



भारतीय रिजर्व बैंक

RESERVE BANK OF INDIA

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September 1, 2016

All Scheduled Commercial Banks
(Excluding Regional Rural Banks)

Dear Sir,

Guidelines on Sale of Stressed Assets by Banks

The Reserve Bank of India, as part of the Framework for Revitalising Distressed Assets in the Economy, had amended certain guidelines relating to sale of non-performing assets (NPAs) by banks to Securitisation Companies (SCs)/ Reconstruction Companies (RCs) (created under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002) vide circular dated February 26, 2014.

2. In order to further strengthen banks' ability to resolve their stressed assets effectively, it has been decided to put in place an improved framework governing sale of such assets by banks to SCs/RCs/other banks/Non Banking Financial Companies /Financial Institutions etc. Detailed guidelines are contained in the Annex.

Yours faithfully,

(Ajay Kumar Choudhary)
Chief General Manager

Guidelines on Sale of Stressed Assets by Banks

Policy on Sale of stressed assets

In terms of extant instructions of the Reserve Bank, the board of banks shall lay down detailed policies and guidelines on sale of their stressed assets to Securitisation Companies (SCs)/Reconstruction Companies (RCs). The policy, inter alia, shall cover the following aspects:

- i. Financial assets to be sold;
- ii. Norms and procedure for sale of such financial assets;
- iii. Valuation procedure to be followed to ensure that the realisable value of financial assets is reasonably estimated;
- iv. Delegation of powers of various functionaries for taking decision on the sale of the financial assets; etc.

2. In order to enhance transparency in the entire process of sale of stressed assets, it is decided as under:

- Identification of stressed assets beyond a specified value, as may be determined by bank's policy, for sale shall be top-down i.e., the head office/corporate office of the bank shall be actively involved in identification of stressed assets, including assets which are classified as Special Mention Account, to be put on sale. Early identification will help in low vintage and better price realisation for banks;
- At least once in a year, preferably at the beginning of the year, banks shall, with the approval of their Board, identify and list internally the specific financial assets identified for sale to other institutions, including SCs/RCs;
- At a minimum, all assets classified as 'doubtful asset' above a threshold amount should be reviewed by the board/board committee on periodic basis and a view, with documented rationale, is to be taken on exit or otherwise. The assets identified for exit shall be listed for the purpose of sale as indicated above;
- Prospective buyers need not be restricted to SCs/RCs. Banks may also offer the assets to other banks/NBFCs/FIs, etc. who have the necessary capital

and expertise in resolving stressed assets. Participation of more buyers will result in better price discovery;

- In order to attract a wide variety of buyers, the invitation for bids should preferably be publicly solicited so as to enable participation of as many prospective buyers as possible. In such cases, it would be desirable to use e-auction platforms. An open auction process, apart from attracting a larger set of borrowers, is expected to result in better price discovery.. Banks should lay down a Board approved policy in this regard;
- Banks must provide adequate time for due diligence by prospective buyers which may vary as per the size of the assets, with a floor of two weeks;
- Banks should have clear policies with regard to valuation of assets proposed to be sold. In particular it must be clearly specified as to in which cases internal valuation would be accepted and where external valuation would be needed. However, in case of exposures beyond Rs.50 crore, banks shall obtain two external valuation reports;
- The cost of valuation exercise shall be borne by the bank, to ensure that the bank's interests are protected;
- The discount rate used by banks in the valuation exercise shall be spelt out in the policy. This may be either cost of equity or average cost of funds or opportunity cost or some other relevant rate, subject to a floor of the contracted interest rate and penalty, if any.

3. Banks shall review the efficacy of their extant policies on sale of NPAs, with focus on valuation of stressed assets, and rework their policies by appropriately adopting the above principles.

Investment by banks in security receipts backed by assets sold by them

4. In order to make sure that sale of stressed assets by banks actually result in 'true sale' of assets and to create a vibrant stressed assets market, it has been decided to progressively restrict banks' investment in SRs backed by their own stressed assets.

- i) With effect from April 1, 2017, where the investment by a bank in SRs backed by stressed assets sold by it, under an asset securitisation, is more than 50 percent of SRs backed by its sold assets and issued under that securitisation, the provisions held in respect of these SRs will be

subject to a floor; this floor shall be progressive provisioning as per extant asset classification and provisioning norms, notionally treating book value of these SRs as the corresponding stressed loans, assuming these had remained, without recovery of principal, on the bank's books. In effect, provisioning requirement on SRs will be higher of the:

- a. provisioning rate required in terms of net asset value declared by the SCs/RCs; and
 - b. provisioning rate as applicable to the underlying loans, assuming that the loans notionally continued in the books of the bank;
- ii) With effect from April 1, 2018, the above threshold of 50 percent will stand reduced to 10 percent.

Disclosure of Investment in SRs

5. In addition to the existing disclosure requirements, banks shall make following disclosures pertaining to their investments in security receipts:

Particulars		SRs issued within past 5 years	SRs issued more than 5 years ago but within past 8 years	SRs issued more than 8 years ago
(i)	Book value of SRs backed by NPAs sold by the bank as underlying			
	Provision held against (i)			
(ii)	Book value of SRs backed by NPAs sold by other banks / financial institutions / non-banking financial companies as underlying			
	Provision held against (ii)			
Total (i) + (ii)				

Debt Aggregation – First right of refusal

6. To enhance SC/RCs ability to aggregate debt faster, a bank offering stressed assets for sale shall offer the first right of refusal to a SC/RC which has already acquired the highest and at the same time a significant share (~25-30%) of the asset, for acquiring the asset by matching the highest bid. This requires the process of price discovery via auction, as described elsewhere, to be done first.

Swiss Challenge Method – Enabling Low Vintage and Debt aggregation

7. In order to bring down the vintage of NPAs sold by banks as well as to enable faster debt aggregation by SC/RCs, banks shall put in place board approved policy on adoption of Swiss Challenge Method for sale of their stressed assets to SCs/RCs/other banks/NBFCs/FIs, etc. For this purpose, as indicated in paragraph 2 of this circular, the board/committee of the board shall conduct periodic review (at least once in a year) of their stressed - asset portfolio, with a view to decide on the proposed course of action to resolve the portfolio in terms of their loan recovery policy. During such review, the bank should identify the assets which will be offered for sale among prospective buyers and an authenticated list of such assets shall be maintained by the bank. The list may, at the discretion of the bank, be disclosed to prospective bidder on entering into confidentiality agreement. The broad contours of the Swiss Challenge Method are as under:

- I. A prospective buyer interested in buying a specific stressed asset may offer a bid to the bank;
- II. If the asset features in the list of assets for sale maintained by the bank, and if the aforesaid bidder offers more than the minimum percentage specified in the bank's policy (say, 30 percent of outstanding loan) in the form of cash, the bank shall be required to publicly call for counter bids from other prospective buyers, on comparable terms;
- III. Once bids are received, the bank shall first invite the SC/RC, if any, which has already acquired highest significant stake (as indicated at paragraph 6 above) to match the highest bid. Ceteris paribus, the order of preference to sell the asset shall be as follows: i) The SC/RC which has already acquired highest significant stake; ii) The original bidder and iii) The highest bidder during the counter bidding process.
- IV. Bank will have the following two options:
 - i. Sell the asset to winning bidder, as determined above;
 - ii. If the bank decides not to sell the asset to winning bidder, bank will be required to make immediate provision on the account to the extent of the higher of:
 - a) The discount on the book value quoted by the highest bidder; and

- b) The provisioning required as per extant asset classification and provisioning norms.

Buy-Back of Financial Assets

8. The extant guidelines of Reserve Bank do not prohibit banks from taking over standard accounts from SCs/RCs. Accordingly, in cases where SCs/RCs have successfully implemented a restructuring plan for the stressed assets acquired by them, banks may, at their discretion, with appropriate due diligence, take over such assets after the 'specified period' (as defined in terms of extant guidelines on restructuring) provided that the account performed satisfactorily during the 'specified period'. Banks may frame a board approved policy containing various aspects governing such take over viz., type of assets that may be taken over, due diligence requirements, viability criteria, performance requirement of asset, etc. However, a bank cannot at any point of time take over from SCs/RCs the assets they have themselves earlier sold.
