

Customer Education Literature Document - New RBI guidelines on Income Recognition, Asset Classification and Provisioning (IRACP) for Advances

Reserve Bank of India (RBI) guidelines on 'Prudential norms on Income Recognition, Asset Classification and Provisioning (IRACP), pertaining to Advances dated October 01, 2021 read with RBI clarification circular issued on November 12, 2021 and February 15, 2022.

With a view to increase awareness amongst the borrowers, placed herewith are concepts / clarifications / illustrative examples on due dates and specification of Special Mention Account (SMA) / Non-Performing Asset (NPA) classification dates.

Q. Why is it important to read this?

A. RBI vide its circular no. RBI/2021-2022/125 DOR.STR.REC.68/ 21.04.048/2021-22 on 'Prudential norms on Income Recognition, Asset Classification and Provisioning, pertaining to Advances – Clarifications' dated November 12, 2021 and IBA letter C&I-III/IRAC/14.12/2021-22 on 'Clarifications/guidance provided by RBI on Prudential norms on IRACP' dated December 30, 2021 have clarified and/or harmonised certain aspects relating to SMA / NPA classification dates, dates of overdue, etc. with a view to bring about uniformity and common understanding regarding the implementation of the guidelines on IRACP in a harmonised manner.

The examples quoted are illustrative and not exhaustive in nature and relate to general scenarios. The IRACP norms and clarifications issued by the RBI will prevail for implementation and may be amended from time to time by the RBI.

Q. Banks classify loan accounts as Special Mention Account (SMA) and Non-Performing Asset (NPA) immediately on default. What is the basis of such classification? When will an account be classified as SMA or NPA?

A. The Bank classifies the borrower as SMA/NPA based on the extant Regulatory guidelines. The same is explained hereunder:

1. Classification as Special Mention Account (SMA):

Lending institutions will recognize the incipient stress in loan accounts, immediately on default, by classifying them as Special Mention Accounts (SMA). The basis of classification of SMA / NPA category shall be as follows:

Loans other than revolving facilities		Loans in the nature of cash credit / overdraft	
SMA sub-categories	Basis for classification – Principal or interest payment or any other amount wholly or partly overdue.	SMA Sub-categories	Basis for classification – Outstanding balance remains continuously in excess of the sanctioned limit or drawing power, whichever is lower, for a period of:
SMA 0	Up to 30 days	NA	NA
SMA 1	More than 30 days and up to 60 days	SMA 1	More than 30 days and up to 60 days
SMA 2	More than 60 days and up to 90 days	SMA 2	More than 60 days and up to 90 days

2. Non-Performing Asset:

In accordance with the provisions of the RBI's Master Circular on Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances dated October 1, 2021, a Non-Performing Asset (NPA) is a loan or an advance where:

- Interest and/or instalment of principal remains overdue for a period of more than 90 days in respect of a term loan
- The account remains 'out of order' as indicated below, in respect of an Overdraft / Cash Credit (OD / CC)
- A Credit Card account will be treated as non-performing, if the minimum amount due, as mentioned in the statement, is not paid fully within 90 days from the due date mentioned in the statement
- The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted
- The instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops
- The instalment of principal or interest thereon remains overdue for one crop season for long duration crops
- The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of the Reserve Bank of India (Securitisation of Standard Assets) Directions, 2021
- In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment

Apart from the above, an Overdraft / Cash Credit ("OD" / "CC") can also be classified as NPA due to the following technical reasons:

- i. An account where the sanction limits have not been reviewed/renewed within 180 days from the due date and/or expiry of the adhoc sanction where the account is not fully renewed
- j. Stock / Book debts statement is older than 180 days

Advances against term deposits, National Savings Certificate (NSCs) eligible for surrender, Indira Vikas Patra (IVPs), Kisan Vikas Patra (KVPs) and life policies will not be treated as NPAs only if stipulated margin is maintained in the accounts. However, advances against gold ornaments, government securities and all other securities are not covered by this exemption.

Q. What is a Project loan? How is a project loan classified as non-performing?

- A. 'Project Loan' means any term loan which has been extended for the purpose of setting up of an economic venture. 'Date of Commencement of Commercial Operations' (DCCO) will be documented by the Bank at the time of financial closure of the project. Bank may restructure project loans, by way of revision of DCCO without classifying the account as NPA subject to regulatory guidelines. A project loan would be classified as NPA as per record of recovery (90 days overdue) or if project has not commenced operations by stipulated DCCO / deferred DCCO or DCCO is extended beyond the regulatory permissible periods or DCCO extensions are not as per regulatory conditions.

Q. When will an account be treated as 'Out of Order'?

- A. An account shall be treated as 'out of order' if:
- a. The outstanding balance in the CC / OD account remains continuously in excess of the sanctioned limit / drawing power for 90 days, or
 - b. The outstanding balance in the CC / OD account is less than the sanctioned limit / drawing power but there are no credits continuously for 90 days, or the outstanding balance in the CC/OD account is less than the sanctioned limit / drawing power but credits are not enough to cover the interest debited during the previous 90 days period (*note: The 'previous 90 days period' for determination of 'out of order' status of a CC/OD account shall be inclusive of the day for which the day-end process is being run*).

Q. What is a stressed account?

- A. Borrower is required to pay the EMI / instalment / interest at periodic intervals as per the terms agreed at the time of availing the loan. In case EMI / instalment / interest due is not paid on or before the due date, as per the agreed terms, such account is termed as 'stressed account'.

Q. As required by the RBI circular, please explain the terms of 'Due' & 'Overdue'. How are they different? When will accounts be flagged as overdue?

A. Banks use these terms to denote principal / interest / any charges levied on the loan account as under:

1. Due: Means the principal / interest / any charges levied on the loan account which are payable within the period stipulated as per the terms of sanction of the credit facility.
2. Overdue: Means the principal / interest / any charges levied on the loan account which are payable but have not been paid within the period stipulated as per the terms of sanction of the credit facility. In other words, any amount due to the Bank under any credit facility is 'overdue' if it is not paid on or before the due date as contracted between the Bank and its customer.

Borrower accounts are to be flagged as overdue by the lending institutions as part of the day-end processes for the due date, irrespective of the time of running such processes.

Q. What is the accounting method used by Banks to arrive at the number of days overdue for determining the SMA/NPA status?

A. IBA has clarified the relevance of the Principle of 'First In First Out' (FIFO) in appropriation of payments into the borrowal account as under:

The principle of FIFO i.e. 'First In, First Out' accounting method is relevant to arrive at the number of days overdue for determining the SMA/NPA status. The FIFO principle assumes that the oldest outstanding dues in the loan account needs to be cleared first. The FIFO method thus requires that what is due first must be paid by the borrower first.

For example, in a loan account as on 01.02.2022, there are no overdues, and an amount of INR 100 is due for payment towards principal instalment / interest / charges. Hence, any payment being credited on or after 01.02.2022 in the loan account will be used to pay off the dues outstanding on 01.02.2022.

Assuming that nothing is paid / or there is partial payment (INR 80) of dues during the month of February, the overdue as on 01.03.2022 will be INR 20 i.e., INR 100 - INR 80. Additionally, an amount of INR 100 becomes due on 01.03.2022. Now a payment / partial payment into the account on or after 01.03.2022 will be first utilised to pay off the partial due of 01.02.2022 i.e. INR 20 of February (INR 100- INR 80).

If there is excess amount available (after recovery of INR 20), then after recovering the dues of 01.02.2022, the remaining amount will be treated as recovery towards due of 01.03.2022.

Q. How do Banks determine the “age of oldest dues”?

- A. The age of oldest dues is calculated in days from the date on which the oldest payment is due and continues to remain unpaid. In the above illustration, if the dues relating to 01.02.2022 remain unpaid till 01.03.2022, the age of the oldest dues is calculated as 29 days on 01.03.2022.

Q. What is the change that is being spoken about? How does it apply to me?

- A. Your loan account classification has changed based on when the payment is received from you. You will therefore need to ensure timely payment of dues / maintain sufficient funds to ensure payment of dues on or before the due date. Mentioned below are a few examples shared for your understanding:

Earlier method of classification	Revised method of classification
If the due date is 31.12.2021 and payment was not received in the account on or before 01.01.2022, the loan account would be treated as overdue and accordingly DPD (Days Past Due) will start from 01.01.2022. In the scenario above, the status of your loan / Credit Card A/c would change only on the next working day in case of non-receipt of payment.	If the due date is 31.12.2021 and payment is not received on or before 31.12.2021, the loan account will be treated as overdue and accordingly the DPD (Days Past Due) will start from 31.12.2021 itself as part of the day end processing activity of the Bank. In the scenario above, the status of your loan / Credit Card A/c will change on the same day as the due date during the day end processing activity of the Bank in case of non-receipt of payment. This is applicable in case of servicing interest for loan accounts. Further, if the due date falls on a non-working day, the borrower has to ensure that the repayment is made on or before the due date.

Q. At what periodicity does the Bank carry out the asset classification of accounts as SMA/NPA?

A. The Bank carries out the asset classification processes on a daily and continuous basis.

Q. What is restructuring and what is asset classification if an account is restructured?

A. Restructuring may involve modification of terms of the advances / securities, which would generally include, among others, alteration of payment period / payable amount / the amount of instalments / rate of interest; roll over of credit facilities; sanction of additional credit facility / release of additional funds for an account in default to aid curing of default / enhancement of existing credit limits; compromise settlements where time for payment of settlement amount exceeds three months. Any restructuring of facility on account of financial difficulty of borrower will result in classification of account as NPA.

However, in case of loans at floating rate of interest (ROI), the EMI amount and/or tenor of the loan, etc. may undergo a change, if the ROI rate has changed. Such change in the EMI amount or the tenor of the loan is not construed as restructuring.

Q. When will upgradation of accounts classified as NPAs happen?

A. It is clarified that loan accounts classified as NPAs are upgraded to 'Standard' asset only if the entire arrears of interest and principal pertaining to all the credit facilities are paid by the borrower. With regard to upgradation of accounts classified as NPA due to restructuring, non-achievement of Date of Commencement of Commercial Operations (DCCO), etc., the instructions as per the specific regulatory circular will continue to be applicable.

Q. How does SMA/NPA classification happen at borrower level?

A. SMA/NPA reporting at borrower level is as per regulatory guidelines and thus, overdue in any one account of the borrower will result in reporting of the borrower as SMA or NPA, as the case may be.

Q. Whom can I contact in case of queries or further assistance on this?

A. For any retail / individual account related queries, kindly connect with the nearest Branch / Loan Centre (<https://www.axisbank.com/contact-us>). If you are a non-retail /

corporate borrower, you may reach out to your Service Relationship Manager / Relationship Manager for any grievances and clarifications.

Q. What is the impact on the borrower if the account is slipped to SMA/NPA?

A. As per the extant regulatory guidelines, the Bank has to report the account as SMA/NPA to Central Repository Information of Large Credit (CRILC), Credit Information Companies (CICs), etc. from time to time, which impacts the credit history of the borrower.

Q. When will an account move into SMA or NPA? Can this be explained with an illustrative example?

A. The following table illustrates the movement of an account to SMA and further to NPA based on delay / non-payment of dues and subsequent upgrade to Standard category at day end process:

Due date of payment	Payment date	Payment covers	Age of oldest dues in days	SMA/NPA	SMA/NPA since date
01.01.2022	01.01.2022	Entire dues up to 01.01.2022	0	NIL	NA
01.02.2022	01.02.2022	No payment or Part payment of dues of 01.02.2022	1	SMA-0	01.02.2022
01.02.2022	02.02.2022	No payment or Part payment of dues of 01.02.2022	2	SMA-0	01.02.2022
01.03.2022		Dues of 01.02.2022 not fully paid 01.03.2022 is also due at EOD 01.03.2022	29	SMA-0	01.02.2022
		Dues of 01.02.2022 fully paid, Due for 01.03.2022 is not paid at EOD 01.03.2022	1	SMA-0	01.03.2022
		No payment of full dues of 01.02.2022 and 01.03.2022 at EOD 03.03.2022	31	SMA-1	01.02.2022/ 03.03.2022
		Dues of 01.02.2022 fully paid, due for	1	SMA-0	01.03.2022

Due date of payment	Payment date	Payment covers	Age of oldest dues in days	SMA/NPA	SMA/NPA since date
		01.03.2022 not fully paid at EOD 01.03.2022			
01.04.2022		No payment of dues of 01.02.2022, 01.03.2022 and amount dues on 01.04.2022 at EOD 01.04.2022	60	SMA-1	01.02.2022/ 02.04.2022
		No payment of dues of 01.02.2022 till 01.04.2022 at EOD 02.04.2022	61	SMA-2	01.02.2022 / 02.04.2022
01.05.2022		No payment of dues of 01.02.2022 till 01.05.2022 at EOD 01.05.2022	90	SMA-2	01.02.2022 / 02.04.2022
		No payment of dues of 01.02.2022 till 01.05.2022 at EOD 02.05.2022	91	NPA	02.05.2022
01.06.2022	01.06.2022	Fully paid dues of 01.02.2022 at EOD 01.06.2022	93	NPA	02.05.2022
01.07.2022	01.07.2022	Paid entire dues of 01.03.2022 & 01.04.2022 at EOD 01.07.2022	62	NPA	02.05.2022
01.08.2022	01.08.2022	Paid entire dues of 01.05.2022 & 01.06.2022 at EOD 01.08.2022	32	NPA	02.05.2022
01.09.2022	01.09.2022	Paid entire dues of 01.07.2022 & 01.08.2022 at EOD 01.09.2022	1	NPA	02.05.2022
01.10.2022	01.10.2022	Paid entire dues of 01.09.2022 & 01.10.2022	0	Standard account with no overdue	STD from 01.10.2022

For detailed guidelines on asset classification and provisioning, please refer to the RBI's Master Circular - Prudential Norms on IRACP pertaining to Advances dated October 1, 2021. The above asset / SMA classification norms are subject to changes as per regulatory instructions issued from time to time.

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