



Classification of Advances – IRACP Norms

Jabalpur Branch of CIRC of ICAI

28th March, 2023



Objective

The overall objective of the branch audit should be to have **transaction testing** and provide inputs to the Statutory Central Auditors on **adequacy of implementation of various policies and regulatory requirements**, including **efficacy of the system and assurance functions** (risk management, compliance and internal audit) at branch level.

Large Advances

List of accounts examined for audit

Account No.	Account Name	Balance as at year end – Funded	Balance as at year end – Non Funded	Total
Total		A	B	$C=A+B$
Total Outstanding of the Branch		X	Y	$Z=X+Y$
Percentage Examined		A as % of X	B as % of Y	C as % of Z

Bank Branch Audit

1. Challenge to do quality audit in a limited time frame.
2. Proper audit planning is critical.
3. Quality of audit and value addition are the key issues.
4. Adverse comment having impact on financial statements or NPA/ provisions should be reported in main audit report based on professional judgement in each case.



Master Circular on IRAC Dt. 01.04.2022

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

Consolidates instructions issued upto March 31, 2022



Types of Advances

Fund Based

- Term Loans
- Cash Credit/ Overdraft Facility
- Bills purchased & discounted

Non Fund Based

- Letter of Credit
- Bank Guarantee

Non Performing Assets – When??

If interest/
installment is
overdue for
more than 90
days

Bills purchased /
discounted remains
overdue for more
than 90 days.

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- CC/ OD remains **out of order** for 90 days
 - Concept of sanctioned limit, drawing power



Types of NPA

Substandard Asset
Doubtful Asset
Loss Asset

- NPAs should be classified borrower wise and not facility wise.
- Credit facility to co-borrower is also marked as NPA.
- Banks should establish appropriate internal systems on Automation of Income Recognition, Asset Classification and Provisioning processes in banks.

DBR.No.BP.BC.45/21.04.048/2018-19 Dt June 7, 2019

Prudential Framework for Resolution of Stressed Assets

SMA Sub Category	Basis for classification – Principal or interest payment or any other amount wholly or partly overdue between
SMA 00	1-30 days
SMA 01	31- 60 days
SMA 02	61- 90 days

Reasons for NPA

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graph TD; A[Reasons for NPA] --> B[Inherent financial weakness and non-recovery]; A --> C[Due to Technical reasons];
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Inherent financial
weakness and non-
recovery

Due to Technical reasons



Term Loans

- Advances against term deposits, NSCs eligible for surrender, KVPs and life insurance policies need not be treated as NPAs, provided adequate margin is available in the accounts
- Advances against gold ornaments, government securities and all other securities are not covered by this exemption.
- 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.

Term Loans

Verification of Master Data affecting classification

- ✓ Whether EMI/ Instalment is properly setup
- ✓ Whether EMI/ Instalment is matching with sanctioned terms
- ✓ Error in multiple sets of EMI/ Instalments
- ✓ Incorrect Moratorium Period
- ✓ Incorrect entry of instalment start date/ Interest Demand date
- ✓ Multiple Customer ID for the same customer
- ✓ Fictitious credits through Office Accounts/ Inter Branch Accounts and through some other account including dormant accounts

Cash Credit/Overdraft

CC/OD will be treated as NPA if out of order

Out of Order if the outstanding balance in CC/OD Account-

- Remains continuously **in excess of the sanctioned limit**/drawing power for **90 days**
- Is **less than the sanctioned limit**/drawing power but there are **no credits** continuously for **90 days**
- Is **less than the sanctioned limit**/drawing power but credits are **not enough to cover the interest** debited during the previous **90 days** period

Cash Credit/Overdraft

Technical reasons for NPA

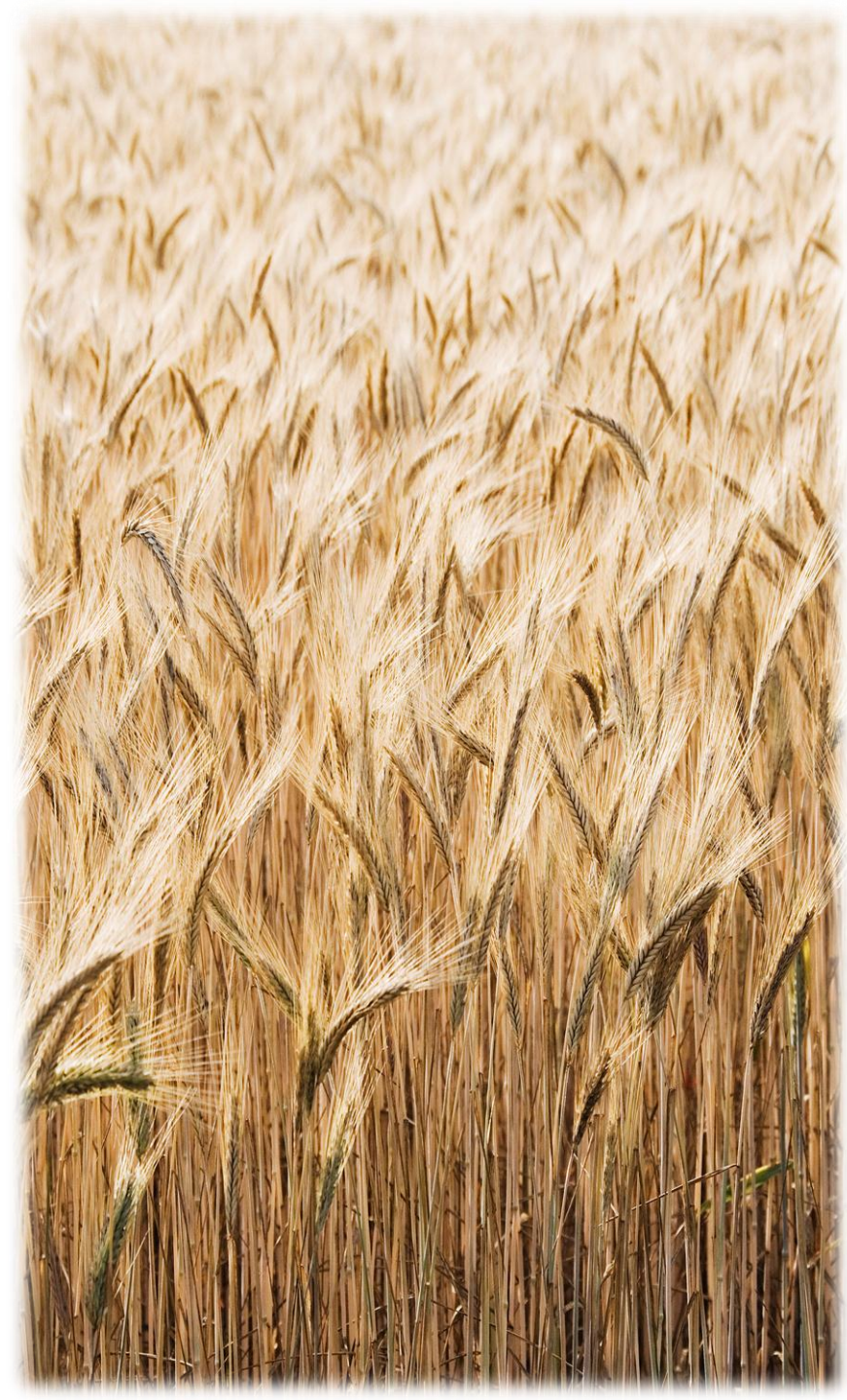
- Renewal dates entered in the system without actual renewals being done.
- Renewals done without supporting financial statements/ unit visit reports.
- Renewals pending at Regional Office – Short review can be done for 2 times of 90 days each.
- Only Interest and Bank Charges serviced – such accounts are not classified as NPAs.
- Alteration of Drawing Power limits

Bills Purchased and Discounted

- The bill remains overdue for a period of **more than 90 days** in the case of bills purchased and discounted , then it is NPA.
- The bills discounted under LC favouring a borrower **may** not be classified as a NPA, even if any other facility granted to the borrower is classified as NPA, **except in case where-**
 - ✓ documents under LC are not accepted on presentation
 - ✓ The payment under the LC is not made on the due date by the LC issuing bank for any reason and the borrower does not immediately make good the amount disbursed
- The outstanding bills discounted will immediately be classified as NPA from the date when the other facilities had been classified as NPA.

Agriculture Loans

- A loan granted will be treated as NPA if the instalment of principal or interest thereon remains overdue-
 - In case of **short** duration crops for **two crop seasons**
 - In case of **long** duration crops for **one crop season**
- Housing loans under Indira Awas Yojana / Pradhan Mantri Gram Awas Yojana and Golden Jubilee Rural Housing Finance Scheme
- Refer Annex 2 of RBI Master Circular dated 01.04.2022
- Loan to Mandi Vyapari (Market Traders) is not an Agricultural Advance



Agriculture Loans

- If natural calamities impair the repaying capacity, **banks** may **decide** on their own as a **relief measure** conversion of the **short-term** production loan into a **term loan** or **reschedulement** of the repayment period; and the sanctioning of fresh short-term loan.
- In such cases the term loan as well as fresh short-term loan may be treated as **current dues** and **not** to be classified as **NPA**.
- Such loans may turn into NPA if it remains outstanding as per prevailing IRAC norms

Agriculture Loans to PACS/ FSS

- Agricultural advances as well as advances for other purposes granted by banks to PACS/ FSS under the on-lending system, only that particular credit facility granted to PACS/ FSS which is in default for a period mentioned in case of short duration crops and long duration crops, 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, 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.

Consortium

- Recovery of the individual member bank and other aspects having a bearing on the recoverability of the advances
- Where the remittances by the borrower are pooled with one bank and/or where the bank receiving remittances is not parting with the share of other member banks, the account treated as not serviced in the books of the other member banks and then considered NPA.

Classification based on Value of Security

- When realisable value of the security is less than 50% of the value assessed at the time of the last inspection, such accounts may directly be classified under doubtful category
- When realisable value of the security is less than 10% of the value assessed at the time of the last inspection, the existence of security should be ignored and asset should directly be classified as Loss asset
- The accounts which are already classified as NPA as doubtful there would be no change in the classification and it will only have impact on the provision

Reversal Of Income

- Interest, fee, commission and similar income should cease to accrue from the date of NPA and any **such unrealised income** should be reversed with respect to past periods.
- This applies to Government guaranteed accounts also
- If loans with moratorium on payment of interest (permitted at the time of sanction of the loan) become NPA after the moratorium period is over, the capitalized interest, if any, corresponding to the interest accrued during such moratorium period need not be reversed.

Provisioning

Category	Provisioning requirement (%)
Sub-standard (SS)	15% (plus 10% on unsecured exposures)
Doubtful Up to one year (D1)	25% (plus 100% to the extent advance is not covered by realizable security)
Doubtful between one to three years (D2)	40% (plus 100% to the extent advance is not covered by realizable security)
Doubtful for more than three years (D3)	100% (plus 100% to the extent advance is not covered by realizable security)

100% provision in respect of fraud in 4 quarters from the date of detection

Provision requirement on Standard Asset	%
Farm Credit to agricultural activities, individual housing loans and Small and Micro Enterprises (SMEs) sectors	0.25
Advances to Commercial Real Estate (CRE) Sector	1.00
Advances to Commercial Real Estate – Residential Housing Sector (CRE - RH)	0.75
Housing loans extended at teaser rates	2
Restructured advances – as stipulated in the prudential norms for restructuring of advances	As stipulated in the prudential norms for restructuring of advances.
Advances restructured and classified as standard	5.00
All other loans and advances not included above	0.40

Recovery in NPA Accounts



Entire arrears are to be recovered for upgradation

Regularized after Balance Sheet date

Apportionment of recovery

Restructuring

- An act in which a lender, for **economic** or **legal** reasons relating to the borrower's financial difficulty, grants concessions to the borrower.
- Involve modification of terms of the advances / securities, which would generally include-
 - ❖ **Alteration** of payment period / payable amount / the amount of instalments / rate of interest;
 - ❖ **Roll over** of credit facilities;
 - ❖ Sanction of **additional credit facility**/ release of additional funds for an account in default to aid curing of default / enhancement of existing credit limits;
 - ❖ **Compromise settlements** where time for payment of settlement amount exceeds three months.
 - ❖ **Interchangeability** within sanctioned limits



Exception to Restructuring



Change in DCCO of Project Loans

Change in MCLR/ Floating Rate



Change in ROI due to internal/ external rating

Interchangeability in terms of sanction letter

Restructuring in terms of natural calamities





Eligibility Criteria for Restructuring

- ✓ Financial viability is established and there is a reasonable certainty of repayment from the borrower as per the terms of restructuring package.
- ❑ Parties indulging in frauds and malfeasance are not eligible for restructuring

Downgrading of Restructured Advances

- In case of restructuring, the accounts classified as 'standard' shall be immediately downgraded i.e., 'sub-standard' to begin with.
- The NPAs upon restructuring would continue to have the same asset classification as prior to restructuring.

Consideration for Verification

Whether parameters are met ?

Educational Institutions are not MSME

Whether documents for restructuring are executed ?

Rephasement without reporting it as restructured

Upgradation of Restructured Accounts

For MSME accounts where aggregate exposure of the lenders is less than ₹ 25 crores

- ✓ only if it demonstrates **satisfactory performance** during the **specified period**





All other accounts with exposure up to ₹ 100 crores

- ✓ when **all** outstanding loan / facilities in the account demonstrate ‘**satisfactory performance**’ during the period from the date of implementation of RP up to the date by which at least 10 % of the sum of outstanding principal debt as per the RP and interest capitalisation sanctioned as part of the restructuring, if any, is repaid.
- ✓ Account cannot be upgraded before one year from the commencement of the first payment of interest or principal (whichever is later) on the credit facility with longest period of moratorium under the terms of RP.

Upgradation where the aggregate exposure of lenders is \geq 100 crores and above

- Qualify for an upgrade at time of RP implementation, in addition to demonstration of satisfactory performance
- The credit facilities shall be **rated** as **investment grade18** (BBB- or better), at the time of upgrade, by CRAs accredited by RBI
- Accounts with aggregate exposure of \geq 500 crores and above shall require two rating
- If the ratings are obtained from more than the required number of CRAs, all such ratings shall be investment grade for the account to qualify for an upgrade

What if the restructuring fails

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- If the borrower fails to demonstrate satisfactory performance during the monitoring period, asset classification upgrade shall be subject to implementation of a fresh restructuring/ change in ownership.
 - Additional provision of 15% for such accounts at the end of the review period. This additional provision, along with other additional provisions, may be reversed as per the norms.
 - Provisions held on restructured assets may be reversed when the accounts are upgraded to standard category.
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Project Loans

Deferment of DCCO and consequential shift in repayment schedule for **equal or shorter duration** will **not** be treated as **restructuring** provided that:

- a) The revised DCCO falls within the period of **two years and one year** from the original DCCO for infrastructure projects and non-infrastructure projects respectively; and
- b) All **other terms** and conditions of the loan remain **unchanged**.

Additional Time Limits

Infrastructure Project (Court Cases)

- Additional two years time will be given in this case i.e total extension of four years

Infrastructure Project (other reasons beyond the control of promoters)

- Additional upto one year extension for DCCO i.e total three years extension

Non-Infrastructure (other than Commercial Real Estate)

- Additional upto one year extension i.e total two years extension for DCCO

Commercial Real Estate Exposures

- Additionally upto one year extension i.e total two years extension given for DCCO **provided** that the revised repayment schedule is extended only by a period equal to or shorter than the extension in DCCO and all provisions of the Real Estate (Regulation and Development) Act, 2016 are complied with.

Extension of DCCO

- Restructuring application should be received before the expiry of period mentioned and when the account is still standard as per record of recovery.
- Other conditions applicable:
 - a) Moratorium for payment of interest, then income not to be booked on accrual basis beyond two years and one year from the original DCCO for infrastructure and non-infrastructure projects respectively,
 - b) Provisions maintained on such accounts as long as these are classified as standard assets.



Other Conditions

- Projects financed by the FIs/ banks, the **DCCO** of the project clearly spelt out at the time of financial closure of the project and the same should be **formally documented**.
- NPA classification will be from the original date

DCCO Provision Requirements

Particulars	Provision Requirement
If the revised DCCO is within two years/one year from the original DCCO prescribed at the time of financial closure for infrastructure and non-infrastructure projects (including commercial real estate projects) respectively	0.4 per cent
<p>If the DCCO is extended:</p> <p>i) Beyond two years and upto four years or three years from the original DCCO, as the case may be, for infrastructure projects depending upon the reasons for such delay;</p> <p>ii) Beyond one years and upto two years from the original DCCO, for non-infrastructure projects (including real estate projects)</p>	<p>5.00 per cent From the date of such restructuring till the revised DCCO or 2 years from the date of restructuring, whichever is later</p>

Restructuring of MSME Advances

RBI Circular dated January 1, 2019

- One time relaxation without downgrading subject to following conditions;
 - (i) Borrower meets the criteria of MSME (Registration was not required)
 - (ii) Aggregate exposure should be less than 25 crores
 - (iii) Asset should be standard as on 01.01.2019
 - (iv) Restructuring should be implemented by 31.03.2020
 - (v) There should be a Board approved policy

RBI Circular dated February 11, 2020

Extended the benefits of previous Circular till 31.12.2020

Restructuring of MSME Advances

RBI Circular dated August 6, 2020

- Extended One Time Relaxation without downgrading subject to following conditions;
 - (i) Aggregate exposure should be less than 25 crores
 - (ii) Asset should be standard as on 01.03.2020
 - (iii) Restructuring should be implemented by 31.03.2021
 - (v) Borrower should have been registered under GST unless exempted from registration

RBI Circular dated June 24, 2020

- Credit facilities extended under the above scheme are backed by a guarantee from CGTMSE
- Circular dated July1, 2020 on Distressed Assets Fund - Subordinate Debt for Stressed MSMEs permitted the banks to reckon the funds infused by the promoters in their MSME units through loans availed under the captioned scheme as equity/ quasi equity for debt-equity computation.

COVID 19 Relief

Two horizontal bars, one green and one olive green, positioned below the title.

RBI Circular dated May 5, 2021 for individuals, small business & MSME

- Extended One Time Relaxation without downgrading subject to following conditions;
 - (i) Account is not restructured under any previous Circulars
 - (ii) Borrower should be classified as MSME as on 31.03.2021 and registration should be obtained before implementation of restructuring plan
 - (iii) Aggregate exposure should be less than 25 crores (subsequently enhanced to 50 crores by Notification Dated June 4, 2021)
 - (iv) Asset should be standard as on 01.03.2021
 - (v) Restructuring should be invoked by 30.09.2021 and completed within 90 days
 - (vi) Borrower should have been registered under GST unless exempted from registration as on 31.03.2021

“Sometimes when you’re in a dark place you think you’ve been buried, but you’ve actually been planted.” — Christine Caine



Thank You

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