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Resolution Framework For Covid-19-Related Stress

With the loan moratorium extended by the Reserve Bank of India (**RBI**) on account of COVID-19 expiring on 31st August, the RBI has provided yet another breather to the corporates and individuals facing the brunt of economic fallout due to COVID-19, by introducing one-time restructuring scheme vide '*Resolution Framework for COVID-19-related Stress*' dated August 06, 2020 **(Restructuring Framework).**

The Restructuring Framework has come as a window under the existing Reserve Bank of India (Prudential Framework for Resolution of Stressed Assets) Directions, 2019 (**Prudential Framework**), to enable the lenders, to implement a resolution plan in respect of eligible borrowers without change in ownership, while retaining the asset classification as 'Standard'.

Snapshot Of The Restructuring Framework

- **Applicable Lending Institutions –** The Restructuring Framework is applicable to (i) Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks); (ii) All Primary (Urban) Co-operative Banks/State Co-operative Banks/ District Central Co-operative Banks; (iii) All-India Financial Institutions; and (iv) All Non-Banking Financial Companies (including Housing Finance Companies).
- **Excluded Borrowers –** Certain categories of borrowers *inter-alia* (i) MSME's having an aggregate exposure of less than INR 25 crore to the lending institution as on March 01, 2020; (ii) financial service providers; and (iii) exposures to Central and State Governments; Local Government bodies and body corporates established by legislature(s), are excluded from the purview of the Restructuring Framework.
- **Eligible Borrowers** – Except the categories of excluded borrowers and credit facilities granted by lending institution to its own staff, all exposures of the lending institutions to borrowers, who are facing stress on account of COVID-19, can be subject to the Restructuring Framework.
- **Eligible Accounts** – Loan accounts having standard asset classification, and which as on March 01, 2020 (**Reckoning Date**) have not been in default for more than 30 days, can be considered under the Restructuring Framework. Further, the account should continue to remain standard till the date on which the borrower and the lending institution have agreed to proceed with a resolution plan under the Restructuring Framework (**Reference Date**).

- **Time Bound** – The Reference Date should not be beyond December 31, 2020 and any resolution under the Restructuring Framework is required to be implemented within 180 days from the Reference Date. A conjoint reading of the requirement of asset classification being standard as on the Reference Date and the maximum time period for Reference Date i.e. December 31, 2020, denotes the intent that any default committed between a date not earlier than 30 days prior to March 01, 2020, and December 31, 2020 will get covered under the Restructuring Framework, subject to asset classification being standard as on the Reference Date.
- **Consent of Lenders** – Whilst, in case of sole lending, the decision regarding the request of a borrower in relation to resolution under the Restructuring Framework, is to be approved basis board backed policies of the lending institution, however, in case of multiple lending institutions, the same has to be approved by the lending institutions representing 75% by value of the total outstanding credit facilities (fund based as well non-fund based), and not less than 60% of the lending institutions by number (**Minimum Threshold**).
- **Inter Creditor Agreement** – Inter creditor agreement (**ICA**) shall be signed by all the lenders within a period of 30 days from the Reference Date. Non execution of ICA by the lenders representing at least Minimum Threshold (both by value and number), within a period of 30 days from the Reference Date, will cause the invocation of the Restructuring Framework to have lapsed, and no further reference can be made under the Restructuring Framework, in relation to that specific account.
- **Breach of timeline** – A breach of any of the timelines stipulated under the Restructuring Framework will cause the resolution process to have ceased and any resolution plan which is implemented in breach of the stipulated timelines would then be governed by the Prudential Framework or in case of lenders to which the Prudential Framework does not apply, the instructions as applicable to that specific category of lending institutions.
- **Expert Committee** – An expert committee to be constituted by RBI, will recommend the financial parameters to be factored into each of the resolution plan and the sector specific ranges. The same will be subject to final confirmation from/ changes suggested by RBI. In respect of accounts having exposure of at least INR. 1500 crores, the expert committee will also check and verify the resolution plan to ensure that all the processes have been followed by the parties without interfering with the commercial wisdom of the lending institution.
- **Resolution Plan** – The resolution plan may comprise of any action/ plan, sanctioning of additional credit facilities, extension of residual loan tenor by upto 2 years, grant of moratorium, reorganization including regularisation of the account by payment of all over dues by the borrower entity, sale of the exposures to other entities / investors, change in ownership and restructuring other than a compromise settlement. It may also include sanctioning of additional credit facilities to the borrower, even if there is no renegotiation of existing debt.
- **Independent Credit Evaluation** – Accounts with aggregate exposure of at least INR. 100 crore will require an independent credit evaluation by any one credit rating agency authorized by the RBI under the Prudential Framework.
- **Escrow Agreement** – Post implementation of a resolution plan, all proceeds of the borrower are to be routed through an escrow account to be maintained with any of the lending institution.

- **Provisioning Norms** – In case the ICA is executed within the stipulated time, the lending institution has to make provision which is higher of the provisioning stipulated in the Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances (**IRAC Norms**) (as applicable before implementation) or 10% of the residual debt. Where, the ICA is not executed within the stipulated time, the applicable provisioning is higher of 20% or the quantum stipulated in the IRAC Norms. Further, as a deterrence, the lenders who did not execute the ICA within 30 days from the Reference Date, are required to maintain provisioning of 20% of the debt on their books.
- **Reversal of provisioning** – The Restructuring Framework allows 50% of the provisioning to be written back after the borrower make payment of at least 20% of the residual debt and balance 50%, when the borrower repays another 10% of the residual debt.
- **Monitoring Period –** Any default by the borrower during the monitoring period[1] triggers a review period of 30 days and post expiry of the review, if the default is not cured, the asset classification of the borrower across all its lenders shall be considered as NPA. The said asset classification applies from the date which is earlier of the implementation of the resolution plan or the date when the borrower was classified as NPA prior to implementation of resolution plan.

The one-time restructuring scheme is yet another positive reaffirmation of the steps being taken to ensure business continuity in India and it aptly balances the interests the lenders and the borrowers. The success of the Restructuring Framework will largely depend on the financial parameters and the sector specific range, which are to be announced by the expert committee.

1 *Monitoring period, for this purpose, is defined as the period starting from the date of implementation of the resolution plan till the borrower pays 10 percent of the residual debt, subject to a minimum of one year from the commencement of the first payment of interest or principal (whichever is later) on the credit facility with longest period of moratorium.*

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