



# BANK LENDINGS AND LOANS

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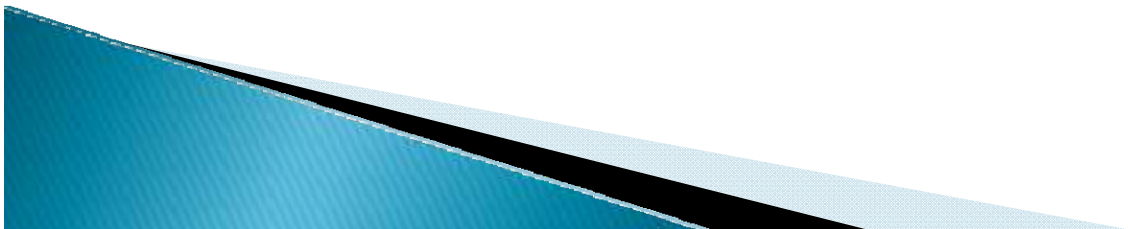
UNIT 4

# *I. Principles of Lending and Loan Policy:*

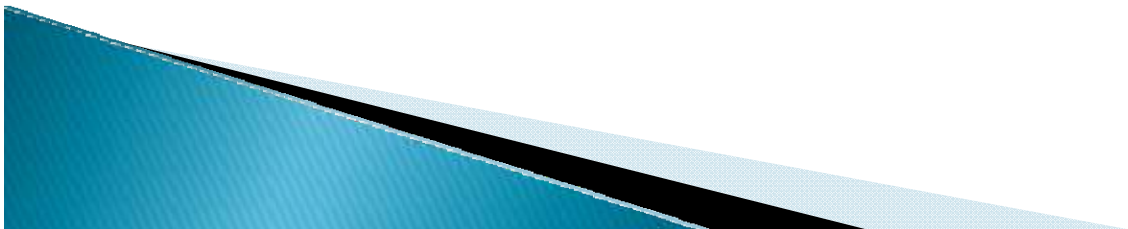
- ▶ **Safety:-** Banks need to ensure that advances are safe and money lent out by them will come back. Since the repayment of loans depends on the borrowers' capacity to pay, the banker must be satisfied before lending that the business for which money is sought is a sound one.



- ▶ **Liquidity:-** To maintain liquidity, banks have to ensure that money lent out by them is not locked up for long time by designing the loan maturity period appropriately.
- ▶ **Profitability:-** To remain viable, a bank must earn adequate profit on its investment. This calls for adequate margin between deposit rates and lending rates. In this respect, appropriate fixing of interest rates on both advances and deposits is critical.



- ▶ **Risk Diversification:-** To mitigate risk, banks should lend to a diversified customer base. Diversification should be in terms of geographic location, nature of business etc.



# DIFFERENT TYPES OF LOANS



ADDITIONAL  
SKILL ACQUISITION  
PROGRAMME



# INTRODUCTION.

A bank is an institution which accepts deposits from the public as well as lend money to the public.

From the definition itself it is clear that one of the primary function of a bank is lending of money. The main earnings of a banking institution is the interest from their customers(i.e., debtors). So, it is very essential to lend money to the public via loans and advances.

a loan is a debt provided by one entity to another entity at an interest rate ,For a specific period of time.



# PROCESS OF GRANTING A LOAN

Loan application

Submission of Required documents

CIBIL check

Approval of loan



# FORMS OF LOANS.

There are many forms of loans as follows:-

- ❑ Overdraft
- ❑ Cash credit
- ❑ Credit cards
- ❑ Housing loan
- ❑ Vehicle loans
- ❑ Education loan
- ❑ Personal loan
- ❑ Gold loan
- ❑ Festival loans
- ❑ Consumer loans
- ❑ Gold loans
- ❑ Loan against pension
- ❑ Loans to doctors for Opening clinic





# 1. OVER DRAFT

The word overdraft means the act of overdrawing from a Bank account. In other words, the account holder withdraws more

money from a Bank Account than has been deposited in it.



PHOTO: THINKSTOCK

## 2. CASH CREDIT

Cash Credit is one type of Advance made by Banks to its Borrowers. By granting this facility Bank allows borrower to withdraw money up to certain fixed amount sanctioned by the Bank. Certain securities and guarantees are to be provided by the borrower as per Bank's rules and it is to be renewed every year as specified at the time of granting this facility. If borrower fails to repay the amount Bank can take action as per rules and conditions fixed by banks.



### 3. HOUSING LOANS.

The basic needs of a human include, food, cloth, water, shelter and security. Housing is an important need. Banks provide different types of loans for building house known as **HOUSING LOANS**. There are different types of housing loans:-

- ❑ **Home purchase loan-** for purchase a new house.
- ❑ **Home construction loan-** construction of a house



□ **Home improvement loan-** for repair works and renovations of an existing house  
□ **Home extension loan-** for making extensions for the house i.e., building additional rooms, floors etc.  
□ **Land purchase loan-** purchase of land for building a house.



- **Home conversion loan-** for building a new house by loan during the payment of an existing home loan. New loan is added to the existing one.
- **Balance transfer loan-** existing home loan is transferred to another bank.
- **Bridge loan-** for those who wish to sell the existing house and buy or build a new one.

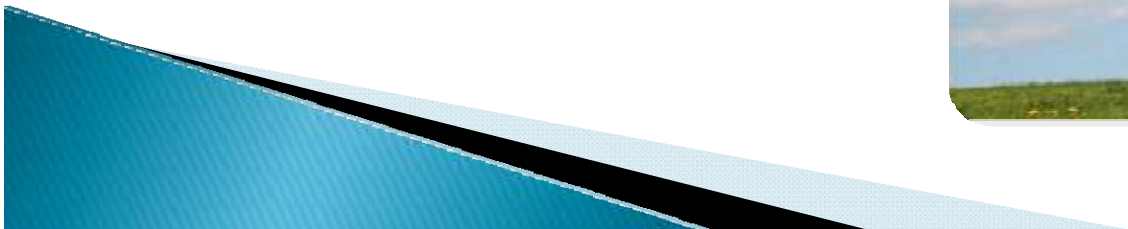


# 4.PERSONAL LOANS

Personal loans are intended to meet any kind of personal expenses.

The loan can be for any of the following purposes:-

- ❑ Family functions
- ❑ Meeting travel expenses in India or abroad
- ❑ Marriage expenses of children
- ❑ Buying a laptop / pc
- ❑ Interior decoration of house



# 5. VEHICLE LOANS

Vehicle loans particularly car loans are offered by all the banks in the country . the terms and conditions of vehicle loans vary from bank to bank . the purpose of vehicle loan is to finance for purchase of ;

- A. a new car , bike , scooter , jeep or MUVs
- B. a used car , bike , scooter , jeep (not more than 5 years old)
- C. Take over of existing vehicle loan from other bank or financial institution.



# 6. EDUCATION LOANS

The purpose of education loan is to provide better educational opportunity to bright and financially backward students and brings within their reach all types of education. Education loans are provided for pursuing plus two, graduation courses, PG courses and other professional courses. It can be availed for:

- A. Tuition fees payable to college
- B. Hostel fees
- C. Examination/ library / laboratory fees
- D. Purchase of books/equipment/instruments/uniforms
- E. Travel expenses
- F. Purchase of computer ,if it is necessary for completion of course.
- G. Cost of two wheeler upto Rs 50,000





## 7. AGRICULTURAL LOANS

It is always said that, most of the people India are depending agriculture or farming as their livelihood. So, it is very important to develop the rural sector. In order to fulfill that banks provides various credit facilities to the farmers. The loans are provided for:-

- ❖ Purchase of asset like farm machinery, bullocks, sheep etc.
- ❖ Creation of assets such as poultry, dairy development etc.
- ❖ For rural activities under agriculture, horticulture, plantation, animal husbandry fisheries etc.



# 8. CREDIT CARDS

Credit card is any card , plate or device that may be used from time to time and over and over again to borrow money or buy goods and services on credit. Credit card enable card holders to avail credit facilities for a specified period of time without giving any security to the issuing bank.



# PRINCIPLES OF SOUND LENDING



# Loan Policy

Based on the general principles of lending stated above, the Credit Policy Committee (CPC) of individual banks prepares the basic credit policy of the Bank, which has to be approved by the Bank's Board of Directors.

## **Lending Guidelines**

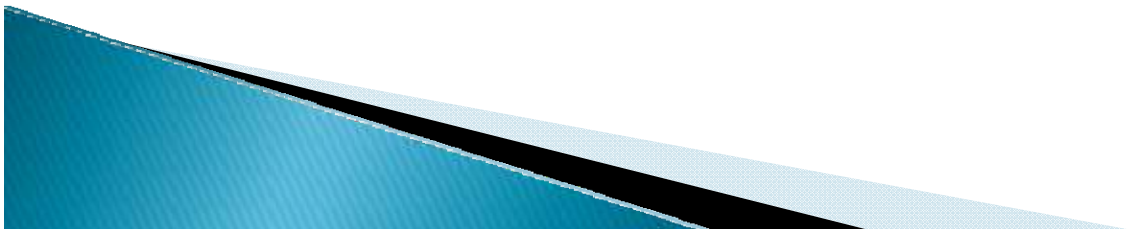
- ▶ •Level of credit-deposit ratio
- ▶ •Targeted portfolio mix
- ▶ •Hurdle ratings
- ▶ •Loan pricing
- ▶ •Collateral security



# CD Ratio

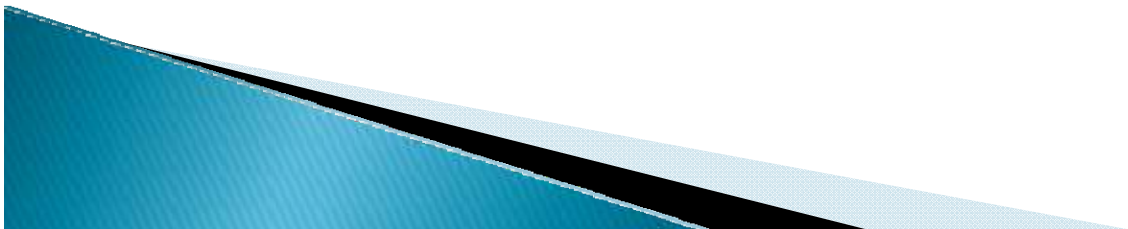
- A bank can lend out only a certain proportion of its deposits
- As Cash Reserve Ratio (CRR), and an additional part has to be used for making investment in prescribed securities i.e. Statutory Liquidity Ratio or SLR requirement

Therefore, the CPC has to lay down the quantum of credit that can be granted by the bank as a percentage of deposits available.



# Targeted Portfolio Mix

- ▶ The CPC aims at a targeted portfolio mix keeping in view both risk and return towards different sectors.
- ▶ It lays down guidelines on choosing the preferred areas of lending as well as the sectors to avoid. Banks typically monitor all major sectors
- ▶ They target a portfolio mix in the light of forecasts for growth and profitability for each sector.
- ▶ This entails active portfolio management.
- ▶ It may also like to avoid certain kinds of loans keeping in mind general credit discipline, say loans for speculative purposes, unsecured loans, etc.

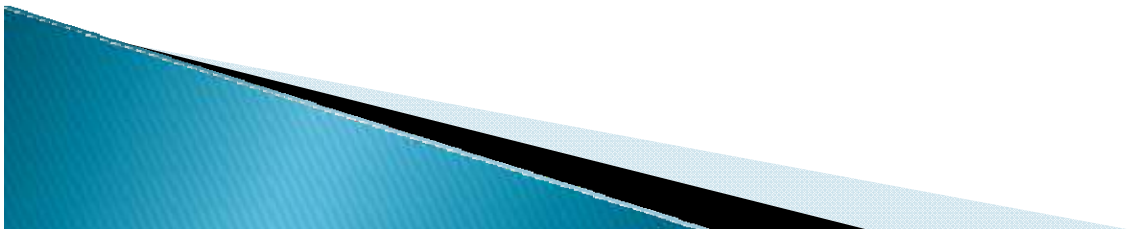


# Hurdle Ratings

There are a number of diverse risk factors associated with borrowers.

Banks should have a

- ▶ Comprehensive risk rating system that serves as a single point indicator of diverse risk factors of a borrower. This helps taking credit decisions in a consistent manner.
- ▶ A substantial degree of standardization is required in ratings across borrowers.
- ▶ The risk rating system should be so designed as to reveal the overall risk of lending.
- ▶ For new borrowers, a bank usually lays down guidelines regarding minimum rating to be achieved by the borrower to become eligible for the loan.



# Loan Pricing

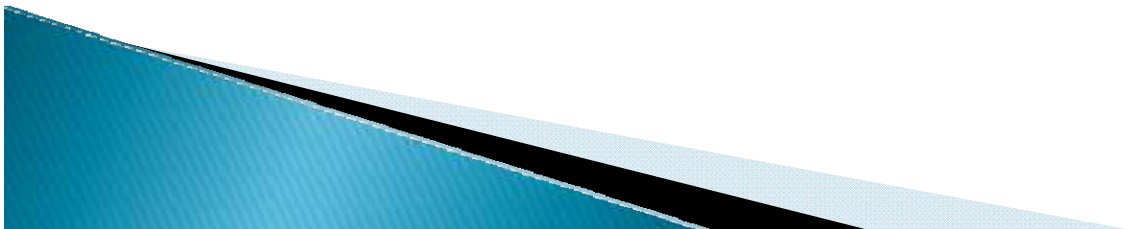
- ▶ Risk-return trade-off is a fundamental aspect of risk management. Borrowers with weak financial position and, hence, placed in higher risk category are provided credit facilities at a higher price (that is, at higher interest).
- ▶ The higher the credit risk of a borrower the higher would be his cost of borrowing.
- ▶ To price credit risks, if the risk rating of a borrower deteriorates, his cost of borrowing should rise and vice versa.
- ▶ At the macro level, loan pricing for a bank is dependent upon a number of its cost factors
- ▶ Loan pricing is also dependent upon competition.



# Collateral Security

- ▶ As part of a prudent lending policy, banks usually advance loans against some security. The loan policy provides guidelines for this.
- ▶ In the case of term loans and working capital assets, banks take as 'primary security' the property or goods against which loans are granted.
- ▶ Banks often ask for additional security or 'collateral security' in the form of both physical and financial assets to further bind the borrower.

This reduces the risk for the bank.

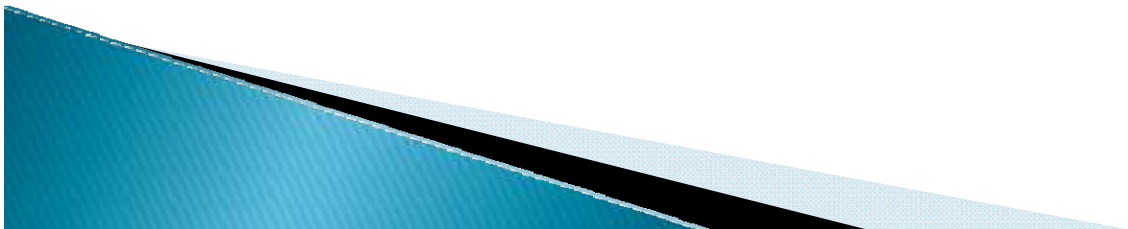




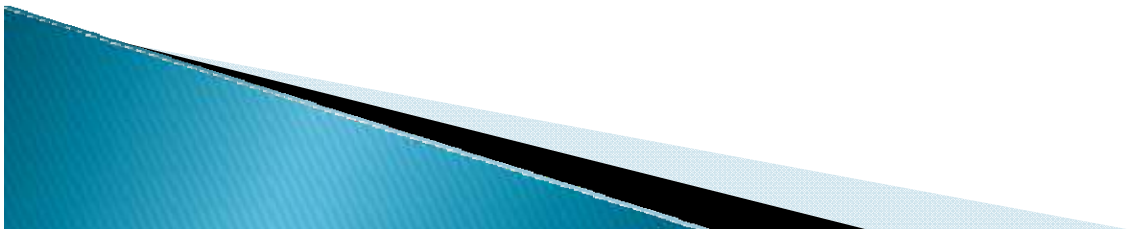
# Compliance with the RBI Guidelines

The credit policy of a bank should be conformant with RBI guidelines.

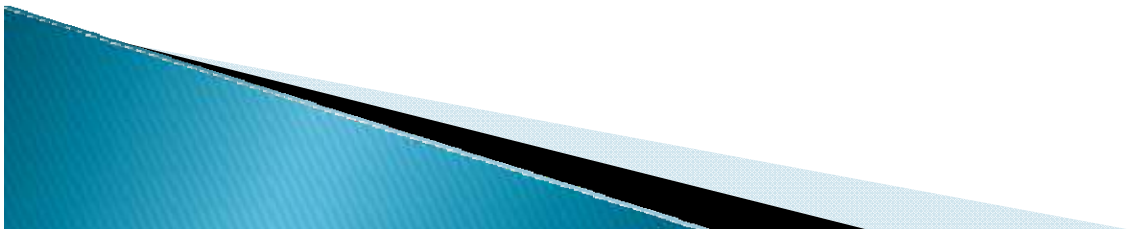
Directed Credit Stipulation:- The RBI lays down guidelines regarding minimum advances to be made for priority sector advances, export credit finance, etc. These guidelines need to be kept in mind while formulating credit policies for the Bank.



- ▶ **Capital Adequacy:-** If a bank creates assets-loans or investment-they are required to be backed up by bank capital; the amount of capital they have to be backed up by depends on the risk of individual assets that the bank acquires. The riskier the asset, the larger would be the capital it has to be.
- ▶ Through this bank capital provides a cushion against unexpected losses of banks.
- ▶ The Basel Committee for Bank Supervision (BCBS) has prescribed a set of norms for the capital requirement for the banks for all countries to follow. These norms ensure that capital should be adequate to absorb unexpected losses. In addition, all countries, including India, establish their own guidelines for risk based capital framework known as Capital Adequacy Norms. These norms have to be at least as stringent as the norms set by the Basel committee. A key norm of the Basel committee is the Capital Adequacy Ratio (CAR), also known as Capital Risk Weighted Assets Ratio, is a simple measure of the soundness of a bank.



- ▶ The ratio is the capital with the bank as a percentage of its risk-weighted assets. Given the level of capital available with an individual bank, this ratio determines the maximum extent to which the bank can lend.
- ▶ The Basel committee specifies a CAR of at least 8% for banks. This means that the capital funds of a bank must be at least 8 percent of the bank's risk weighted assets. In India, the RBI has specified a minimum of 9%, which is more stringent than the international norm. In fact, the actual ratio of all scheduled commercial banks (SCBs) in India stood at 13.2% in March 2009. The RBI also provides guidelines about how much risk weights banks should assign to different classes of assets (such as loans).
- ▶ This regulatory requirement that each individual bank has to maintain a minimum level of capital, which is commensurate with the risk profile of the bank's assets, plays a critical role in the safety and soundness of individual banks and the banking system.



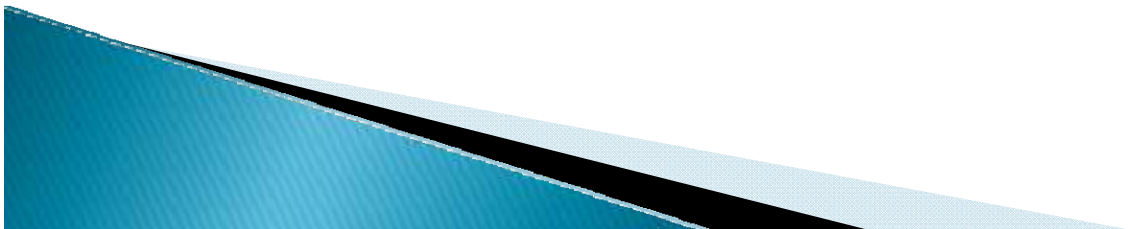
▶ **Credit Exposure Limits:-**


- ▶ For better risk management and avoidance of concentration of credit risks, the Reserve Bank has fixed limits on bank exposure to the capital market as well as to individual and group borrowers with reference to a bank's capital.
- ▶ Limits on inter-bank exposures have also been placed.
- ▶ Banks are further encouraged to place internal caps on their sectoral exposures, their exposure to commercial real estate and to unsecured exposures. These exposures are closely monitored by the Reserve Bank. Prudential norms on banks' exposures to NBFCs and to related entities are also in place.



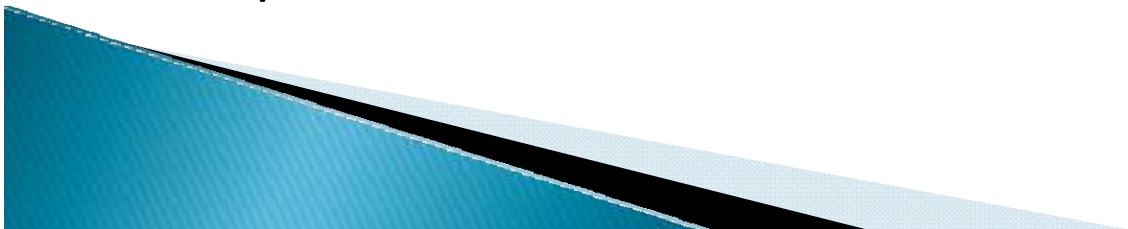
# Exposure Norms for Commercial Banks

- ▶ Single Borrower 15 per cent of capital fund (Additional 5 percent on infrastructure exposure)
- ▶ Group Borrower 40 percent of capital fund (Additional 10 percent on infrastructure exposure)
- ▶ NBFC 10 percent of capital fund
- ▶ NBFC - AFC 15 percent of capital fund
- ▶ Indian Joint Venture/Wholly owned 20 percent of capital fund subsidiaries abroad/ Overseas step down subsidiaries of Indian corporates

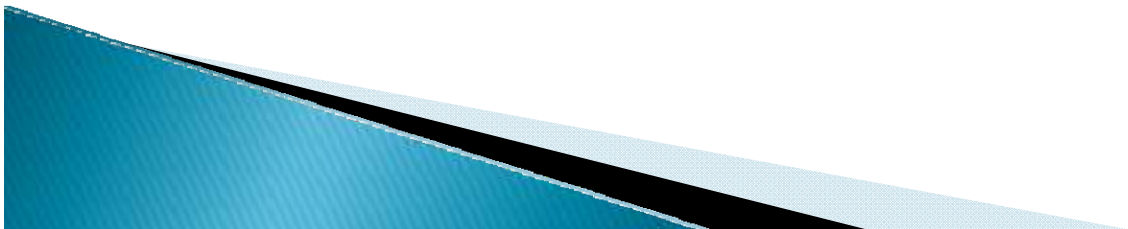


- ▶ Capital Market Exposure
  - ▶ (a) Banks' holding of shares in any The lesser of 30 percent of paid-up share
  - ▶ company capital of the company or 30 percent of the paid-up capital of banks
  - ▶ (b) Banks' aggregate exposure to 40 percent of its net worth capital market (solo basis)
  - ▶ (c) Banks' aggregate exposure to 40 percent of its consolidated net worth capital market (group basis)
  - ▶ (d) Banks' direct exposure to capital 20 percent of net worth market (solo basis)
  - ▶ (e) Banks' direct exposure to capital 20 percent of consolidated net worth market (group basis)
  - ▶ Gross Holding of capital among 10 per cent of capital fund banks / financial institutions
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- ▶ **Individual Borrowers:** A bank's credit exposure to individual borrowers must not exceed 15 % of the Bank's capital funds. Credit exposure to individual borrowers may exceed the exposure norm of 15 % of capital funds by an additional 5 % (i.e. up to 20 %) provided the additional credit exposure is on account of infrastructure financing.
- ▶ **Group Borrowers:** A bank's exposure to a group of companies under the same management control must not exceed 40% of the Bank's capital funds unless the exposure is in respect of an infrastructure project. In that case, the exposure to a group of companies under the same management control may be up to 50% of the Bank's capital funds.●

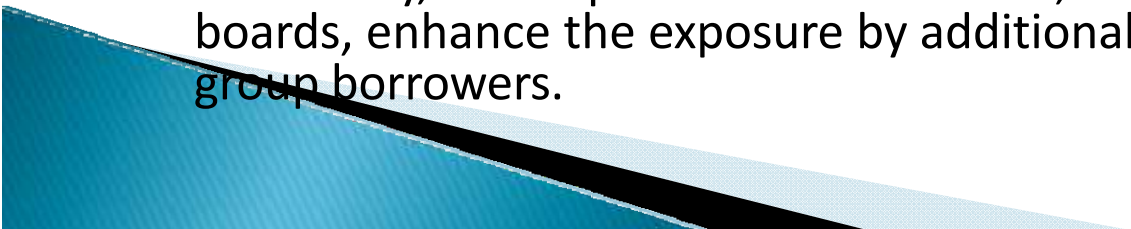


- ▶ **•Aggregate exposure to capital market:** A bank's aggregate exposure to the capital market, including both fund based and non-fund based exposure to capital market, in all forms should not exceed 40 percent of its net worth as on March 31 of the previous year.
- ▶ In addition to ensuring compliance with the above guidelines laid down by RBI, a Bank may fix its own credit exposure limits for mitigating credit risk. The bank may, for example, set upper caps on exposures to sensitive sectors like commodity sector, real estate sector and capital markets. Banks also may lay down guidelines regarding exposure limits to unsecured loans.

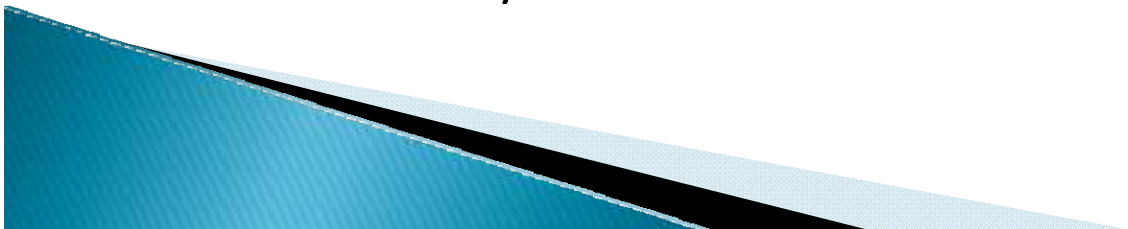




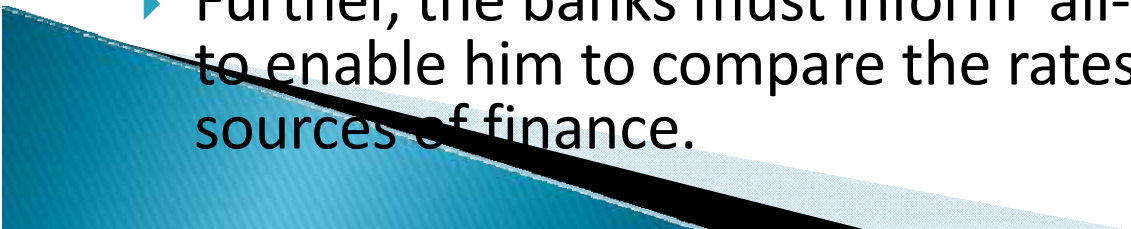
# Lending Rates

- ▶ Banks are free to determine their own lending rates on all kinds of advances except a few such as export finance; interest rates on these exceptional categories of advances are regulated by the RBI.
  - ▶ It may be noted that the Section 21A of the BR Act provides that the rate of interest charged by a bank shall not be reopened by any court on the ground that the rate of interest charged is excessive.
  - ▶ The concept of benchmark prime lending rate (BPLR) was however introduced in November 2003 for pricing of loans by commercial banks with the objective of enhancing transparency in the pricing of their loan products.
  - ▶ A bank's BPLR is the interest rate to be charged to its best clients; that is, clients with the lowest credit risk.
  - ▶ However, BPLR lost its relevance over time as a meaningful reference rate, as the bulk of loans were advanced below BPLR. The RBI therefore set up a Working Group on Benchmark Prime Lending Rate (BPLR) in June 2009 to go into the issues relating to the concept of BPLR and suggest measures to make credit pricing more transparent.
  - ▶ Banks may, in exceptional circumstances, with the approval of their boards, enhance the exposure by additional 5% for both individual, and group borrowers.
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- ▶ Following the recommendations of the Group, the Reserve Bank has issued guidelines in February 2010.
- ▶ According to these guidelines, the 'Base Rate system' will replace the BPLR system with effect from July 01, 2010.
- ▶ All categories of loans should henceforth be priced only with reference to the Base Rate. Each bank will decide its own Base Rate.
- ▶ The actual lending rates charged to borrowers would be the Base Rate plus borrower-specific charges, which will include product specific operating costs, credit risk premium and tenor premium.
- ▶ Since transparency in the pricing of loans is a key objective, banks are required to exhibit the information on their Base Rate at all branches and also on their websites.
- ▶ Changes in the Base Rate should also be conveyed to the general public from time to time through appropriate channels.
- ▶ Apart from transparency, banks should ensure that interest rates charged to customers in the above arrangement are non-discriminatory in nature.

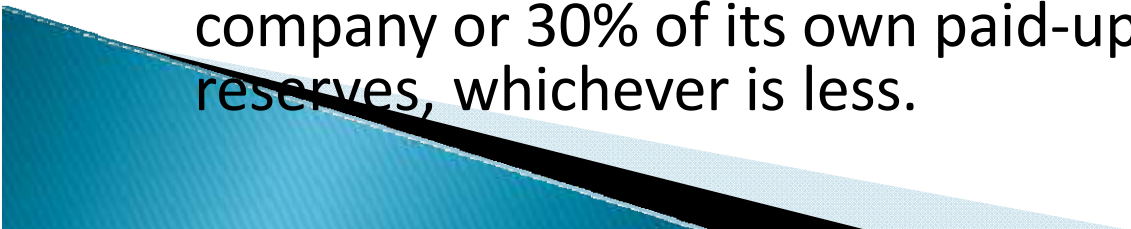


# Guidelines on Fair Practices Code for Lenders

- ▶ RBI has been encouraging banks to introduce a fair practices code for bank loans.
  - ▶ Loan Application forms in respect of all categories of loans irrespective of the amount of loan sought by the borrower should be comprehensive.
  - ▶ It should include information about the fees/ charges, if any, payable for processing the loan, the amount of such fees refundable in the case of non-acceptance of application, prepayment options and any other matter which affects the interest of the borrower, so that a meaningful comparison with the fees charged by other banks can be made and informed decision can be taken by the borrower.
  - ▶ Further, the banks must inform 'all-in-cost' to the customer to enable him to compare the rates charged with other sources of finance.
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# Regulations relating to providing loans

The provisions of the Banking Regulation Act, 1949 (BR Act) govern the making of loans by banks in India. RBI issues directions covering the loan activities of banks. Major guidelines of RBI:

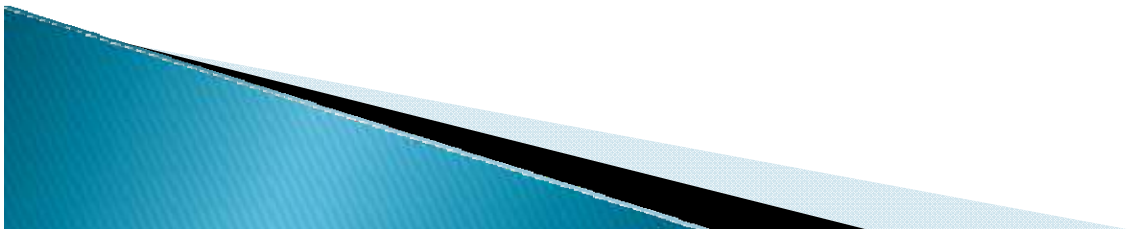
- ▶ •Advances against bank's own shares: a bank cannot grant any loans and advances against the security of its own shares.
  - ▶ •Advances to bank's Directors: The BR Act lays down the restrictions on loans and advances to the directors and the firms in which they hold substantial interest.
  - ▶ Restrictions on Holding Shares in Companies: In terms of Section 19(2) of the BR Act, banks should not hold shares in any company except as provided in sub-section (1) whether as pledgee, mortgagee or absolute owner, of an amount exceeding 30% of the paid-up share capital of that company or 30% of its own paid-up share capital and reserves, whichever is less.
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## II. Basics of Loan Appraisal, Credit Decision-Making and Review:



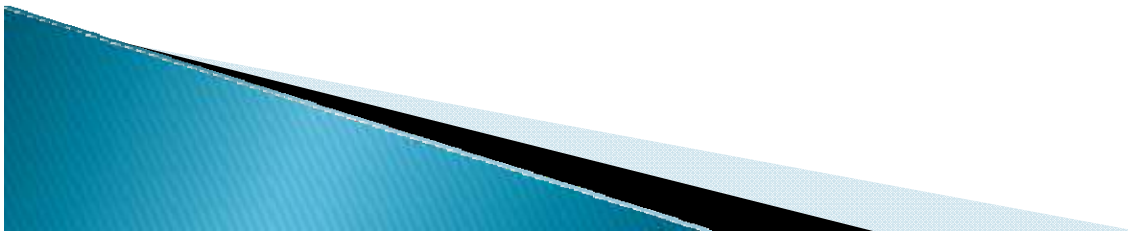
- ▶ **Credit Approval Authorities**
- ▶ The Bank's Board of Directors also has to approve the delegation structure of the various credit approval authorities. Banks establish multi-tier credit approval authorities for corporate banking activities, small enterprises, retail credit, agricultural credit, etc.
- ▶ Concurrently, each bank should set up a Credit Risk Management Department (CMRD), being independent of the CPC. The CRMD should enforce and monitor compliance of the risk parameters and prudential limits set up by the CPC.

- ▶ Credit approving authority: multi-tier credit approving system with a proper scheme of delegation of powers.
- ▶ • In some banks, high valued credit proposals are cleared through a Credit Committee approach consisting of, say 3/ 4 officers. The Credit Committee should invariably have a representative from the CRMD, who has no volume or profit targets.



- ▶ **Credit Appraisal & Credit Decision Making**

When a loan proposal comes to the bank, the banker has to decide how much funds does the proposal really require for it to be a viable project and what are the credentials of those who are seeking the project. In checking the credentials of the potential borrowers, Credit Information Bureaus play an important role



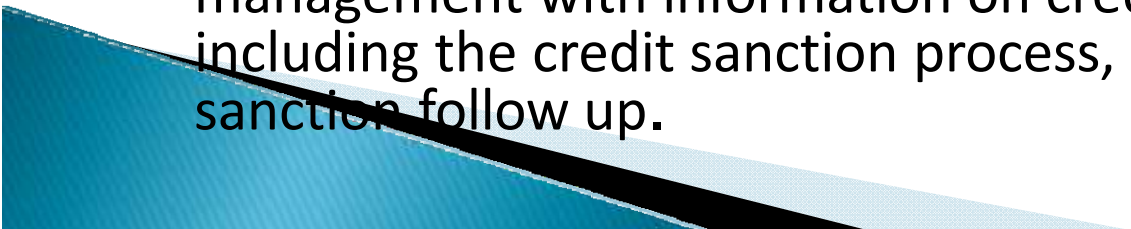
# Credit Information Bureaus

The Parliament of India has enacted the Credit Information Companies (Regulation) Act, 2005, pursuant to which every credit institution, including a bank, has to become a member of a credit information bureau and furnish to it such credit information as may be required of the credit institution about persons who enjoy a credit relationship with it.

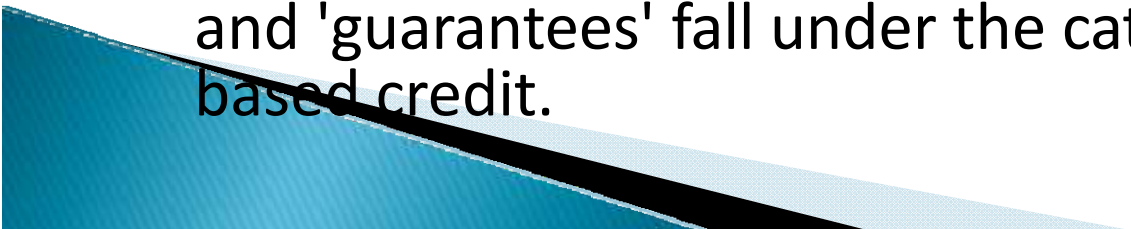
- ▶ Credit information bureaus are thus repositories of information, which contains the credit history of commercial and individual borrowers. They provide this information to their Members in the form of credit information reports.
- ▶ Credit information bureaus collect commercial and consumer credit related data and collate such data to create credit reports, which they distribute to their Members.
- ▶ A Credit Information Report (CIR) is a factual record of a borrower's credit payment history compiled from information received from different credit grantors. Its purpose is to help credit grantors make informed lending decisions - quickly and objectively. As of today, bureaus provide history of credit card holders and SMEs.



# Monitoring and Review of Loan Portfolio

- ▶ It is not only important for banks to follow due processes at the time of sanctioning and disbursing loans, it is equally important to monitor the loan portfolio on a continuous basis.
  - ▶ Banks need to constantly keep a check on the overall quality of the portfolio. They have to ensure that the borrower utilizes the funds for the purpose for which it is sanctioned and complies with the terms and conditions of sanction.
  - ▶ Banks have set up Loan Review Departments or Credit Audit Departments in order to ensure compliance with extant sanction and post-sanction processes and procedures laid down by the Bank from time to time. This is especially applicable for the larger advances.
  - ▶ The Loan Review Department helps a bank to improve the quality of the credit portfolio by detecting early warning signals, suggesting remedial measures and providing the top management with information on credit administration, including the credit sanction process, risk evaluation and post-sanction follow up.
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### *III. Types of Advances:*

- ▶ Fund Based Lending:- This is a direct form of lending in which a loan with an actual cash outflow is given to the borrower by the Bank. In most cases, such a loan is backed by primary and/or collateral security. The loan can be to provide for financing capital goods and/or working capital requirements.
  - ▶ Non-Fund Based Lending:- In this type of facility, the Bank makes no funds outlay. However, such arrangements may be converted to fund-based advances if the client fails to fulfill the terms of his contract with the counterparty. Such facilities are known as contingent liabilities of the bank. Facilities such as 'letters of credit' and 'guarantees' fall under the category of non-fund based credit.
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# Fund Based Lending

- ▶ Working Capital Finance

- 1.Short-term loan component

- 2.Cash credit component

- ▶ Project Finance

- ▶ Loans to Small & Medium Enterprises

- ▶ Rural & Agricultural Loans

- ▶ Directed Lending

1. Priority Sector Lending

2. Export Credit

- ▶ Retail Loan

- 1.Home Finance

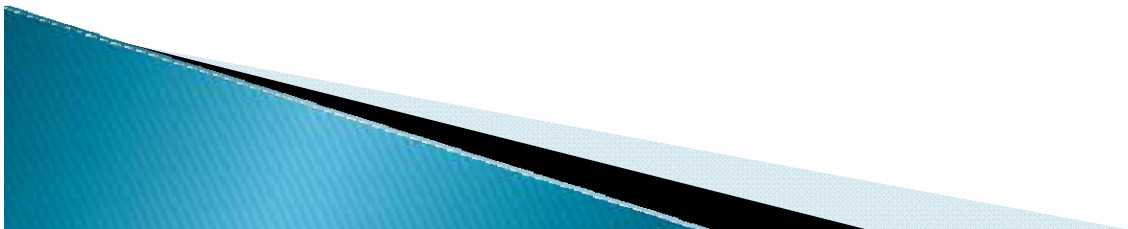
- 2.Personal Loans

- ▶ International Loans Extended by Banks




## ***IV. Management of Non-Performing Assets***

An asset of a bank (such as a loan given by the bank) turns into a non-performing asset (NPA) when it ceases to generate regular income such as interest etc for the bank. In other words, when a bank which lends a loan does not get back its principal and interest on time, the loan is said to have turned into an NPA

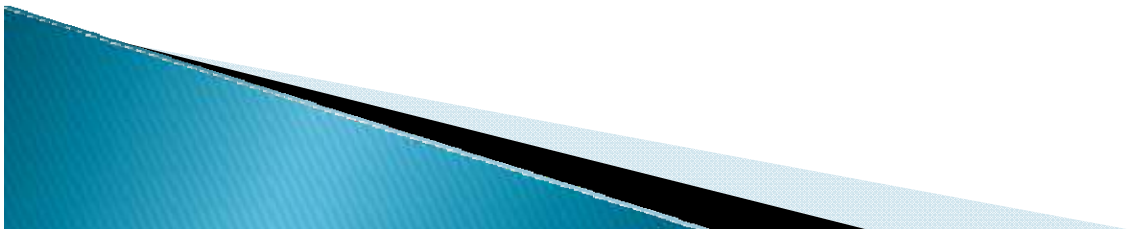


# Level of Non Performing Assets

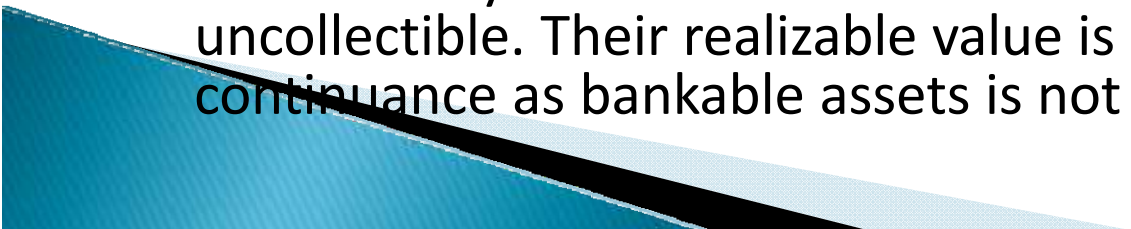
- ▶ The gross non-performing assets of the banking segment were Rs. 68, 973 crores at the end of March 2009, and the level of net NPAs (after provisioning) was Rs.31, 424 crores.
  - ▶ The ratio of gross non-performing loans to gross total loans has fallen sharply over the last decade and is at 2.3 per cent as at end-March 2009.
  - ▶ This ratio, which is an indicator of soundness of banks, is comparable with most of the developed countries such as France, Germany and Japan.
  - ▶ The low level of gross NPAs as a percent of gross loans in India is a positive indicator of the Indian banking system
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# Classification of Non-Performing Assets

- ▶ According to the RBI guidelines, banks must classify their assets on an on-going basis into the following four categories:
- ▶ Standard Assets- Sub- standard, Doubtful & Loan Assets
- ▶ Debt Restructuring
- ▶ Other recovery options
- ▶ SARFAESI Act, 2002



# Standard Assets

- ▶ Standard assets service their interest and principal installments on time; although they occasionally default up to a period of 90 days. Standard assets are also called performing assets. They yield regular interest to the banks and return the due principal on time and thereby help the banks earn profit and recycle the repaid part of the loans for further lending. The other three categories are discussed below.
  - ▶ Sub-standard assets: Sub-standard assets are those assets which have remained NPAs (that is, if any amount of interest or principal installments remains overdue for more than 90 days) for a period up to 12 months.
  - ▶ Doubtful assets: An asset becomes doubtful if it remains a sub-standard asset for a period of 12 months and recovery of bank dues is of doubtful.
  - ▶ Loss assets: Loss assets comprise assets where a loss has been identified by the bank or the RBI. These are generally considered uncollectible. Their realizable value is so low that their continuance as bankable assets is not warranted.
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# Debt Restructuring

- ▶ Once a borrower faces difficulty in repaying loans or paying interest, the bank should initially address the problem by trying to verify whether the financed company is viable in the long run. If the company/ project is viable, then rehabilitation is possible by restructuring the credit facilities. In a restructuring exercise, the bank can change the repayment or interest payment schedule to improve the chances of recovery or even make some sacrifices in terms of waiving interest etc.
- ▶ RBI has separate guidelines for restructured loans. A fully secured standard/ sub-standard/ doubtful loan can be restructured by rescheduling of principal repayments and/or the interest element. The amount of sacrifice, if any, in the element of interest, is either written off or provision is made to the extent of the sacrifice involved. The sub-standard accounts/doubtful accounts which have been subjected to restructuring, whether in respect of principal instalment or interest amount are eligible to be upgraded to the standard category only after a specified period.
- ▶ To create an institutional mechanism for the restructuring of corporate debt, RBI has devised a Corporate Debt Restructuring (CDR) system. The objective of this framework is to ensure a timely and transparent mechanism for the restructuring of corporate debts of viable entities facing problems.



# Other recovery options

- ▶ If rehabilitation of debt through restructuring is not possible, banks themselves make efforts to recover. For example, banks set up special asset recovery branches which concentrate on recovery of bad debts. Private and foreign banks often have a collections unit structured along various product lines and geographical locations, to manage bad loans. Very often, banks engage external recovery agents to collect past due debt, who make phone calls to the customers or make visits to them. For making debt recovery, banks lay down their policy and procedure in conformity with RBI directives on recovery of debt.
- ▶ The past due debt collection policy of banks generally emphasizes on the following at the time of recovery:
  - ▶ •Respect to customers
  - ▶ •Appropriate letter authorizing agents to collect
  - ▶ •Due notice to customers
  - ▶ •Confidentiality of customers' dues
  - ▶ •Use of simple language in communication and maintenance of records of communication
- ▶ In difficult cases, banks have the option of taking recourse to filing cases in courts, Lok Adalats,
- ▶ Debt Recovery Tribunals (DRTs), One Time Settlement (OTS) schemes, etc. DRTs have been established under the Recovery of Debts due to Banks and Financial Institutions Act, 1993 for expeditious adjudication and recovery of debts that are owed to banks and financial institutions.
- ▶ Accounts with loan amount of Rs. 10 lakhs and above are eligible for being referred to DRTs.
- ▶ OTS schemes and Lok Adalats are especially useful to NPAs in smaller loans in different segments, such as small and marginal farmers, small loan borrowers and SME entrepreneurs. If a bank is unable to recover the amounts due within a reasonable period, the bank may write off the loan. However, even in these cases, efforts should continue to make recoveries.

# SARFAESI Act, 2002

- ▶ Banks utilize the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI) as an effective tool for NPA recovery. It is possible where non-performing assets are backed by securities charged to the Bank by way of hypothecation or mortgage or assignment. Upon loan default, banks can seize the securities (except agricultural land) without intervention of the court.
- ▶ The SARFAESI Act, 2002 gives powers of "seize and desist" to banks. Banks can give a notice in writing to the defaulting borrower requiring it to discharge its liabilities within 60 days. If the borrower fails to comply with the notice, the Bank may take recourse to one or more of the following measures:
  - ▶ •Take possession of the security for the loan
  - ▶ •Sale or lease or assign the right over the security
  - ▶ •Manage the same or appoint any person to manage the same
- ▶ The SARFAESI Act also provides for the establishment of asset reconstruction companies regulated by RBI to acquire assets from banks and financial institutions.
- ▶ The Act provides for sale of financial assets by banks and financial institutions to asset reconstruction companies (ARCs). RBI has issued guidelines to banks on the process to be followed for sales of financial assets to ARCs.

**THANK YOU**

