RBI Issues Revised ‘Master Direction’ for ARCs

Source: LM

Why in News?

Reserve Bank of India (RBI) has revised the **'Master Direction - Reserve Bank of India (Asset Reconstruction Companies-ARCs) Directions, 2024**.

- The revised norms for **ARCs** aim to **streamline operations, ensure transparency, protect creditor interests**, and emphasize due diligence in settlement processes.

What are the Key Points of the RBI's Revised Master Direction on ARC?

- **Board-Approved Policy:** Each **asset reconstruction company (ARC)** must establish a **board-approved policy** for settling borrower dues, covering various key elements such as:
  - **Cut-off date** for eligibility of **one-time settlement.**
  - **Permissible sacrifice** for different categories when deciding the settlement amount.
  - **Methodology** for evaluating the **realizable value** of the security.
- **Settlement Process: Settlement** should be considered only after **all recovery options** have been explored.
  - Preferably, the settlement amount should be **paid in a lump sum** (one- time payment).
  - **Non-lump sum** payment plans must align with **business models, borrower cash flows, and projected earnings**.
- **Independent Advisory Committee (IAC):** An IAC, with technical, financial, or legal experts, should **review settlement proposals** and advise the **ARC's board committee**.

What are ARCs?

- **About:** An ARC is a **special type of financial institution** that buys **non-performing assets (NPAs)** from banks and financial institutions and **attempts to recover the debts or associated securities** by itself.
- **Background of ARCs:** The concept of ARCs was introduced by the **Narasimham Committee – II (1998)**, leading to the establishment of **ARCs** under the **Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act, 2002)**.
- **Registration and Regulation of ARCs:** ARC is registered under the **Companies Act, 2013** and must also be **registered with the RBI** under **section 3** of the **SARFAESI Act, 2002**.
  - It operates under the SARFAESI Act, 2002, and follows **guidelines issued by the RBI.**
- **Working of the ARCs:**
  - **Asset Reconstruction:** It involves acquiring a bank's or financial institution's rights in **loans, advances, bonds, guarantees, or other credit facilities** for recovery, known as **'financial assistance'.**
  - **Securitisation:** It involves acquiring financial assets by issuing **security receipts** to **Qualified Buyers (QB).**
    - QBs include **insurance companies, banks, state financial corporations, ARCs** under SARFAESI, and SEBI-registered asset management companies.
  - **Security Receipts:** ARCs issue **security receipts to lenders**, redeemable upon loan recovery, charge a management fee, and **share recovery gains** with the selling financial

institutions.

Non-Performing Asset (NPA)

- **About:** NPA is a loan classified as an **NPA** when the loan payments have not been made for a **minimum period of 90 days.**
    - For **agriculture**, a loan is classified as an NPA if the **principal or interest is not paid for two cropping seasons.**
- **Types:** Banks classify NPAs into **three categories** based on the duration of non-performance and recovery chances.
    - **Sub-standard Assets:** NPAs for **12 months or less**.
    - **Doubtful Assets:** NPAs for **over 12 months.**
    - **Loss Assets:** Uncollectible assets with **little or no chance of recovery,** needing full write-off.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims

Q. Which of the following statements best describes the term 'Scheme for Sustainable Structuring of Stressed Assets (S4A)', recently seen in the news?(2017)

(a) It is a procedure for considering ecological costs of developmental schemes formulated by the Government.

(b) It is a scheme of RBI for reworking the financial structure of big corporate entities facing genuine difficulties.

(c) It is a disinvestment plan of the Government regarding Central Public Sector Undertakings.

(d) It is an important provision in 'The Insolvency and Bankruptcy Code' recently implemented by the Government.

Ans: (b)