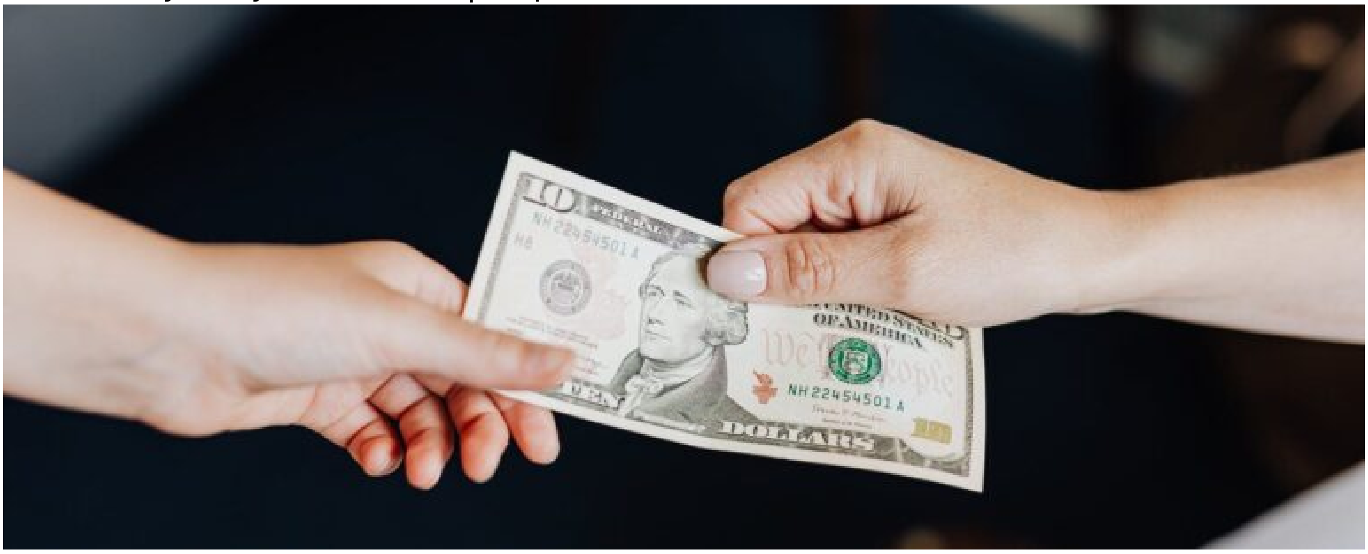
RBI Allows One-Time Loan Restructuring For The Stressed Borrowers
written by Priyanka Barik | September 21, 2020



RBI Allows Loan Restructuring: Relief to Stressed Borrowers during COVID 19

The Reserve Bank of India ("RBI") in order to curb the effect of COVID-19 over the economy, has introduced a Resolution Framework ("Resolution") for dealing with the stressed assets during the pandemic. It is important to assess the stress induced by the pandemic as it can hamper the ability of the borrowers to repay the loans. Therefore, RBI on August 6, 2020[1] announced a one-time special window for lenders in order to restructure the current loans, which will further allow them to change repayment terms for their borrowers who have been hit by the COVID-19 lockdown. The intention behind bringing out the Resolution is to help borrowers who are dealing with the liquidity and repayment issues due to the pandemic.

Loan Re-Structuring

Restructuring of loans means when a moneylender alters the terms of credit in order to help the borrower when its facing financial distress. This is generally done to avoid the loan being classified as a Non-Performing Assets ("NPA") and the borrower further being considered as a defaulter. An NPA classification brings with it the requirement for lenders to set aside some amount of funds in lieu of potential losses going forward in order to increase the "risk weighting" of that particular loan given to the borrower. However, it has always been the concern of the lenders because NPAs are a drag on the resources of the lenders as they lose out on interests over such assets. Therefore, generally in a loan approval process, banks or lenders investigate their borrowers during the application process to know their creditworthiness and expect the borrower to periodically submit updates and reports in order to keep a check. Further, a loan whose interest and/or instalment of the principal have remained overdue for a period of 90 days is considered as an NPA.

However, due to the pandemic, the gross NPA ratio of banks increased from 8.5% to 12.5% following the sharp slowdown in the economic conditions in the country.

Since extraordinary times calls for extraordinary solutions, therefore, a first-of-its-kind one-time restructuring framework, for both personal as well as corporate loans, was introduced. The restructuring process would happen without classifying these accounts as NPAs which will be a relief to both the stressed borrower as well as the lender. Further, this framework will be available till December 31st, 2020 and must be implemented within 90 days of invocation.

Furthermore, restructuring of the terms of a loan would include rescheduling the repayment time period for the loans, lowering the interest rate, amending the repayable amount, changing the number of instalments required for the repayment of the loans, converting interests accrued into another credit facility, etc.

Eligibility Criteria

The facility of loan restructuring is only available to businesses or individuals who are suffering the COVID-induced stress. Further, only those borrower’s accounts which are not in default for more than 30 days with the lending institution as on March 1st, 2020 are eligible for the loan restructuring. Moreover, the following entities would not be included:

1. As on March 1, 2020, the MSME borrowers whose aggregate exposure to lending institutions collectively is ₹25cr or less
2. Loans given to the Central and State Governments, local Government bodies, Primary Agricultural Credit Societies (PACS) or Farmers' Service Societies (FSS)
3. Loans granted by lenders to their own personnel or staff; and

Further, it is very important to note that the loans taken from non-banking organisations are also included in the Resolution framework’s ambit. Therefore, organisations whose loans are eligible for resolution would include all Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks), all Primary (Urban) Co-operative Banks/State Co-operative Banks/ District Central Co-operative Banks, all All-India Financial Institutions, all Non-Banking Financial Companies (including HFCs).

Restructuring Of Corporate Loans

Corporate restructuring could be done by converting the debt into equity or other marketable security instruments, or non-convertible debt securities issued by the borrower. During the 30 days time period for invocation of the restructuring facility, an Inter-Creditor Agreement (“ICA”) would have to be signed with the concerned corporate entity. Once a borrower avails this scheme, the RBI has prescribed a clear monitoring period till the day the borrower repays at least 10% of residual debt.

Restructuring Of Personal Loans

For personal loans, lenders would be allowed a maximum of 90 days to implement the resolution plan. If they do not abide by the prescribed timeline then they will not get any benefit under the restructuring scheme and will have to declare the loan as an NPA.

Restructuring Of MSMEs Debt

Further regarding the MSMEs, a restructuring framework has been already provided that were in default but would be considered as ‘standard’ as on January 1, 2020, subject to the restructuring being implemented up to December 31, 2020. The scheme has provided relief to a large number of MSMEs. However, the stressed assets[2] in the MSME sector have increased due to the economic fallout because of the pandemic.

However, due to the requirement of strong support to the MSMEs, the pandemic, lending institutions may restructure the debt under the existing framework, provided the borrower’s account was classified as standard with the lender as on March 1, 2020. Further, this restructuring shall be implemented by March 31, 2021.[3]

Conclusion

It is understandable why RBI has been hesitant regarding the implementation of the Resolution Framework during this time. Earlier when such levy was provided amidst the 2008 global economic crisis, the corporates and the lending institutions misused the opportunity to pool in a big number of NPAs, which lead to a severe downfall in the economy, pursuant to which the RBI had to tighten the regulations in 2015. However, the regulator now does not want to undo several years' gains from its NPA clean-up efforts by diving straight back into the very cause for it.

As the apex regulator, RBI's primary concern currently is to maintain the financial health of the economy. This pandemic threatens that. However, on one hand, it is a welcome step since borrowers struggling with decreased cash flow will now have more time for the repayment of the debts. Further, a six month break on the loan repayment may act like temporary solution, but it will certainly not make the problem go away. Whether it comes in the form of one-time restructuring or another financial package, a more structural solution is the need of the hour.

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[1] https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=50176

[2] https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11580&Mode=0

[3] https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=50176

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