FIDC

Finance Industry Development Council

(A Representative Body of Assets and Loan Financing NBFCs)

101/103, Sunflower, 1st Floor, Rajawadi Road No.2, Ghatkopar (East), Mumbai – 400 077

Tel: 022 21029898/9820035553 • E-mail: directorgeneral@fidcindia.org Website: www.fidcindia.org

Shri Shaktikanta Das
Governor
Reserve Bank of India
Central Office Building
Shahid Bhagat Singh Marg
Fort, Mumbai – 400 001.

May 15, 2020

Respected Sir,

RELIEF IN TERMS OF ONE-TIME RESTRUCTURING AND ASSET CLASSIFICATION AND PROVISIONING UNDER IndAS

At the outset, we express our grateful thanks for the patient hearing provided to us on 4th May, 20 and we have shared the difficulties faced by our members, retail NBFCs who primarily cater to the funding needs of MSMEs, truck/taxi drivers, machine operators and marginal farmers and provide loans for acquiring the vehicles/tractors/equipments for productive purposes and these customers are mostly new to credit and having very little/no banking history. These are also the customers who earn and pay and therefore most vulnerable in any economic cycle and in the present pandemic, they have been mostly locked down and unable to deploy their assets and make even their two ends meet. While we have provided the moratorium to all our customers and more than 80% of them have opted for it, we feel that with extended lock down till 17th May all over India and expected phased opening of the markets from 18th May onwards, it will take quite a while for our customers to return to normalcy and deploy their assets and earn revenue and pay the instalments.

The feedback from most of our members across India is that our retail customers in the tier towns and rural areas are seeking much more than 3 months moratorium to restart the payment and also seeking lower EMIs in the current environment so that they do not default and seek extension in the overall tenure. On the other hand, these customers have also been seeking working capital support from our NBFC members to restart their operations and replace tires, Mobil/filter and pay to their drivers/cleaners to get them back on duty and provide the vehicles and equipment on site for deployment. It is only fair that in the current uncertain environment, we evaluate and provide case on case, the request for extension in original tenure of the loans and also lower the EMI obligation during FY21 to ease the burden on the informal segment customers that we cater to as well as provide working capital support so that they can restart their operations.

In respect of the above, RBI has been kind enough to allow 3 months' moratorium as per 27th March circular and then also allowed standstill on existing overdues in standard accounts as per 17th April circular and it has provided some relief to the NBFCs which have provided moratorium to their own customers.

However, given the extension in lock down twice till 18th May and very bleak scenario for full revival of the economy which will take place over next few quarters, we humbly submit for your kind consideration the following relief to manage the circumstances arising out of Covid-19:

1. **Request to Allow One Time Restructuring of Loans:**

Given the requirement to provide cash flow relief to our customers during the Financial Year 2020-21 and extend the moratorium period beyond May, 2020 and also reduce the EMI obligation for few months post the lock down, we request to allow a one-time restructuring of all the loan accounts including extension of loan tenure by the NBFCs as per the board approved policies.

RBI had allowed onetime restructuring of standard MSME advances without any downgrade, though with additional provision of 5%, vide Circular No. DOR.No.BP.BC.34/21.04.048/2019-20 dated February 11, 2020 read with DBR.No.BP.BC.18/21.04.048/2018-19 dated January 1, 2019. The economy is in a far worse state today due to the impact of COVID-19 and therefore requires more financial considerations and support.

***<u>Request</u>*:**

<u>It is therefore requested to allow a one-time window for restructuring of all the Loans. This facility is currently available for loans to MSMEs (as per RBI Circular dt. 11th February 2020) and could now be considered for all other borrowers as well, given the environment. This restructuring may kindly be allowed without the need for a 5% provisioning as mandated by the current scheme.</u>

2. <u>Request to allow utilising Reserves to make additional provision for COVID19:</u>

RBI has vide its circular dt 17th April, 2020 advised NBFCs which follow Ind AS accounting to be guided by the board approved guidelines in terms of asset classification and provisioning and as per ICAI advisories for recognition of the impairments. The ICAI has vide its advisory dt. 31st March, 2020 advised measuring the impact of Covid-19 on the portfolio quality in the form of risk of default (PD), estimated amount of default (LGD) with adverse impact on the business of the borrowers or debtors due to Covid-19 on one hand and prudential regulatory actions to sustain the economy such as loan repayment holidays, reduction in interest rates etc. on the other hand. As per Ind AS 109 and Ind AS 107 both of which are applicable in respect of ECL measurement and disclosure in the financial statements, the NBFCs will be required to make additional provisioning in terms of ICAI advisory and it will surely make a severe dent on the profitability and net worth of the respective NBFCs particularly considering the impact of Covid-19 on the vulnerable sections of society viz. daily wage earners and informal segment self-employed customers and marginal farmers.

NBFCs appropriate profits to Statutory (earmarked) and Other Reserves. Utilization of these Reserves is governed by the statute requiring its creation. The pre-existing economic slow-down with its significant impact on NBFC/HFCs loan book further exacerbated by the Covid-19 is an unprecedented adverse event for the financial sector. There is an imminent need for extra ordinary measures to deal with the emergent situation.

While NBFCs would create normal ECL provisions out of their current year profits, we urge upon RBI to consider, as a one-time measure, to allow NBFCs to draw-down from their Reserves including those also created under section 45-IC of the RBI Act and adjust towards additional ECL provision requirement, in excess of provision calculated as per normal Probability of Default (PD) and Loss given Default (LGD). This will enable the NBFCs to shore-up their balance sheet strength by reporting a more fortified ECL provision cover against their likely increase in delinquent loans and remain eligible to access equity/debt capital when situation normalizes.

Request:

RBI may favourably consider allowing one-time draw-down from Statutory Reserves and Other Reserves with the approval of the Board of Directors of the NBFCs to be adjusted to enhance ECL provision, in excess of provision calculated as per normal Probability of Default (PD) and Loss given Default (LGD).

3. To allow Stage 2 provision to be included for calculation of Tier II Capital

The RBI Circular on Implementation of Indian Accounting Standards dated March 13, 2020, requires that lifetime ECL shall not be reckoned for regulatory capital (numerator) while it shall be reduced from the risk weighted assets. Under Ind-AS, lifetime ECL is computed where the NBFC determines that there is a significant increase in credit risk and is relevant for both stage 2 (31 to 90 days overdue) and stage 3 (over 90 days overdue) assets. In respect of stage 2 assets that are delinquent but not classified as NPA, ECL provisions are invariably much higher (on an average 2%) than the comparable 0.40% standard asset provisions as applicable under the RBI IRAC norms. Hence, NBFCs are not only required to make higher provisions under ECL but are also denied the benefit of treating this provision as Tier II, which is available under the IRAC norms.

Request:

RBI may, therefore, consider permitting any provisions made as per ECL, in respect of the standard assets to be reckoned with for the purpose of Tier II capital.

4. Request to increase Ceiling on including Standard Assets Provision for Tier II capital:

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For Capital Adequacy calculation, the extant RBI guidelines cap utilization of standard assets provision at 1.25%. The ceiling of 1.25% was set up in the context of the Standard Assets provisioning @ 0.40% under IRAC norms.

The standard asset provisioning has substantially increased under Ind AS and shall further increase as NBFCs make additional provisions under RBI circulars dated March 27 and April 17, 2020. The NBFC would need support to maintain / augment capital while they fortify their Balance Sheet by making additional provisioning.

Request:

Increase the ceiling of 1.25% for considering standard asset provision for calculation of Capital Adequacy to 2.50% for NBFCs following provisioning norms under IndAS. This shall be in tune with the stricter provisioning norms under IndAS.

We sincerely appeal to the Reserve Bank of India to consider these measures to help NBFCs manage the current situation and to enable them to play a due role in the economy rebuilding efforts.

Thanking you,

Yours faithfully,

For FINANCE INDUSTRY DEVELOPMENT COUNCIL

MAHESH THAKKAR
DIRECTOR GENERAL
98200 35553