RBI ANNOUNCES RESOLUTION FRAMEWORK 2.0 FOR INDIVIDUALS, SMALL BUSINESSES AND MSMEs

May 7, 2020

Introduction

On August 6, 2020, the Reserve Bank of India ("**RBI**") had issued a circular on 'Resolution Framework for COVID-19-related Stress' ("**Resolution Framework 1.0**"), providing for a window under the existing RBI (Prudential Framework for Resolution of Stressed Assets) Directions, 2019, dated June 7, 2019 ("**Prudential Framework**") for all Commercial Banks, Primary (Urban) Co-Operative Banks/ State Co-Operative Banks/ District Central Co-Operative Banks, All-India Financial Institutions and Non-Banking Financial Companies (including Housing Finance Companies) ("**Lender(s)**") to implement resolution plans in respect of eligible borrowers without change in ownership, as well as personal loans, while classifying such exposures as 'standard' subject to the prescribed conditions. RBI had issued another circular, on August 6, 2020, on 'Micro, Small and Medium Enterprises ("**MSME**") sector – Restructuring of Advances' permitting existing loans to MSMEs, classified as 'standard', to be restructured without a downgrade in the asset classification ("**Resolution Framework 1.0-MSME"**).

In light of the resurgence of the COVID-19 pandemic in India in the recent weeks and the impact that consequent containment measures may have on the recovery process, RBI has issued two circulars, dated May 5, 2021, on 'Resolution Framework – 2.0: Resolution of COVID-19 related stress of Individuals and Small Businesses' permitting Lenders to offer a limited window to individual borrowers and small businesses to implement resolution plans in respect of their credit exposures while classifying the credit exposures as 'standard' upon implementation of the resolution plan ("**Resolution Framework 2.0**") and on 'Resolution Framework – 2.0: Resolution of COVID-19 related stress of MSMEs' further extending the benefit conferred by Resolution Framework 1.0-MSME ("**Resolution Framework 2.0-MSME**").

Individual and small businesses

Resolution Framework 2.0 permits the Lenders to offer a limited window to individual borrowers and small businesses to implement resolution plans in respect of their credit exposures while classifying the credit exposures as 'standard' upon implementation of the resolution plan subject to the conditions specified below:

Eligibility

The following borrowers shall be eligible for the resolution process under Resolution Framework 2.0:

(a) Individuals who have availed personal loans (i.e. loans given to individuals consisting of (a) consumer credit, (b) education loan, (c) loans given for creation/ enhancement of immovable assets (e.g., housing, etc.), and (d) loans given for investment in financial assets (shares, debentures, etc.), excluding the credit facilities sanctioned by the Lenders to their own personnel/ staff;

(b) Individuals who have availed loans and advances for business purposes and to whom the Lenders have an aggregate exposure of not more than Rs. 25,00,00,000 (Rupees twenty five crore) as on March 31, 2021; and

(c) Small businesses, including those engaged in retail and wholesale trade, other than those classified as MSME, as on March 31, 2021, and to whom the Lenders have aggregate exposure of not more than Rs. 25,00,00,000 (Rupees twenty five crore), as on March 31, 2021.

It is pertinent to note that the aforementioned borrowers will be eligible for the resolution process under Resolution Framework 2.0 only if the following conditions are satisfied:

(a) The borrower accounts/ credit facilities shall not belong to the following categories, as provided in Resolution Framework 1.0:

   (i) MSME borrowers whose aggregate exposure to the Lenders, collectively, is Rs. 25,00,00,000 (Rupees twenty five crore) or less, as on March 1, 2020;
   (ii) Farm credit as mentioned in the 'Master Direction - Priority Sector Lending – Targets and Classification' issued by RBI on priority sector lending, except for the following loans:
      - loans to allied activities, viz., dairy, fishery, animal husbandry, poultry, bee-keeping and sericulture;
      - loans given to farmer households if they do not meet any other conditions for exclusions listed in Resolution Framework 1.0;
   (iii) Loans to primary agricultural credit societies, farmers' service societies and large-sized Adivasi multi-purpose societies for on-lending to agriculture;
   (iv) Exposures of the Lenders to financial service providers, as defined in the Insolvency and Bankruptcy Code, 2016; and
   (v) Exposures of the Lenders to central, state and local government bodies and body corporates established by an Act of Parliament or State Legislature.

(b) The borrower accounts should not have availed any resolution in terms of the Resolution Framework 1.0, subject to the exemption that, where resolution plans implemented under Resolution Framework 1.0, had either permitted no moratorium or a moratorium of less than 2 (two) years, and/ or extension of residual tenor by a period of less than 2 (two) years, the Lenders shall be permitted to use the window provided for under Resolution Framework 2.0 to modify such resolution plans to the extent of increasing the period of moratorium/ extension of residual tenor, and the consequent changes in relation to such increase/ extension. However, the overall cap on moratorium and/ or extension of residual tenor granted under Resolution Framework 1.0 and Resolution Framework 2.0, shall be 2 (two) years.

(c) The credit facilities/ investment exposure to the borrower must have been classified as 'standard' by the Lenders as on March 31, 2021.

Invocation of resolution process

Resolution Framework 2.0 requires the Lenders to frame Board approved policies within 4 (four) weeks from the date of Resolution Framework 2.0 (May 5, 2021) on implementation of viable resolution plans for eligible borrowers and ensure that the resolution under Resolution Framework 2.0 is extended only to borrowers having stress on account of COVID-19.

Further, the Board approved policy should set out the eligibility criteria for borrowers, the due diligence considerations to be fulfilled for evaluating the need for a resolution plan, and the system for redressing the grievances of borrowers. Such board approved policies also have to be set out for borrowers who have availed credit facilities for which, the resolution plans implemented under Resolution Framework 1.0 have been modified pursuant to the window provided for under Resolution Framework 2.0.

The resolution process under Resolution Framework 2.0 shall be treated as invoked when the Lender and the borrower reach an agreement on finalising a resolution plan in respect of the borrower. On receipt of applications from the borrowers, the Lenders shall have 30 (thirty) days to assess the eligibility for resolution as per Resolution Framework 2.0 and the Board approved policy in this regard and communicate the decision on the application to the borrower in writing.

The Lenders shall take a decision on invocation of the resolution process, in relation to a borrower, under Resolution Framework 2.0, independent of the decision on invocation taken by the other Lenders having exposure in the borrower.

The last date for invocation of resolution permitted under Resolution Framework 2.0 is September 30, 2021. This timeline will also be applicable for the credit facilities for which, the resolution plans implemented under Resolution Framework 1.0 have been modified pursuant to the window provided for under Resolution Framework 2.0.

Permitted features of resolution plans and implementation

The resolution plans may include rescheduling of payments, conversion of interest accrued/ to be accrued into another credit facility or granting of moratorium based on an assessment of income streams of the borrower. However, compromise settlements are not permitted as a resolution plan under Resolution Framework 2.0.

The moratorium period, if any, granted under the resolution plan, shall be for a maximum period of 2 (two) years, starting immediately upon the implementation of the resolution plan. The borrowers may also be granted an extension of the residual tenor of loan facilities, with or without a payment moratorium, subject to an overall cap of 2 (two) years (including the moratorium period, if any).

The resolution plan may also envisage conversion of a portion of the debt into equity or any other marketable, non-convertible debt security issued by the borrower. Such conversion shall be governed by the provisions of Resolution Framework 1.0.

The resolution plan under Resolution Framework 2.0 should be finalised and implemented within 90 (ninety) days from the date of invocation of the resolution process. The resolution plan will be deemed to be implemented only after all the necessary documentation is completed, the revised terms are reflected in the books of the relevant Lenders and the borrower is not in default as per the revised terms. This timeline shall also be applicable to the credit facilities for which, the resolution plans implemented under Resolution Framework 1.0 have been modified pursuant to the window provided for under Resolution Framework 2.0.

It is imperative to note that any resolution plan which is implemented in breach of Resolution Framework 2.0 shall be fully governed by the Prudential Framework, or the relevant instructions as applicable to specific category of the Lenders where the Prudential Framework is not applicable

Asset classification and provisioning

If a resolution plan is implemented in accordance with Resolution Framework 2.0, the asset classification of the concerned borrowers' accounts classified as 'standard' may be retained as such upon implementation of the plan. Borrowers' accounts which may have slipped into 'non-performing assets' ("**NPA**") between the invocation and implementation of the resolution plan can be upgraded as 'standard', as on the date of implementation of the plan.

The subsequent asset classification for such exposures will be governed by the criteria laid out in the Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances dated July 1, 2015, or other relevant instructions as applicable to specific category of the Lenders ("**IRAC Norms**").

Resolution Framework 2.0 permits the Lenders to sanction additional credit facilities to the borrower before implementation of the resolution plan to meet the interim liquidity requirements of the borrower. Such additional facilities may be classified as 'standard' by the Lenders till the implementation of the plan regardless of the actual performance of the borrower with respect to such facilities in the interim. However, if the resolution plan is not implemented within the stipulated timeline, the asset classification of such additional credit facilities will be as per the actual performance of the borrower with respect to the same or the rest of the credit facilities, whichever is worse.

On implementation of the resolution plan, the Lenders shall keep provisions from the date of implementation of the resolution plan as per the extant IRAC Norms immediately before implementation, or 10% (ten percent) of the renegotiated debt exposure of the Lenders post implementation (residual debt including the portion of non-fund based facilities that may have devolved into fund based facilities after the date of implementation), whichever is higher.

In relation to the aforementioned provisions, half of the provisions can be written back upon the borrower paying at least 20% (twenty percent) of the residual debt without slipping into NPA post implementation of the plan, and the remaining half can be written back upon the borrower paying another 10% (ten percent) of the residual debt without slipping into NPA subsequently. However, in respect of exposures other than personal loans, the provisions shall not be written back before 1 (one) year from the commencement of the first payment of interest or principal (whichever is later) on the credit facility with the longest period of moratorium.

The provisions that are required to be maintained under Resolution Framework 2.0, to the extent not already reversed, shall be available for the provisioning requirements when any of the accounts, where a resolution plan had been implemented, is subsequently classified as NPA.

It is pertinent to note that the credit facilities for which, the resolution plans implemented under Resolution Framework 1.0 have been modified pursuant to the window provided for under Resolution Framework 2.0, the instructions regarding asset classification and provisioning shall continue to be as provided for under Resolution Framework 1.0.

Working capital support for small businesses where resolution plans were implemented previously

In relation to:

(a) individuals who have availed loans and advances for business purposes and to whom the Lenders have an aggregate exposure of not more than Rs. 25,00,00,000 (Rupees twenty five crore) as on March 31, 2021; and
(b) small businesses, including those engaged in retail and wholesale trade, other than those classified as MSME as on March 31, 2021, and to whom the Lenders have aggregate exposure of not more than Rs. 25,00,00,000 (Rupees twenty five crore) as on March 31, 2021,

where resolution plans have been implemented under Resolution Framework 1.0, the Lenders are permitted under Resolution Framework 2.0, as a one-time measure, to review the working capital sanctioned limits and/ or the drawing power, without the same being treated as restructuring. However, the Lenders shall have to reach a decision in relation to the same by September 30, 2021, with the margins and working capital limits being restored to the levels as per the resolution plan implemented under Resolution Framework 1.0, by March 31, 2022.

The aforementioned measures shall be contingent on the Lenders being satisfied that the measures are necessitated on account of the economic situation created by COVID-19. The accounts that were provided relief under these instructions shall also be subject to subsequent supervisory review with regard to their justifiability vis-a-vis the economic situation created by COVID-19.

The Lenders shall be required to implement board approved policies to implement the aforementioned measures, and such policies should be disclosed in the public domain.

Disclosures and credit reporting

The Lenders are required to make necessary disclosures in their quarterly/ half-yearly/ annual financial statements, as applicable, as per the prescribed formats, in respect of the accounts where resolution plans were implemented.

The Lenders shall also be required to disclose the number of borrower accounts where the resolution plans implemented under Resolution Framework 1.0 were modified pursuant to the window provided for, under Resolution Framework 2.0, on a quarterly basis, starting from the quarter ending June 30, 2021.

Further, the credit reporting by the Lenders in respect of the borrowers where a resolution plan is implemented under Resolution Framework 2.0 should reflect the status of the account as "restructured due to COVID-19".

MSMEs

Resolution Framework 2.0-MSME extends the benefits conferred by Resolution Framework 1.0-MSME, and permits restructuring of the existing loans availed by MSMEs without a downgrade in the asset classification, subject to the conditions mentioned hereinbelow.

It is pertinent to note that in addition to the conditions/ instructions mentioned below, all other conditions/ instructions specified in Resolution Framework 1.0-MSME shall remain applicable to the restructuring of existing loans under Resolution Framework 2.0-MSME.

Eligibility

The following borrowers shall be eligible for the restructuring process under the Resolution Framework 2.0-MSME:

(a) The borrower is classified as an MSME as on March 31, 2021, as per the Gazette notification (S.O. 2119 (E)) dated June 26, 2020;

(b) The borrower is GST-registered on the date of implementation of the restructuring, save and except the borrowers which are exempted from the registration as on March 31, 2021;

(c) The aggregate exposure, including non-fund based facilities of the Lender's to the borrower, does not exceed Rs. 25,00,00,000 (Rupees twenty five crore) as on March 31, 2021;

(d) The borrower's account was a 'standard asset' as on March 31, 2021; and

(e) The borrower's account has not been restructured in terms of Resolution Framework 1.0-MSME, and the circulars issued by RBI on 'MSME sector – Restructuring of Advances' dated February 11, 2020 and January 1, 2019 (hereinafter collectively referred to as "**MSME Restructuring Circulars**").

Invocation and implementation of the restructuring process

Resolution Framework 2.0-MSME directs the Lenders to frame Board approved policies within 1 (one) month from the date of Resolution Framework 2.0-MSME (May 5, 2021) on restructuring of MSME advances.

The restructuring process under Resolution Framework 2.0-MSME shall be treated as invoked when the Lender and the borrower reach an agreement on finalising a resolution plan in respect of the borrower. On receipt of applications from the borrowers, the Lenders shall have 30 (thirty) days to assess the eligibility of the restructuring process as per Resolution Framework 2.0-MSME and the Board approved policy in this regard and communicate the decision on the application to the borrower in writing. The Lenders shall take a decision on invocation of the restructuring process, in relation to a borrower, under Resolution Framework 2.0-MSME, independent of the decision on invocation taken by the other Lenders having exposure in the borrower.

The last date for invocation of restructuring permitted under Resolution Framework 2.0 is September 30, 2021.

The restructuring of the borrower's account, under Resolution Framework 2.0-MSME has to be implemented within a period of 90 (ninety) days from the date of invocation of the restructuring process. The borrower is required to register on the Udyam Registration portal before the implementation of the restructuring plan under Resolution Framework 2.0-MSME, for the plan to be treated as implemented.

Asset classification and provisioning

If a restructuring plan is implemented in accordance with Resolution Framework 2.0-MSME, the asset classification of the concerned borrowers' accounts classified as 'standard' may be retained as such upon implementation of the plan. Borrowers' accounts which may have slipped into NPA between April 1, 2021 and the date of implementation of the restructuring plan can be upgraded as 'standard', as on the date of implementation of the restructuring plan.

Pursuant to the implementation of the restructuring plan, the Lenders are required to keep a provision of 10% (ten percent) of the residual debt of the borrower.

Working capital support for MSMEs where restructuring plans were implemented previously

In respect of the accounts of the borrowers that were restructured under the MSME Restructuring Circulars, Resolution Framework 2.0-MSME permits the Lenders, to review the working capital sanctioned limits and/ or drawing power, as a one-time measure, based on working capital cycle, reduction of margin etc., without the same being treated as restructuring. However, the Lenders shall have to reach a decision in relation to the same by September 30, 2021. The Lenders are required to review at least on half yearly basis the reassessed sanctioned limit/ drawing power and on annual basis the renewal/ reassessment.

The measures taken by the Lenders under Resolution Framework 2.0-MSME shall be contingent on the Lenders being satisfied that the measures are necessitated on account of the economic situation created by COVID-19. The accounts that were provided relief under these instructions shall also be subject to subsequent supervisory review with regard to their justifiability vis-a-vis the economic situation created by COVID-19.

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