

What are Non-Performing Assets?

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Introduction

Classification of loans and/or advances which constitute to be default or act as arrears in the schedule of payments of the whole principal or the interest is a non performing asset (NPA). A debt is non performing when the payment is not made for a period of 90 days. The credit of which the interest or instalments remain past due for a specified period of time. Financial institutions which refer to loans in jeopardy use NPA. These financial institutions depend upon payment of interest for their income. The 90 day overdue rule was decided to be adopted from 31st March 2004 for the identification of NPA.

Definition According to the RBI

When an asset (including a leased asset) fails to generate income for the bank, it becomes non-performing.

Classification of Non Performing Assets:

Non Performing assets could be classified under three heads basis the period for which the asset has remained non-performing and the realisability of the dues:

Sub-standard assets: Those assets which are classified as NPA for less than 12 months.

Doubtful Assets: Doubtful assets classified as NPA for more than 12 months.

Loss assets: When a bank, internal or external auditor or central bank inspectors identify a loss and the amount, whether wholly or partly has not been written off.

Further Non Performing Assets could be classified as:

- When the principal amount/instalment of the principal amount and/or the interest remain due for more than 90 days in respect of a term loan.
- When in respect of a Overdraft/Cash Credit (OD/CC), the account is 'out of order' for more than 90 days.
- When bills remain overdue for more than 90 days when, purchased and discounted

- When for two harvest seasons and for a period of less than two and a half years, the principal remains overdue with respect to the principal amount or interest thereof in case of an advance granted for the purpose of agriculture.
- In respect of other accounts, overdue for more than 90.
- When stock statements are not submitted for 3 consecutive quarters with respect to Cash Credit Facility.
- When in an account, (Cash Credit/Over Draft/EPC/PCFC), there are no active transactions for more than 91days.

Reasons behind Non Performing Assets

Bad loans are the reason behind NPAs and a failure to meet financial obligations are the reason behind it. The main reasons include:

- Bad lending practices
- Banking crisis
- Overhang component
- Incremental

Difficulties Posed NPAs

The national economy is impacted by NPAs and some of their repercussions include:

- Rightful returns are not received by depositors and uninsured deposits may be lost by them. Higher interest rates may be charged by banks to meet NPA losses.
- Adverse effect on Bank shareholders
- The scenario of bad loans implies that the funds are redirected to the bad projects from the good ones and thus leading to the economy suffering loss on good projects and bad projects failing.
- Liquidity problems may ensue when a loan repayment or payment of interest is not received by a bank

Various steps taken to tackle NPAs

Several steps have been taken by the Indian Government to tackle non performing assets. The steps include legal, financial and reformatory policies. The Narsimham committee in 1991 gave away many recommendations which included:

- ***The Debt Recovery Tribunals (DRTs) – 1993***

The tribunals are for the speedier settlement of cases and are governed by the provisions of the Recovery of Debt Due to Banks and Financial Institutions Act, 1993.

- ***Credit Information Bureau – 2000***

It acts as an information system which prevented the falling of loan money into bad hands to reduce NPAs and helped banks maintain a record of defaulters.

- ***Lok Adalats – 2001***

They tackle meagre loans which are limited to 5 lakhs and avoid cases to enter the judicial system

- ***Compromise Settlement – 2001***

They are for the recovery of Non Performing Assets which are related to advances of less than Rs. 10 Crores. Lawsuits with Debt Recovery Tribunals and courts are covered, excluding frauds and wilful defaults.

- ***The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002***

Banks and financial institutions are permitted to recover their NPAs under the act without the Court in involvement.

- ***ARC (Asset Reconstruction Companies)***

After the amendment of the aforementioned 2002 act, 14ARCs were given a license by the RBI who were created to unlock a value from stressed loans.

Corporate Debt Restructuring – 2005

It is for reducing the burden of the debts on the company by decreasing the rates paid and increasing the time the company has to pay the obligation back.

- ***5:25 rule – 2014 (Flexible Structuring of Long Term Project Loans to Infrastructure and Core Industries)***

The same was aimed at maintaining cash flow of companies with long term project lines and as the repayment of money into their books is not for a long period of time, the loans are refinanced every 5-7 years.

- ***Joint Lenders Forum – 2014***

Included all the Public Sector Banks (PSBs) which became stressed by their loans. It was aimed at preventing an individual to get a loan from different companies and prevents instances of taking a loan from one bank to pay another.

- ***Mission Indradhanush – 2015***

It is the most comprehensive reform system to transform the Public Sector Banks since the nationalisation of banks in 1970 and aims at improving appointments within banks, increases their capital with support from the government, distressing PSBs, create a Framework of Accountability and bringing in Governance Reforms.

- ***Strategic debt restructuring (SDR) – 2015***

Banks who have lend corporate borrower can convert complete or part of their loans into equity shares in the loan taken company.

- ***Asset Quality Review – 2015***

It classified and made provisions for stressed assets with the aim to protect the future of banks and initiate an early identification of assets involving appropriate action to prevent them from being stressed

- ***Sustainable structuring of stressed assets (S4A) – 2016***

Largely stressed accounts are aimed by it and includes the determination of sustainable debt level for a stressed borrower. Also involves equity and quasi equity

instruments as well as as the bifurcation of the outstanding debt into sustainable debt and equity/quasi-equity instruments.

- ***Insolvency and Bankruptcy code Act-2016***

The code was aimed to handle the Chakravyuaha Challenge (Economic Survey) of the exit problem in India. The same is aimed promoting entrepreneurship, making credit available, and to balance the interests of all stakeholders. The same is done by the consolidation and amendment of laws which relate to insolvency as well as reorganization of individuals, partnership firms and corporate persons which is in a time bound manner.

- ***Bad Banks – 2017***

Bad banks are talked about in the Economic survey 16-17 which would tackle stressed loans by flexible rules and mechanism. The same will ease the balance sheet of Public Sector Banks as well as give them a chance of funding new projects and continue the funding of development projects.

Conclusion

Thus, a more comprehensive system and remedial measures are to be developed to tackle non performing assets.