

International Asset Reconstruction Company Pvt. Ltd.

Policy in respect of identifying and disseminating credit information pertaining to Willful Defaulters

1. Definition of Willful default:

The term Willful Default has been defined as under:

A willful default would be deemed to have occurred if any of the following events is noted:

- a. The unit has defaulted in meeting its payment / repayment obligations to the lender, even when it has the capacity to honor the said obligations. (The term 'unit' will include individuals, juristic persons and other forms of business enterprises, whether incorporated or not.)
- b. The unit has defaulted in meeting its payment / repayment obligations to the lender and has not utilized the finance from the lender for the specific purposes for which finance was availed of, but has diverted the funds for other purposes.
- c. 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 utilized for the purpose for which the finance was availed of, nor are the funds available with the unit in the form of other assets.
- d. The unit has defaulted in meeting its payment / repayment obligations to the lender and has also disposed of 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.

"Diversion of Funds" referred to above would be construed to include any one of the undernoted occurrences:

1. Utilization of short term working capital funds for long term purposes, not in conformity with the terms of sanction
2. Deploying borrowed funds for purposes / activities of creation of assets other than those for which the loan was sanctioned
3. Transferring borrowed funds to subsidiaries / group companies or other corporates by whatever modalities
4. Routing of funds through any bank other than the lender bank or members of consortium without prior permission of the lender
5. Investment in other companies by way of acquiring equity / debt instruments without approval of lenders

6. Shortfall in deployment of fund vis-à-vis the amounts disbursed / drawn and the difference not being accounted for

“Siphoning of Funds” referred to above would be construed to occur if any funds borrowed from banks / FIs are utilized for purposes unrelated to the operations of the borrower, to the detriment of the financial health of the entity or of the lender. The decision as to whether a particular instance amounts to siphoning of funds would have to be a judgment of the lenders based on objective facts and circumstances of the case.

2. Cut-off Limit:

Willful defaulters would be identified and reported in respect of borrowers whose aggregate outstanding balance is Rs 25 lacs and above. The limit of Rs 25 lacs will also be applied for the purpose of taking cognizance of instances of siphoning or diversion of funds.

3. Procedure for Identification:

- i. The identification of willful default would be made keeping in view the track record of the borrowers and would not be decided on the basis of isolated transactions / incidents. The default, to be classified as willful, should be intentional, deliberate and calculated.

- ii. The policy will apply to all units, including individuals, juristic persons and all other forms of business enterprises, whether incorporated or not.

- iii. IARC will classify a borrower - the expression includes guarantor(s) - as willful defaulter based on actions of the borrower subsequent to the acquisition of the financial asset by IARC. It is expected that if such classification is warranted by earlier events, the originator may forward the evidence of willful default to IARC for such action as may be deemed necessary by IARC.

- iv. A transparent mechanism will be put in place for identifying Willful Defaulters on the following lines:

- a) The evidence of willful default on the part of the borrowing company and its promoter/whole-time director at the relevant time should be examined by a Committee headed by a President and consisting of two other senior officers of the rank not below Vice President. The exact composition of the Committee will be decided by the Managing Director & CEO from time to time. The decision on classification should be well documented and supported by requisite evidence. The decision should clearly spell out the reasons for which the borrower is being declared a willful defaulter, vis-à-vis RBI guidelines.

- b) Such action as referred to in para (a) above for classification of borrower as willful defaulter may also be initiated on the basis of evidence of such default forwarded by the originators or any one of them to IARC.

- c) If the Committee concludes that an event of willful default has occurred, it shall issue a Show Cause Notice to the concerned borrower and the promoter/whole-time director and call for their submissions and after considering their submissions issue an order recording the fact of

willful default and the reasons for the same. An opportunity should be given to the borrower and the promoter/whole-time director for a personal hearing if the Committee feels such an opportunity is necessary.

d) The order of the Committee shall be reviewed by another Committee headed by the MD & CEO and consisting, in addition, of two independent directors of IARC and the order shall become final only after it is confirmed by the said Review Committee.

e) As regard a non-promoter/non-whole time director, it should be kept in mind that Section 2(60) of the Companies Act, 2013 defines an officer who is in default to mean only the following categories of directors:

- Whole-time director
- ii) where there is no key managerial personnel, such director or directors as specified by the Board in this behalf and who has or have given his or their consent in writing to the Board to such specification, or all the directors, if no director is so specified;
- iii) every director, in respect of a contravention of any of the provisions of this Act, who is aware of such contravention by virtue of the receipt by him of any proceedings of the Board or participation in such proceedings and who has not objected to the same, or where such contravention had taken place with his consent or connivance.

Therefore, except in very rare cases, a non-whole time director shall not be considered as a willful defaulter unless it is conclusively established that

- he was aware of the fact of willful default by the borrower by virtue of any proceedings recorded in the Minutes of the Board or a Committee of the Board and has not recorded his objection to the same in the Minutes, or,
- the willful default had taken place with his consent or connivance.

(However, the above exception will not apply to a promoter director even if not a whole time director.)

A similar process as detailed in sub paras (a) to (c) above should be followed when identifying a non-promoter/non-whole time director as a willful defaulter.

4. End-use of Funds:

Cases of Willful Default are more likely to arise in cases taken up by IARC for restructuring, rehabilitation or rescheduling, especially where additional funding is provided or arranged by IARC, though instances of Willful Default cannot be totally ruled out even in other cases. In view of this, while approving restructuring or rescheduling, IARC will put in place adequate safeguards for ensuring and monitoring the end-use of funds. These will include, as appropriate in each case, the following:

- Scrutiny of periodical progress reports, operating statements, balance sheets etc. of the borrower,
- Regular inspection of assets charged as security
- Periodical scrutiny of borrower's books of accounts and no-lien accounts maintained with other banks
- Periodical visits to the assisted units
- Chartered Accountant's certificate regarding end-use of funds, especially when project finance is involved
- Periodical stock audits in case of working capital finance

5. Penal Measures in Respect of Willful Defaulters:

1. No additional facility will be granted by IARC to an entity which has been declared a Willful Defaulter either by IARC or by any other institution or bank.
2. Legal process, wherever warranted, for recovery of dues and foreclosure would be initiated expeditiously against the borrowers and guarantors.
3. Criminal proceedings may be initiated, wherever necessary, after obtaining prior approval of MD & CEO.
4. Wherever possible, a proactive approach would be adopted for a change of management.
5. In respect of restructuring packages and restructuring support finance, a covenant will be included in the relative facility documents, to the effect that the assisted company would not induct on its Board, a person whose name appears in the list of Willful Defaulters (and in case such a person is already on the Board, it would take expeditious steps for removal of the person from its Board).

Penal processes arising out of this paragraph will be enforced judiciously and it will be ensured that a solitary or isolated instance is not made the basis for imposing a penal action. It will also be ensured that the penal provisions are not misused and the scope of discretionary powers is kept to the barest minimum. Penal provisions will be imposed after recording the reasons for the same and obtaining the prior approval of MD & CEO.

6. Guarantees from Group Companies or Non-Group Entities:

The track record of the individual entity, with reference to its repayment performance, will be considered separately while dealing with willful default of a single borrowing entity in a Group. However, in cases where guarantees furnished by the companies within the Group on behalf of

the willfully defaulting units are not honored when invoked, such Group companies will also be reckoned as Willful Defaulters.

In case a demand is made on a guarantor, who may be an individual or a non-group entity, on account of the default made by the principal debtor, and the said guarantor refuses to comply with the demand despite having sufficient means to make payment of the dues, such guarantor will also be treated as a Willful Defaulter. This will apply only prospectively and not to cases where guarantees were taken prior to 9th September 2014 (date of the relative RBI circular). This position will be made known to prospective guarantors at the time of accepting guarantees in respect of Restructuring Packages and Restructuring Support Finance.

7. Role of Auditors:

In case any falsification of accounts on the part of the borrowers is observed and if it is observed that the auditors were negligent or deficient in conducting the audit, IARC will lodge a formal complaint against the auditors of the borrowers with the Institute of Chartered Accountants of India (ICAI) to enable the ICAI to examine and fix accountability of the auditors. Pending disciplinary action by ICAI, IARC may also forward the complaint to the RBI (Department of Banking Supervision, Central Office) and IBA for records.

With a view to monitoring the end-use of funds, IARC may seek a specific certification from the borrowers' auditors regarding diversion / siphoning of funds by the borrower, by giving a separate mandate to the borrowers' auditors for the purpose. However, in most cases, it would be preferred that IARC engage its own auditors for such specific certification purpose without relying on certification given by borrower's auditors. To facilitate such certification by the auditors, IARC will also ensure that appropriate covenants are incorporated in the facility agreements.

8. Role of Internal Audit / Inspection

The aspect of diversion of funds by borrowers would be adequately looked into as part of internal audit or inspection and a quarterly review of willful defaults would be submitted to the Audit Committee.

9. Reporting to Credit Information Companies:

IARC will submit the following periodical reports to Credit Information Companies (CICs):

1. List of suit-filed accounts of Willful Defaulters of Rs 25 lacs and above to CICs on the format prescribed by them, at the end of each calendar quarter.
2. List of non-suit-filed accounts of Willful Defaulters of Rs 25 lacs and above as on the 31st December 2014 and thereafter on a monthly basis to CICs on the format prescribed by them.

If IARC acquires an account already classified as Willful Defaulter by the seller Bank, IARC will continue to treat the account as Willful Defaulter and report it to RBI/CIBIL accordingly. While acquiring such assets IARC should ensure that all records relating to such classification are obtained from the Bank and maintained by IARC.

The periodicity and format of reporting may change according to the requirements of the Credit Information Companies.

10. Reporting Names of Directors / Guarantors:

Every effort should be made to ensure accuracy of facts and figures in the reports submitted to RBI and to Credit Information Companies.

While reporting the names of Directors, a distinguishing mark would be made to identify those Directors who are "Independent Directors". Similarly, the names of Directors who are nominees of Government or financial institutions would be reported with a remark "Nominee Director".

In respect of Government undertakings, the names of the Directors will not be reported. Instead, a legend "Government of Undertaking" will be added.

To ensure correct identification of Directors, especially when there is likelihood of misidentification of persons with similar names, the Director Identification Number (DIN) will be included as one of the fields in the reports.

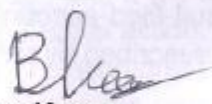
In respect of business enterprises other than companies, the names of persons, who are in charge of and responsible for the management of the affairs of the business enterprise, will be reported in column for Directors.

The names of guarantors who have been identified as Willful Defaulters will be reported with a mention of (Gaur) in brackets and will be reported in the column for Directors.

11. Annual Review

The policy will be reviewed annually and submitted to the Board for review and approval.

Mumbai
May 2, 2015


Birendra Kumar
Managing Director & CEO