NPA –ASSETS CLASSIFICATION & INCOME RECOGNITION

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Objectives

- The R B I. introduced the NPA norms relying on the Narsimham Committee recommendations & prudential norms for Income Recognition, Asset Classification and provisioning for the advance portfolio of the banks with the intention for proper disclosure of profit & loss and reflect the financial health of bank.
- The classification of assets has to be done on the basis of objective criteria and based on record of recovery rather than on any subjective considerations.
- The provisioning should be made on the basis of classification of assets based on the period for which the assets has remained non performing and the availability of security and the realisable value thereof.

Non Performing Asset Identification

An asset becomes non-performing when it ceases to generate income for the bank & or becomes non-productive assets & it can be broadly classified as given below.

Type of loan	Identification
Term Loan	Account is treated Interest and/ or instalment remains over due for a period of more than 90 days.
Cash Credit & Overdraft accounts	Account is treated as NPA if it remains out of order for a period of more than 90 days. An account is treated as out of order if, •The outstanding balance remains continuously in excess of sanctioned/drawing power limit or •Though the outstanding balance is less than the sanctioned limit/drawing power. •There are no credits continuously for more than 90 days in the account i.e. the account is non-operative. •The credits during the aforesaid period in accounts are not sufficient to cover the interest debited during the same period.

Non Performing Asset Identification

Type of loan	Identification
Bill Purchased/ Discounted	Bill remains over due for a Discounted period of more than 90 days.
Agricultural Advances	• In case of Short duration crops, the installment of principle or interest thereon remains overdue for two crop seasons • In case of long duration crops, the installment of principle or interest thereon remains overdue for one crop season.
Liquidity facility	Remains outstanding for more than 90 days in respect of securitization transaction.
Derivative Transactions	Overdue receivables representing positive mark to market value of a derivative contract remaining unpaid for a period of 90 days from specified due date.

An account is classified as NPA only if interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter

Asset Classification

After identification NPA assets are classified into four categories in view of their status as NPA, availability of security and factors affecting the recovery of their dues. On the basis of said classification provisions are to be made.

i) **Standard assets: -**

These are assets which are regular in paying interest/installment & its operations are normal.

ii) **Sub-standard assets: -**

If the loan is NPA upto 12 months the same is called Sub Standard Assets.

Asset Classification

iii) **Doubtful assets: -**

If an asset is a sub-standard asset for a period exceeding 12 months, it should be classified as doubtful asset. The said doubtful assets are further classified age-wise i.e. doubtful assets upto 1 year, 1to 3 years & over three years respectively.

Doubtful Assets upto	**NPA**
1 year	Of twenty four months
1 to 3 years	Over twenty four month & upto forty eight month
3 years & above	Above forty eight months.

iv) **Loss Assets :-**

An asset identified by Bank or by internal/external auditor/RBI as loss assets with a little salvage value.

Asset Classification

v) In respect of accounts where there are potential threats to recovery because of erosion in value of Security or fraud by borrower, such accounts should directly be classified as doubtful/ loss irrespective of period for which is remained as NPA.

vi) Upgradation of Accounts

- Reschedule of recovery cannot give the advance a better classification than the previous one.
- NPA accounts can be upgraded to Performing Accounts, provided all overdues are adjusted or atleast reduced to a period of less than 90 days.
- Upgradation within the NPA category is not permitted i.e. Doubtful account cannot be made substandard even if the overdues are reduced to less than 18 months.

Notes To Be Considered for calculation of NPA

- Accounts should not be classified as NPA merely due to existence of some deficiencies of temporary nature such as non-availability of adequate drawing power, balance outstanding exceeding the limit, non submission of stock statements (Stock statement older than 90 days temporary deficiency & becomes NPA on 90 days thereafter) subject to overall performance of conduct is satisfactory.

- An account where the regular/Adhoc credit limits has not been reviewed/renewed within 90 days from the due date/date of ad-hoc sanction will be treated as NPA.

- The accounts are regularised before Balance Sheet date by repaying overdues through genuine sources ***(Not by sanction of additional facilities or transfer of funds between accounts)*** then these accounts need not be treated as N.P.A. However, such classification should be handled with due care and without any subjectivity.

NPA – Asset Classification & Income Recognition

- In case of consortium advances – classification be done on the recoverability of advance in the books of account of the individual member bank. Bank needs to arrange to get their share of recovery or obtain an express consent from the Lead Bank.

- Asset Classification to be borrower-wise and not facility-wise
  - If one facility of borrower is NPA, all the facilities of that borrower are to be treated as NPA under the same category of classification. It may be noted that if a borrower has cash credit & term loan and if one becomes NPA, both these facilities will have to be treated as NPA and classified either as substandard/doubtful/as the case of first NPA facility.

- Credit facility backed by Central Government guarantee though overdue may be treated as NPA only when the Govt. repudiates its guarantee when invoked.

NPA – Asset Classification & Income Recognition

- Advances against Gold Ornaments, Shares, other Govt. Securities and other securities not exempt from provisioning norms.
- Staff loans should not be treated NPA unless problematic cases.
- Loans against Banks Fixed Deposits, NSC's, LIC, UTI, Indira Vikas Patra, LIC Policies are of self liquidating nature and where outstanding are within the maturity value not treated as NPAs.
- The restructured substandard account would be eligible to be upgraded to the standard category only after one year after the date when the first payment of interest or of principal, whichever is earlier fails due subject to satisfactory performance during the period.

NPA – Asset Classification & Income Recognition

- In case where after restructuring the performance is not as per revised repayment schedule for one year, then the account will be downgraded / classified as per original repayment schedule.

    - In case of accounts where there is erosion in the value of security or fraud has been committed by borrower, the same should be straightaway be classified as doubtful or loss; specifically-

- where value of security has eroded by more than 50%, account should be classified as 'doubtful' and
- where realisable value of security is less than 10% of the outstanding amount, the existence of security should be ignored and the account should be classified as 'loss'.

Provisioning Norms

The provisions should be made on the basis of classification of assets into four different categories as stated above i.e. standard, substandard, doubtful & loss assets.

	Category	Period	NPA	Provisioning
A.	Standard	-	Non NPA	0.25%,1%, 2% & 0.40% on gross amount in phased manner as shown in Note 1 hereunder
B	Sub-standard	-	NPA upto 12 months	Secured Exposure - 15 % Unsecured Exposure – 25% Unsecured exposure in respect of Infrastructure loan - 20%

Provisioning Norms

	Category	Period	NPA	Provisioning
C	Doubtful	Upto One year	NPA upto 24 months	100% on unsecured portion & 25% on realizable value of Assets.
		One to Three years	NPA upto 48 months	100% on unsecured portion & 40% on realizable value of assets.
		Over three years	NPA above 48 months	100 %
D.	Loss	-	-	100%

Provisioning Norms

1. **Provision in respect of Standard Advances**
   a. 0.25% of gross amount for advances to agricultural and SME sectors.
   b. 1% of advances to Commercial Real Estate (CRE)
   c. 2% of advances to Housing loan at teaser rates. However after 1 year from the date on which the rates are reset at higher rates, the provision should be 0.40%
   d. 2% in case of Restructuring accounts classified as Standard advances
   e. 0.40% of gross account for advances other than (a), (b), (c) & (d).

2. Realisable Value of Security shall be include Principal Security, Collateral Security, DIGCC/CGS Claim, Sundry Credits, Net Worth of Borrower and Guarantors, Deposits as per court order and Value of attached assets as per Court Order.

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NPA – Asset Classification & Income Recognition

3. For all NPA accounts provisioning should be made on amounts outstanding less amount of interest/other charges debited not recovered by the year end.

4. The country based risk provision ranging from 0.25 % to 100 % to be made.

5. A bank may voluntarily make specific provisions for advances at rates which are higher than the rates prescribed under existing regulations, to provide for estimated actual loss in collectable amount, provided such higher rate are approved by Board of Directors

6. The amount of liquidity facility drawn and outstanding for more than 90 days, in respect of securitization transactions, should be fully provided for.

7. In respect of NPA balance of Rs.5 crores & above, bank needs to formulate policy for annual stock audit by external agencies & in respect of immovable properties, valuation to be carried once in 3 years by approved value.

Provisioning Coverage Ratio

- Provisioning Coverage Ratio (PCR) is the ratio of provisioning to gross non-performing assets and indicates the extent of funds a bank has kept aside to cover loan losses.

- Banks should have total provisioning coverage ratio of not less than 70%.

- The surplus provision under PCR vis-à-vis as required as per norms should be segregated into an account styled as “countercyclical provisioning buffer”. The buffer will be allowed to be used by banks for making specific provisions for NPAs during periods of system wide downturn, with the prior approval of RBI

Income Recognition

- Banks should not charge and take to income accounts interest accrued on non-performing assets. Income from non performing assets is not recognized on accrual basis but is booked as income only when it is actually received.

- Interest on advance against Term deposits, NSC, Indira & Kisan Vikas Patra & LIC may be taken to income subject to availability of Margin.

- In the absence of clear agreement between the Bank and the Borrower, an appropriate policy to be followed in uniform and consistent manner.

Income Recognition

- On an account turning NPA, banks should reverse the interest already charged and not collected by debiting Profit and Loss account, and stop further application of interest. However, banks may continue to record such accrued interest in a Memorandum account in their books. For the purpose of computing Gross Advances, interest recorded in the Memorandum account should not be taken into account.

THANK YOU

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