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July 1, 2009

The Chief Executive Officers of
All Primary (Urban) Co-operative Banks

Dear Sir / Madam,

**Master Circular on Income Recognition, Asset
Classification, Provisioning & Other Related Matters - UCBs**

Please refer to our Master Circular [UBD.PCB.MC.No. 3 / 09.14.000 / 2008-09 dated July 1, 2008](#) on the captioned subject. The enclosed Master Circular consolidates and updates all the instructions / guidelines issued on the subject up to June 30, 2009.

Yours faithfully,

(A.K Khound)
Chief General Manager-in-Charge

Encl: As above.

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बैंक हिन्दी में पत्राचार का स्वागत करता है ।

Master Circular on Income Recognition, Asset Classification, Provisioning & Other Related Matters-

Contents

1.	GENERAL	4
2.	NON-PERFORMANCE ASSETS (NPA) ..	4
2.1	Classification of assets as Non-Performing ..	4
2.2	Treatment of Accounts as NPAs ..	7
2.2.1	Record of Recovery ..	7
2.2.2	Treatment of NPAs – Borrower – wise and not Facility-wise	8
2.2.3	Agricultural Advances ..	8
2.2.4	Housing Loans to staff	8
2.2.5	Credit Facilities backed by Guarantees by Government of India/ State Governments ..	8
2.2.6	Project Financing ..	9
2.2.7	Prudential Guidelines on Restructuring of Advances ...	9
2.2.8	Other Advances ..	15
2.2.9	Recognition of Income on Investment treated as NPA	15
2.2.10	NPA Reporting to Reserve Bank..	15
3.	ASSET CLASSIFICATION	16
3.1	Classification ..	16
3.2	Definitions..	17
3.3	Guidelines for Classification of Assets ..	17
3.3.1	Basic Considerations ..	17
3.3.2	Advances Granted under Rehabilitation Packages Approved by BIFR/Term Lending Institutions ..	17
3.3.3	Internal System for Classification of Assets as NPAs	18
4.	INCOME RECOGNITION	18
4.1	Income Recognition – Policy ..	18
4.2	Reversal of Income on Accounts Becoming NPAs ..	19
4.3	Booking of Income on Investments in Shares & Bonds	19
4.4	Partial Recovery of NPAs ..	19
4.5	Interest Application ..	20
5.	PROVISIONING NORMS	21
5.1	Norms for provisioning on Loans & Advances ..	21
5.2	Provisioning for retirement benefits ..	24
5.3	Provisioning norms for sale of assets to SC/ RC ..	24
5.4	Guidelines for provisions in specific cases ..	24
6.	Divergence in asset classification & provisioning due to non compliance with RBI guidelines	26
	Annex 1: Direct Finance to Farmers for Agricultural Purposes..	27
	Annex 2: Proforma ..	28
	Annex 3: Illustrative Accounting Entries to be passed in respect of Accrued Interest on both the Performing and NPAs...	30
	Annex 4: Deviations in extant Prudential Norms-to Tier I and Tier II banks	32
	Annex 5: Illustrative entries on the provisioning requirement for secured portion of assets that are doubtful for more than three years	34
	Annex 6: Clarification on certain frequently asked questions..	35
	Annex 7: Prudential guidelines on restructuring – key concepts	38
	Annex 8: Prudential guidelines on restructuring – Report format	40
	Annex 9: Prudential guidelines on restructuring – Illustrations	41
Appendix	43

1. GENERAL

- 1.1 In order to reflect a bank's actual financial health in its balance sheet and as per the recommendations made by the Committee on Financial System (Chairman Shri M. Narasimham), the Reserve Bank has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks.
- 1.2 Broadly, 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. The provisioning should be made on the basis of the classification of assets into different categories.
- 1.3 The requirements of the State Co-operative Societies Acts and / or rules made thereunder or other statutory enactments may continue to be followed, if they are more stringent than those prescribed hereby.
- 1.4 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. also ceased to be a supervisory requirement, but could be continued in the banks entirely at their discretion and the management policy, if felt necessary.

2. NON-PERFORMING ASSETS (NPA)

2.1 Classification of Assets as Non-Performing

- 2.1.1 An asset becomes non-performing when it ceases to generate income for the bank. Earlier an asset was considered as non-performing asset (NPA) based on the concept of '**Past Due**'. A 'non performing asset' (NPA) was defined as credit in respect of which interest and/ or installment of principal has remained 'past due' for a specific period of time. The specific period was reduced in a phased manner as under:

Year ended March, 31 -----	Specific period -----
1993	4 quarters
1994	3 quarters
1995	2 quarters

An amount is considered as past due, when it remains outstanding for 30 days beyond the due date. However, with effect from March 31, 2001 the 'past due' concept has been dispensed with and the period is reckoned from the due date of payment.

2.1.2 With a view to moving towards international best practices and to ensure greater transparency, '90 days' **overdue*** norms for identification of NPAs have been made applicable from the year ended March 31, 2004. As such, with effect from March 31, 2004, a non-performing asset shall be a loan or an advance where:

- (i) Interest and/or installment 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,
- (iv) In the case of direct agricultural advances as listed in Annex 1, the overdue norm specified at para 2.1.5 would be applicable. In respect of agricultural loans, other than those specified in Annex 1, identification of NPAs would be done on the same basis as non-agricultural advances.
- (v) Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

** Any amount due to the bank under any credit facility, if not paid by the due date fixed by the bank becomes **overdue**.*

*@ "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 90 days or credits are not enough to cover the interest debited during the same period, these accounts should be treated as '**out of order**'".*

2.1.3 **Tier I Banks** (for definition please see annex 4) were permitted to classify loan accounts including gold loans and small loan upto Rs 1 lakh as NPAs based on 180 days delinquency norm instead of the extant 90 days norm. This relaxation was in force upto March 31, 2009. For the above category of banks, an account would be classified as Non Performing Asset if the :

- (i) Interest and/or installment 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) Any amount to be received remains overdue for a period of more than 180 days in respect of other accounts.

The relaxations were given for the explicit purpose of enabling the UCBs concerned to transit to the 90 day NPA norm in the year 2009-10 by building up adequate provisions and strengthening their appraisal, disbursement and post disbursement procedures.

- 2.1.4 **Tier II banks** shall classify their loan accounts as NPA as per 90 day norm as hitherto.

Note : A comparative analysis of the prudential norms as applicable for Tier I and Tier II banks are given in the Annex 4.

2.1.5 **Agricultural Advance:**

- (i) With effect from September 30, 2004 the following revised norms are applicable to all direct agricultural advances (Annex 1):
 - a) A loan granted for short duration crops will be treated as NPA, if the installment of principal or interest thereon remains overdue for two crop seasons.
 - b) A loan granted for long duration crops will be treated as NPA, if the installment of principal or interest thereon remains overdue for one crop season.
- (ii) For the purpose of these guidelines, "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.
- (iii) 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.
- (iv) Depending upon the duration of crops raised by an agriculturist, the above NPA norms would also be made applicable to agricultural term loans availed of by him. In respect of agricultural loans, other than those specified in the Annex 1 and term loans given to non-agriculturists, identification of NPAs would be done on the same basis as non-agricultural advances, which, at present, is the 90 days delinquency norm.
- (v) Banks should ensure that while granting loans and advances, realistic repayment schedules are fixed on the basis of cash flows / fluidity with the borrowers.

2.1.6 **Identification of assets as NPAs should be done on an ongoing basis**

The system should ensure that identification of NPAs is done on an on-going basis and 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 prescribed norms. Banks should also make provisions for NPAs as at the end of each calendar quarter i.e as at the end of

March/ June/ September/ December, so that the income and expenditure account for the respective quarters as well as the P&L account and balance sheet for the year end reflects the provision made for NPAs.

2.1.7 Charging of interest at monthly rests

- (i) Banks should charge interest at monthly rests in the context of adoption of 90 days norm for recognition of loan impairment w.e.f. from the year ended March 31, 2004 and consequential need for close monitoring of borrowers' accounts. However, the date of classification of an advance as NPA as stated in preceding paras, should not be changed on account of charging of interest at monthly basis.
- (ii) The existing practice of charging /compounding of interest on agricultural advances would be linked to crop seasons and the instructions regarding charging of interest on monthly rests shall not be applicable to agricultural advances.
- (iii) While compounding interest at monthly rests effective from April 1, 2003, banks should ensure that in respect of advances where administered interest rates are applicable, they should re-align the rates suitably keeping in view the minimum lending rate charged by the bank (in view of the freedom given to them for fixing lending rates) so that they comply with the same. In all other cases also, banks should ensure that the effective rate does not go up merely on account of the switchover to the system of charging interest on monthly rests.
- (iv) Banks should take into consideration due date/s fixed on the basis of fluidity with borrowers and harvesting/ marketing season while charging interest and compound the same if the loan/ installment becomes overdue in respect of short duration crops and allied agricultural activities.

2.2 Treatment of Accounts as NPAs

2.2.1 Record of Recovery

- (i) The treatment of an asset as NPA should be based on the record of recovery. Banks should not treat an advance as NPA merely due to existence of some deficiencies which are of temporary in nature such as non-availability of adequate drawing power, balance outstanding exceeding the limit, non-submission of stock statements and the non-renewal of the limits on the due date, etc. Where there is a threat of loss, or the recoverability of the advances is in doubt, the asset should be treated as NPA.
- (ii) A credit facility should be treated as NPA as per norms given in paragraph 2.1 above. However, where the accounts of the

borrowers have been regularised by repayment of overdue amounts through genuine sources (not by sanction of additional facilities or transfer of funds between accounts), the accounts need not be treated as NPAs. In such cases, it should, however, be ensured that the accounts remain in order subsequently and a solitary credit entry made in an account on or before the balance sheet date which extinguishes the overdue amount of interest or installment of principal is not reckoned as the sole criteria for treatment the account as a standard asset.

2.2.2 Treatment of NPAs – Borrower-wise and not Facility-wise

- (i) In respect of a borrower having more than one facility with a bank, all the facilities granted by the bank will have to be treated as NPA and not the particular facility or part thereof which has become irregular.
- (ii) However, in respect of consortium advances or financing under multiple banking arrangements, each bank may classify the borrowal accounts according to its own record of recovery and other aspects having a bearing on the recoverability of the advances.

2.2.3 Agricultural Advances – Default in repayment due to natural calamities

- (i) Where natural calamities impair the repaying capacity of agricultural borrowers, as a relief measure, banks may decide on their own to:
 - (a) convert the short-term production loan into a term loan or re-schedule the repayment period, and
 - (b) sanction fresh short-term loans
- (ii) 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 non performing asset (NPA). The asset classification of these loans would, therefore, be governed by the revised terms and conditions and these would be treated as NPA under the extant norms applicable for classifying agricultural advances as NPAs.

2.2.4 Housing Loan to Staff

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.

2.2.5 Credit facilities Guaranteed by Central /State Government

- (i) The credit facilities backed by guarantee of the Central Government though overdue should not be treated as NPA
- (ii) This exemption from classification of government guaranteed advances as NPA is not for the purpose of recognition of income.
- (iii) From the year ended March 31, 2006, State Government guaranteed advance and investment in State Government guaranteed securities would attract asset classification and provisioning norms, if interest and/or principal or any other amount due to the bank remains overdue for more than 90 days irrespective of the fact whether the guarantee have been invoked or not.

2.2.6 Project Financing

In the case of bank finance given for industrial projects 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.

2.27 Prudential Guidelines on Restructuring of Advances

The prudential guidelines on restructuring of advances are detailed as under:

(a) Asset classification norms

2.2.7.1 Restructuring of advances could take place in the following stages :

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

2.2.7.2 The accounts classified as 'standard assets' should be immediately re-classified as 'sub-standard assets' upon restructuring.

2.2.7.3 The non performing assets, upon restructuring, would slip into further lower asset classification category as per extant asset classification norms with reference to the pre-restructuring repayment schedule.

2.2.7.4 All restructured accounts which have been classified as non-performing assets upon restructuring, would be eligible for up-gradation to the 'standard' category after observation of 'satisfactory performance' during the 'specified period' (Annex-VII).

2.2.7.5 In case, however, satisfactory performance after the specified 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***.

2.2.7.6 Any additional finance may be treated as 'standard asset', up to a period of one year after the first interest / principal payment, whichever is earlier, falls due under the approved restructuring package. However, in the case of accounts where the pre-restructuring facilities were classified as 'sub-standard' and 'doubtful', interest income on the additional finance should be recognised only on cash basis. If the restructured asset does not qualify for upgradation at the end of the above specified one year period, the additional finance shall be placed in the same asset classification category as the restructured debt.

2.2.7.7 In respect of loan accounts which enjoy special regulatory treatment as per para 2.2.7.25, upon restructuring, such non-performing assets would continue to have the same asset classification as prior to restructuring. In case satisfactory performance of the account is not evidenced during the 'specified period', it would slip into further lower asset classification categories as per extant asset classification norms with reference to the ***pre-restructuring repayment schedule***.

2.2.7.8 In case a restructured asset, which is a standard asset on restructuring, is subjected to restructuring on a subsequent occasion, it should be classified as substandard. If the restructured asset is a sub-standard or a doubtful asset and is subjected to restructuring, on a subsequent occasion, its asset classification will be reckoned from the date when it became NPA on the first occasion. However, such advances restructured on second or more occasion may be allowed to be upgraded to standard category after one year from the date of first payment of interest or repayment of principal whichever falls due earlier in terms of the current restructuring package subject to satisfactory performance.

(b) Income recognition norms

2.2.7.9 Subject to provisions of paragraphs 2.2.7.6 and 2.2.7.22 interest income in respect of restructured accounts classified as 'standard assets' will be recognized on accrual basis and that in respect of the account classified as 'non performing assets' will be recognized on cash basis.

(c) Provisioning norms

2.2.7.10. Normal provisions

Banks will hold provision against the restructured advances as per the existing provisioning norms.

2.2.7.11. Provision for diminution in the fair value of restructured Advances

The erosion in the fair value of the advance should be computed as the difference between the fair value of the loan **before** and **after** restructuring. *Fair value of the loan before restructuring* will be computed as the present value of cash flows representing the interest at the existing rate charged on the advance before restructuring and the principal, discounted at a rate equal to the bank's BPLR as on the date of restructuring plus the appropriate term premium and credit risk premium for the borrower category on the date of restructuring". *Fair value of the loan after restructuring* will be computed as the present value of cash flows representing the interest at the rate charged on the advance on restructuring and the principal, discounted at a rate equal to the bank's BPLR as on the date of restructuring plus the appropriate term premium and credit risk premium for the borrower category on the date of restructuring".

2.2.7.12. It may please be noted that the above formula moderates the swing in the diminution of present value of loans with the interest rate cycle and will have to be followed consistently in future. No request for changing the same, particularly for reversion to the present formula, will be entertained in future.

2.2.7.13. Further, it is reiterated that the provisions required as above arise due to the action of the banks resulting in change in contractual terms of the loan upon restructuring which are in the nature of financial concessions. These provisions are distinct from the provisions which are linked to the asset classification of the account classified as NPA and reflect the impairment due to deterioration in the credit quality of the loan. Thus, the two types of the provisions are not substitute for each other.

2.2.7.14. It is also re-emphasised that the modifications effected to the guidelines on restructuring of advances by RBI are aimed at providing an opportunity to banks and borrowers to preserve the economic value of the units and should not be looked at as a means to evergreen the advances.

2.2.7.15 . In their published annual Balance Sheets for the year ending March 2009, in addition to the disclosures regarding restructured loans required in terms of paragraph 9 of the guidelines enclosed to circular dated March 6, 2009, banks should also disclose the amount and number of accounts in respect of which applications for restructuring are under process, but the restructuring packages have not yet been approved.

2.2.7.16 In the case of working capital facilities, the diminution in the fair value of the cash credit / overdraft component may be computed as indicated in para 2.2.7.11 above, reckoning the higher of the

outstanding amount or the limit sanctioned as the principal amount and taking the tenor of the advance as one year. The term premium in the discount factor would be as applicable for one year. The fair value of the term loan components (Working Capital Term Loan and Funded Interest Term Loan) would be computed as per actual cash flows and taking the term premium in the discount factor as applicable for the maturity of the respective term loan components.

2.2.7.17 In the event any security is taken in lieu of the diminution in the fair value of the advance, it should be valued at Re.1/- till maturity of the security. This will ensure that the effect of charging off the economic sacrifice to the Profit & Loss account is not negated.

2.2.7.18 The diminution in the fair value may be re-computed on each balance sheet date till satisfactory completion of all repayment obligations and full repayment of the outstanding in the account, so as to capture the changes in the fair value on account of changes in BPLR, term premium and the credit category of the borrower. Consequently, banks may provide for the shortfall in provision or reverse the amount of excess provision held in the distinct account.

2.2.7.19 If due to lack of expertise / appropriate infrastructure, a bank finds it difficult to ensure computation of diminution in the fair value of advances extended by small branches, as an alternative to the methodology prescribed above for computing the amount of diminution in the fair value, banks will have the option of notionally computing the amount of diminution in the fair value and providing therefor, at five percent of the total exposure, in respect of all restructured accounts where the total dues to bank(s) are less than rupees one crore till the financial year ending March 2011. The position would be reviewed thereafter.

2.2.7.20. The total provisions required against an account (normal provisions plus provisions in lieu of diminution in the fair value of the advance) are capped at 100% of the outstanding debt amount.

(d) Prudential Norms for Conversion of Unpaid Interest into 'Funded Interest Term Loan' (FITL)

2.2.7.21 Asset classification norms

The FITL created by conversion of unpaid interest will be classified in the same asset classification category in which the restructured advance has been classified. Further movement in the asset classification of FITL would also be determined based on the subsequent asset classification of the restructured advance.

2.2.7.22 Income recognition norms

(i) The income, if any, generated may be recognised on accrual basis, if FITL is classified as 'standard', and on cash basis in the cases where the same has been classified as a non-performing asset.

(ii) The unrealised income represented by FITL should have a corresponding credit in an account styled as "Sundry Liabilities Account (Interest Capitalization)".

(iii) Only on repayment in case of FITL, the amount received will be recognized in the P&L Account, while simultaneously reducing the balance in the "Sundry Liabilities Account (Interest Capitalisation)".

(e) Special Regulatory Treatment for Asset Classification

2.2.7.23 The special regulatory treatment for asset classification, in modification to the provisions in this regard stipulated in para 2.2.7.1 to 2.2.7.8, will be available to the borrowers engaged in important business activities, subject to compliance with certain conditions as enumerated in para 2.2.7.29 below. Such treatment is not extended to the following categories of advances :

- (i) Consumer and personal advances including advances to individuals against the securities of shares/bonds/debentures etc
- (ii) Advances to traders

2.2.7.24 The asset classification of the above two categories of accounts as well as that of other accounts which do not comply with the conditions enumerated in para 2.2.7.29, will be governed by the prudential norms in this regard described in para 2.2.7.1 to 2.2.7.8 above.

2.2.7.25 As real estate sector is facing difficulties, it has been decided to extend special regulatory treatment to commercial real estate exposures, which are restructured up to June 30, 2009. Further,

housing loans granted by banks would also be eligible for special regulatory treatment, if restructured.

(f) Elements of special regulatory framework

2.2.7.26 The special regulatory treatment has the following three components :

- (i) Incentive for quick implementation of the restructuring package.
- (ii) Retention of the asset classification of the restructured account in the pre restructuring asset classification category

2.2.7.27 Incentive for quick implementation of the restructuring package

During the pendency of the application for restructuring of the advance with the bank, the usual asset classification norms would continue to apply. The process of reclassification of an asset should not stop merely because the application is under consideration. However, as an incentive for quick implementation of the package, if the approved package is implemented by the bank within 120 days from the date of receipt of application by the bank, the asset classification status may be restored to the position which existed when the restructuring application was received by the bank: Further, all accounts which were standard accounts as on September 1, 2008 would be treated as standard accounts on restructuring provided the restructuring package is put in place within 120 days from the date of taking up the restructuring package. The 120 days norm for quick implementation of the restructuring package would stand reduced to 90 days in respect of all restructuring packages implemented after June 30, 2009.

2.2.7.28 Asset classification benefits

Subject to the compliance with the undernoted conditions in addition to the adherence to the prudential framework laid down in para 2.2.7.1 to 2.2.7.8:

- (i) In modification to para 2.2.7.2, an existing 'standard asset' will not be downgraded to the sub-standard category upon restructuring.

(ii) In modification to para 2.2.7.3 during the specified period, the asset classification of the sub-standard / doubtful accounts will not deteriorate upon restructuring, if satisfactory performance is demonstrated during the specified period.

2.2.7.29 However, these benefits will be available subject to compliance with the following conditions:

i) The dues to the bank are 'fully secured' as defined in Annex VII. The condition of being fully secured by tangible security will not be applicable in the following cases:

a) SSI borrowers, where the outstanding is up to Rs.25 lakh.

(b) infrastructure projects, provided the cash flows generated from these projects are adequate for repayment of the advance, the financing bank(s) have in place an appropriate mechanism to escrow the cash flows, and also have a clear and legal first claim on these cash flows.

(c) The value of security is relevant to determine the likely losses which a bank might suffer on the exposure should the default take place. This aspect assumes greater importance in the case of restructured loans. However, owing to the current downturn, the full security cover for the WCTL created by conversion of the irregular portion of principal dues over the drawing power, may not be available due to fall in the prices of security such as inventories. In view of the extraordinary situation, this special regulatory treatment is available to '**standard**' and '**sub standard accounts**' even where full security cover for WCTL is not available, subject to the condition that provisions are made against the **unsecured portion of the WCTL**, as under:

- Standard Assets : 20%
- Substandard Assets: 20% during the first year and to be increased by 20% every year thereafter until the specified period (one year after the first payment is due under the terms of restructuring)
- If the account is not eligible for upgradation after the specified period, the unsecured portion will attract provision of 100%

ii) The unit becomes viable in 10 years, if it is engaged in infrastructure activities, and in 7 years in the case of other units.

iii) The repayment period of the restructured advance including the moratorium, if any, does not exceed 15 years in the case of infrastructure advances and 10 years in the case of other advances. However the ceiling of 10 years would not apply in case of housing loans and the Board of Directors of the banks should prescribe the maximum period not exceeding 15 years for restructured advances keeping in view the safety and soundness of advances.

(iv) The restructured housing loans would be assigned additional risk weight of 25 percentage points over the prescribed risk weights.

iv) Promoters' sacrifice and additional funds brought by them should be a minimum of 15% of banks' sacrifice.

v) Personal guarantee is offered by the promoter except when the unit is affected by external factors pertaining to the economy and industry.

vi) The restructuring under consideration is not a 'repeated restructuring' as defined in para (iv) of Annex VII. However, as a one time measure, second restructuring carried out by banks of exposures (other than commercial real estate, capital market exposures, personal/consumer loans and loans to traders) upto June 30, 2009 shall be eligible for special regulatory treatment.

(g) Disclosures

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

(h) Illustrations

2.2.7.31 A few illustrations on the asset classification of restructured accounts are given in Annex-IX.

2.2.8 Other Advances

- (i) Advances against term deposits, NSCs eligible for surrender, IVPs, KVPs and Life policies need not be treated as NPAs although interest thereon may not have been paid for more than 90 days provided adequate margin is available in the accounts.
- (ii) Banks should fix monthly/quarterly instalments for repayment of gold loans for non-agricultural purposes taking into account the pattern of income generation and repayment capacity of the borrowers and such gold loan accounts may be treated as NPAs if instalments of principal and/ or interest thereon are overdue for more than 90 days.
- (iii) As regards gold loans granted for agricultural purposes, interest is required to be charged as per Supreme Court judgement at yearly intervals and payment should coincide with the harvesting of crops. Accordingly, such advances will be treated as NPA only if instalments of principal and/or interest become overdue after due date.

2.2.9 Recognition of Income on Investment Treated as NPAs

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

2.2.10 NPA Reporting to Reserve Bank

Banks should report the figures of NPAs to the Regional Office of the Reserve Bank at the end of each year within two months from the close of the year in the prescribed proforma given in the Annex 2.

3 ASSET CLASSIFICATION

3.1 Classification

3.1.1 Banks should classify their assets into the following broad groups, viz.

- (i) Standard Assets
- (ii) Sub-standard Assets
- (iii) Doubtful Assets
- (iv) Loss Assets

3.2 Definitions

3.2.1 Standard Assets

Standard Asset is one which does not disclose any problems and which does not carry more than normal risk attached to the business. Such an asset should not be an NPA.

3.2.2 Sub-standard Assets

- (i) With effect from March 31, 2005 an asset would be classified as sub-standard if it remained NPA for a period less than or equal to 12 months. In such cases, the current net worth of the borrowers/ guarantors 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 assets 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.
- (ii) An asset where the terms of the loan agreement regarding interest and principal have been re-negotiated or rescheduled after commencement of production, should be classified as sub-standard and should remain in such category for at least 12 months of satisfactory performance under the re-negotiated or rescheduled terms. In other words, the classification of an asset should not be upgraded merely as a result of rescheduling, unless there is satisfactory compliance of this condition.

3.2.3 Doubtful Assets

With effect from March 31, 2005, an asset is required to be classified as doubtful, if it has remained NPA for more than 12 months. For Tier I banks, the 12-month period of classification of a substandard asset in doubtful category is effective from April 1, 2009. As in the case of sub-standard assets, rescheduling does not entitle the bank to upgrade the quality of an advance automatically. A loan classified as doubtful has all the weaknesses inherent as that 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.

Note: *Consequent to change in asset classification norms w.e.f. March 31, 2005 banks are permitted to phase the consequent additional provisioning over a five year period commencing from the year ended March 31, 2005, with a minimum of 10 % of the required provision in each of the first two years and the balance in equal instalments over the subsequent three years.*

3.2.4 Loss Assets

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

3.3 Guidelines for Classification of Assets

3.3.1 Basic Considerations

- (i) Broadly speaking, classification of assets into above categories should be done taking into account the degree of well defined credit weaknesses and extent of dependence on collateral security for realisation of dues.
- (ii) In respect of accounts where there are potential threats to recovery on account of erosion in the value of security and existence of other factors such as, frauds committed by borrowers, it will not be prudent for the banks to classify them first as sub-standard and then as doubtful after expiry of 12 months from the date the account has become NPA. Such accounts should be straight away classified as doubtful asset or loss asset, as appropriate, irrespective of the period for which it has remained as NPA.

3.3.2 Advances Granted under Rehabilitation Packages Approved by BIFR/Term Lending Institutions

- (i) 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 and asset classification norms will become applicable after a period of one year from the date of disbursement.

- (ii) A similar relaxation be made in respect of SSI units which are identified as sick by banks themselves and where rehabilitation packages/nursing programmes have been drawn by the banks themselves or under consortium arrangements.

3.3.3 Internal System for Classification of Assets as NPA

- (i) 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.
- (ii) Responsibility and validation levels for ensuring proper asset classification may be fixed by the bank.
- (iii) 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.
- (iv) RBI would continue to identify the divergences arising due to non-compliance, for fixing accountability. Where there is wilful non-compliance by the official responsible for classification and is well documented, RBI would initiate deterrent action including imposition of monetary penalties.

4. INCOME RECOGNITION

4.1 Income Recognition - Policy

- 4.1.1 The policy of income recognition has to be objective and based on the record of recovery. Income from non-performing assets (NPA) is not recognised on accrual basis but is booked as income only when it is actually received. Therefore, banks should not take to income account interest on non-performing assets on accrual basis.
- 4.1.2 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.
- 4.1.3 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.
- 4.1.4 If Government guaranteed advances become 'overdue' and thereby NPA, the interest on such advances should not be taken to income account unless the interest has been realised.

4.2 Reversal of Income on Accounts Becoming NPAs

- 4.2.1 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.
- 4.2.2 If interest income from assets in respect of a borrower becomes subject to non-accrual, fees, commission and similar income with respect to same borrower that have been accrued should ceased to accrue in the current period and should be reversed or provided for with respect to past periods, if uncollected.
- 4.2.3 Banks undertaking equipment leasing should follow prudential accounting standards. Lease rentals comprises two elements – a finance charge (i.e interest charge) and a charge towards recovery of the cost of the asset. The interest component alone should be taken to income account. Such income taken to income account, before the asset became NPA, and remained unrealised should be reversed or provided for in the current accounting period.

4.3 Booking of Income on Investments in Shares & Bonds

- 4.3.1 As a prudent practice and in order to bring about uniform accounting practice among banks for booking of income on units of UTI and equity of All India Financial Institutions, such income should be booked on cash basis and not on accrual basis.
- 4.3.2 However, in respect of income from Government securities/bonds of public sector undertakings and All India Financial Institutions, where interest rates on the instruments are predetermined, income may be booked on accrual basis, provided interest is serviced regularly and is not in arrears.

4.4 Partial Recovery of NPAs

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.

4.5 Interest Application

- 4.5.1 In case of NPAs where interest has not been received for 90 days or more, as a prudential norm, there is no use in debiting the said account by interest accrued in subsequent quarters and taking this accrued interest amount as income of

the bank as the said interest is not being received. It is simultaneously desirable to show such accrued interest separately or park in a separate account so that interest receivable on such NPA account is computed and shown as such, though not accounted as income of the bank for the period.

- 4.5.2 The interest accrued in respect of performing assets may be taken to income account as the interest is reasonably expected to be received. However, if interest is not actually received for any reason in these cases and the account is to be treated as an NPA at the close of the subsequent year as per the guidelines, then the amount of interest so taken to income in the corresponding previous year should be reversed or should be provided for in full.
- 4.5.3 With a view to ensuring uniformity in accounting the accrued interest in respect of both the performing and non-performing assets, the following guidelines may be adopted notwithstanding the existing provisions in the respective State Co-operative Societies Act:
- (i) Interest accrued in respect of non-performing advances should not be debited to borrowal accounts but shown separately under 'Interest Receivable Account' on the 'Property and Assets' side of the balance sheet and corresponding amount shown under 'Overdue Interest Reserve Account' on the 'Capital and Liabilities' side of the balance sheet.
 - (ii) In respect of borrowal accounts, which are treated as performing assets, accrued interest can alternatively be debited to the borrowal account and credited to Interest account and taken to income account. In case the accrued interest in respect of the borrowal account is not actually realised and the account has become NPA as at the close of subsequent year, interest accrued and credited to income account in the corresponding previous year, should be reversed or provided for.
 - (iii) The illustrative accounting entries to be passed in respect of accrued interest on both the performing and non-performing advances are indicated in the Annex 3.
- 4.5.4 In the above context, it may be clarified that overdue interest reserve is not created out of the real or earned income received by the bank and as such, the amounts held in the Overdue Interest Reserve Account can not be regarded as 'reserve' or a part of the owned funds of the banks. It will also be observed that the Balance Sheet format prescribed under the Third Schedule to the Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) specifically requires the

banks to show 'Overdue Interest Reserve' as a distinct item on the 'Capital and Liabilities' side vide item 8 thereof.

5. PROVISIONING NORMS

5.1 Norms for Provisioning on Loans & Advances

5.1.1 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 paragraph 3 above.

5.1.2 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 loss assets, doubtful assets and sub-standard assets as below:

(i) Loss Assets

(a) The entire assets should be written off after obtaining necessary approval from the competent authority and as per the provisions of the Co-operative Societies Act/Rules. If the assets are permitted to remain in the books for any reason, 100 per cent of the outstanding should be provided for.

(b) In respect of an asset identified as a loss asset, full provision at 100 per cent should be made if the expected salvage value of the security is negligible.

(ii) Doubtful Assets

(a) Provision should be for 100 per cent 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 should be made and the realisable value is estimated on a realistic basis.

(b) In regard to the **secured portion**, provision may be made on the following basis, at the rates ranging from 20 per cent to 100 per cent of the secured portion depending upon the period for which the asset has remained doubtful:

Tier I Bank

Period for which the advance has remained in 'doubtful' category	Provision requirement
Up to one year	20 per cent
One to three years	30 per cent
More than three years (D-III) (i) outstanding stock of NPAs as on March 31, 2010 (ii) advances classified as 'doubtful for more than three years' on or after April 1, 2010	<ul style="list-style-type: none">- 50 per cent .- 60 per cent with effect from March 31, 2011- 75 per cent with effect from March 31, 2012- 100 per cent with effect from March 31, 2013 - 100 percent

Tier II Bank-

Period for which the advance has remained in 'doubtful' category	Provision requirement
Up to one year	20 per cent
One to three years	30 per cent
More than three years (D-III) (i) outstanding stock of NPAs as on March 31, 2007 (ii) advances classified as 'doubtful for more than three years' on or after April 1, 2007	<ul style="list-style-type: none">- 60 per cent with effect from March 31, 2008- 75 per cent with effect from March 31, 2009- 100 per cent with effect from March 31, 2010 - 100 percent

Few illustrations are given at Annex 5

(iii) **Sub-standard Assets**

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

(iv) **Provision on Standard Assets**

(a) From the year ended March 31, 2000, the banks should make a general provision of a minimum of 0.25 per cent on standard assets.

(b) However, Tier II banks (as defined in circular dated May 6, 2009) will be subjected to higher provisioning norms on standard assets as under:

The general provisioning requirement for all types of 'standard advances' shall be 0.40 per cent. However, direct advances to agricultural and SME sectors which are standard assets, would attract a uniform provisioning requirement of 0.25 per cent of the funded outstanding on a portfolio basis, as hitherto.

(c) The provisions towards "standard assets" need not be netted from gross advances but shown separately as "Contingent Provision against Standard Assets" under "Other Funds and Reserves" {item.2 (viii) of Capital and Liabilities} in the Balance Sheet.

(d) If due to changes in the regulatory requirements on provisions to be maintained by banks, the provisions held by banks exceed what is required to be held by banks, such excess provisions should not be reversed. In future, if by applying the revised provisioning norms, any provisions are required over and above the level of provisions currently held for the standard category assets ; these should be duly provided for.

(e) In case banks are already maintaining excess provision than what is required/prescribed by Statutory Auditor/RBI Inspection for impaired credits under Bad and Doubtful Debt Reserve, additional provision required for Standard Assets may be segregated from Bad and Doubtful Debt Reserve and the same may be parked under the head "Contingent Provisions against Standard Assets" with the approval of their Board of Directors. Shortfall if any, on this account may be made good in the normal course.

(f) The above contingent provision will be eligible for inclusion in Tier II capital.

(v) **Higher provisions**

There is no objection if the banks create bad and doubtful debts reserve beyond the specified limits on their own or if provided in the respective State Co-operative Societies Acts.

5.2 **Provisioning for Retirement Benefits**

Banks may have retirement benefit schemes for their staff, viz. Provident Fund, Gratuity and Pension. It is necessary that such liabilities are estimated on actuarial basis and full provision should be made every year for the purpose in their Profit and Loss Account.

5.3 **Provisioning Norms for sale of financial assets to Securitisation Companies(SC)/ Reconstruction Companies(RC)**

- (a) If the sale to SC/RC is at a price below the net book value(NBV) (i.e. book value less the provision held), the short fall should be written off / debited to P&L A/c of that year, subject to the provisions of the co-operative societies acts/rules/administrative guidelines in regard to write-off of debts.
- (b) If the sale is for a value higher than the NBV, the excess provision will not be reserved but will be utilised to meet the shortfall/ loss on account of sale of other assets to SC/RC.

5.4 **Guidelines for Provisions in Specific Cases**

(i) State Government guaranteed advances

From the year ended March 31, 2006, State Government guaranteed advance and investment in State Government guaranteed securities would attract extant provisioning norms, if interest and/or principal or any other amount due to the bank remains overdue for more than 90 days irrespective of the fact whether the guarantee have been invoked or not.

(ii) Advances granted under rehabilitation packages approved by BIFR/term lending institutions

- (a) The existing credit facilities sanctioned to a unit under rehabilitation package approved by BIFR/term lending institutions, should continue to be classified as sub-standard or doubtful asset as the case may be.
- (b) However, the additional facilities sanctioned as per package finalised by BIFR and/or term lending institutions, the income recognition and asset classification norms will become applicable after a period of one year from the date of disbursement.

(c) In respect of additional credit facilities granted to SSI units which are identified as sick 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.

- (iii) Advances against fixed/term deposit, NSCs eligible for surrender, IVPs, KVPs, and life policies are exempted from provisioning requirements.
- (iv) Advances against gold ornaments, government securities and all other kinds of securities are not exempted from provisioning requirements.
- (v) Advances covered by ECGC/DICGC guarantee
- (a) 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 per cent
Period for which the advance has remained doubtful	More than 3 years
Value of security held (excludes worth of borrower/guarantor)	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 per cent of unsecured portion)
Provision for secured portion of advance (as on March 31 2005)	Rs.0.90 lakhs (@ 60 per cent of secured portion of Rs.1.50 lakh).
Total provision required to be made	Rs.2.15 lakhs (as on March 31,2005).

- (b) In case the banks are following more stringent method of provisioning in respect of advances covered by the guarantees of DICGC/ ECGC, as compared to the method given above, they may have the option to continue to follow the same procedure.

6. DIVERGENCE IN ASSET CLASSIFICATION AND PROVISIONING

- (i) Banks should ensure scrupulous compliance with the instructions for recognition of credit impairment and view aberrations by dealing officials seriously.
- (ii) 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. Banks should fix a minimum cut off point to decide what would constitute a high value account depending upon their respective levels. The cut off point should be valid for the entire year.
- (iii) The responsibility and validation levels for ensuring proper asset classification may be fixed by the banks.
- (iv) Where there is wilful non-compliance by the officials responsible for classification and is well documented, RBI would initiate deterrent action including imposition of monetary penalties.

7. Clarification on certain frequently asked questions is given at annex 6

Direct Finance to Agriculture:

(vide para 2.1.2(iv))

1.1. Finance to individual farmers for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.)

1.1.1 Short-term loans for raising crops, i.e. for crop loans. This will include traditional/non-traditional plantations and horticulture

1.1.2 Advances up to Rs. 10 lakh against pledge/hypothecation of agricultural produce (including warehouse receipts) for a period not exceeding 12 months, irrespective of whether the farmers were given crop loans for raising the produce or not.

1.1.3 Working capital and term loans for financing production and investment requirements for agriculture and allied activities.

1.1.4 Loans to small and marginal farmers for purchase of land for agricultural purposes.

1.1.5 Loans to distressed farmers indebted to non-institutional lenders, against appropriate collateral

1.1.6 Loans granted for pre-harvest and post-harvest activities such as spraying, weeding, harvesting, grading, sorting, processing and transporting undertaken by individuals, in rural areas

1.2 Finance to others [such as corporates, partnership firms and institutions] for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.)

1.2.1 Loans granted for pre-harvest and post harvest activities such as spraying, weeding, harvesting, grading, sorting and transporting.

1.2.2 Finance upto an aggregate amount of Rs one crore per borrower for the purposes listed at 1.1.1,1.1.2,1.1.3, and 1.2.1 above.

1.2.3. One-third of loans in excess of Rs one crore in aggregate per borrower for agriculture and allied activities.

Annex 2
(vide para 2.2.11)

PROFORMA

Name of the Bank.....
Category Tier I /Tier II

Classification of Assets and Provisioning made against
Non-Performing Assets as on March 31, -----

(Rs.in lakh)

Classification of Assets	No. of A/Cs	Amount Outstanding	Percent age of Col.3 to total loan outstanding	Provision required to be made		Existing provision at the beginning of the year	Provisioning made during the year under report	Total provisions as at the end of the year	Remarks
				%	Amount				
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.
Total loans and advances									
Of which									
A. Standard Assets									
B. Non-Performing Assets									
1. Sub-standard									
2. Doubtful									
i) Upto 1 year									
a) Secured									
b) Unsecured									
ii) Above 1 year & upto 3 years									
a) Secured									
b) Unsecured									
iii) Above 3 years Secured									
a) Outstanding stock of NPAs as on March 31,									
b) Advances classified as 'doubtful more than 3 years' on or after April 1,									
b) Unsecured									
Total doubtful assets (i+ii+iii)									
a) Secured									
b) Unsecured									
3. Loss Assets									
Gross NPAs B1+B2+B3)									

Note: Please indicate the manner in which the provision (item 8) has been made/proposed to be made out of the profit of the current year.

Position of Net Advances/Net NPAs

(Rs. in lakh)

Sr.No.	Particulars	Current Year	Previous Year
1.	Gross Advances		
2.	Gross NPAs		
3.	Gross NPAs as percentage to Gross Advances		
4.	Deductions		
	- Balance in interest suspense account/OIR*		
	- DICGC/ECGC claims received and held pending adjustment		
	- Part payment of NPA accounts received and kept in suspense account		
	Total Deductions		
5.	Total NPA provisions held (BDDR, Special BDDR Balance after appropriation)		
6.	Net Advances (1-4-5)		
7.	Net NPAs (2-4-5)		
8.	Net NPAs as percentage of Net Advances		

* i.e. accrued interest on NPA accounts if included (capitalised) in loans and advances

CERTIFIED that the non-performing assets have been worked out as per RBI instructions and provisions made accordingly.

Chief Executive Officer

Statutory Auditors

(ii) Subsequently, if interest is actually realised, the following accounting entries may be passed:

(Dr) Cash/Bank Account	Rs.20,000.00
(Cr) Interest account	Rs.20,000.00
(Dr) Overdue Interest Reserve Account	Rs.20,000.00
(Cr) Interest Receivable Account	Rs.20,000.00

III. Accounting of Overdue Interest in Loan Ledgers & Balance Sheet

(i) With a view to facilitating the banks to work out the amount of interest receivable in respect of each non-performing borrowal account, banks can consider opening a separate column in the individual ledger accounts of such borrowers and interest receivable shown therein. This would enable the banks to determine at a particular point of time, the amount of interest actually to be recovered from the borrowers. Total of the amounts shown under the separate columns in the loan ledgers would be interest receivable in respect of non-performing advances and it would get reflected as such on the 'assets' side of balance sheet with a corresponding item on the liabilities side of the balance sheet as 'Overdue Interest Reserve'.

(ii) Similarly, a separate column should be provided in the loan ledger in respect of performing advances for showing accrued interest taken to income account on 31 March every year so that a watch can be kept on them. If the accrued interest is not realised and the account becomes NPA in the subsequent year, the amount has to be reversed or provided for

**Deviations in extant Prudential Norms as applicable
to Tier I and Tier II banks
(Vide para 2.1.4)**

	Tier I bank	Tier II bank
Definition	<p>(i) Banks having deposits below Rs.100 crore, operating in a single district.</p> <p>ii) Banks with deposits below Rs.100 crore operating in more than one district, provided the branches are in contiguous districts and deposits and advances of branches in one district separately constitute at least 95% of the total deposits and advances respectively of the bank.</p> <p>iii) Banks with deposits below Rs.100 crore, whose branches were originally in a single district but subsequently, became multi-district due to reorganization of the district.</p> <p>The deposits and advances as referred to in the definition may be reckoned as on 31st March of the immediate preceding financial year.</p>	Bank which is not a Tier I bank.
NPA norm	180 days loan delinquency norm for loan (including gold loans and small loan upto Rs 1 lakh). This relaxation is upto March 31, 2009.	90 days loan delinquency norm for loan accounts including gold loans and small loans up to Rs. 1 lakh.
Asset Classification norm.	With effect from March 31, 2005, an asset is required to be classified as doubtful, if it has remained NPA for more than 12 months. However, for Tier I banks, the 12-month period for classification of a substandard asset in doubtful category will be effective from April 1, 2009	With effect from March 31, 2005, an asset is required to be classified as doubtful, if it has remained NPA for more than 12 months.
Provisioning Norm.	<p>(i) Standard Assets: 0.25 % for all type of standard advances.</p> <p>(ii) Sub standard- 10%</p> <p>(iii) Doubtful (up to one year):100% of unsecured portion plus 20% of secured portion</p>	<p>(i) Standard Asset: 0.40 per cent. For agricultural and SME sectors it is 0.25 per cent.</p> <p>ii) Sub standard- 10%</p> <p>(iii) Doubtful (up to one year):100% of unsecured portion plus 20% of secured portion</p>

	<p>(iv) Doubtful (one to three years): 100% of unsecured portion plus 30% of secured portion</p> <p>(v) Doubtful for more than 3 years D-III) : 100% of unsecured portion plus 50% of secured portion</p> <p>(vi) Loss: 100%.</p> <p>W.e.f April 1, 2010- the provisioning norms for secured portion of the doubtful assets more than three years (D –III) are as under:</p> <p>(i) outstanding stock of D-III assets as on March 31, 2010</p> <p>-50 per cent -60 per cent with effect from March 31, 2011 -75 per cent with effect from March 31, 2012 -100 per cent with effect from March 31, 2013</p> <p>(ii) advances classified as ‘doubtful for more than three years’ on or after April 1, 2010- 100 %.</p>	<p>(iv) Doubtful (one to three years) : 100% of unsecured portion plus 30% of secured portion</p> <p>(v) Doubtful for more than 3 years (D-III) : 100% of unsecured portion plus 50% of secured portion</p> <p>(vi) Loss: 100%.</p> <p>W.e.f April 1, 2007- the provisioning norms for the secured portion of the doubtful assets more than three years (D –III) are as under</p> <p>(i) outstanding stock of D -III as on March 31, 2007</p> <p>-50 per cent -60 per cent with effect from March 31, 2008 -75 per cent with effect from March 31, 2009 -100 per cent with effect from March 31, 2010</p> <p>(ii) advances classified as ‘doubtful for more than three years’ on or after April 1, 2007- 100 %</p>
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(Illustrative entries on the provisioning requirement for secured portion of assets that are doubtful for more than three years D-III)

(vide para 5.1.2 (ii)(b))

Illustration 1. Existing stock of advances classified as 'doubtful more than 3 years' as on March 31, 2007

The outstanding amount as on March 31, 2007: Rs 25,000

Realisable value of security: Rs 20,000

Period for which the advance has remained in 'doubtful' category as on March 31, 2007: 4 years (i.e. Doubtful more than 3 years)

Provisioning requirement:

As on ...	Provisions on secured portion		Provisions on unsecured portion		Total (Rs)
	%	Amount	%	Amount	
March 31, 2007	50	10000	100	5000	15000
March 31, 2008	60	12000	100	5000	17000
March 31, 2009	75	15000	100	5000	20000
March 31, 2010	100	20000	100	5000	25000

Illustration 2: Advances classified as 'doubtful more than three years' on or after April 1, 2007

The outstanding amount as on March 31, 2007: Rs 10,000/-

Realisable value of security: Rs 8,000/-

Period for which the advance has remained in 'doubtful' category as on March 31, 2007: 2.5 years

Provisioning requirement:

As on	Asset classification	Provisions on secured portion		Provisions on unsecured portion		Total (Rs)
		%	Amt	%	Amt	
March 31, 2007	Doubtful 1 to 3 years	30	2400	100	2000	4400
March 31, 2008	Doubtful more than 3 years	100	8000	100	2000	10000

**(Clarification on certain frequently asked questions)
(vide para no 7)**

1. Whether a working capital account will become an NPA if the stock statements are not submitted regularly? What should be the period for which the stock statements can be in arrears before the account is treated as an NPA?

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. Considering the practical 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 90 days (with effect from March 31, 2004).

2. Whether an account will become an NPA if the review/renewal of regular/ad-hoc credit limits are not done when due? What should be periodicity of review/renewal to decide the present status of an account?

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 or have not been renewed within 180 days from the due date/date of ad-hoc sanction will be treated as NPA, which period will be reduced to 90 days with effect from March 31, 2004.

3 Regularisation of the account around the date of balance sheet - Whether it will be in order to treat a borrowal account as 'standard', if it has been irregular for a major part of the year, but has been regularised near 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 Classification of NPAs where there is a threat to recovery
How should the instructions on classification of NPAs straightaway as doubtful or a loss asset be interpreted and what can be termed as a 'significant credit impairment'?**

An NPA need not go through the various stages of classification in case of serious credit impairment and such assets should be straightway classified as a doubtful/loss asset as appropriate. Erosion in the value of security can be reckoned as significant when the realizable 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.

5 Classification of credit facilities under consortium

In certain cases of consortium accounts, though the record of recovery in the account with a member bank may suggest that the account is a NPA, the banks submit that, at times, the borrower has deposited adequate funds with the consortium leader/member of the consortium and the bank's share is due for receipt. In such cases, will it be in order for the member bank to classify the account as 'standard' in its books?

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.

6 Appropriation of recoveries - What is the practice to be adopted by banks regarding appropriation of recoveries in NPA accounts?

In the absence of a clear agreement between the bank and the borrower for the purpose, banks should adopt an accounting principle and exercise the right of appropriation of recoveries in a uniform and consistent manner.

7 Activities allied to agriculture - Our existing guidelines stipulate that advances granted for agricultural purposes may be treated as NPA if interest and/or instalments towards repayment of principal remains unpaid for two harvest seasons but for a period not exceeding two half years. Whether the same norm can be extended to floriculture and allied agriculture activities like poultry, animal husbandry, etc.?

As indicated in para 2.1.3, the norms for classifying direct agricultural advances (listed in Annex 1), as NPAs have since been revised w.e.f. September 30, 2004.

8 Overdues in other credit facilities - There are instances where banks park the dues from a borrower in respect of devolved letters of credit and invoked guarantees in a separate account, irrespective of whether the borrower's credit facilities are regular or not. How to determine when the account in which such dues are parked has become an NPA?

A number of banks adopt the practice of parking the dues of the borrower in respect of devolved letters of credit and invoked guarantees in a separate account which is not a regular sanctioned facility. As a result these are not reflected in the principal operating account of the borrower. This renders application of the prudential norms for identification of NPAs difficult. It is, therefore, advised that if the debts 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.

9 Treatment of loss assets - An NPA account will be classified as a loss asset only when there is no security in the account or where there is considerable erosion in the realisable value of the security in the account. What can be termed as a 'considerable' erosion for the account to be classified as a loss asset?

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 after obtaining necessary permission from the competent authority as per the Co-operative Societies Act/Rules, or fully provided for by the bank.

10 Valuation of Security - A major source of divergence in provisioning requirement was the realisable value of the primary and collateral security. Can uniform guidelines be prescribed for adoption in this area, at least for large value accounts?

With a view to bringing down divergence arising out of difference in assessment of the value of security it has been decided that in cases of NPAs with balance of Rs.10 lakh and above:

- (a) The current assets and their valuation are looked into at the time of Statutory Audit/Concurrent audit. However, in order to enhance the reliability on stock valuations, stock audit at annual intervals by external agencies could be considered in case of larger advances. The cut off limit and the names of the external agencies may be finalised by the Board.
- (b) 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.

Prudential Guidelines on Restructuring of Advances-Annex - VII

Key Concepts

(i) Advances

The term 'Advances' will mean all kinds of credit facilities including cash credit, overdrafts, term loans, bills discounted / purchased, receivables, etc. and investments other than that in the nature of equity.

(ii) Fully Secured

When the amounts due to a bank (present value of principal and interest receivable as per restructured loan terms) are fully covered by the value of security, duly charged in its favour in respect of those dues, the bank's dues are considered to be fully secured. While assessing the realisable value of security, primary as well as collateral securities would be reckoned, provided such securities are tangible securities and are not in intangible form like guarantee etc., of the promoter / others. However, for this purpose the bank guarantees, State Government Guarantees and Central Government Guarantees will be treated on par with tangible security.

(iii) Restructured Accounts

A restructured account is one where the bank, for economic or legal reasons relating to the borrower's financial difficulty, grants to the borrower concessions that the bank would not otherwise consider. Restructuring would normally involve modification of terms of the advances / securities, which would generally include, among others, alteration of repayment period / repayable amount/ the amount of instalments / rate of interest (due to reasons other than competitive reasons).

(iv) Repeatedly Restructured Accounts

When a bank restructures an account a second (or more) time(s), the account will be considered as a 'repeatedly restructured account'. However, if the second restructuring takes place after the period up to which the concessions were extended under the terms of the first restructuring, that account shall not be reckoned as a 'repeatedly restructured account'.

(v) SMEs

Small and Medium Enterprises is an undertaking defined in circular UBD.PCB.Cir.No. 35 / 09.09.001 / 06-07 dated April 18, 2007.

(vi) Specified Period

Specified Period means a period of one year from the date when the first payment of interest or installment of principal falls due under the terms of restructuring package.

(vii) Satisfactory Performance

Satisfactory performance during the specified period means adherence to the following conditions during that period.

Non-Agricultural Cash Credit Accounts: In the case of non-agricultural cash credit accounts, the account should not be out of order any time during the specified period, for duration of more than 90 days / 180 days as applicable to Tier I and Tier II UCBs respectively. In addition, there should not be any overdues at the end of the specified period.

Non-Agricultural Term Loan Accounts: In the case of non-agricultural term loan accounts, no payment should remain overdue for a period of more than 90 days. In addition there should not be any overdues at the end of the specified period.

All Agricultural Accounts: In the case of agricultural accounts, at the end of the specified period the account should be regular.

Prudential Guidelines on Restructuring of Advances- Annex - VIII

Particulars of Accounts Restructured

(Rs. in lakh)

		Housing Loans	SME Debt Restructuring	Others
Standard advances restructured	No. of Borrowers			
	Amount outstanding			
	Sacrifice (diminution in the fair value)			
Sub standard advances restructured	No. of Borrowers			
	Amount outstanding			
	Sacrifice (diminution in the fair value)			
Doubtful advances restructured	No. of Borrowers			
	Amount outstanding			
	Sacrifice (diminution in the fair value)			
TOTAL	No. of Borrowers			
	Amount outstanding			
	Sacrifice (diminution in the fair value)			

Prudential Guidelines on Restructuring of Advances- Annex – IX

Asset Classification of Restructured Accounts under the Guidelines						
	Particulars	Case 1	Case 2	Case 3	Case 4	
I	Assumed due date of payment	31.01.2007	31.01.2007			
	Assumed date of restructuring	31.03.2007	31.03.2007	31.03.2007	31.03.2007	
	Period of delinquency as on the date of restructuring	2 months	2 months	18 months	18 months	
	Asset Classification (AC) before restructuring	'Standard'	'Standard'	'Doubtful - less than one year'	'Doubtful - less than one year'	
	Date of NPA	NA	NA	31.12.05 (Assumed)	31.12.05 (Assumed)	
II	Asset classification (AC) on restructuring					
	Assumed status of the borrower	Eligible for special regulatory treatment	Not eligible for special regulatory treatment	Eligible for special regulatory treatment	Not eligible for special regulatory treatment	
	AC after restructuring	'Standard'	Downgraded to 'Substandard' w.e.f 31.03.07 (i.e., on the date of restructuring)	'Doubtful - less than one year'	'Doubtful - less than one year'	
	Assumed first payment due under the revised terms	31.12.07	31.12.07	31.12.07	31.12.07	
III	Asset classification after restructuring					
	A	The account performs satisfactorily as per restructured terms				
	(a)	AC during the specified one year period (i.e., from 31.12.07 to 31.12.08)	No change (i.e., remains 'Standard')	'Doubtful - less than one year' w.e.f. 31.03.08 (i.e. one year after classification as	No change (i.e., remains 'Doubtful - less than one year')	'Doubtful - one to three years' w.e.f. 31.12.07 (i.e., one year after classification as 'Doubtful less than one year')

				'Substandard')		
	(b)	AC after the specified one year period	Continues in 'Standard' category	Upgraded to 'Standard' category	Upgraded to 'Standard' category	Upgraded to 'Standard' category
B	If performance not satisfactory vis-a-vis restructured terms					
	(a)	AC during the specified one year period (in case the unsatisfactory performance is established before completion of one year period)	Treated as substandard w.e.f 30.4.2007 and downgraded to 'Doubtful less than one year' with effect from 30.04.08.	'Doubtful - less than one year' w.e.f. 31.03.08 (i.e. one year after classification	'Doubtful one to three years' w.e.f. 31.12.07	'Doubtful - one to three years' w.e.f. 31.12.07 (i.e., one year after classification as 'Doubtful less than one year' (on 31.12.06)
	(b)	AC after the specified one year period, if the unsatisfactory performance continues	Will migrate to 'Doubtful - one to three years' w.e.f. 30.04.09 and 'Doubtful more than three years' w.e.f. 30.04.2011.	Will migrate to 'Doubtful - one to three years' w.e.f. 31.03.09 and 'Doubtful more than three years' w.e.f. 31.03.2011.	Will migrate to 'Doubtful - more than three years' w.e.f. 31.12.09	Will migrate further to 'Doubtful more than three years' w.e.f. 31.12.09

Appendix

Master Circular on Income Recognition, Asset Classification, Provisioning & Other Related Matters

A. List of Circulars as of June 30, 2009 consolidated in the Master Circular

Sr.No	Circular No.	Date	Subject
1	UBD.CO.LS.Cir.No 66 /07.01.000/2008-09	6/5/2009	Annual Policy Statement for 2009-10-Extension of area of operation – Liberalisation
2	UBD.PCB.BPD. 53/13.05.000/2008-09	6/3/2009	Prudential Guidelines on Restructuring of Advances
3	UBD.PCB.Cir No 29 / 09.11.600 / 2008-09	1/12/2008	Provisioning for Standard Assets and Risk Weights for exposures
4	UBD.PCB.Cir.No.47 / 09.11.600 / 07-08	26.05.2008	Provisioning Requirement for Standard Assets
5	UBD.PCB.Cir No.38/ 09.14.000 / 2007-08	02.04.2008	Income Recognition, Asset Classification & Provisioning Norms
6	UBD (PCB).Cir.No.35 / 09.20.001 / 07-08	07.03.2008	Classification of UCBs for Regulatory Purposes
7	UBD. PCB.Cir No. 38/ 9.14.000/ 06-07	30.04.2007	Annual Policy Statement for the year 2007-08-Income recognition, asset classification and provisioning norms
8	UBD.PCB.Cir.No.30/ 9.11.600/06-07	19.02.2007	3rdQuarter Review of Annual Statement on Monetary Policy for 2006-07-Provisioning for Standard Assets
9	UBD.PCB.Cir.57/09.11. 600/05-06	15.06.2006	Annual Policy Statement for the Year 2006-07-additional provisioning requirements for standard assets.
10	UBD.PCB.Cir..20/09.11. 600/05-06	24.11.2005	Mid Term Review of Annual Policy Statement for the year 2005-06-additional provisioning for standard assets
11	UBD.PCB.Cir. 1/09.140.00/05-06	04.07.2005	Income recognition and asset classification norms
12	UBD.PCB.Cir 42/09.140.00/04-05	30.03.2005	Prudential Norm- IRAC and other related matters- procedure for accounting of accrued interest
13	UBD.PCB.Cir26/09.140. 00/04-05	01.11.2004	Prudential Norms-State Govt Guaranteed Exposures.
14	UBD. PCB.Cir 21/12.05.05/04-05	27.09.2004	Annual Policy Statement for the Year 2004-05-additional provisioning requirements for NPAs.
15	UBD.PCB.cir22/12.05.0 5/04-05	27.09.2004	Income recognition, asset classification, provisioning- adoption of 90 days norms
16	UBD.PCB.Cir 17/13.04.00/04-05	04.09.2004	Income recognition, asset classification, provisioning- adoption of 90 days norms
17	UBD.PCB.Cir 9/13.04.00/04-05	04.08.2004	Income recognition, asset classification, provisioning- adoption of 90 days norms
18	UBD.PCB.Cir.No.55/12. 05.05/	30-06-2004	Annual Policy Statement for the year 2004-05. Additional Provisioning requirement for NPAs.
19	UBD.PCB.Cir.No.53/13. 05.03/	30-06-2004	Annual Policy Statement for the year 2004-05. Prudential Norms for Agricultural Advances
20	UBD.PCB.No.49/12.05. 03/2003-04	1/6/2004	Income recognition, asset classification, provisioning norms
21	UBD.CIR.48/13.04.00/2 002-03	22-05-2003	IRAC – 90 days norm for recognition of loan impairment – exemptions
22	UBD.BSD-I No.15 /12.05.05/2002-03	11/9/2002	Income recognition, asset classification, provisioning and other related matters
23	UBD.BSD.I.15/12.05.05/ 2002-03	11/9/2002	Income recognition, asset classification, provisioning – 12 months norms

24	UBD.BSD.I.PCB.No.44/ 12.05.05/	21-05-2002	Classification of Agricultural Advances
25	UBD.BSD.I.PCB.22/12. 05.05/2001-02	12/11/2001	Treatment of restructured accounts
26	UBD.No.BSD.I.PCB13/1 2.05.05/200102	6/10/2001	Divergence in asset classification and provisioning
27	UBD.No.BSD.I.PCB.12/ 12.05.05/01-02	5/10/2001	Income Recognition and asset classification – Adoption of 90 days norm
28	UBD.No.BSD.I.16/12.05 .05/2000-2001	8/12/2000	Income Recognition and asset classification, provisioning and related matters – "Past Due" concept.
29	UBD.No.BSD.I.PCB/14/ 12.05.05/	20-11-2000	Income recognition, Asset Classification and Provisioning
30	UBD.CO.BSD-I.PCB 34/12.05.05/99-2000	24-5-2000	Income Recognition, Asset Classification, Provisioning and Valuation of Investments
31	UBD.No.BSD.PCB./25/1 2.05.05/99-00	28-2-2000	Income Recognition, Asset Classification, Provisioning and other related matters
32	UBD.No.BSD.I/22/12.05 .00/99-2000	8/2/2000	IRAC – Agricultural loans affected by natural calamities
33	UBD.No.BSD.I/11/12.05 .00/1999-2000	12/10/1999	Clarification on classification of gold loans into Non-performing Assets
34	UBD.No.BSD.I/2/12.05. 05/1999-2000	28-7-1999	Income Recognition, Asset Classification and Provisioning – Concept of Commencement of Commercial Production
35	UBD.No.BSD- I.29/12.05.05/98-99	23-4-1999	Income recognition asset classification and other related matters
36	UBD.No.BSD- I.2/12.05.01/98-99	17-07-1998	Prudential norms for Income Recognition, Asset classification and provisioning – Agricultural Advances
37	UBD.No.I&L.(PCBs)42/1 2.05.00/	20-03-1997	Prudential norms – Income Recognition, Asset Classification, Provisioning and other related matters.
38	UBD.No.I&L.(PCBs)68/1 2.05.00/	10/6/1996	Income Recognition, assets classification, provisioning and other related matters Clarifications
39	UBD.No.I&L (PCB) 61/12.05.00/94-95	6/6/1995	Income recognition, asset classification, provisioning and other related matters Valuation of investment and others
40	UBD.No.I&L(PCB)46/12 .05.00/94-95	28-02-1995	IRAC and other related matters – Procedure for accounting accrued interest
41	UBD.I&L (PCB) 37/12.05.00/94-95	9/1/1995	Income recognition, assets classification, provisioning and other related matters
42	UBD.No.I&L 86/12.05.00/93-94	28-06-1994	Income recognition, assets classification, provisioning and other related matters
43	UBD.No.I&L 63/12.05.00/93-94	1/3/1994	Income recognition, assets classification, provisioning and other related matters
44	UBD.No.48/12.05.00/93 -94	14-1-1994	Income recognition, assets classification, provisioning and other related matters
45	UBD.No.45/12.05.00/93 -94	24-12-1993	IRAC and other related matters clarification regarding credit facilities backed by Government Guarantees
46	UBD.I&L.71/J.1/92-93	17-6-1993	Income recognition assets classification, provisioning and other related matters – clarification
47	UBD.No.I&L.63J-I/92-93	16-4-1993	Income recognition, assets classification, provisioning and other related matters
48	UBD.No.I&L.38/J.1- 92/93	9/2/1993	Income recognition, assets classification, provisioning and other related matters
49	UBD.No.I&L 51/J.1- 90/91	23-2-1991	Classification of Non-Performing Loans

B. List of Other Circulars from which instructions have also been consolidated in the Master Circular

No.	Circular No.	Date	Subject
1.	UBD.No.DS.PCB.Cir.3/13.04.00/2002-03	20-07-2002	Charging of interest at monthly rests
2.	UBD.No.POT.PCB.CIR.No.45/09.116.00/2000-01	25-04-2001	Application of Capital Adequacy Norms to PCBs
3.	UBD.No.DS.PCB.20/13.04.00/97-98	10-11-1997	Compounding of Interest by Banks on Agricultural Advances