

ॐ सह नाववतु ।
सह नौ भुनक्तु ।
सह वीर्यं करवावहै ।
तेजस्वि नावधीतमस्तु मा विद्विषावहै ।
ॐ शान्तिः शान्तिः शान्तिः ॥

Om, May God Protect us Both (the Teacher and the Student),
May God Nourish us Both,
May we Work Together with Energy and Vigour,
May our Study be Enlightening and not give rise to Hostility,
Om, Peace, Peace, Peace.

VERIFICATION OF ADVANCES

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**CA Govind Batra
(Partner)
BATRA & BATRA**

QUIZ

- What is the difference between primary security and collateral security?
- What is the difference in hypothecation of pledge?
- What is difference between sole banking consortium arrangement of multiple banking ?
- What is the difference between equitable mortgage and legal mortgage?
- What is the meaning of repo rate and reverse repo rate?
- What is the meaning of PCA?

PRACTICE BEFORE THE MATCH

- **Annual Closing Guidelines**
- **Periodical Returns filed Fortnightly/Quarterly**
- **RBI Masters Circular (1st July 2015)**
- **Banking Regulation Act,1949**
- **Reserve Bank of India Act,1934(Guidance note on audit of bank by ICAI)**
- **Stamp Act of State**
- **Transfer of Property Act, 1882**
- **SARFAESI Act ,2002**

TYPES OF FACILITIES

EXTENDED BY BANKS

**BASED ON
FUNDS**

FUNDED

**NON-
FUNDED**

**BASED ON
GEOGRAPHY**

INLAND

EXPORT

**BASED ON
SECURITY**

SECURED

UNSECURED

**BASED ON
SECTOR**

PRIORITY

**NON-
PRIORITY**

FUND BASED ADVANCES

TERM LOANS

- **Granted for creation of fixed assets required for long-term use by the unit.**
- **Repayable in Installments.**
- **Classified in three categories :**
 - **1) Short term - repayable in < 3 years.**
 - **2) Medium term - repayable in 3 to 7 years.**
 - **3) Long term - repayable in > 7 years.**

CC/OD A/Cs

- **Limit based account mainly given for Business purposes.**
- **Mostly to meet the Working capital gap**
- **Primary security being Stock & Debtors**
- **No Fixed EMI repayment to this loan.**
- **Borrower to route all business turnover through this account.**
- **Bank fixes the Drawing power periodically**
- **Bank reviews the functioning & operation of this account periodically**
- **TOL, Overdraft, TOD (Meaning).**

NON-FUNDED ADVANCES

- **Called off balance sheet items**
- **Form the contingent liability items of the bank**
- **Banks pass contra entries in its books to have control on these**
- **Shown in the balance sheet of the bank only as part of Notes to Accounts**



BANK GUARANTEE

- **Promise by the banker to pay the stated amount to the beneficiary**
- **Financial guarantee and performance guarantee**
- **Counter guarantee by borrower to banker**
- **Generally guarantee shall be avoided to those who don't enjoy credit facilities with bank**
- **Specific guarantee and continuing guarantee**
- **Margin in the form of cash/term deposits as per norms**

LETTER OF CREDIT

- **Promise by a buyer's banker to honour the payments to be made to the seller**
- **Generally used in international trade**
- **At the request of the buyer, banker opens an L.C which is sent to the seller**
- **Seller dispatches the goods, sends the bill**
- **Buyer's banker is liable to make payment only if buyer defaults**

PRIORITY SECTOR ADVANCES

- Agriculture, MSME, Education, Housing, Export and Others
- Carrying lower rate of interest (DRI)
- Stipulated portion for priority sector – 40%
- Agriculture Sector -18%

AGRICULTURAL ADVANCES

- No service charges for loan upto 25000
- Receipts/Sanction/Rejection/Disbursement Register
- Acknowledgement of loan Application

NOTE: SPECIAL CARE FOR FRAUD IN AGRICULTURAL LOAN

BRIEF STUDY OF BRANCH OPERATIONS

- I. Types of advances –SSI, Housing ,Industrial, Agricultural, Vehicle loan etc.
- II. Whether advances increased/reduced substantially
- III. Number of takeover loan cases.
- IV. Whether substantially increase/decrease in NPA.
- V. Whether various awards received by branch head for achieving extraordinary work.
- VI. Whether any frauds reported.
- VII. Whether any key staff working in the same position for very longer period.
- VIII. Critical analysis of final account and statements of branch.

List of Documents to be obtained before starting Audit

- Obtain user-id & password for computer system
- Facility/Party wise list at borrowers along with outstanding balance as on 31/03/2019
- Sanctioning Power at Branch & higher authority.
- Precedings year's Statutory Audit Report & it's closure.
- Concurrent Audit Report of all 12 months.
- Internal Audit Report of Branch by their internal Auditor.
- RBI inspections Report, if any.
- Various Stock Audit Report.
- Revenue Audit Report.

Objection Raised from Bankers

SANCTION/ RENEWED

WITHOUT PROPER APPRAISAL OR DOCUMENTATION

1. Banker : Appraisal of loan is not covered under your purview! It is our discretion to give loan to whom we want ?

LFAR Point No. 5(a) :

In your opinion, has the branch generally complied with the procedures/instructions of controlling authorities of the bank regarding loan applications, preparation of proposals for grant/ renewal of advances, enhancement of limits, etc. including adequate appraisal documentation in respect thereof.

2. Banker : Why do you need our DFP (Delegation of Financial Power) ?

LFAR Point No. 5(b) :

In the case examined by you, have you come across instances of credit facilities having been sanctioned beyond the delegated authority or limit fixed for the branch? Are such cases promptly reported to higher authorities?

3. Banker : Why is there a need to verify original documents?

They are kept in the safe custody in the BANK LOCKER!

LFAR Point No. 5(c) :

- i. In the cases examined by you, have you come across instances of credit facilities released by the branch without execution of all the necessary documents? If so, give details of such cases.**

- I. In respect of advances examined by you, have you come across instances of deficiencies in documentation, non registration of charges, non-obtaining of guarantees etc.? If so give details of such cases.**
- II. Whether advances against lien of deposits have been properly granted by marking lien on the deposits in accordance with the guidelines of the controlling authorities of the bank.**

4.Banker : Your work is only to look after the loans sanctioned during the period covered under audit and not the renewal documents of old files?

LFAR Point No. 5(d) :

Is the procedure laid down by the controlling authorities of the bank for periodic review of advances including periodic balance confirmation /acknowledgement of debts , followed by the branch?

Provide analysis of the accounts overdue for review/renewal

**5. Banker : Why are you analyzing the report of stock auditors?
They are expert in their field.**

LFAR Point No. 5(d) :

Are the stock/book debt statements and other periodic operational data and financial statements etc. received regularly from the borrowers and duly scrutinized?

Is suitable action taken on the basis of such scrutiny in appropriate cases?

6.Banker : Why do you need the minutes of consortium meeting? All records are kept with the consortium leader?

LFAR Point No. 5(a)

Auditor should verify that in case of lending under consortium arrangement/ Multiple banking Arrangements' bank, any sanction of fresh loans/ ad hoc loans/ Renewals of loans to new/existing borrowers should be done only after obtaining/sharing necessary information among banks. Report the cases where prescribed guidelines are not followed

Auditor should verify that bank branch has on its record a due diligence certificate/report in the form and manner required by the RBI in respect of advances under consortium and multiple banking. Give the list of accounts where certificate is not obtained or on record.

Advances - Stages

➤ Pre – Sanction

- Credit Appraisal
- Restrictions
- Sanctioning
- Documentation
- Audit/ Inspection
- Disbursement

➤ Post – Sanction

- Monitoring/Supervision
- Review

Loan Application

- **Prescribed Application Form from the borrower for fresh or renewal proposal (deed, M/A)**
- **KYC Compliance as per RBI Requirements**
- **Project Report, Projected P&L, Balance Sheet & Cash Flow**
- **Latest audited financial statements**
- **Net worth statement of borrower/ Guarantor**
- **Board Resolution for the availment of the facility obtained**
- **Udyog ADHAR, NOC from Government Departments**
- **CIBIL Report of Borrower/Guarantor**

Sanctioning / Credit Appraisal

1. **Fresh Loans & Renewals : Whether appraised properly?**
2. **Verify whether Appraisal note of Bank is proper and done by competent person**
3. **Proper assessment of Financial viability of projects**
4. **Review projections , whether realistic or not**

- **Proposal has been routed through appropriate authorization levels.**
- **Recommendations are properly documented and noted.**
- **Limits sanctioned - discretionary powers of the sanctioning authority within Delegated Powers.**
- **Whether adverse remarks of field officer are over ruled by seniors?**
- **Whether adverse remarks of CIBIL reports are duly addressed in the proposal**
- **Sanctions are within the discretionary powers**

Sanctioning / Credit Appraisal

- **Pre disbursements unit inspection report.**
- **Compliance with RBI Guidelines / Bank Guidelines**
- **Nature of securities (primary/ collateral) offered and to confirm the adequacy of security cover.**
- **Credit Rating – Internal / External**
- **Adverse comments by auditors, inspectors, etc.**
- **Any change in the terms of sanction is ratified by appropriate authority.**

Sanctioning / Credit Appraisal

- Projections, repayment schedule, genuine sources of margin.
- Adequacy of security cover, credit worthiness of borrower,
- Title clearance, with clear opinion.
- Valuation of Securities.(Mostly immovable properties are valued through mechanical engineer)
- Exposure limit – Group/Industry wise

- **Nayak Committee Recommendations**
- **Due Diligence Certificate [Multiple/Consortium]**
- **CIBIL Report – Adverse comments / Score**
- **Confidential report & NOC from existing banker.**
- **Important Financial Ratios (DSCR, Current, Debt-Equity Ratio)**
- **Interchangeability of Limits – Main / Sub Limits**
- **Interchangeability can be between two sub limits within the same facility or two different facilities.**

Statutory Restrictions

- **Advances to Bank's Directors – Section 20(1) of Banking Regulation Act.**
- **Advances to Relatives of Bank's Directors – Not without prior approval of Board.**
- **Loans to Officers and relatives of senior officers of bank – Any officers in Nationalized Banks Grade IV and above, equivalent grade in SBI and Associate Banks, in any banking company incorporated in India.**

- **Loans to companies for buy back of shares – not permitted**
- **Loans to industries consuming Ozone depleting substances such as Foam, Refrigerators, Air Conditioners, Aerosol Products, Solvents, Fire Extinguishers etc.**
- **Restriction on payment of commission to staff members**
- **Restrictions on offering incentives for loan products.**

Documentation

- **Sanctioned Limits conveyed to borrower.**
- **Sanction T & C to be accepted by the borrower.**
- **Loan documents, as per the sanction letter and loan policy have been executed.**
- **Vetting by legal expert, if required.**
- **Fresh loan documents are obtained on change in limit, change in constitution of the borrower**
- **Original documents, share certificate, title deeds, title clearance certificate, valuation report are held on record**
- **Stamp Duty: As per the applicable Stamp Act.**
- **Insurance: All securities charged to the Bank – Insured adequately /Policy to have Bank Clause.**

Documentation

– w.r.t. Securities offered

- **Original documents are kept in safe custody.**
- **Charge on securities offered have been registered with registrar of companies / appropriate authority within stipulated time.**
- **Lien marking – FD, NOC & Lien confirmation**
- **Special Documentation for Consortium/ Multiple Banking advances**
- **No Blank /Partly filled documents to be kept.**

Disbursement

- **Client Master in CBS Properly recorded.**
- **Verify that Disbursement done only after compliance of all terms and conditions of Sanction.**
- **Acceptance of the borrower confirming the terms & conditions of sanction is obtained.**
- **Home Loans/term loans to be disbursed directly to the Builder / Owner/supplier.**
- **Post Disbursement Inspection.**

Monitoring of End Use of Funds

GENERAL NON-COMPLAINTS OBSERVED IN DISBURSEMENT

- I. Promoters contribution not brought in.
- II. Guarantors net worth not furnished.
- III. Unit not inspected.
- IV. Borrower instructed to close other bank accounts. But the same is not complied with.
- V. Security not created e.g. Equitable mortgage of immovable property
- VI. End use of the loan not verified.
- VII. Share application money – not converted to share capital.
- VIII. Confidential reports of other banks not obtained before disbursement.
- IX. In case of takeover of limits from other banks, pay order should be made in favour of the said bank and no-due certificate obtained. Also , loan documents should be obtained from that bank on timely basis.
- X. Advances given to a group in excess to RBI norms during the year.

Review / Monitoring

- **In case of short review/ Technical review, check the application from party**
- **Review / Renewal of facilities carried out as per the policy of the bank.**
- **Verify Follow up of accounts pending renewal.**
- **Stock Inspection reports.**
- **Regular submission of stocks / book debts statements and calculation of correct D.P.**
- **Stock/debts statements and other periodic operational data and financial statements, etc. received regularly from borrowers and duly scrutinized.**

- **Important registers – Discretionary power, insurance, limitation, security verification.**
- **Scrutiny of Exceptional Transactions**
- **End use of Funds (Specially in new accounts of cash credit)**
- **Penal interest to be charged if,**
- **Credit Discipline - Timely adjustment of adhoc limits / Servicing of Interest.**
- **Monthly turnover to commensurate with Annual Projection.**
- **Credit Turnover in the account to match with sales (stock statement)**
- **Monitoring of sub limits in other branch**

- **Consortium meetings: Read Minutes & exchange of Information between the Banks**
- **Management explanation of unusual items / large transactions**
- **Over limit - TOD**
- **Any comment by inspectors/auditors**
- **Insufficient security**
- **Correct feeding of interest rates in the system**
- **Scrutiny of QIS- Regularity in submission, Achievement of performance vis-à-vis Projection, Reasons for Variance.**
- **Diversion of funds /operation in Account**
- **Frequent devolvment of l/c or invocation of bank guarantee.**

Drawing Power Calculation

- **Based on Stocks, Debtors and Share value- Critical review of stock / Book Debts statements**
- **Stock & Debtors - sister/ associate concern**
- **DP limits to be set as per latest statements. If stock statements is older than 3 months accounts to be classified as “irregular”**
- **Verify banks guidelines for DP calculation specially for unpaid stocks**
- **Inventory & equity shares valuation important in the current scenario**
- **Verify Stock audit report for NPA's more than Rs. 1.00 Crore**

Stock Statements / Unit Visit

- **Regularity in submission of statements.**
- **Slow/non moving/ obsolete stock to be deducted for D.P.**
- **Unpaid Stock / Stock under Usance L/C to be declared separately and deducted for D.P. calculation.**
- **Age of the book debts. Certification from a C.A.**
- **Value of stock / Book Debts as on 31st March**
- **Physical Inspection of Securities...**
- **Periodic Inspections of Stocks - Deficiencies/Irregularities**
- **Consortium Account - inspection reports exchanged.**

Term Loan

- **End-use of funds (direct payment/third party verification)**
- **Disbursement by way of DD/PO/Cheques directly in favour of Suppliers**
- **Disbursement by way of reimbursement and after meeting all sanction terms.**
- **Disbursement strictly as per project implementation.**
- **Repayment schedule to be as per the sanction and verify record of repayment**
- **Stipulated installments/interests are being paid regularly**

IMPORTANT OBSERVATIONS IN CASH CREDIT ACCOUNTS

- Whether turnover in then account is adequate compared to the turnover of business .
- Whether cash withdrawals are excessive compared to business needs.
- Whether cash withdrawn immediately after sanction.
- Where cheque payments are not substantial whether stock is fully paid for.
- Whether inter transfer of funds between associate concerns are observed.
- Whether term loans have been given by crediting the same to cash credit account.
- Whether diversion of funds for purchasing fixed assets noted.
- Whether payment of loan installments to other banks or institution or private parties observed.
- Whether payment to parties unrelated to business observed.
- Whether frequent bouncing of cheques deposited as well as issued noted.
- Whether cash deposits sufficient to clear cheques to clear issued noted.
- Whether irregular or infrequent credits observed.
- Whether last months transaction include discounting of cheques of sister concerns.
- Whether there are few credits in the last month and cheques deposited at the end of the year bounced in the subsequent year.

FREQUENTLY ASKED QUESTIONS

- **Impact of stamp duty when registered office of the borrower is different from the state where loan documents are executed?**
- **What to do when annual closing guidelines differ from accounting standards and statutory guidelines?**
- **What to do when borrower having current accounts other than cash credit accounts?**
- **Whether insurance upto the cash credit limit or of actual stock as per stock statement?**

OLD FILES

(Documents to be verified)

- Letter of Acknowledgement of debt and securities (LAD or ADS)
- Balance Confirmation Certificate
- Latest valuation reports (atleast once in 3 years)
- Insurance policies are in force
- Regular Visits/inspection reports by branch official/concurrent auditor.

VERIFICATION FOR RESPECTFUL TREATMENT

Notice of Intimation with registrar

Noting with CERSAI (Central Registry)

- **Charge with ROC is noted**
- **Mutation in Akhiv Patra 7/12 to be noted**
- **Charge with RTO is to be noted**
- **Latest tax receipt must be obtained**
- **Documents obtained shall be kept as per the instruction of search report**
- **Lien on FDR is duly noted**
- **Certified book-debt statement shall be obtained (atleast quarterly)**

- **All NOC's and licenses as mentioned in search reports & sanction letters must be obtained before disbursement e.g.**
 - **NOC for sale/mortgage (specially in case of lease expired property)**
 - **Udyog Adhar of SSI Unit**
 - **Permanent Gumasta**
 - **Consent to establish before term loan**
 - **Consent to operate before cash credit**
 - **MSEB connection before release of cash credit with the requisite**

HP

- **Registration of partnership firm is a must**
- **Sanction Map of NIT specially underdeveloped Industrial Areas**
- **Confidential report of all banker's lying in financial statement of borrower**
- **CIBIL of borrowers and guarantors**
- **Special care while take over proposals (specially in accounts which has been sanctioned to borrower of other bank)**
- **CGTSME Funding (Fees Paid)**
- **Insurance of all primary and collateral securities**

VERIFICATION FOR SPECIAL TREATMENT

- Debtors/Stock statement at 31st march shall be tallied with the balance sheet
- Critical analysis of stock statement and its compilation with bank statement
- Verification of original documents in ultra-violet rays(Housing Loan)
- Disbursement directly to the third party in case of term loan
- C/C devolvement A/c shall not be separate. It must be debited to cash credit account only.
- Unit visit of potential NPA Accounts
- Sanction of loan to group concerns

INCOME RECOGNITION

(Based on Record of Recovery)

ASSETS CLASSIFICATION

(Objective Criteria rather than security basis)

PROVISIONING PERTAINING TO ADVANCES

(On the basis of period for which assets remain NPA and availability of security
and the realizable value of security)

DOCUMENTS TO BE ANALYSED BEFORE CLASSIFICATION

1. Quarterly returns/statement of overdrawn & potential NPA A/C for the third Quarter (December).
2. 12 Months Concurrent Audit Report.
3. Internal Audit Report by Bank's Staff
4. Stock statements pending since last 6 months.
5. Pending Renewals since 2nd Quarter.
6. Preceding years NPA Chart (A/C - wise).
7. Preceding years MOC statement.
8. Statement of upgraded NPA (A/C – wise).
9. WCTL sanctioned during the year.

NON PERFORMING ASSET

An asset, including a leased asset, becomes non performing when it ceases to generate income for the bank.

- Term loans.
- Cash credit / overdrafts.
- Bills purchased/discounted.
- Short duration crops.
- Long duration crops.
- Accounts with temporary deficiencies.
- Restructured Accounts.

NON PERFORMING ASSETS

TYPE OF FACILITY TO BE CLASSIFIED AS NPA IF

- TERM LOAN

Interest and/ or installment of principal remain overdue for a period of more than 90 days in respect of a term loan.

DEFINITION OF OVERDUE :

“An amount due to the bank under any credit facility is overdue if it is not paid on the date fixed by the bank”

TYPE OF FACILITY

TO BE CLASSIFIED AS NPA IF

- CASH CREDIT/
OVERDRAFTS

The account remains 'out of order' continuously for 90 days.

CASE - 1

An account should be treated as 'out of order' if the outstanding balance remains continuously in excess of the sanctioned limit/drawing power.

CASE - 2

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 90 days as on the date of Balance Sheet.

CASE - 3

Or the credits are not enough to cover the interest debited during the same period, these accounts should be treated as 'out of order'.

TYPE OF FACILITY

TO BE CLASSIFIED AS NPA IF

- BILLS PURCHASED / DISCOUNTED

The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

- AGRICULTURAL ADVANCES
(SHORT DURATION CROPS)

The installment of principal or interest thereon remains overdue for two crop seasons.

“long duration” crops would be crops with crop season longer than one year and crops, which are not “long duration” crops, would be treated as “short duration” crops. The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers’ Committee in each State. Depending upon the duration of crops raised by an agriculturist.

TYPE OF FACILITY

(LONG DURATION CROPS)

(NATURAL CALAMITIES)

TO BE CLASSIFIED AS NPA IF

The installment of principal or interest thereon remains overdue for one crop season.

- ✓ Other than Crop loans, all agricultural advances are to be classified as per Term loans and / or Cash credit.

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-scheduling of the repayment period subject to guidelines contained in the RBI circular.

TYPE OF
FACILITY

*(DERIVATIVE
TRANSACTION)*

(CREDIT CARD)

TO BE CLASSIFIED AS NPA
IF

The overdue Receivables representing positive mark to market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

Credit card accounts are as classified as non- performing if the minimum amount paid not fully paid within 90 days of the payment due date mentioned in the credit card statement

TYPE OF FACILITY

TO BE CLASSIFIED AS NPA IF

- ACCOUNTS WITH TEMPORARY DEFICIENCIES

The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular. The account will become NPA if such irregular drawings are permitted in the account for a continuous period of 90 days even though the unit may be working or the borrower's financial position is satisfactory.

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.

A few credits are recorded before the balance sheet date should be handled with care and without scope for subjectivity.

SPECIFIC GUIDELINES FOR ASSETS CLASSIFICATIONS

- ✓ What are the NPA Norms for:
 1. Government guaranteed advances.
 2. Loans against TDR/LIC policies/NSC, etc.
 3. Loan against Gold / Jewel loans /Government securities.
 4. When assets regularized just before the balance sheet date.
 5. Loans with Moratorium period for payment of interest.
 6. Loans to staff, when interest is payable after recovery of principal.
 7. Loan under Consortium Funding.
 8. When Letter of Credits devolved or Bank Guarantee invoked.

POINTS TO BE CONSIDERED WHILE CLASSIFYING ADVANCES

1. Whether classification shall be made Borrower-wise/ Facilities-wise ?
State the exception to it, if any ?
2. What is the impact of availability of security/ Net Worth of the Borrower on the classification of advances ?
3. Whether NPA accounts can be upgraded ?
4. What is the practice for Appropriation of recovery in NPAs ?

INCOME RECOGNITION

- ❑ Income recognition based on record of recovery.
- ❑ Income from NPA is not recognized on accrual basis.
- ❑ Booked as income only when it is actually received.
- ❑ However, interest on advances against Term deposits, NSCs, IVPs, KVPs, Life policies may be accounted as income on the due date, provided adequate margin is available.
- ❑ Fees and commission, as a result of re-negotiations or re-scheduling of out standing debts : recognized on an accrual basis over the period of time covered by the re-negotiations or re-scheduled extension of credit.
- ❑ If Government guaranteed advances become NPA : Interest should not be accounted, unless it has been realized.

REVERSAL OF INCOME

- ❖ For Advances that become NPA : The interest accrued and credited in the past periods, should be reversed if the same is not realized.
- ✓ *This will apply to government guaranteed advances also.*
- ❖ Fees, Commission and similar Income should cease to accrue in the current period and should be reversed with respect to past periods, if collected.

CLASSIFICATION OF ASSETS

- STANDARD ASSETS
- SUB STANDARD ASSETS.
- DOUBTFUL ASSETS.
- LOSS ASSETS.

SUBSTANDARD ASSETS

A substandard asset would be one, which has remained NPA for a period **LESS THAN OR EQUAL TO 12 MONTHS**.

Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and there is a possibility that the bank will sustain some losses, if the deficiencies are not corrected.

DOUBTFUL ASSETS

With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the **SUBSTANDARD CATEGORY FOR A PERIOD OF 12 MONTHS.**

For provisioning, doubtful assets are further classified as per age in doubtful category, in sub-categories generally called as

D-1, D-2 and D-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.

- ✓ *In cases of serious credit impairment (i.e. accounts where there is erosion in the value of security/frauds committed by the borrower) the assets should be straight away classified as doubtful or loss assets as appropriate:*

VALUE

CLASSIFICATION TO BE DONE

LESS THAN 50%

DOUBTFUL ASSET

LESS THAN 10%

LOSS ASSET - FULL PROVISION

PROVISIONS – STANDARD ASSETS

- a) Direct advances to agricultural and Small and Micro Enterprises (SMEs) sectors at 0.25 per cent.
 - b) Advances to Commercial Real Estate (CRE) Sector at 1.00 per cent
 - c) advances to Commercial Real Estate – Residential Housing Sector (CRE - RH) at 0.75 per cent.
 - d) housing loans extended at teaser rates and restructured advances as 2.0
 - e) all other loans and advances not included in (a) (b) and (c) above at 0.40 per cent.
- ✓ *Separate provision norms for accounts covered under Project Finance.*

PROVISIONS – SUB STANDARD ASSETS

- a) A general provision of 15% on total outstanding should be made without making any allowance for ECGC guarantee cover and securities available.
 - b) The 'unsecured exposures' which are identified as 'substandard' would attract additional provision of 10% , i.e., a total of 25% on the outstanding balance.
- ✓ *Unsecured exposure is defined as an exposure where the realizable value of the security, as assessed by the bank/approved valuers/Reserve Bank's inspecting officers, is not more than 10 percent, ab-initio, of the outstanding exposure.*

PROVISIONS – DOUBTFUL ASSETS

- ✓ 100% 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 realizable value is estimated on a realistic basis(i.e. UNSECURED PORTION)

Where security is available (i.e. UNSECURED PORTION) :

⌘ Up to one year	-	25%
⌘ One to three years	-	40%
⌘ More than three years	-	100%

PROVISIONS – LOSS ASSETS

- LOSS ASSETS SHOULD BE WRITTEN Off.

If loss assets are permitted to remain in the books for any reason,

100% of the outstanding should be provided for.

- What are the norms for valuation of securities for provisioning purposes ?

ADVANCES COVERED BY ECGC GUARANTEE

- In the case of advances classified as doubtful and guaranteed by ECGC, provision should be made only for the balance in excess of the amount guaranteed by the Corporation.
- For the provision required to be made for doubtful assets, realizable value of the securities should first be deducted from the outstanding balance in respect of the amount guaranteed by the Corporation and then provision made as illustrated hereunder:

Outstanding Balance : Rs. 4 lakhs

ECGC Cover : 50%

Period for which the advance has remained doubtful : More than 2 years remained doubtful (say as on March 31, 2014)

Value of security held : Rs. 1.50 lakhs

PROVISION REQUIRED TO BE MADE

Outstanding balance	Rs. 4.00 lakhs
<u>Less:</u> Value of security held	Rs. 1.50 lakhs
Unrealized balance	Rs. 2.50 lakhs
<u>Less:</u> ECGC Cover	Rs. 1.25 lakhs
(50% of unrealizable balance)	
<i>Net unsecured balance</i>	<i>Rs. 1.25 lakhs</i>
Provision for unsecured portion of advance	Rs. 1.25 lakhs (@ 100 percent of unsecured portion)
Provision for secured portion of advance (as on March 31, 2012)	Rs.0.60 lakhs (@ 40 per cent of the secured portion)
	<i>Rs.1.85 lakhs (as on March 31,</i>

Advance covered by guarantees of Credit Guarantee Fund Trust For Micro And Small Enterprises (CGTMSE) or Credit Risk Guarantee Fund Trust for Low Income Housing (CRGFTLIH)

- ⌘ In case the advance covered by CGTMSE or CRGFTLIH guarantee becomes nonperforming, 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 assets.

- *An illustrative example is given below:*

Outstanding Balance:	Rs. 10 lakhs
CGTMSE/CRGFTLIH Cover:	75% of the amount outstanding or 75% of the unsecured amount or Rs.37.50 lakh, whichever is the least
Period for which the advance : has remained doubtful	More than 2 years remained doubtful (say as on March 31, 2014)
Value of security held:	Rs. 1.50 lakhs

Balance outstanding	Rs.10.00 lakh
<u>Less:</u> Value of security	Rs. 1.50 lakh
Unsecured amount	Rs. 8.50 lakh
<u>Less:</u> CGTMSE/CRGFTLIH cover (75%)	Rs. 6.38 lakh
<i>Net unsecured and uncovered portion:</i>	<i>Rs. 2.12 lakh</i>
Provision for Secured portion @ 40% of Rs.1.50 lakh	Rs.0.60 lakh
Provision for Unsecured & uncovered portion @ 100% of Rs.2.12 lakh	Rs.2.12 lakh
<i>Total provision required</i>	<i>Rs.2.72 lakh</i>

Certain Clues For Finding NPA

- **Statements>Returns of Potential NPA's in December quarter.**
- **A/c's Overdue for Renewal for more than 180 days.**
- **Stock Statements not submitted since last 6 months.**
- **Other regular loans Sanctioned to clear irregular accounts.**
- **WCTL(Working Capital Term Loan) sanctioned to same NPA accounts.**
- **Year end deposit in irregular account**
- **irregular account is regularized by purchasing cheque etc.**

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