



# RBI Committee on Asset Reconstruction Companies

## Why in News

A [Reserve Bank of India \(RBI\)](#) committee has come out **with a host of suggestions** in a bid to streamline the functioning of [Asset Reconstruction Companies \(ARCs\)](#).

## Asset Reconstruction Companies (ARCs)

- It is a **specialized financial institution** that buys the **Non Performing Assets (NPAs)** from banks and financial institutions so that they can clean up their balance sheets.
  - A **NPA is a loan or advance** for which the principal or interest payment remained overdue for a period of 90 days.
  - Typically, ARCs buy banks' bad loans by paying a portion as cash upfront (15% as mandated by the RBI), and **issue security receipts (SRs)** for the balance (85%).
- This **helps banks to concentrate on normal banking activities**. Banks, rather than going after the defaulters by wasting their time and effort, can sell the bad assets to the ARCs at a mutually agreed value.
- The [Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest \(SARFAESI\) Act, 2002](#) provides the legal basis for the setting up of ARCs in India.
  - The Act **helps reconstruction of bad assets** without the intervention of courts. Since then, a large number of ARCs were formed and were registered with the RBI.
- **RBI has got the power to regulate the ARCs.**

## Key Points

- **Background:**
  - The **performance of the ARCs** has so far **remained lacklustre**, both in ensuring recovery and in revival of businesses.
  - Lenders could **recover only about 14.29% of the amount** owed by borrowers in respect of stressed assets sold to ARCs in the 2004-2013 period.
  - To **improve the performance of ARCs**, the RBI had appointed the committee (**headed by Sudarshan Sen**) to examine the issues and recommend measures for enabling ARCs to meet the growing requirements of the financial sector.
- **Suggestions:**
  - **Online Platform for Sale of Stressed Assets:**
    - Recognising the **need for transparency and uniformity of processes** in sale of stressed assets to ARCs, the Committee feels that an online platform may be created for sale of stressed assets.
  - **Expanding Scope of SARFAESI Act:**
    - The **scope of Section 5 of the SARFAESI Act** may be expanded to **allow ARCs to acquire 'financial assets'**, for the purpose of reconstruction, **not only from banks and 'financial institutions' but also from such entities** as may be

notified by the RBI.

- Under these proposed powers, the RBI may consider permitting ARCs to acquire financial assets from all regulated entities, including [Alternative Investment Fund \(AIFs\)](#), [Foreign Portfolio Investors \(FPIs\)](#), [Asset Management Company \(AMCs\)](#) making investment on behalf of [Mutual Funds \(MFs\)](#) and all [Non-Banking Financial Companies \(NBFCs\)](#).
- **Providing Additional Resources:**
  - ARCs are to **be allowed to sponsor SEBI-registered Alternative Investment Funds** to raise resources for facilitating restructuring of bad loans purchased by them.
- **Using IBC:**
  - Envisaging ARCs as a prime vehicle for resolution of stressed assets, the regulations **should allow ARCs to also use the [Insolvency and Bankruptcy Code \(IBC\)](#) framework for this purpose.**
- **Large Loans for sale to ARCs:**
  - **Large loans and loans that have been in default for over two years should be considered for sale to ARCs by banks. Final approval of the reserve price should be given by a high-level committee.**
    - Reserve price plays a critical role in ensuring true price discovery in auctions conducted for sale of stressed assets.
- **For Ensuring Debt Aggregation:**
  - The Committee has said that **if 66% of lenders (by value) decide to accept an offer by an ARC**, the same may be binding on the remaining lenders and it must be implemented within 60 days of approval by majority lenders (66%).
    - **Aggregate Debt** means the total of principal and interest that is owed by the debtor to the creditors at the time of execution of the debt settlement agreement.
- If a lender fails to agree, it will be subjected to **100% provisioning on the loan outstanding.**
  - **Provisioning of loan:** Booking a provision means that the bank recognises a loss on the loan ahead of time.
- **For NARCL:**
  - In respect of the proposed [National Asset Reconstruction Company Limited \(NARCL\)](#) by India for cleaning the books of Public Sector Banks (PSBs), the RBI **should ensure fair competition** between the NARCL and private ARCs to promote the objectives of true price discovery through the market mechanism.
- **Expected Benefits:**
  - **Get Rid of Stressed Loans:**
    - The suggestions are aimed at **enabling banks to get rid of stressed loans** in the early stage of default and nudge reluctant minority lenders into joining the sale. The norms also seek to appoint valuers for large-value loans that are sold.
  - **Help ARCs Raise Resources:**
    - The recommendations are timely and will **help ARCs raise resources by tapping different categories** of market participants eligible for investment in security receipts.
    - Banks have also been incentivised for sale of [NPA \(Non-Performing Asset\)](#) early with provision to spread loss over two years.

[Source: TH](#)