

Bank Branch Audit Seminar

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Loans & Advances

By

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Disclaimer

- The views expressed in the following presentation should **not be construed** as the view of **ICAI** or my firm.
- The views opined herein, should **not be considered as a professional advice.**

Importance

- Most **Important** Area in Bank Audit
- Expected **100 % checking** in All Audit
- Various types of **frauds and queries** are observed in this area
- Specialized **skill and** thorough **Knowledge** required
- Various **Act** and Rules, **RBI Circulars** , Credit Policies of Bank ,Powers ,need to be studied.

Loans and Advances

- Loans and advances is a **principal businesses** activity of banks.
- Loans are sanctioned on certain **terms and conditions** and usually **borrower offer** some assets as a **security** for the loans given.
- These assets may be **movable or immovable** upon which **charge is created** in favor of the bank.

Audit is Skill

- Requires

- General Knowledge
- Common sense
- Logic

Plus

- Understanding of Economy
- Nature of Activity
- Facility Demanded

Certificate From CA

- Case against CA Decided on 26 September, 2016 wrongly certifying **margin money while share listing** in market in this case SEBI has filed case and **3 years suspension** from practice is ordered by supreme court .
- CBI - **Fabricated audited Balance Sheets and Profit and Loss Account** to help a fictitious company to get **huge trade finance**.
- CBI, the said **CA certified provisional balance sheet**, provisional profit & loss account of a company wherein inflated profit was shown.

Para's from Reports on Fraud – Central Vigilance Commission , 15.10.2018

- Bank must immediately **delist** such third party valuers, **Chartered Accountants**/Chartered Engineers, Advocates etc. who have questionable credentials/have been **negligent in their professional duties** or have **caused financial loss** to the bank by their wilful acts of omission/commission/dishonesty.
- A **periodical review** of all **empanelled professionals** should to be ensured by banks for weeding out undesirable third party service providers.

Paras from Reports on Fraud Central Vigilance Commission , 15.10.2018

- **Mismatch were noticed in the stocks/debtors** as per the books of the company and as per the stock statement submitted by the company.
- **Inspection system should not be for name sake** and it should be manned by knowledgeable and experienced persons to prevent, detect and report malpractices in the bank to the top management.
- **Selection of** Concurrent Auditors & Statutory ,Auditors should be appointed in **consultation** of Institute of Chartered Accountants of India (**ICAI**).

Acts Applicable for Bank Audits

- Reserve Bank of India Act, 1934
- Banking Regulation Act, 1949
- Banking Companies (Acquisition and Transfer of Undertakings) Act 1970
- Banking Companies (Acquisition and Transfer of Undertakings) Act 1980
- Negotiable Instruments Act, 1881
- Regional Rural Banks Act, 1976
- The Companies Act, 2013
- The Co-Operative Societies Act, 1912

Acts Applicable for Bank Audits

- The Maharashtra Co-Operative Societies Act, 1960
- The Information Technology Act, 2000
- Prevention Of Money Laundering Act, 2002
- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- Limitation Act, 1963
- The Indian Contract Act, 1872
- Transfer of Property Act, 1882
- The Insolvency And Bankruptcy Code, 2016

List of RBI Circular

Practically Speaking All circulars are important

List of such IMP circulars is available in Guidance
Note 2025 for bank branch Audit

Points For Discussion

- **Types** of Loans & Advances
- **Sector** Wise Classification
- **Security** wise Classification
- **Prudential** Norms Wise Classification
- Pre Sanction Verification
- Importance of Documentation
- Verification of Loans & Advances in Detail
- Various Charges Created in Loans & Advances.
- Monitoring
- Other Related Topics

Types of Loans & Advances

Types of Loans & Advances

- **Fund Based** :- **Actual transfer** of funds from the bank to the borrower.
 - Term Loans
 - Cash Credit
 - WCTL
 - Overdraft
 - Bill Discounting / Bill Purchase / Foreign Bills for collection / Advance against bills for collection
 - Exports Credit–Pre/Post Shipment
 - Imports Credit–Capital Goods/RM

Types of Loans & Advances

- **Non Fund Based** :- Advances are those where there is **no transfer of funds** from the bank to the borrower.
 - Letter Of Credit (**LC**)
 - Bank Guarantees, (**BG**)
 - Co-acceptance Of Bill.

Non fund facility may **TURN** into a **funded** facility.

E.g. letter of credit – **devolved**,
 Bank Guarantee – **Invoked**

Sector wise classification

Sector wise classification

- Priority

- Agriculture
- Education
- Housing
- Export credits
- MSME
- Social Infrastructure
- Renewable energy
- Others

- Non Priority

- Sectors other than priority are covered under non priority sector

Priority Sector – Target of Lending

- Domestic scheduled commercial banks and Foreign banks **with 20 branches** and above
 - **40 %** of **Adjusted Net Bank Credit (ANBC)** or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher
- Foreign banks with **less than 20** branches
 - **40 %** of Adjusted Net Bank Credit (**ANBC**) or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher; to be **achieved in a phased manner by 2020**

Priority Sector - Target

- Total priority sector lending – 40%
- Agriculture Loan - 18%
- Micro Enterprises – 7.5%
- Advance to Weaker Section – 12 %

What is priority Advances ?

- i. Agriculture
- ii. Micro, Small and Medium Enterprises
- iii. Export Credit
- iv. Education
- v. Housing
- vi. Social Infrastructure
- vii. Renewable Energy
- viii. Others

Definition of Micro, Small and Medium Enterprises (MSMEs)

- In terms of Gazette Notification S.O. 2119 (E) dated June 26, 2020, an enterprise shall be classified as a **micro, small or medium** enterprise on the basis of the following criteria viz.,
 - i. a **micro** enterprise, where the investment in **plant and machinery or equipment does not exceed ₹1 crore and turnover does not exceed ₹5 crore;**
 - ii. a **small** enterprise, where the investment in **plant and machinery or equipment does not exceed ₹10 crore and turnover does not exceed ₹50 crore; and**
 - iii. a **medium** enterprise, where the investment in **plant and machinery or equipment does not exceed ₹50 crore and turnover does not exceed ₹250 crore**

Education

- Loans to individuals for educational purposes, including vocational courses, **not exceeding ₹ 20 lakh** will be considered as eligible for priority sector classification. Loans currently classified as priority sector will continue till maturity.

Housing

- Loans to individuals up to ₹35 lakh in metropolitan centres (with population of ten lakh and above) and up to ₹25 lakh in other centres for purchase/construction of a dwelling unit per family
- provided the overall cost of the dwelling unit in the metropolitan centre and at other centres does not exceed ₹45 lakh and ₹30 lakh respectively.

Repairing Home

- **Loans** up to ₹10 lakh in metropolitan centres
- and
- **up to ₹6 lakh in other centres** for repairs to damaged dwelling units
- conforming to the overall cost of the dwelling unit as prescribed

Security Wise Classification

Security wise classification

- Security Wise classification
 - Secured - by **tangible assets**
 - Unsecured
 - **Improper classification** results in over / under provisioning .

VIMP

Ex :- For vehicle / P& M after accident

Prudential Norms Wise Classification

Prudential Norms Wise Classification

Standard Loans

Regular

Special **M**entioned **A**ccounts (**SMA**)

(SMA 0 = 0- 30 days , SMA 1 = 30-60 days ,SMA 2 =60-90 days)

NPA loans

Sub standard Loans

Doubtful (I in year , II 1 to 3 year , III 3 year & above)

Loss

Provisioning

STANDARD

• GENERAL	0.40%
• AGRICULTURE & MSME	0.25%
• COMMERCIAL REAL ESTATE WITH RESIDENTIAL	0.75 %
• COMMERCIAL REAL ESTATE	1.00%

SUBSTANDARD

• SECURED PORTION	15%
• UNSECURED	25%

DOUBTFUL

• D-1 (UPTO 1 YEAR)	25%
• D-2 (1 TO 3 YEARS)	40%
• D-3 (OVER 3 YEARS)	100%
• UNSECURED PORTION	100%
• Loss assets should be written off	100%

Verification Of Advances

Steps in Verification

- Loan Application
- Pre Sanction Verification
- Documentation
- Post Sanction verification
- Monitoring of the Advance
- Recovery
- Report

Loan Application

- Must be in **Bank Format**
- **Details of the Borrower** ID proof / Income Proof / Residential Address Proof
- Details of the **Guarantors** ID proof / Income Proof / Residential Address Proof
- KYC To be **Verified from Original**
- Required **Purpose** of loan
- Assets to be purchased details / **Project Report**

Pre Sanction

- Basic **policies** of the Bank for Finance
- Verification of **status** of borrower , proprietorship proof / Partnership Deed / MA & AA / Society registration / trust registration , deed etc ,
- **Financial Documents** of Borrower and Guarantor like ITR, Balance Sheet , Audit reports etc
- **Various registrations** like PAN / TAN registration , IEC Registration / SSI registration , GST ,Pollution Control , FDA registration etc

Pre Sanction

- Due diligence for identification of the borrower including pre sanction visit
- Direct third party verification of documents
- Generation of CIBIL reports, CRIF , reference to RBI defaulters list, ECGC caution list
- Satisfactory status report from the existing bankers
- Credit risk rating done
- Site verification and valuation of immovable properties by approved valuer and branch official

Pre Sanction

- **CERSAI Verification** for any existing charge on immovable property. (Central Registry of Securitisation Asset Reconstruction and Security Interest of India)
- **ROC** search
- **Assessment of limit** as per the guidelines
- Loan granted within **the discretionary power**
- Compliance of **Bank's lending policy** stipulations
- Compliance of **take over norms**
- Issuance of sanction letter

Documentation

Documentation- Definition

- Section 29 of Indian Penal Code, 1860 states that the document denotes any matter expressed or described upon any substance by means of letters, figures or marks or by more than one of these means, intended to be used or which may be used as evidence of that matters.

Documentation - Definition of Instrument

- Section 2(14) of Indian Stamp act, 1899 defines instrument.
- Instrument is also a “document and includes affidavits”.
- A document creates or purports to create a right or liability.
- However, a copy of document cannot be termed as instrument because it does not itself create any right or liability.
- It is also required that a document must be executed by the parties concerned to make a document an instrument.

Documentation - Importance

- Documents are the **means** which prove and establish before a **court of law** that the **money was lent** and the same has not been repaid.
- **Invalid/Time barred documents affect** the Bank 's **right to recover** the loans through the court of law.
- **Process of execution** of documents known as **Documentation**

Documentation - Commonly Used Documents

- Demand Promissory note
- Loan Agreement
- Hypothecation deed
- Guarantee Agreement
- Various other as per normal bank's policy
- Every type of loan will have different sets of Documents as per each bank

Documentation - Ingredients of Documents

- Properly filled, duly stamped and signed by the borrower and guarantor
- Proper value of stamp or stamp paper to be used
- Date of stamp paper to be before the date of execution
- Stamp Paper to be in the name of the borrower or the Bank
- Stamp Paper should not be expired on the date of execution

Documentation - Ingredients of Documents

- Overwriting/Cuttings to be duly authenticated
- Execution of documents by the legally competent persons
- Documents on the printed format of the Bank.
- No computer generated documents except through LAPS (Loan Application Processing System)

Documentation - Who Can Not Execute

- Persons **not legally competent to execute** the documents:
 - a. Minor,
 - b. Insolvent,
 - c. Insane,
 - d. Person of unsound mind,
 - e. Heavily drunk person

Documentation - Limitation Period

- Normally 3 years.
- In case of term loans, 3 years to be reckoned from the date of default
- Limitation period can be extended through
 - Obtaining fresh documents / Letter of Revival
 - Section 18 of the Limitation Act extends the period of limitation :-
“when an acknowledgement of debt is obtained in writing “

Documentation - Limitation Period

- Obtaining Balance confirmation
- Part payment in the account
- A debit entry shown on the Liability side of a borrower's balance sheet i.e., of a Limited Company, signed by its agents is considered an acknowledgement of debt

(Babulal Rukmandand vs. Official Liquidator 1968, 1, com.lj).

Documentation - General

- **Acceptance** of sanction by Borrower and Guarantor
- **All** required documents **executed**.
- Requisite stamp duty as per **the state laws**
- **Entry in document register** made
- **Vetting** of documents by panel advocate
- **Creation of Equitable** Mortgage as per the guidelines
- **CERSAI registration** in case of Equitable Mortgage of property

Documentation – General

- Charge registration **with ROC** in case of company (Explained in detail)
- **Insurance of assets** taken as primary or collateral security
- Entry in the **system with proper masters**
- **End use confirmation** Like Tax Invoice or Purchase of Assets or Agreement copy etc
- **Margin confirmation** Like certificate from CA

Documentation - Important Aspects Of ROC Charge Registration

- Covered under **Section 77** of the Companies Act 2013
- Charge is required to be **registered within 30 days** . However, additional 30 + 60 days are allowed to file charge with additional fee.
- Charge is required to be created **for all assets** (tangible as well as intangible)
- charge”, ‘pledges’ and ‘liens’ were also required to be registered.

Verifications OF Loans

Fund Based

Term Loans

- Available for acquiring fixed assets
- Assets may be Movable or immovable
- Repayment in a fixed period
- Generally Fixed Rate is applied
- Moratorium may be available
- Project Report needs to be submitted
- End use verification and visit is expected
- May be for original or for Resale Assets

Term Loans

- **TEV** (Techno Economic Viability)**study** wherever applicable done
- All **project approval obtained** and held in records
- **Satisfactory credit report** of suppliers of machineries from the **approved rating agency** available
- **Funds released** on basis of **quotations available after keeping prescribed margin**
- **Bills in support** of assets acquired available in records
- **Insurance** of machineries done
- **Post** disbursement **inspection made**

Term Loans - Retail loans

- Housing Loan
- Car Loan
- Education Loan
- Loan against FDR's
- Loan against LIC Policies
- Loan against securities
- Gold Loan
- Agricultural Loans

As per RBI Housing Loan LTV

Category of Loan	LTV Ratio (%)	Risk Weight (%)	Standard Asset Provisioning (%)
(a) Individual Housing Loans			
(i) Up to Rs. 20 lakh	90	50	0.40
(ii) Above Rs. 20 lakh and up to Rs. 75 lakh	80	50	0.40
(iii) Above Rs.75 lakh	75	75	0.40
b) CRE-RH	NA	75	0.75
(c) CRE	NA	100	1.00

As per RBI Housing Loan LTV After June 7, 2017

Category of Loan	LTV Ratio (%)	Risk Weight (%)	Standard Asset Provisioning (%)
(a) Individual Housing Loans			
(i) Up to Rs. 30 lakh	≤ 80	35	0.25
	> 80 and ≤ 90	50	0.25
Above Rs.30 lakh and up to Rs.75 lakh	≤ 80	35	0.25
(iii) Above Rs.75 lakh	≤ 75	50	0.25

LTV for Housing Loan

- RBI circular **February 03, 2012 on – Inclusion** of stamp duty, registration and other documentation charges **in the cost of the house property**
- banks should **NOT include these charges** in the cost of the housing property they finance so that the **effectiveness of LTV norms is not diluted.**

LTV for Housing Loan

- RBI Circular **March 15 , 2015**
- It Has Been Decided That In Cases Where The Cost Of The House/Dwelling Unit **Does Not Exceed Rs.10 Lakh**, Banks **May Add** Stamp Duty, Registration And Other Documentation Charges To The Cost Of The House/Dwelling Unit For The **Purpose Of Calculating LTV Ratio.**

Term Loan - Housing Loan

- **Original Agreement** between builder and borrower
- If in **2nd sale then chain Agreement** till last sales agreement between buyer and seller
- Along with **registration receipts & payment of stamp duty in original**
- **NOC** from society or Builder
- **Letter of Awareness** to builder / society
- **Non Encumbrance Certificate** (NEC) from panel advocate

Term Loan - Housing Loan

- Or **Title** clearance
- **Valuation by approved valuer** in case of 2 nd sale
- Creation of valid **mortgage**
- **CERSAI** registration
- **Insurance of house** property
- Notice of Intimation in some states

Term Loan - Housing Loan

- Construction of House :
- As per RBI circular No DIR.BC.13/08.12.001/2015-16 dated 1/7/2015 , **compliance of following guidelines :**
- Availability of **sanction plan from the competent** authority in the name of the applicant
- **affidavit-cum-undertaking** - not violate the sanctioned plan
- **Submission of completion certificate within 3 months** from the date of completion.
- **Failure** leads to giving right to the Bank to **recall the loan.**

Term Loan - CAR LOAN

- Loan Application
- Vehicle Quotation
- Margin Money deposition
- KYC and due diligence
- Proper appraisal of limit
- Release of loan on basis of quotation of car

Term Loan - CAR LOAN....

- Either **Direct transfer** to the car dealer or transfer to borrower account subject to proof of full payment
- **Bill and insurance** of car to be obtained
- **RC to be submitted** by the borrower and **charge Noting**
- **Post disbursement** inspection of the car
- Cost May change **in quote and actual bill SO be careful** - due to some discount / gifts

Term Loan - Education Loan

- Proper KYC and due diligence
- Education from accredited Institution/University
- Original payment receipts of fee paid
- Periodic progress report of student borrower
- Interest on interest collection flag to be marked as 'Y' after the start of EMIs.

Term Loan - Education Loan

- Repayment period: **Course period + 1 year or 6 months after getting job, whichever is earlier.**
- Maximum quantum of finance in **India Rs. 10 lakhs and abroad Rs. 20 lakhs**
- **1% int. concession** if interest is serviced during moratorium period (concession available for moratorium period only)
- Every year you need to confirm with university

TL Education loan - Security and Margin

Particulars	Margin	Security
Upto ₹ 4 lakhs	Nil	Parents to be joint borrower(s). Banks have a discretion to waive this.
Above ₹ 4 lakhs and upto ₹ 7.5 lakhs	In India – 5% Abroad – 15%	Parents to be joint borrower(s). Plus third party guarantee.
Above ₹ 7.5 lakhs	In India – 5% Abroad – 15%	Parents to be joint borrower(s). Plus tangible collateral security.

Term Loan - GOLD LOAN

- Loans against **pledge of gold ornaments**
- Bullet payment of loan **up to Rs 2.00 lakhs**
- Banks required to maintain a **minimum LTV** (Loan to value ratio) of **75%** of value of gold ornaments
- LTV to be maintained **through out the tenure** of the loan and will be computed **against total outstanding including interest**
- average of the closing **price of 22 carat** gold for **the preceding 30 days** as quote

Term Loan - GOLD LOAN

- Gold ornaments to be the **approved valuer** of the Bank
- If Period of tenure **exceed 12 months from the date of sanction**
- **Interest will be charged to the account at monthly rests**
- To Complete **detail of inventory in the Security register** duly signed by the borrower

Cash Credit

- To **finance working capital** requirements
- Requires periodic **renewal** (usually yearly)
- Requires **monthly stock** statement for calculation **of drawing power**
- Requires **monitoring of end use** of funds
- Requires **project report**
- **Yearly visit** and evaluation necessary

Cash credit - Verification

- Appraisal of Sanction limit
 - Turnover Method 20% of projected sales
 - Traditional Method

Based on MPBF calculated on basis of working capital gap
- Verification of drawing power
 - DP is the amount of working capital funds allowed to borrower to draw from the working capital limit allotted to him
 - Calculated on basis of stock statements submitted by the borrower
 - It is DP allowed or Sanction Limit whichever is lower .

CC - DP Calculation

- $\text{Stock} + \text{Debtors} - \text{creditors} = \text{Working Capital}$
- $\text{Working Capital} - \text{Margin} = \text{Allowed Dp}$
- In some banks Margin for debtors and stock is different
- While calculating Debtors need to remember whether Bill Discounting is given to the said borrower
- Need to check No of days permitted as debtors
- Need to see that constant stock is not there for last 3 months or more which is slow moving stock

CC- Points For Verification Of Stock Statements

- Stock statements to be in the Bank's **prescribed format**
- Submission of Stock Statement **at prescribed interval**
- Stock statement as **on last date** of the month.
- **Age wise classification** of Sundry Debtors
- **No DP** on book debts against **associate concerns** if stipulated in sanction

CC- Points For Verification Of Stock Statements

- Quarterly certification of book debts by the Statutory Auditors of the borrower.
- Detail of Sundry Creditors provided
- Stocks purchased under LC to be shown separately
- Margin calculated correctly
- Correct. entry in system
- Penal interest flag for non submission is “ Y”

CC - Insurance

- See the same for **primary & collateral**
- See **for type of security** like fire, earthquake, burglary, terrorism etc.
- See for **all locations of Stocks** and stock in transit as well
- Also **confirm address** of risk cover on policy
- **Bank's clause** in insurance policy
- **Validity period** to be alive

CC- Monitoring of accounts

- Withdrawals from the account for purchase of material and meeting day to day operational expenses
- See whether any heavy withdrawal observed
- See sufficient credits are available to cover interest is covered
- Confirm that any credit is not due to sale of any assets and unusual credits not related to business activity

CC- Monitoring of accounts

- Or **Credit from sister concern** and rotation of funds just to arrive at proper report in the system
- Also confirm whether **from related party** .
- **Annual review of accounts – Non renewal for over 180 days amount to slippage of accounts to NPA**

Bill Discounting

- ‘invoice discounting’ or ‘bills discounting’ or ‘purchase of bills’ are all same
- source of **working capital** finance for the seller of goods on credit.
- Bill discounting is an arrangement whereby the **seller recovers an amount of sales bill from the financial intermediaries before it is due.**

Bill Discounting

- Bill discounting against **sanctioned limit** of the borrower
- Bills to represent **genuine trade transaction-no accommodation bills**
- Facility to be allowed to **only customer availing regular credit facilities. Walk in customers to be avoided.**
- Bills to be **accompanied by GRs of IBA** approved transporters. Now E way Bill

Bill Discounting

- Bills to be realized on due dates.
- If bills are drawn under LC, ensure that LC is issued through SFMS
- (Structured Financial Messaging System - A secured messaging software developed for inter banks and intra bank applications)

WCTL

- Working Capital Term Loan
- In some Banks this Loan is given
- Is for Actually for project finance
- Loan Sanction as per the stage of the project
- But repayable in Installments as per the recovery
- Always funded on stage basis on net required Amount.

Overdraft

- Normally against FDR or
- Immovable property or
- Against NSC / LIC etc
- Annual renewal if allowed against property
- Renewal on maturity of deposit also.
- No requirement for submission of stock statements / or only once in half year

OD - Loan Against FDR

- No loans against other bank's deposits as per RBI's guidelines (as seen earlier)
- No loan against third party deposits if prohibited by Bank's loan policy
- Loan against FDR if in joint name- to be applied and documents to be executed by joint holders
- Prescribed margin maintained
- FDR discharged and bank's lien marked on FDR as well in system
- Correct rate of interest charged

OD - Loan Against LIC Policies

- LIC Policy to be in the name of the applicant and it is alive
- Surrender value obtained and advance granted on basis of surrender value after keeping prescribed margin
- Up-to-date premium paid
- Policy is assigned in favour of the Bank

OD - Loan Against Shares / Securities

- No loan against partly paid up shares allowed
- Maximum amount of loan against shares to individuals :
 - Rs 10 lacs held in physical form - Margin 50 %
 - Rs. 20 lacs held in DEMAT form – Margin 25 %
- Not to Large Group of Individuals to support any script
- No loans to be granted to partnership / proprietorship concerns against the primary security of shares and debentures.

Agricultural Advance

- What are the **categories under 'Agriculture'**
- Classified Under **Three Sub-categories** Viz
 1. **Farm credit**, (which will include short-term crop loans and medium/long-term credit to farmers)
 2. Agriculture **infrastructure**
 3. **Ancillary** activities.

Exports Credit – Pre-Shipment

- Pre-shipment finance refers to the financial assistance provided to the **exporters before actual shipment of goods.**
- Pre-shipment finance is provided to the exporters for **the purposes like purchase of raw materials, their processing and converting into finished goods** and packaging them.

Export Credits - Pre Shipment (Packing Credit)

- To be released **against LC or confirmed order** from the overseas buyer
- Normally should maintain **separate account** for each packing credit facility
- May have **Running account** – depends on banks judgement
- Satisfactory **credit report of overseas buyers** from approved credit Agencies - available
- Packing credit **utilized for purchasing goods for export purposes only** NOT for Indian Sale
- **ECGC coverage obtained.**
- ECGC premium to be **borne by the borrower.**

Export Credits - Pre Shipment (Packing Credit)

- Packing credit granted for a **maximum period of 270** days with further extension allowed upto 90 days with permission of higher authorities.
- **Reporting to RBI** case Packing Credit **not adjusted within 360 days.**

Export Credits - Pre Shipment (Packing Credit)

- In case of **over due Packing Credit**, **ECGC to be duly notified**
- **If export does not take place**, interest at commercial rate to be recovered from the date of released.
- **Interest subvention**, if granted, to be **duly claimed**.
- **No interest subvention on overdue packing credits.**
- Monthly stock statements submitted and release restricted to allowable DP
- To be **liquidated out of proceeds of export bills** .
- If liquidated from **inland proceeds**, commercial rate of interest from the date of release to be charged.

Exports Credit–Post Shipment

- Post-shipment finance may be as “any loan or advance granted or any other credit provided by a bank **to an exporter of goods from India** from the date of extending the credit **after shipment of goods to the date of realization of** export proceeds.”
- Exporter may **opt both post** and pre shipment finance .
- Pre shipment is **adjusted by post** shipment finance
- post-shipment finance serves as **bridge loan for the period between shipment of goods and the realization of proceeds**

Export Credits - Post Shipment Credit

- Extended in the form of **discounting of export bills** or advance against export bills for collection.
- **Satisfactory credit report** of overseas buyer available from the approved rating agency
- **No existing overdue export bills** while discounting new bill.
- **Fresh bills not to be discounted to adjust old overdue bills**
- Interest **subvention claimed** .
- **No interest subvention on overdue bills**

Export Credits - Post Shipment Credit

- Bills liquidated from **export proceeds**
- **ECGC coverage available**. Premium on post shipment to be borne by the bank.
- In case of **extension of bills**, ECGC to be duly **notified**.
- Timely submission of **claim to ECGC in case of default by the borrower**.
- Bills accompanied by export documents including **shipping bill, bill of lading, invoice**
- Authenticity of Shipping Bill issued by the customs verified from the site “Icegate.gov.in”

Trade Credits (TC)

- Trade Credits (TC) refer to the credits extended by the **overseas supplier, bank, financial institution and other permitted recognised lenders** for maturity, as prescribed in this framework, for **imports of capital/non-capital goods permissible** under the **Foreign Trade Policy** of the Government of India. Depending on the source of finance, such TCs include suppliers' credit and buyers' credit from recognised lenders.

Imports Credit–Capital Goods /RM OR Letter of Comfort

- **Buyer credit** is a short **term credit** available to an importer (buyer) **from overseas lenders** such as **banks and other financial** institution for goods they are importing.
- The overseas banks usually lend the importer (buyer) **based on the letter of comfort** (a bank **guarantee**) issued by the **importer's bank**.
- For this service the importer's bank or buyer's **credit consultant charges a fee called an arrangement fee**.

Imports Credit–Capital Goods /RM OR Letter of Comfort

- Examine **Application** form carefully.
- Check whether it is **for Raw Material or Capital Goods**
- Check the **terms of sanction by intermediary foreign bank**
- Check the **documentation**
- **Interest Payments** and Repayment of Loan
- **Income booking** by the Bank
- **Settlement / Roll over of LoC**

Non Fund based

Letter Of Credit

- Appears in Balance sheet at both sides
- Just as Information Purpose (CONTRA)
- List of LC issued during period and O/s List should be obtained and checked
- An undertaking from the Bank on behalf of the customer (buyer) to the seller of the goods to pay the contracted amount.
- In case the buyer fails to pay on the stipulated date , Known as LC devolvment
- I.e default by the customer.

Documents Generally Required For L/C

- 1) Proforma invoice / **purchase order**- certified copy
- 2) L/C **application form** dully filled and signed
- 3) Particular of **insurance** (except CIF)
- 4) **Board resolution** – stating the L/C facility and the amount of L/C, for corporation OR photo copy of **partnership deed** and partner consent letter OR **request letter** in case of **proprietary firm**
– as applicable
- 5) **FEMA Declaration** in prescribed form
- 6) Import Export Code certificate (**IEC**)

Documents Generally Required For L/C

- 7) **Counter indemnity** for 0.10% of the L/C value equivalent to rupee (on stamp paper / franking)
- 8) **Margin money** as per the understanding between the importer and his bank. **Generally 10% to 25% of L/C** amount is considered as margin money. The amounts of the margin are given by way of Fixed Deposit. The margin money is depends upon the creditworthiness of the applicant. For a new customer bank **may ask for 100%** of L/C amount as margin money.
- 9) **Import license** in case of restricted items of import
- 10) Any other documents as per the request of the bank

Documents Generally Required For L/C

- Commercial invoice (Proof of value)
- Bill of lading (Proof of shipment)
- Packing list (Proof of packing)
- Certificate of origin(Proof of origin)
- Inspection certificate(proof of quality)
- Insurance certificate(Proof of insurance)
- Draft of bill of exchange

Letter of credit

- Issue of LCs through SFMS / SWIFT
- Satisfactory credit report of the beneficiary from the approved rating agency available
- LCs cover goods in which the customer deals
- Applicable commission charged
- LC within the sanctioned limit.
- Prescribed margin maintained.
- Goods transported through IBA approved transporters
- Expired LC reversed - VIMP
- No fresh LC in case of existing devolved LC

Bank Guarantee

- Appears in B/s at both side just for information
- Obtain list of BG issued and O/s and check
- **Financial** : to meet financial obligations
(like security deposits)
- **Performance** : To meet contractual obligations
(like satisfactory project completion)
- **Binding on the issuing Bank to pay** to the beneficiary the guarantee amount in **case of default by the customer.**
- Exercise of the right by the beneficiary known as **Invocation** of guarantee.

Bank guarantee

- Issue of Bank Guarantee through SFMS
- Bank guarantee issued within the sanctioned limit
- Prescribed margin maintained
- Application commission including commission for claim period recovered
- In case of Performance Guarantee, periodical progress report from competent engineer obtained
- Expired Bank Guarantees reversed

Bank Guarantees RBI Guidelines

- not to provide guarantees or equivalent commitments for issuance of bonds or debt instruments of any kind.
- no bank guarantee should normally have a maturity of more than 10 years
- banks may evolve a policy on issuance of guarantees beyond 10 years as considered appropriate with the approval of their Board of Directors Apr 22,2009

Bank Guarantees RBI Guidelines

- Bank Guarantees **exceeding Rs. 50,000/-** to be signed **by 2 branch** officials jointly.
- Bank Guarantees to Stock Exchange on share brokers- maintenance of minimum 50% margin out of which minimum 25% cash margin to be maintained
- If Invoked then check whether **tagged as Claim Registered** and converted to fund base
- **Immediate payment of invoked Bank guarantees**

Co-acceptance Of Bill.

- **Bill of exchange** drawn by the supplier on the buyer of goods (customer of the Bank) **co accepted by Bank.**
- Acts as **a guarantee by the Bank** to the supplier to make payment in case of non payment by the buyer

Co-acceptance of bills

- Represent **genuine trade bills**
- Co acceptance of **bills of Rs. 10,000/- or more** to be **signed by 2 branch** officials jointly
- Facility to **customers already enjoying credit** facilities from the Bank
- Thus very much similar Like LC only
- What is difference ?

Difference

- Due to **Monetary benefit** compared to buying goods under LC
- Since LC commission needs to be paid **before shipment** of the goods i.e from the date of opening of the LC
- This is only **after shipment** of goods and after getting to importer documents of title of the goods.
- Its therefore **short term facility** and can be rotated no. times by the importer

Monitoring

Monitoring

- All terms of **sanction duly complied** with
- **Disbursement** as per the terms of sanction.
- Prescribed **margin** obtained.
- **Rate of interest** correctly fed in system
- Applicable **charges recovered** like processing fee , valuation charges , legal fees , any other if applicable .
- **Overdrawing's in the account need based**, properly reported, within discretionary power, adjusted in time

Monitoring

- Primary securities created and necessary bills held as proof of purchase
- Post disbursement inspection made
- Submission of stock statement at prescribed interval, calculation of DP as per lending policy
- Stock audit in applicable cases
- Balance confirmation letter at periodic intervals

Monitoring

- Monitoring Of Operations In Account .
- Prompt Action In Case Of Early Warning Signals
- Including Low Turnover,
- Frequent Excess,
- Frequent Returning Of Cheques,
- Huge Cash Deposits And Withdrawals,
- Frequent LC Devolvement

Monitoring

- Submission of statements of financial performance (QIS etc)
- Renewal of Insurance of primary and collateral securities
- Submission of NO dues statutory statement certified by CA for each year .
- Renewal of working capital limits on annual basis

Types Of Securities And Charges:

Types Of Securities And Charges:

- **Immovable properties** like house properties, plots of land; leaseholds are the most common.
- Amongst **movables**, shares, insurance policies, debentures, book debts, bank deposits, stock in trade etc., are a few examples.
- Whereas, an immovable property is **mortgaged**, the movables are **pledged or hypothecated**,
- In the case of companies **all are charged by way of a floating charge**.

TYPES OF CHARGES: PLEDGE

- Under **section 172 of Indian Contract Act** pledge means “Bailment of Goods as a security for repayment of a debt or performance of a promise”.
- Important **features** of Pledge are –
- Actual or **constructive delivery** of security is given to the Bank.
- **Ownership remains** with bailers (**Borrower**).
- **Liable to returned** after fulfilment of promise or repayment of loan amount.

TYPES OF CHARGES: PLEDGE...

- Disposal possible only after default and giving due notice to the bailer (Borrower).
- A common example of pledge is gold ornaments, which are pledged with the Bank as a
- security against which Gold Loan is given.

TYPES OF CHARGES: HYPOTHECATION

- It is **not defined under any law**. Extended idea of pledge.
- It relates to **goods/commodities, movable machinery, vehicles, book-debts**.
- **Ownership** remains with **the borrower**.
- **Possession is also** with the borrower.
- **Symbolic/constructive possession** with creditor (Bank).

TYPES OF CHARGES: HYPOTHECATION...

- It creates **an equitable charge**.
- Hypothecation Agreement gives Banker a **right to take possession of hypothecated goods, machines**.
- Examples of Hypothecation charge are hypothecation of **stocks, receivables, vehicles etc.**

TYPES OF CHARGES: ASSIGNMENTS

- It is covered under **section 130 of Transfer of Property Act 1882.**
- Only actionable claims can be assigned. (**LIC policies, Supply, Bills, Book Debts etc.**)
- **Transfer of existing/future debts, right or property** belonging to a person in favour of another person.
- Assignee gets **absolute right over money/debts** assigned to in his favour or to him.
- **Assignee has priority over other's claim.**

TYPES OF CHARGES : SET OFF

- “Right of a Banker to appropriate the credit balance in one account of the customer towards sums due by customer to the Banker in another account in order to arrive at the net sum due”.
- Can be executed in the absence of any contract to the contrary.
- Account should be in identical names of the same person.
- All branches of the Bank can be treated as one.

TYPES OF CHARGES : SET OFF...

- Debts should be due immediately.
- Debts should be recoverable.
- Right of set-off is applicable to Banker alone and not to the customer.
- Banker has a priority over other attachment orders.

TYPES OF CHARGES : BANKER'S LIEN

- “A lien is a right of the creditor in possession of goods, securities or any other asset belonging to the debtor to retain them until the liability is discharged, provided that there is no contract expressed or implied to the contrary”.
- A lien confers only the right to the creditor to retain goods, until debt is discharged, but does not give right of sale.
- No agreement is necessary.
- The debt should arise out of some service rendered or money spent on the goods/securities on which the right of lien is to be exercised.
- Best examples of lien are Goldsmith's, Tailor's, Carrier's and Watch Repairer's etc.

TYPES OF CHARGES : MORTGAGE

- Transfer of Property Act 1882 defines Mortgage as: -
- “Transfer of an interest in specific immovable property for the purpose of securing the payment of money advanced by way of loan, on existing or future debt or the performance of an engagement which may give rise to pecuniary liability”.

TYPES OF CHARGES : MORTGAGE...

- Thus the essentials of mortgage are:
 - Mortgagor must be the owner or a person having interest in immovable property.
 - Mortgagor must have a contractual capacity.
 - Property must be a specific immovable property.
 - Purpose is to secure the loan repayment.

TYPES OF MORTGAGES

- **Simple Mortgage**

- It is like a charge.
- Mortgagee does **not enjoy right of foreclosure**, right to **enter into possession** or **even sale without court's intervention**.
- Can be **created anywhere, by any person, anywhere for any property**.
- **Needs to be registered** with Sub-Registrar of Assurances.

- **Usufructuary Mortgage**

- Confers on mortgagee a **right of possession** of the property **and right to enjoy rents/profits**, until the debt is paid.
- **No rights to sale**.

TYPES OF MORTGAGES

- **English Mortgage Or Registered Mortgage**
 - Property is transferred absolutely to the mortgagee.
 - Mortgagor agrees to bind himself to repay the mortgage money on a certain day.
 - Provision to reconvey the property to the mortgagor on payment on due date.
 - Mortgagee has a right of private sale (subject to restrictions under section 69 of Transfer of Property Act 1882)
 - Registration compulsory.

TYPES OF MORTGAGES

- Mortgage by Deposit of Title Deeds (Equitable Mortgage)
 - No registration required.
 - Created by depositing Original Title Deeds of the Property by owner with the Bank.
 - Can be created at specific centres only.
 - Attracts stamp duty.
 - No right to enter into possession.
 - No right of appointment of receiver is available.

TYPES OF MORTGAGES

- Persons Not Entitled to do the Mortgadge :-
 - Under Section 7 of Transfer of Property Act, any **person competent to contract can transfer property.**
 - Therefore a **minor; insolvent, insane, idiot,** alien enemy; felon, drunkard cannot execute a mortgage deed.

TYPES OF MORTGAGES Case of Company Property

- A mortgage by a company should be duly authorised by a resolution according to the Articles of Association and transaction should not be ultra vires the Memorandum of Association.
- The charge thus created shall be registered with the Registrar of Companies.
- Mortgage affected by the promoters of a company before its incorporation is invalid. It cannot be ratified after incorporation because the principal was not in existence at the time of the transaction by an agent.

TYPES OF MORTGAGES Case of Company Property

- In the event of a default, the mortgagee is entitled to file a suit for Foreclosure or a Suit for Sale as per the terms of the Mortgage in terms in the Mortgage deed.
- Banks being financial institutions file suits only for sale and for money.

Other Related Issues

Adhoc Limits / Temporary limits

- **Application** from the borrower
- For **genuine** reasons
- All the relevant **supporting's submitted** by the borrower
- Corresponding **changes made in the security and loan agreements**
- Appropriate **authority to sanction**
- Given for a **specified period and adjusted** within the said time
- Should **not be accommodation** facility

Transfer of borrower accounts from one bank to another

- Banks should put in place a board approved policy with regard to take-over of accounts from another bank.
- Authority levels for sanction of takeover,
- Reporting of takeover to higher authorities,
Monitoring mechanism
- Credit audit
- Examination of staff accountability especially in case of quick mortality
- Periodic review of taken over accounts at board / board committee level, top management level, etc.

Transfer of borrower accounts from one bank to another

- obtain **necessary credit information** from the transferor bank as per the format prescribed in Annex II of RBI circular DBOD.No.BP.BC.94/08.12.001/2008-09 dated December 8, 2008
- The transferor bank, on receipt of a request from the transferee bank, **should share necessary credit information as per the prescribed format at the earliest**

Consortium Arrangement

- Number of lending banks is **more than one**.
- The **lending banks form a** formal consortium.
- Main features:
 - Bank with the **largest exposure is the lead bank**
 - **Common set of loan documents**, which is obtained by the lead bank on behalf of all the consortium member banks.
 - **Lead bank is responsible** for overall **monitoring**.
 - The **securities are shared by the member banks in an agreed proportion** based on their exposures.
 - Borrower maintains direct business relationship with all the member banks of consortium

Lending under Consortium Banking Arrangement

- Various restrictions in consortium finance, withdrawn by Reserve Bank of India in October 1996
- Central Vigilance Commission, shown concern due to various frauds in such type of lending because of lack of sharing of information
- Matter has examined in consultation with the Indian Banks Association

Lending under Consortium Banking Arrangement

- DBOD.No.BP.BC.94/08.12.001/2008-09 dated December 8, 2008 the **banks are encouraged to strengthen their information back-up** about the borrowers enjoying credit facilities from multiple banks as under:
 - obtain **declaration from the borrowers** about the credit facilities already enjoyed by them from other banks in the format prescribed in Annex 6.
 - **exchange information** about the conduct of the borrowers' accounts

Lending under Consortium Banking Arrangement

- Obtain **regular certification** by a professional, preferably a Company Secretary, Chartered Accountant or Cost Accountant, regarding compliance of various statutory Dues - **VIMP**
- greater use of **credit reports** available from a credit information company
- **suitable clauses** in the loan agreements so as to address confidentiality issues.

Revenue Leakage

Revenue leakage - Charges

- **Processing Fee:**
 - Non charging of Processing fee
 - Non Charging of Processing fee for broken period
 - Non Charging of Processing fee on non fund based limits
- **Service Charges:**
 - Non charging of commitment charges
 - Non Charging of annual lead bank charges

Revenue leakage - Interest

- **Non Charging** of interest in the account
- **Reversal of penal interest** for non renewal due to back dated history change
- Loan against FDR- **Increase in rate of interest of FDR** without corresponding change in the rate of interest of the Loan account
- **Non charging of penal interest for non submission of stock statement**, non renewal of account
- Non charging for penal interest for non **compliance of terms of sanction like failure to obtain external rating**

Revenue leakage - Interest

- Continuation of **charging concessional rate of interest/applicable charges** after the lapse of sanction
- Non charging **commercial rate of interest** from the date of release in export limits where export has not taken place
- Charging of **rate of interest lower than** applicable rate of interest
- Continuation of charging **simple interest instead of compounded interest** in case of education loans where repayment has started

Questions ???

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Thank You