RULES AND REGULATIONS FOR LOAN RESTRUCTURING BY FINANCIAL SERVICE PROVIDER(S), 2022

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PART A: Background and Objectives

Addressing asset quality issues is one of the key priorities for the Royal Monetary Authority (RMA) of Bhutan. The RMA's focus on this issue began with the comprehensive assessment of current non-performing loans (NPLs) of the Bhutanese financial sector. The credit risk and the heightened levels of NPLs are being considered as one of the main risks facing the Bhutanese financial service providers (FSP).

A comprehensive approach, consisting of different policy actions, is needed with the objective to address the existing stock of NPLs as well as to prevent the emergence and accumulation of new NPLs on FSP's balance sheets. In this regard, RMA has identified a number of best practices on loan restructuring, set out in these Rules and Regulations, to ensure that FSP effectively addresses and manages NPLs. These Rules and Regulations are written from a prudential perspective but also taking into account the need to ensure that borrowers who have taken out loans are treated fairly at every stage of the loan life cycle.

PART B: Title, Extent and Commencement

1. These rules and regulations shall be known as Rules and Regulations on Loan Restructuring by Financial Service Providers, 2022;
2. These rules and regulations shall apply to all FSPs;
3. These rules and regulations will come into force from 01st May 2022.
4. These rules and regulations shall be only applicable for ordinary course of the business activity. Any restructuring mechanism or facilities targeted towards special relief packages or policy responses, shall be issued separately by the Authority.

PART C: Eligibility of loans for restructuring facility

5. All loans that are in default, which are deemed viable upon fulfillment of the criteria specified under Section 8 of these rules and regulations, shall be eligible for loan restructuring facility.

6. For providing loan restructuring facility for viable loans which are non-performing, the FSPs shall assess if the borrower is a willful defaulter or not in line with the criteria specified under Section 9 of these rules and regulations; and

7. A borrower who has been determined as 'willful defaulter' shall not be eligible for loan restructuring facility.

8. Criteria for determining viable loans:

8.1 The defaulted loans for which the FSPs foresee repayments in future as per the revised loan contract/agreement after availing loan restructuring facility under these rules and regulations will be assessed to determine if the loan is viable.

8.2 For determining viable loans, the following criteria shall be followed by the FSPs based on the type of loans provided the borrowers has a satisfactory credit history with underlying collateral or securities still being relevant:

Sl.no	Corporate	Retail
1	Business may be under-performing but is still in operation.	Borrower may have lost the source of income but remains in the capacity to be employed for a new source of loan repayment.
2	Facing temporary cash flow problem from reduction or loss of income	Facing temporary cash flow problem from reduction or loss of income
3	FSPs foresee future business prospect of the borrower.	FSPs foresee repayment of loan in future

8.3. The FSPs shall collect evidence (as per *annexure I*) from the borrowers including a written statement justifying that the borrower is facing temporary liquidity hardship and can afford future repayments under the loan restructuring facility.

8.4 The FSPs shall include consequences such as immediate filing of recovery suit or seizure of collateral or declining future loan proposals or any action deemed appropriate by the FSPs, in the contractual terms for borrowers who fail to comply or cooperate with terms and conditions of the revised contract/agreement.

9. Criteria for determining willful defaulter

Willful defaulters are those borrowers who have defaulted on their loan repayment obligations owing to any of the following reasons/events:

9.1. The borrower has defaulted in meeting its loan repayment obligation even when it has the capacity to honor the said obligation. The capacity of the borrower to honor the obligation shall be assessed by the respective FSPs.

9.2. The borrower has not utilized the loan sanctioned for the intended purposes for which the loan was availed but has diverted/siphoned-off the funds.

9.3. The borrower has disposed of or removed the movable or immovable property given for the purpose of securing the loan without the knowledge of the FSP or sold/closed the business against whose income the loan was sanctioned, without the consent of the FSP.

9.4. The borrower has changed contact address and mobile number without informing the FSP and is not contactable through all channels provided by the borrower in the loan document for a period of 60 days from the day of default.

9.5. Any other reason/events determined by the Authority from time to time.

PART D: Process of loan restructuring for loan rehabilitation and revival

10. All loan restructuring shall be carried out by FSPs within 270 days from the day of default.

11. In the event FSP fails to restructure the NPLs, FSP shall initiate the foreclosure process as per the Rules and Regulations for foreclosure and loan write off of NPLs 2022.

12. The FSPs shall conduct loan restructuring affordability assessment of the borrower based on the borrower’s current and prospective servicing capacity for the loan account.

13. Depending on the nature of the loan, the minimum information and expected documentation required for FSPs to assess the borrower affordability for availing loan restructuring facility is specified in *Annexure 2*.

14. Before entering into a loan restructuring facility, the arrangement shall be agreed between the borrower and the FSP.

15. The FSP shall seek approval from the respective board/board sub-committee/any committee constituted by the board based on the delegation of power accorded by the board for loan restructuring. The approving authority shall be independent of the units or functions involved in carrying out affordability assessment of the borrowers.

16. Among other things, the delegation of authority shall include provisions on limits and responsibilities related to monitoring of restructured loans.

17. In case of consortium loan, the lead FSP shall conduct the credit assessment including, but not limited to, review of payment history and the final decision shall be unanimous among the participating FSPs.

18. The facilities available for the loan restructuring are as follows:

Sl.no	Loan restructuring facility	Description
1	Interest only payment (only allowed for maximum up to period of 2 years)	Only interest is paid on the loan and no principal repayment is made. The principal amount remains unchanged and the terms for the repayment structure are reassessed at the end of the interest-only period, subject to the assessed repayment ability.
2	payment moratorium (only up to allowed period of 2 years)	An agreement allowing the borrower a defined delay in fulfilling the repayment obligations. The interest shall continue to accrue during the grace period.
3	Capitalization	Addition of those unpaid amounts (interest and late fees) to the principal balance for repayment under a sustainable rescheduled programme.
4	Extension of maturity term/ rescheduling	Extension of the maturity of the loan which allows a reduction in installment amounts by spreading the repayments over a longer period. *Details covered in Annexure 1*

5	Enhancement of credit facilities (loan top up) with adequate collateral coverage	Providing additional financing arrangements to provide cash flow but shall not be used to finance repayment of existing loan obligations.
7	Loan splitting	Splitting of loan outstanding into multiple smaller amounts to reduce EMIs (Applicable with huge amount loans and used along with other loan restructuring facilities such as payment moratorium). The revised loan document shall clearly specify that the FSP have the right to foreclose the collateral should any of the split loans is in default that triggered the foreclosure event.
8	Conversion to term loan	Conversion of working capital or overdraft loans into terms loan. The tenure of the term loan shall be as per the respective sectors loan tenure mentioned in FSPs credit policy.

19. Depending on the requirement, the FSPs may allow one or a combination of loan restructuring facilities for a single loan account at a time to revive or rehabilitate the loan accounts.

20. Besides the type of restructuring facilities prescribed under section 18, the FSPs may come up with additional facilities which shall be endorsed by their board of directors and approved by the Authority.

PART E: Prudent requirement

21. The asset classification of restructured NPL accounts shall remain in the same category for a period of 6 months. The accounts can be classified as performing 'Standard' only when the repayment term under the revised loan agreement has been regular for 6 months.

22. Any partial repayment (including interest only payment under loan restructuring facilities) shall not be treated as full repayment to reclassify the loans as performing.

23. The provisioning requirement shall be as per S.4.7 of Prudential Regulation 2017 or amendment thereof.

24. FSPs shall be permitted to provide a restructuring facility or facilities mentioned under section 18, 19 and 20 of these rules and regulations for an account, only once every two years and not more than two times during the loan tenure.

25. The FSPs shall take strict follow-up measures if borrowers do not comply with the terms and conditions under the loan restructuring facility such as filling recovery suit within a month from non-compliance with the revised terms and conditions of the restructured loan.

26. The FSPs shall continue to monitor the restructured loan accounts in-line with the Guidelines on loan origination and monitoring issued by the Authority or any amendments thereof.

PART F: Disclosure and other Requirements

27. To ensure equity and transparency, an FSP shall exercise due diligence, maintain objectivity, and avoid conflict-of-interest as per the requirements of Corporate Governance Rules and Regulations 2020, in the process of loan restructuring.

28. The FSP shall require the officials/members involved in the loan restructuring process to declare the conflict of interest before attending any meeting on loan restructuring.

29. The FSP shall align its credit policies in-line with these rules and regulations.

30. With the implementation of said measures, the report of all restructured loans along with the documentary evidence (including the minutes of the committee meetings) shall be submitted to the RMA monthly in the prescribed format as per *Annexure 2*.

31. The FSP shall disclose the details on the total number of accounts and amount as part of the notes to its financial statement in the annual reports.

PART G: General Provisions

32. **Rules of Construction:** Unless the context clearly otherwise requires, wherever used in the Guidelines, the singular includes the plural.

33. **Interpretation**: The Authority shall have the power to interpret any provision under these rules and regulations and its interpretation shall be final and binding upon all parties.

34. **Transitional period:** These rules and regulations shall come into force within a period of three months from the date of issue of these rules and regulations. During this period, the FSP shall carry out a gap analysis and implementation plan and accordingly submit to RMA.

35. **Supersession:** These rules and regulations shall supersede the guidelines on segregation of NPLs into viable and non-viable 2020. Any provisions or rules that are in-conflict with the provisions of these rules and regulations shall be superseded by these rules and regulations to the extent they are inconsistent with the provisions of these rules and regulations.

36. **Amendment:** The additions, changes, or repeal of any provision of these rules and regulations shall be made by the Board based on the recommendation of the Management.

37. **Penalty for violation of these rules and regulations:** The Authority shall take appropriate enforcement measures followed by appropriate penalties on the FSPs if any provision of these rules and regulations are violated.

PART H: Definitions

Borrower: An individual, either natural or a juridical person, who has entered into a contract with the financial institution to borrow or guarantee an agreed amount at agreed terms and conditions for repayment of the borrowed amount as per the agreed repayment schedule. In the case of a borrower with multiple accounts, each NPL account shall be assessed independently for the segregation purpose.

Corporate loans: Those loans which FSPs have sanctioned to a juridical person for a particular project based on a detailed analysis of future cash flows as per the project report submitted by the borrower.

Defaulted loans: For the purpose of these rules and regulations, any loans that have missed repayment schedules or foresee repayment problems as per the terms and conditions as per the loan agreement will be deemed as loan default.

Diversion of fund: Deploying/ utilizing the borrowed funds for purpose/activities or creation of assets other than those for which the loan was sanctioned.

Non-performing loan: The loan repayment obligation is overdue by more than 90 days, as defined under S 4.4 of Prudential Regulation 2017 or amendment thereof.

Non-Viable Loans: Non-performing loans where the FSPs do not foresee any repayments in the future.

Rehabilitation: Process of restoring the borrower's financial condition for loan repayment obligation.

Restructuring of loan: It is the modification of existing loan agreement/contract terms and conditions to help borrowers who have financial difficulties in loan repayment.

Retail loans: Those loans which FSPs have sanctioned to a natural person based on business or rental or salary income without the requirement of detailed future/projected cash flow analysis and project analysis report.

Revival: Improving the financial condition of the borrower for loan repayment obligation.

Siphoning of fund: Utilizing the borrowed funds for purpose/activities other than for which the loan was sanctioned whereby there are no traces/account of how the borrowed fund has been utilized.

Underperforming Business: Businesses which are facing temporary problems in their operation due to either mismanagement or policy impact or economic situation.

Viable Loans: Defaulted loans for which the financial institution foresees a repayment in future as per the revised loan contract/agreement after availing loan restructuring facility under these rules and regulations.

ANNEXURES

Annexure 1: Minimum information and documentation expected for borrower's affordability assessment of availing loan restructuring facility.

1. Retail borrowers

An FSP shall consider the following information wherever applicable to assess the borrower's affordability of availing the loan restructuring facility:

- Assessment of the borrower's current and future repayment ability.

Information to consider for current repayment ability	Information to consider for future repayment ability
• financial information (occupation, income, expenditure) • overall loan exposure • current repayment capacity • repayment history • reason for arrears • age and amount of arrear	• income • years to retirement (in comparison to loan duration) • employment status or prospects • industry/ sector • savings and assets • known future changes • Alternative/secondary repayment source (family members)

- Affordability assessment of guarantors (if applicable).

As a minimum, the following documents should be obtained when restructuring a retail loan:

- Written application from the borrower requesting for loan restructuring facility indicating reasons for financial hardship;
- Financial and non-financial information of a borrower (e.g. pay slips or tax returns for salary and rental incomes, tax returns for formal business entities with licenses and for informal business, any supporting documents demonstrating the borrower's income and ability to service the loan obligations.
- Recent CIB report; Latest valuation of collateral/ mortgage securing the underlying loan facility;
- Information on any other collateral securing the underlying loan facilities (e.g. insurance, third party guarantees); and
- Any other document required by FSPs depending on the requirement of the assessment.
- Letter of undertaking in case of alternative/secondary source of repayment

- Any other document required by FSPs on a case to case basis.

2. Corporate borrowers

In case of a corporate borrower, an FSP shall consider the following information wherever applicable to assess the borrower's affordability of availing the loan restructuring facility:

- Overall loan exposure
- Analysis/assessment of the company's business plan (e.g. SWOT analysis, projected financial ratio analysis, industry sector analysis);
- Company's history on financial data, which may help trace the trigger event of the company experiencing difficulties and may provide an indication as to the viability of its business model;
- Business model/business activity of the borrower or the economic environment both past and future;
- Scrutiny and assessment for reasonableness of projections and assumptions;
- Analysis of current obligations (major expenses, capital expenditure, disposals, equity contribution, other amounts due (fines, taxes, insurance, employee liabilities) etc.;
- Affordability assessment of guarantors (if applicable);
- Industry and sector analysis; and
- Relevant market indicators.

As a minimum, the following documents shall be obtained as evidence when restructuring a corporate loan:

- Written application from the borrower requesting loan restructuring facility indicating reasons for financial hardship;
- Latest audited financial statements and/or latest management accounts;
- Recent CIB report;
- Business plan and/or cash-flow forecast, depending on the size of the borrower and the maturity of the loan;
- Latest valuation report of any collateral/mortgage securing the underlying loan; and
- Information on any other collateral securing the underlying loan facilities (e.g, insurance).

Annexure 2: Reporting template for reporting loans availing loan restructuring facilities

Serial No.	Borrower Name	CID/TPN /Licence No.	Type of loans	Account Number	Sector	Sanctioned Amount	Date of Sanction	Maturity Date	Amount Outstanding
Restructured Amount	**Restructured Date**	**Type of restructuring facilities availed**	**Collateral Type**	**Collateral Value**	**Performing/non-performing at the time of restructuring**	**Is the loan restructured under Current NPL Resolution framework? (Yes/No)**	**Is the loan restructured before (Yes/No)**	**frequency of restructure**	**Documentary Evidence**

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