efficiently and smoothly, it would have to be ensured that each financial institution and bank, as participants of the CDR system, nominates a panel of two or three Eds, one of whom will participate in a specific meeting of the Empowered Group dealing with individual restructuring cases. Where, however, a bank / financial institution has only one Executive Director, the panel may consist of senior officials, duly authorized by its Board. The level of representation of banks/ financial institutions on the CDR Empowered Group should be at a sufficiently senior level to ensure that concerned bank / FI abides by the necessary commitments including sacrifices, made towards debt restructuring.

The Empowered Group will consider the preliminary report of all cases of requests of restructuring, submitted to it by the CDR Cell. After the Empowered Group decides that restructuring of the company is prima-facie feasible and the enterprise is potentially viable in terms of the policies and guidelines evolved by Standing Forum, the detailed restructuring package will be worked out by the CDR Cell in conjunction with the Lead Institution.

The CDR Empowered Group would be mandated to look into each case of debt restructuring, **examine the viability and rehabilitation potential of the Company** and approve the restructuring package within a **specified time frame of 90 days,** or at best 180 days of reference to the Empowered Group.

b) There should be a general authorisation by the respective Boards of the participating institutions / banks in favour of their representatives on the CDR Empowered Group, authorising them to take decisions on behalf of their organization, regarding restructuring of debts of individual corporates.

c) The decisions of the CDR Empowered Group shall be final and action-reference point. If restructuring of debt is found viable and feasible and accepted by the Empowered Group, the company would be put on the restructuring mode. If, however, restructuring is not found viable, the creditors would then be free to take necessary steps for immediate recovery of dues and / or liquidation or winding up of the company, collectively or individually.

(C) CDR Cell

a) The CDR Standing Forum and the CDR Empowered Group will be assisted by a CDR Cell in all their functions. The CDR Cell will make the initial scrutiny of the proposals received from borrowers / lenders, by calling for proposed rehabilitation plan and other information and put up the matter before the CDR Empowered Group, within one month to decide whether rehabilitation is prima facie feasible, if so, the CDR Cell will proceed to prepare detailed Rehabilitation Plan with the help of lenders and if necessary, experts to be engaged from outside. If not found prima facie feasible, the lenders may start action for recovery of their dues.

b) To begin with, CDR Cell will be constituted in IDBI, Mumbai and adequate members of staff for the Cell will be deputed from banks and financial institutions. The CDR Cell may also take outside professional help. The initial cost in operating the CDR mechanism including CDR Cell will be met by IDBI initially for one year and then from contribution from the financial institutions and banks in the Core Group at the rate of Rs.50 lakh each and contribution from other institutions and banks at the rate of Rs.5 lakh each.

c) All references for corporate debt restructuring by lenders or borrowers will be made to the CDR Cell. It shall be the responsibility of the lead institution / major stakeholder to the corporate, to work out a preliminary restructuring plan in consultation with other stakeholders and submit to the CDR Cell within one month. The CDR Cell will prepare the restructuring plan in terms of the general policies and guidelines approved by the CDR Standing Forum and place for the consideration of the Empowered Group within 30 days for decision. The Empowered Group can approve or suggest modifications, so, however, that a final decision must be taken within a total period of 90 days. However, for sufficient reasons the period can be extended maximum upto 180 days from the date of reference to the CDR Cell.

Other features:

(i) CDR will be a Non-statutory mechanism

(ii) CDR mechanism will be a voluntary system based on debtor-creditor agreement and inter-creditor agreement.

(iii)The scheme will not apply to accounts involving only one financial institution or one bank. The CDR mechanism will cover only multiple banking accounts / syndication / consortium accounts with outstanding exposure of Rs.20 crore and above by banks and institutions.

(iv)The CDR system will be applicable only to standard and sub-standard accounts. However, as an interim measure, permission for corporate debt restructuring will be made available by RBI on the basis of specific recommendation of CDR "Core-Group", if a minimum of 75 per cent (by value) of the lenders constituting banks and FIs consent for CDR, irrespective of differences in asset classification status in banks/ financial institutions. There would be **no requirement of the account / company being sick, NPA or being in default for a specified** period before reference to the CDR Group. However, **potentially viable cases of NPAs will get priority.** This approach would provide the necessary flexibility and facilitate timely intervention for debt restructuring. Prescribing any milestone(s) may not be necessary, since the debt restructuring exercise is being triggered by banks and financial institutions or with their consent. In no case, the requests of any corporate indulging in wilful default or misfeasance will be considered for restructuring under CDR.

(i) Reference to Corporate Debt Restructuring System could be triggered by (i) any or more of the secured creditor who have minimum 20% share in either working capital or term finance, or (ii) by the concerned corporate, if supported by a bank or financial institution having stake as in (i) above.

Legal Basis

The legal basis to the CDR mechanism shall be provided by the **Debtor-Creditor Agreement (DCA)** and the **Inter-Creditor Agreement.** The debtors shall have to accede to the DCA, either at the time of original loan documentation (for future cases) or at the time of reference to Corporate Debt Restructuring Cell. Similarly, all participants in the CDR mechanism through their membership of the Standing Forum shall have to enter into a legally binding agreement, with necessary enforcement and penal clauses, to operate the System through laid-down policies and guidelines.

Stand-Still Clause

One of the most important elements of Debtor-Creditor Agreement would be **'stand still' agreement binding for 90 days,** or 180 days by both sides. Under this clause, both the debtor and creditor(s) shall **agree to a legally binding 'stand-still' whereby both the parties commit themselves not to taking recourse to any other legal action** during the 'stand-still' period, this would be necessary for enabling the CDR System to undertake the necessary debt restructuring exercise without any outside intervention judicial or otherwise.

The Inter-Creditors Agreement would be a legally binding agreement amongst the secured creditors, with necessary enforcement and penal clauses, wherein the creditors would commit themselves to abide by the various elements of CDR system. Further , the creditors shall agree that if **75% of secured creditors by value,** agree to a debt restructuring package, the same would be binding on the remaining secured creditors.

Accounting treatment for restructured accounts

The accounting treatment of accounts restructured under CDR would be governed by the prudential norms indicated in circular DBOD. BP. BC. 98 / 21.04.048 / 2000-01 dated March 30, 2001. Restructuring of corporate debts under CDR could take place in the following stages:

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 the asset has been classified as sub-standard.

The prudential treatment of the accounts, subjected to restructuring under CDR, would be governed by the following norms:

Treatment of standard accounts restructured under CDR

a) A rescheduling of the instalments of principal alone, at any of the aforesaid first two stages [paragraph 5(a) and (b) above] would not cause a standard asset to be classified in the sub-standard category, provided the loan / credit facility is fully secured.

b) A rescheduling of interest element at any of the foregoing first two stages would not cause an asset to be downgraded to sub-standard category subject to the condition that the amount of sacrifice, if any, in the element of interest, measured in present value terms, is either written off or provision is made to the extent of the sacrifice involved. For the purpose, the future interest due as per the original loan agreement in respect of an account should be discounted to the present value at a rate appropriate to the risk category of the borrower (i.e. current PLR + the appropriate credit risk premium for the borrower-category) and compared with the present value of the dues expected to be received under the restructuring package, discounted on the same basis.

c) In case there is a sacrifice involved in the amount of interest in present value terms, as at (b) above, the amount of sacrifice should either be written off or provision made to the extent of the sacrifice involved.

Treatment of sub-standard accounts restructured under CDR

a) A rescheduling of the instalments of principal alone, would render a sub-standard asset eligible to be continued in the sub-standard category for the specified period, provided the loan / credit facility is fully secured.

b) A rescheduling of interest element would render a sub-standard asset eligible to be continued to be classified in sub-standard category for the specified period subject to the condition that the amount of sacrifice, if any, in the element of interest, measured in present value terms, is either written off or provision is made to the extent of the sacrifice involved. For the purpose, the future interest due as per the original loan agreement in respect of an account should be discounted to the present value at a rate appropriate to the risk category of the borrower (i.e., current PLR + the appropriate credit risk premium for the borrower-category) and compared with the present value of the dues expected to be received under the restructuring package, discounted on the same basis.

c) In case there is a sacrifice involved in the amount of interest in present value terms, as at (b) above, the amount of sacrifice should either be written off or provision made to the extent of the sacrifice involved. Even in cases where the sacrifice is by way of write off of the past interest dues, the asset should continue to be treated as sub-standard.

The sub-standard accounts at (ii) (a), (b) and (c) above, which have been subjected to restructuring, etc. whether in respect of principal instalment or interest amount, by whatever modality, would be eligible to be upgraded to the standard category **only after the specified period, i.e., a period of one year** after the date when first payment of interest or of principal, whichever is earlier, falls due, subject to satisfactory performance during the period. The amount of provision made earlier, net of the amount provided for the sacrifice in the interest amount in present value terms as aforesaid, could also be reversed after the one-year period.

During this one-year period, the sub-standard asset will not deteriorate in its classification if satisfactory performance of the account is demonstrated during the period. In case, however, the satisfactory performance during the one year period is not evidenced, the asset classification of the restructured account would be governed as per the applicable prudential norms with reference to the pre-restructuring payment schedule.

The asset classification under CDR would continue to be bank-specific based on record of recovery of each bank, as per the existing prudential norms applicable to banks.

4.2.15 Projects under implementation

It was observed that there were instances, where despite substantial time overrun in the projects under implementation, the underlying loan assets remained classified in the standard category merely because the project continued to be under implementation. Recognising that unduly long time overrun in a project adversely affected its viability and the quality of the asset deteriorated, a need was felt to evolve an objective and definite time-frame for completion of projects so as to ensure that the loan assets relating to projects under implementation were appropriately classified and asset quality correctly reflected. In the light of the above background, it was decided to extend the norms detailed below on income recognition, asset classification and provisioning to banks with respect to industrial projects under implementation, which involve time overrun.

(i) The projects under implementation are grouped into three categories for the purpose of determining the date when the project ought to be completed:

Category I: Projects where financial closure had been achieved and formally documented.

Category II: Projects sanctioned before 1997 with original project cost of Rs.100 crore or more where financial closure was not formally documented.

Category: III: Projects sanctioned before 1997 with original project cost of less than Rs.100 crore where financial closure was not formally documented.

Asset classification

(ii) In case of each of the three categories, the date when the project ought to be completed and the classification of the underlying loan asset should be determined in the following manner:

Category I (Projects where financial closure had been achieved and formally documented): In such cases the date of completion of the project should be as envisaged at the time of original financial closure. In all such cases, the asset may be treated as ***standard asset for a period not exceeding two years beyond the date of completion of the project, as originally envisaged at the time of initial financial closure of the project***.

In case, however, in respect of a project financed after 1997, the financial closure had not been formally documented, the norms enumerated for category III below, would apply.

Category II (Projects sanctioned before 1997 with original project cost of Rs.100 crore or more where financial closure was not formally documented): For such projects sanctioned prior to 1997, where the date of financial closure had not been formally documented, an **independent Group** was constituted with experts from the term lending institutions as well as outside experts in the field to decide on the deemed date of completion of projects. The Group, based on all material and relevant facts and circumstances, has decided the deemed date of completion of the project, on a project-by-project basis. In such cases, the asset may be treated as ***standard asset for a period not exceeding two years beyond the deemed date of completion of the project, as decided by the Group***. Banks, which have extended finance towards such projects, may approach the lead financial institutions to which a copy of the independent Group's report has been furnished for obtaining the particulars relating to the deemed date of completion of project concerned.

Category III (Projects sanctioned before 1997 with original project cost of less than Rs.100 crore where financial closure was not formally documented): In these cases, sanctioned prior to 1997, where the financial closure was not formally documented, the date of completion of the project would be as originally envisaged at the time of sanction. In such cases, ***the asset may be treated as standard asset only for a period not exceeding two years beyond the date of completion of the project as originally envisaged at the time of sanction.***

(iii) In all the three foregoing categories, in case of time overruns beyond the aforesaid period of two years, the asset should be classified as sub-standard regardless of the record of recovery and provided for accordingly.

(iv) As regards the **projects to be financed by the FIs/ banks in future**, the date of completion of the project should be clearly spelt out at the time of financial closure of the project. In such cases, if the date of commencement of commercial production extends **beyond a period of six months** after the date of completion of the project, as originally envisaged at the time of initial financial closure of the project, the account should be treated as a sub-standard asset.

Income recognition

(v) There will be no change in the existing instructions on income recognition. Consequently, banks should not recognise income on accrual basis in respect of the projects even though the asset is classified as a standard asset if the asset is a "non performing asset" in terms of the extant instructions. In other words, while the accounts of the project may be classified as a standard asset, banks shall recognise income in such accounts only on realisation on cash basis if the asset has otherwise become 'non performing' as per the extant delinquency norm of 180 days. The delinquency norm would become 90 days with effect from 31 March 2004.

Consequently, banks which have wrongly recognised income in the past should reverse the interest if it was recognised as income during the current year or make a provision for an equivalent amount if it was recognised as income in the previous year(s). As regards the regulatory treatment of income recognised as 'funded interest' and 'conversion into equity, debentures or any other instrument' banks should adopt the following:
a) 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.
b) Conversion into equity, debentures or any other instrument: The amount outstanding converted into other instruments would normally comprise principal and the interest components. If the amount of interest dues is converted into equity **or any other instrument**, and income is recognised in consequence, full provision should be made for the amount of income so recognised to offset the effect of such income recognition. Such provision would be in addition to the amount of provision that may be necessary for the depreciation in the value of the equity or other instruments, as per the investment valuation norms. However, if the conversion of interest is into equity which is quoted, interest income can be recognised at market value of equity, as on the date of conversion, not exceeding the amount of interest converted to equity. Such equity must thereafter be classified in the "available for sale" category and valued at lower of cost or market value. In case of conversion of principal and /or interest in respect of NPAs into debentures, such debentures should be treated as NPA, *ab initio*, in the same asset classification as was applicable to loan just before conversion and provision made as per norms. This norm would also apply to zero coupon bonds or other instruments which seek to defer the liability of the issuer. On such debentures, income should be recognised only on realisation basis. The income in respect of unrealised interest which is converted into debentures or any other fixed maturity instrument should be recognised only on redemption of such instrument. Subject to the above, the equity shares or other instruments arising from conversion of the principal amount of loan would also be subject to the usual prudential valuation norms as applicable to such instruments.

Provisioning

(vi) While there will be no change in the extant norms on provisioning for NPAs, banks which are already holding provisions against some of the accounts, which may now be classified as 'standard', shall continue to hold the provisions and shall not reverse the same.

4.2.16 Availability of security / net worth of borrower/guarantor

The availability of security or net worth of borrower/ guarantor should not be taken into account for the propose of treating an advance as NPA or otherwise, as income recognition is based on record of recovery.

4.2.17 Take-out Finance

Takeout finance is the product emerging in the context of the funding of long-term infrastructure projects. Under this arrangement, the institution/the bank financing infrastructure projects will have an arrangement with any financial institution for transferring to the latter the outstanding in respect of such financing in their books on a pre-determined basis. In view of the time-lag involved in taking-over, the possibility of a default in the meantime cannot be ruled out. The norms of asset classification will have to be followed by the concerned bank/financial institution in whose books the account stands as balance sheet item as on the relevant date. If the lending institution observes that the asset has turned NPA on the basis of the record of recovery, it should be classified accordingly. The lending institution should not recognise income on accrual basis and account for the same only when it is paid by the borrower/ taking over institution (if the arrangement so provides). The lending institution should also make provisions against any asset turning into NPA pending its take over by taking over institution. As and when the asset is taken over by the taking over institution, the corresponding provisions could be reversed. However, the taking over institution, on taking over such assets, should make provisions treating the account as NPA from the actual date of it becoming NPA even though the account was not in its books as on that date.

4.2.18 Post-shipment Supplier's Credit

(i) In respect of post-shipment credit extended by the banks covering export of goods to countries for which the ECGC's cover is available, EXIM Bank has introduced a guarantee-cum-refinance programme whereby, in the event of default, EXIM Bank will pay the guaranteed amount to the bank within a period of 30 days from the day the bank invokes the guarantee after the exporter has filed claim with ECGC.

(ii) Accordingly, to the extent payment has been received from the EXIM Bank, the advance may not be treated as a non-performing asset for asset classification and provisioning purposes.

4.2.19 Export Project Finance

(i) In respect of export project finance, there could be instances where the actual importer has paid the dues to the bank abroad but the bank in turn is unable to remit the amount due to political developments such as war, strife, UN embargo, etc.

(ii) In such cases, where the lending bank is able to establish through documentary evidence that the importer has cleared the dues in full by depositing the amount in the bank abroad before it turned into NPA in the books of the bank, but the importer's country is not allowing the funds to be remitted due to political or other reasons, the asset classification may be made after a period of one year from the date the amount was deposited by the importer in the bank abroad.

4.2.20 **Advances under rehabilitation approved by BIFR/ TLI**

Banks are not permitted to upgrade the classification of any advance in respect of which the terms have been re-negotiated unless the package of re-negotiated terms has worked satisfactorily for a period of one year. While the existing credit facilities sanctioned to a unit under rehabilitation packages approved by BIFR/term lending institutions will continue to be classified as sub-standard or doubtful as the case may be, in respect of additional facilities sanctioned under the rehabilitation packages, the Income Recognition, Asset Classification norms will become applicable after a period of one year from the date of disbursement.

5 PROVISIONING NORMS

5.1 General

5.1.1 In order to narrow down the divergences and ensure adequate provisioning by banks, t was suggested that a bank's statutory auditors, if they so desire, could have a dialogue with RBI's Regional Office/ inspectors who carried out the bank's inspection during the previous year with regard to the accounts contributing to the difference.

5.1.2 Pursuant to this, regional offices were advised to forward a list of individual advances, where the variance in the provisioning requirements between the RBI and the bank is above certain cut off levels so that the bank and the statutory auditors take into account the assessment of the RBI while making provisions for loan loss, etc.

5.1.3 The primary responsibility for making adequate provisions for any diminution in the value of loan assets, investment or other assets is that of the bank managements and the statutory auditors. The assessment made by the inspecting officer of the RBI is furnished to the bank to assist the bank management and the statutory auditors in taking a decision in regard to making adequate and necessary provisions in terms of prudential guidelines.

5.1.4 In conformity with the prudential norms, provisions should be made on the non-performing assets on the basis of classification of assets into prescribed categories as detailed in paragraphs 4 supra. Taking into account the time lag between an account becoming doubtful of recovery, its recognition as such, the realisation of the security and the erosion over time in the value of security charged to the bank, the banks should make provision against sub-standard assets, doubtful assets and loss assets as below:

5.2 Loss assets

The entire asset should be written off. If the assets are permitted to remain in the books for any reason, 100 percent of the outstanding should be provided for.

5.3 Doubtful assets

i) 100 percent of the extent to which the advance is not covered by the realisable value of the security to which the bank has a valid recourse and the realisable value is estimated on a realistic basis.

ii) In regard to the secured portion, provision may be made on the following basis, at the rates ranging from 20 percent to 50 percent of the secured portion depending upon the period for which the asset has remained doubtful:

Period for which the advance has been considered as doubtful	**Provision requirement (%)**
Up to one year	20
One to three years	30
More than three years	50

iii) Additional provisioning consequent upon the change in the definition of doubtful assets (vide para 4.1.2 above) effective from March 31, 2001 has to be made in phases as under:

- **As on 31.03.2001**, 50 percent of the additional provisioning requirement on the assets which became doubtful on account of new norm of 18 months for transition from sub-standard asset to doubtful category.

- As on **31.03.2002**, balance of the provisions not made during the previous year, in addition to the provisions needed, as on **31.03.2002**.

iv) Banks are permitted to phase the additional provisioning consequent upon the reduction in the transition period from substandard to doubtful asset from 18 to 12 months over a four year period commencing from the year ending March 31, 2005, with a minimum of 20 % each year.

Note: <u>Valuation of Security for provisioning purposes</u>

With a view to bringing down divergence arising out of difference in assessment of the value of security, in cases of NPAs with balance of Rs. 5 crore and above stock audit at annual intervals by external agencies appointed as per the guidelines approved by the Board would be mandatory in order to enhance the reliability on stock valuation. Collaterals such as immovable properties charged in favour of the bank should be got valued once in three years by valuers appointed as per the guidelines approved by the Board of Directors.

5.4 Sub-standard assets

A general provision of 10 percent on total outstanding should be made without making any allowance for DICGC/ECGC guarantee cover and securities available.

5.5 Standard assets

(i) From the year ending **31.03.2000**, the banks should make a general provision of a minimum of 0.25 percent on standard assets on **global loan portfolio** basis.

(ii) The provisions on standard assets should not be reckoned for arriving at net NPAs.

(iii)The provisions towards Standard Assets need not be netted from gross advances but shown separately as 'Contingent Provisions against Standard Assets' under 'Other Liabilities and Provisions - Others' in Schedule 5 of the balance sheet.

5.6 Floating provisions

Some of the banks make a 'floating provision' over and above the specific provisions made in respect of accounts identified as NPAs. The floating provisions, wherever available, could be set-off against provisions required to be made as per above stated provisioning guidelines. Considering that higher loan loss provisioning adds to the overall financial strength of the banks and the stability of the financial sector, banks are urged to voluntarily set apart provisions much above the minimum prudential levels as a desirable practice.

5.7 Provisions on Leased Assets

i) Sub-standard assets

a) 10 percent of the **'net book value'**.

b) As per the 'Guidance Note on Accounting for Leases' issued by the ICAI, **'Gross book value'** of a fixed asset is its historical cost or other amount substituted for historical cost in the books of account or financial statements. Statutory depreciation should be shown separately in the Profit & Loss Account. Accumulated depreciation should be deducted from the Gross Book Value of the leased asset in the balance sheet of the lessor to arrive at the **'net book value'**.

c) Also, balance standing in 'Lease Adjustment Account' should be adjusted in the 'net book value' of the leased assets. The amount of adjustment in respect of each class of fixed assets may be shown either in the main balance sheet or in the Fixed Assets Schedule as a separate column in the section related to leased assets.

ii) Doubtful assets

100 percent of the extent to which the finance is not secured by the realisable value of the leased asset. Realisable value to be estimated on a realistic basis. **In addition to the above** provision, the following provision on the **net book value** of the **secured portion** should be made, depending upon the period for which asset has been doubtful:

Period	**%age of provision**
Up to one year	20

One to three years	30
More than three years	50

iii) Loss assets

The entire asset should be written-off. If for any reason, an asset is allowed to remain in books, 100 percent of the **'net book value'** should be provided for.

5.8 Guidelines for Provisions under Special Circumstances

5.8.1 Government guaranteed advances

(i) With effect from 31 March 2000, in respect of advances sanctioned against State Government guarantee, if the guarantee is invoked and remains in default for more than two quarters (180 days at present), the banks should make normal provisions as prescribed in paragraph 4.1.2 above.

(ii) As regards advances guaranteed by State Governments, in respect of which guarantee stood invoked as on **31.03.2000**, necessary provision was allowed to be made, in a phased manner, during the financial years ending **31.03.2000** to **31.03.2003** with a minimum of 25 percent each year.

5.8.2 Advances granted under rehabilitation packages approved by BIFR/term lending institutions

(i) In respect of advances under rehabilitation package approved by BIFR/term lending institutions, the provision should continue to be made in respect of dues to the bank **on the existing credit facilities** as per their classification as sub-standard or doubtful asset.

(ii) As regards the additional facilities sanctioned as per package finalised by BIFR and/or term lending institutions, provision on additional facilities sanctioned need not be made for a period of **one year** from the date of disbursement.

(iii) In respect of additional credit facilities granted to SSI units which are identified as sick [as defined in RPCD circular No.PLNFS.BC.57 /06.04.01/2001-2002 dated 16 January 2002] and where rehabilitation packages/nursing programmes have been drawn by the banks themselves or under consortium arrangements, no provision need be made for a period of one year.

5.8.3 Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs, and life policies are exempted from provisioning requirements.

5.8.4 However, advances against gold ornaments, government securities and all other kinds of securities are not exempted from provisioning requirements.

5.8.5 Treatment of interest suspense account

Amounts held in Interest Suspense Account should not be reckoned as part of provisions. Amounts lying in the Interest Suspense Account should be deducted from the relative advances and thereafter, provisioning as per the norms, should be made on the balances after such deduction.

5.8.6 Advances covered by ECGC/DICGC guarantee

In the case of advances guaranteed by DICGC/ECGC, provision should be made only for the **balance in excess of** the amount guaranteed by these Corporations. Further, while arriving at the provision required to be made for doubtful assets, realisable value of the securities should first be deducted from the outstanding balance in respect of the amount guaranteed by these Corporations and then provision made as illustrated hereunder:

Example

Outstanding Balance	Rs. 4 lakhs
DICGC Cover	50 percent
Period for which the advance has remained doubtful	More than 3 years remained doubtful
Value of security held (excludes worth of Rs.)	Rs. 1.50 lakhs

Provision required to be made

Outstanding balance	Rs. 4.00 lakhs
Less: Value of security held	Rs. 1.50 lakhs
Unrealised balance	Rs. 2.50 lakhs
Less: DICGC Cover (50% of unrealisable balance)	Rs. 1.25 lakhs
Net unsecured balance	Rs. 1.25 lakhs
Provision for unsecured portion of advance	Rs. 1.25 lakhs (@ 100 percent of unsecured portion)
Provision for secured portion of advance	Rs. 0.75 lakhs (@ 50 percent of secured portion)
Total provision required to be made	Rs. 2.00 lakhs

5.8.7 Advance covered by CGTSI guarantee

In case the advance covered by CGTSI guarantee becomes non-performing, no provision need be made towards the guaranteed portion. The amount outstanding in excess of the guaranteed portion should be provided for as per the extant guidelines on provisioning for non-performing advances. Two illustrative examples are given below:

Example I

Asset classification status:	Doubtful – More than 3 years;	
CGTSI Cover	75% of the amount outstanding or 75% of the unsecured amount or Rs.18.75 lakh, whichever is the least	
Realisable value of Security	Rs.1.50 lakh	
Balance outstanding	Rs.10.00 lakh	
Less Realisable value of security	Rs. 1.50 lakh	
Unsecured amount	Rs. 8.50 lakh	
Less CGTSI cover (75%)	Rs. 6.38 lakh	
Net unsecured and uncovered portion:	Rs. 2.12 lakh	
		Provision Required
Secured portion	Rs.1.50 lakh	Rs. 0.75 lakh (@ 50%)
Unsecured & uncovered portion	Rs.2.12 lakh	Rs. 2.12 lakh (100%)

Total provision required		Rs. 2.87 lakh

Example II

Asset classification status	Doubtful – More than 3 years;	
CGTSI Cover	75% of the amount outstanding or75% of the unsecured amount or Rs.18.75 lakh, whichever is the least	
Realisable value of Security	Rs.10.00 lakh	
Balance outstanding	Rs.40.00 lakh	
Less Realisable value of security	Rs. 10.00 lakh	
Unsecured amount	Rs. 30.00 lakh	
Less CGTSI cover (75%)	Rs. 18.75 lakh	
Net unsecured and uncovered portion:	Rs. 11.25 lakh	
		Provision Required
Secured portion	Rs.10.00 lakh	Rs. 5.00 lakh (@ 50%)
Unsecured & uncovered portion	Rs.11.25 lakh	Rs.11.25 lakh (100%)
Total provision required		Rs. 16.25 lakh

5.8.8 Take-out finance

The lending institution should make provisions against a 'take-out finance' turning into NPA pending its take-over by the taking-over institution. As and when the asset is taken-over by the taking-over institution, the corresponding provisions could be reversed.

5.8.9 Reserve for Exchange Rate Fluctuations Account (RERFA)

When exchange rate movements of Indian rupee turn adverse, the outstanding amount of foreign currency denominated loans (where actual disbursement was made in Indian Rupee) which becomes overdue, goes up correspondingly, with its attendant implications of provisioning requirements. Such assets should not normally be revalued. In case such assets need to be revalued as per requirement of accounting practices or for any other requirement, the following procedure may be adopted:

- The loss on revaluation of assets has to be booked in the bank's Profit & Loss Account.

- Besides the provisioning requirement as per Asset Classification, banks should treat the full amount of the Revaluation Gain relating to the corresponding assets, if any, on account of Foreign Exchange Fluctuation as provision against the particular assets.

5.9 Writing-off of NPAs

5.9.1 In terms of Section 43(D) of the Income Tax Act 1961, income by way of interest in relation to such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the RBI in relation to such debts, shall be chargeable to tax in the previous year in which it is credited to the bank’s profit and loss account or received, whichever is earlier.

5.9.2 This stipulation is not applicable to provisioning required to be made as indicated above. In other words, amounts set aside for making provision for NPAs as above are not eligible for tax deductions.

5.9.3 Therefore, the banks should either make full provision as per the guidelines or write-off such advances and claim such tax benefits as are applicable, by evolving appropriate methodology in consultation with their auditors/tax consultants. Recoveries made in such accounts should be offered for tax purposes as per the rules.

5.10 Write-off at Head Office Level

Banks may write-off advances at Head Office level, even though the relative advances are still outstanding in the branch books. However, it is necessary that provision is made as per the classification accorded to the respective accounts. In other words, if an advance is a loss asset, 100 percent provision will have to be made therefor.

Annexure I

Reporting Format for Non-Performing Assets – Gross and Net Position

[Vide paragraph 3.5]

Name of the Bank:
Position as on …………………………..

(Rupees in crore up to two decimals)	
Particulars	Amount
1. GROSS ADVANCES *	
2. Gross NPAs *	
3. GROSS NPAS AS A PERCENTAGE OF GROSS ADVANCES	
4. Total Deductions (i+ii+iii+iv)	
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 **	
5. Net advances (1-4)	
6. Net NPAs (2-4)	
7. NET NPAS AS A PERCENTAGE OF NET ADVANCES	

*excluding Technical write off of Rs. ………. crore.
** excluding amount of technical write off (Rs…….. …crores) and provision on standard assets (Rs………..crore)
$ banks which do not maintain an Interest Suspense account to park the accrued interest on NPAs, may furnish the amount of interest receivable on NPAs as a foot note to this statement
Note: For the purpose of this Statement, 'gross advances' mean all outstanding loans and advances including advances for which refinance has been received but excluding rediscounted bills, and advances written off at Head Office level (Technical write off).

Annexure II

Relevant extract of the list of direct agricultural advances from the Master Circular on lending to priority sector
- RPCD. PLAN. BC. 12/ 04.09.01/ 2001-02 dated 1 August 2001

1.1 **Direct Finance to Farmers for Agricultural Purposes**
1.1.1 Short-term loans for raising crops i.e. for crop loans. In addition, advances upto Rs.1 lakh to farmers against pledge/ hypothecation of agricultural produce (including

warehouse receipts) for a period not exceeding 6 months, where the farmers were given crop loans for raising the produce, provided the borrowers draw credit from one bank.

1.1.2 Medium and long-term loans (**Provided directly to farmers** for financing production and development needs).

(i) **Purchase of agricultural implements and machinery**

(a) Purchase of agricultural implements - Iron ploughs, harrows, hose, land-levellers, bundformers, hand tools, sprayers, dusters, hay-press, sugarcane crushers, thresher machines, etc.

(b) Purchase of farm machinery - Tractors, trailers, power tillers, tractor accessories viz., disc ploughs, etc.

(c) Purchase of trucks, mini-trucks, jeeps, pick-up vans, bullock carts and other transport equipment, etc. to assist the transport of agricultural inputs and farm products.

(d) Transport of agricultural inputs and farm products.

(e) Purchase of plough animals.

(ii) **Development of irrigation potential through –**

(a) Construction of shallow and deep tube wells, tanks, higher etc., and purchase of drilling units.

(b) Constructing, deepening clearing of surface wells, boring of wells, electrification of wells, purchase of oil engines and installation of electric motor and pumps.

(c) Purchase and installation of turbine pumps, construction of field channels (open as well as underground), etc.

(d) Construction of lift irrigation project.

(e) Installation of sprinkler irrigation system.

(f) Purchase of generator sets for energisation of pumpsets used for agricultural purposes.

(iii) **Reclamation and Land Development Schemes**

Bunding of farm lands, levelling of land, terracing, conversion of dry paddy lands into wet irrigable paddy lands, wasteland development, development of farm drainage, reclamation of soil lands and prevention of salinisation, reclamation of ravine lands, purchase of bulldozers, etc.

(iv) **Construction of farm buildings and structures, etc.**

Bullock sheds, implement sheds, tractor and truck sheds, farm stores, etc.

(v) **Construction and running of storage facilities**

Construction and running of warehouses, godowns, silos and loans granted to farmer for establishing cold storages used for storing own produce.

(vi) **Production and processing of hybrid seeds for crops**.

(vii) **Payment of irrigation charges, etc.**

Charges for hired water from wells and tube wells, canal water charges, maintenance and upkeep of oil engines and electric motors, payment of labour charges, electricity charges, marketing charges, service charges to Customs Service Units, payment of development cess, etc.

(viii) **Other types of direct finance to farmers**

(a) Short-term loans

To traditional/non-traditional plantations and horticulture.

(b) Medium and long term loans

Development loans to all plantations, horticulture, forestry and wasteland.

PRUDENTIAL NORMS

Part-A

List of Circulars consolidated by the Master Circular

No.	Circular No.	Date	Subject	Para No.
1.	DBOD No.BP.BC. 108/ 21.04.048/2001-2002	28.05.2002	Income recognition, asset classification and provisioning on advances - treatment of projects under implementation involving time overrun	4.2.15
2.	DBOD No.BP.BC. 101/ 21.01.002/ 2001- 02	09.05.2002	Corporate Debt Restructuring	4.2.14
3.	DBOD No.BP.BC. 100/ 21.01.002/ 2001- 02	09.05.2002	Prudential norms on asset classification	4.1.2
4.	DBOD No.BP.BC. 59/ 21.04.048/2001-2002	22.01.2002	Prudential norms on income recognition, asset classification and provisioning- agricultural advances	4.2.11(i)
5.	DBOD No.BP.BC. 25/ 21.04.048/2000-2001	11.09.2001	Prudential norms on income recognition, asset classification and provisioning	4.2.13 (v)
6.	DBOD No.BP.BC. 15 / 21.04.114/2000-2001	23.08.2001	Corporate Debt Restructuring	4.2.14
7.	DBOD No.BP.BC. 132/ 21.04.048/2000-2001	14.06.2001	Income Recognition, Asset Classification and Provisioning for Advances	4.2.2, 4.2.3, 4.2.4, 4.2.5(ii), 4.2.6, 4.2.7
8.	DBOD No. BP.BC. 128/ 21.04.048/2000-2001	07.06.2001	SSI Advances Guaranteed by CGTSI –Risk-weight and provisioning norms	5.8.7
9.	DBOD No. BP. BC. 116 /21.04.048/ 2000-2001	02.05.2001	Monetary & Credit Policy Measures 2001-02	2.1.2, 2.1.3
10.	DBOD No. BP. BC. 98/ 21.04.048/ 2000-2001	30.03.2001	Treatment of Restructured Accounts	4.2.13
11.	DBOD No. BP. BC. 40 / 21.04.048/ 2000-2001	30.10.2000	Income Recognition, Asset Classification and Provisioning - Reporting of NPAs to RBI	3.5
12.	DBOD.No.BP.BC.161/21.04.048/ 2000	24.04.2000	Prudential Norms on Capital Adequacy, Income Recognition, Asset Classification and Provisioning, etc.	5.5

No.	Circular No.	Date	Subject	Para No.
13.	DBOD.No.BP.BC.144/21.04.048/ 2000	29.02.2000	Income Recognition, Asset Classification and Provisioning and Other Related Matters and Adequacy Standards - Takeout Finance	4.2.17, 5.8.8
14.	DBOD.No.BP.BC.138/21.04.048/ 2000	07.02.2000	Income Recognition, Asset Classification and Provisioning - Export Project Finance	4.2.19
15.	DBOD.No.BP.BC.103/21.04.048/ 99	21.10.99	Income Recognition, Asset Classification and Provisioning - Agricultural Finance by Commercial Banks through Primary Agricultural Credit Societies	4.2.8
16.	DBOD.No.FSC.BC.70/24.01.001/ 99	17.07.99	Equipment Leasing Activity - Accounting/ Provisioning Norms	3.2.3, 5.7
17.	DBOD.No.BP.BC.45/21.04.048/99	10.05.99	Income Recognition, Asset Classification and Provisioning - Concept of Commencement of Commercial Production	4.2.13
18.	DBOD.No.BP.BC.120/21.04.048/ 98	29.12.98	Prudential Norms on Income Recognition, Asset Classification and Provisioning - Agricultural Loans Affected by Natural Calamities	4.2.11(ii) & (iii)
19.	DBOD.No.BP.BC.103/21.01.002/ 98	31.10.98	Monetary & Credit Policy Measures	4.1.1, 4.1.2, 5.5, 5.8.1
20.	DBOD.No.BP.BC.17/21.04.048/98	04.03.98	Prudential Norms on Income Recognition, Asset Classification and Provisioning - Agricultural Advances	4.2.11
21.	DOS. No. CO.PP. BC.6/ 11.01.005/ 96-97	15.05.97	Assessments relating to asset valuation and loan loss provisioning	5.1.3
22.	DBOD.No.BP.BC.29/21.04.048/97	09.04.97	Income Recognition, Asset Classification and Provisioning - Agricultural Advances	4.2.11

No.	Circular No.	Date	Subject	Para No.
23.	DBOD.No.BP.BC.14/21.04.048/97	19.02.97	Income Recognition, Asset Classification and Provisioning - Agricultural Advances	4.2.11
24.	DBOD.No.BP.BC.9/21.04.048/97	29.01.97	Prudential Norms - Capital Adequacy, Income Recognition, Asset Classification and Provisioning	4.2.3, 4.2.4, 4.2.6
25.	DBOD.No.BP.BC.163/21.04.048/ 96	24.12.96	Classification of Advances with Balance Less than Rs. 25,000/-	4.1
26.	DOS. No.CO.BC.21/ 11.02.826/ 96-97	31.10.96	Assessments relating to asset valuation and loan loss provisioning	5.1.1
27.	DBOD.No.BP.BC.65/21.04.048/96	04.06.96	Income Recognition, Asset Classification and Provisioning	4.2.6
28.	DBOD.No.BP.BC.26/21.04.048/96	19.03.96	Non-Performing Advances - Reporting to RBI	3.5
29.	DBOD.No.BP.BC.25/21.04.048/96	19.03.96	Income Recognition, Asset Classification and Provisioning	4.2.6, 4.2.12, 5.10
30.	DBOD.No.BP.BC.134/21.04.048/ 95	20.11.95	EXIM Bank's New Lending Programme Extension of Guarantee-cum-Refinance to Commercial Bank in respect of Post-shipment Supplier's Credit	4.2.18
31.	DBOD.No.BP.BC.36/21.04.048/95	03.04.95	Income Recognition, Asset Classification and Provisioning	3.2.2, 3.3, 4.2.18, 5.8.2(i), (ii)
32.	DBOD.No.BP.BC.134/21.04.048/ 94	14.11.94	Income Recognition, Asset Classification, Provisioning and Other Related Matters	4.2.18, 5.8.2
33.	DBOD.No.BP.BC.58/21.04.048-94	16.05.94	Income Recognition, Asset Classification and Provisioning and Capital Adequacy Norms - Clarifications	5.8.6
34.	DBOD.No.BP.BC.50/21.04.048/94	30.04.94	Income Recognition, Asset Classification and Provisioning	5.8.6

No.	Circular No.	Date	Subject	Para No.
35.	DOS.BC.4/16.14.001/93-94	19.03.94	Credit Monitoring System - Health Code System for Borrowal Accounts	1.3
36.	DBOD.No.BP.BC.8/21.04.043/94	04.02.94	Income Recognition, Provisioning and Other Related Matters	3.1.2, 3.4, 4.2.9, 4.2.20, 5.6,5.8.3, 5.8.4, 5.8.5
37.	DBOD.No.BP.BC.195/21.04.048/ 93	24.11.93	Income Recognition, Asset Classification and Provisioning - Clarifications	4.2.12
38.	DBOD.No.BP.BC.95/21.04.048/93	23.03.93	Income Recognition, Asset Classification, Provisioning and Other Related Matters	5.9.1 to 5.9.3
39.	DBOD.No.BP.BC.59/21.04.043-92	17.12.92	Income Recognition, Asset Classification and Provisioning - Clarifications	2.1.2,3.2.1, 3.2.2, 4.2.5(i), 4.2.6, 4.2.7(ii), 4.2.10, 4.2.11, 4.2.12, 4.2.14
40.	DBOD.No.BP.BC.129/21.04.043-92	27.04.92	Income Recognition, Asset Classification, Provisioning and Other Related Matters	1.1, 1.2, 2.1.1, 2.2, 3.1.1,3.1.3, 4.1, 4.1.1, 4.1.2, 4.1.3, 4.2, 5.1, 5.1.2, 5.2, 5.3, 5.4
41.	DBOD.No.BP.BC.42/C.469 (W)-90	31.10.90	Classification of Non-Performing Loans	3.1.1
42.	DBOD.No.Fol.BC.136/C.249-85	07.11.85	Credit Monitoring System - Introduction of Health Code for Borrowal Accounts in Banks	1.3

Part-B

List of Other Circulars containing Instructions/ Guidelines/ Directives related to Prudential Norms

No.	Circular No.	Paragraph in the circular which is superseded	Date	Subject	Para No.

No.	Circular No.	Paragraph in the circular which is superseded	Date	Subject	Para No.
1.	DBOD.No.BP.BC.35/21.01.002/99	2(iii)	24.04.99	Monetary & Credit Policy Measures	4.2.13(i), 4.2.13 (iv)
2.	DBOD.No.FSC.BC.18/24.01.001/ 93-94	1(ii), 1(v)	19.02.94	Equipment Leasing, Hire Purchase, Factoring, etc. Activities	2.1, 3.2.3