Prompt NPA Labeling for Willful Defaulters

For Prelims: Willful Defaulter**,** NPA**,** RBI**,** ARCs

For Mains: GS Paper-3, Challenges of NPA, Provisions to NPA resolution, Banking Sector ,Mobilisation of Resources, Bad Bank

Source:IE

Why in News ?

The **Reserve Bank of India (RBI)** in a **recent draft proposed** that **lenders should classify** a borrower as a wilful defaulter **within six months** of their account being declared a **non-performing asset (NPA).**

What are Key Highlights of the RBI Draft ?

- Under the new regime, the lender must identify wilful defaulter borrowers within a specified six-month timeframe, whereas in the previous system, there was no such time constraint.
  - Lenders must assess wilful default for **accounts over Rs 25 lakh within 6 months of becoming NPAs.**
- An **Identification Committee** formed by lenders reviews evidence of wilful default.
- Policies require **non-discriminatory photo publishing for wilful defaulters,** and no credit is given to them for up to 1 year post removal from the **List of Wilful Defaulters (LWD)**; additionally, no credit for new ventures is allowed for 5 years after LWD removal.
- Guarantors can be pursued without exhausting remedies against principal debtors, and **investigation of wilful default is necessary** before transferring credit to others or ARCs.

Who is a Wilful Defaulter?

- **About:**
  - A **wilful defaulter means a borrower or a guarantor who has committed** wilful default and the outstanding amount is **Rs 25 lakh and above.**
  - A **large defaulter refers** to a borrower with an **outstanding balance of Rs 1 crore** or more, whose account has been categorized as doubtful or a loss.
- **Events Constituting Wilful Default:**
  - The unit has defaulted in meeting its payment/repayment obligations to the lender **even when it has the capacity** to honour the said obligations.
  - The unit has defaulted in meeting its payment/repayment obligations to the lender and has not utilised the finance from the lender **for the specific purposes for which finance was availed** of but has diverted the funds for other purposes.
  - The unit has defaulted in meeting its payment/repayment obligations to the lender and has **siphoned off the funds so that the funds have not been utilised for the specific purpose** for which finance was availed of, nor are the funds available with the unit in the form of other assets.

- The unit has defaulted in meeting its payment/repayment obligations to the lender and has also **disposed off or removed the movable fixed assets or immovable property** given by him or it for the purpose of securing a term loan without the knowledge of the bank/lender.

What is a Non-Performing Asset?

- **About:**
  - NPA refers to a **classification for loans** or advances that are in **default or are in arrears on scheduled payments of principal or interest.**
  - In most cases, debt is classified as non-performing, when the loan payments have not been made for a **minimum period of 90 days.**
  - **For agriculture,** if principle and interest is not paid for **two cropping seasons,** the loan is classified as NPA.
- **Types:**
  - **Gross NPA**:Gross NPAs are the sum of all the loans that have been defaulted by the individuals
  - **Net NPA:** Net NPAs are the amount that is realized after provision amount has been deducted from the gross non-performing assets.
- **Laws and provisions related to NPAs:**
  - **Bad Bank:**
    - The bad bank in India is called **National Asset Reconstruction Ltd (NARC).**
    - This NARC will work as an asset reconstruction company.
    - It will buy bad loans from the banks, relieving banks of the NPA. NARC will then attempt to sell the stressed loans to distressed debt buyers.
    - The government has already set up **India Debt Resolution Company Ltd (IDRCL)** to sell these stressed assets in the market. Accordingly, IDRCL will attempt to sell them in the market.
  - **The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002:**
    - The **SARFAESI Act** allows banks and financial institutions to take **possession of collateral assets** and **sell them to recover** outstanding dues without the intervention of the court.
    - It provides **provisions for the enforcement of security interests** and **allows banks** to issue demand notices to defaulting borrowers.
  - **The Insolvency and Bankruptcy Code (IBC), 2016:**
    - The **IBC provides a comprehensive framework** for the **insolvency and bankruptcy resolution** process in India.
    - It aims to facilitate the **time-bound resolution** of stressed assets and **promote a creditor-friendly environment.**
    - Under the IBC, **a debtor or creditor can initiate insolvency** proceedings against a defaulting borrower.
    - It established the **National Company Law Tribunal (NCLT)** and the **Insolvency and Bankruptcy Board of India (IBBI)** to oversee the process.
  - **Importance of NPA Recovery:**
    - The **recovery of NPAs** is crucial to **protect** the **interests of depositors** and stakeholders.
    - **Compromise settlements** should **prioritize the maximum recovery of dues** with minimal expense and within a shorter time frame.
    - **Consideration of Public Interest:**
    - During compromise settlements, **banks,** being public sector entities, should **consider the interests of the tax-paying public** over the borrowers' interests.

UPSC Civil Services Examination Previous Year Question (PYQ)

Prelims

Q. With reference to the governance of public sector banking in India, consider the following statements: (2018)

1. Capital infusion into public sector banks by the Government of India has steadily increased in the last decade.
2. To put the public sector banks in order, the merger of associate banks with the parent State Bank of India has been affected.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Ans: (b)

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