

## INTRODUCTION OF Prudential norms in P.A.C.S

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**Background-:** with a view to making the profit & Loss account and Balance sheet more transparent there by reflecting the actual financial position of Banks, the Reserve Bank of India issued instruction to Banks for implementation of prudential norms as per recommendation of the Narasimhim committee. All commercial Banks introduced prudential norms from the year 1992-93 and all co-operative Banks adopted these norms from the year 1996-97. Now as per the recommendation of the Baidyanathan committee all P.A.C.S. in India have to adopt prudential norms from the year 2009-10.

**What are prudential norms?** -: The prudential norms are divided into the following 4(four) broad heads, viz.-:

1. Income recognition.
2. Assets classification.
3. Provisioning norms.
4. Capital Adequacy.

**1 Income recognition** -: (a) The prudential norms for income recognition should be based on the record of recovery and therefore unrealized income should not be taken to profit & Loss accounts. Only current interest accrued but not realized on standard Loan is recognized to profit & Loss accounts on accrual basis. No overdue interest on standard Loan and N.P.A. Loan is recognized to profit & Loss accounts on accrual basis, but is booked as income only when it is actually received. If societies charge interest on over due Loan and if such interest remains unrealized, the same may be taken into income account provided matching provision is made. In other manner the interest accrued but not realized on over due Loan and N.P.A. Loan may be shown separately under “interest receivable account” on the Assets side of the Balance sheet and corresponding amount shown under “overdue interest reserve account” on the Liabilities side of the Balance sheet.

(b) Fee, commission and other income may be treated as income only when the Account is classified as “standard “

(c) Similar treatment for accrued interest on investments.

**2. Classification of Assets** -: classification of agricultural and non agricultural Loan of P.A.C.S. is required to be done in to two broad categories “performing Assets i.e. standard Assets and “non performing Assets (N.P.A.)” which have to be further classified as substandard, doubtful and Loss Assets on the basis of the age of overdue.

**(a) Performing Assets or Standard Assets** -: The Loans & Advances which are generating incomes regularly and do not disclose any problem and do not carry more than normal risk attached to business qualify for classification as standard Assets ; In other words all current agricultural and non agricultural Loans which have not become N.P.A. may be treated as standard Assets.

**(b) Non performing Assets -:** The Loans & Advances are treated as non performing Assets when these Loans & Advances remain overdue for 90 days or more. The non performing Assets are divided into 3 broad heads viz, (i) sub standard, (ii) Doubtful and (iii) Loss Assets as per details below -:

- (i) **Substandard Assets -:** The non performing Agricultural and non Agricultural Loans which have remained over due for a period not exceeding 3 years from due date to date of Balance sheet may be treated as “ Sub standard “.
- (ii) **Doubtful Assets -:** The non performing Agricultural and non Agricultural Loans which have remained over due for a period of over 3 years to 4 years from due date to date of Balance sheet may be treat as “Doubtful Assets”. Doubtful Assets are mainly divided in to two parts; one is “secured Doubtful Assets “and other is “unsecured Doubtful Assets “.

(a) **Secured Doubtful Assets -:** The secured Doubtful Assets (Loan) is one which is fully covered with realizable securities.

(b) **Unsecured Doubtful Assets -:** The unsecured Doubtful Assets (Loan) is one which is not covered with realizable securities.

The secured Doubtful Assets (Loans) are further sub divided into 3(three) categories viz. Doubtful-I, Doubtful-II and Doubtful-III according to age of over due as details below -:

**(a) Doubtful-I (D-1) -:** The non performing Loans which have remained overdue for a period over 3 years to 4 years from de date to date of Balance sheet may be treated as “ sub standard “.

**(b) Doubtful-II (D-2)-:** The non performing Loans which have remained overdue for a period over 4 years to 6 years from due date to date of Balance sheet may be treated as “Doubtful-II.”

(non 100 %100 %performing Loans which have remained over due for a period above 6 years from due date to date of Balance sheet may be treated as “Doubtful-III.”

**(iii) Loss Assets -:** Loss assets (Loans) are those where Loss is identified by the Bank/P.A.C.S/Auditor/RBI/NABARD inspectors but the amount has not been written off wholly or partly. In other words, an assets which is considered unrealizable and/or of such little value that its continuance as a doubtful Assets is not worthwhile, should be treated as a Loss Asset. Such Loss Assets will include overdue Loans in cases (a) where decrees or execution petition have been time barred or documents are lost or no other legal proof is available to claim the debt, (b) where the members and their sureties are declared insolvent by court or have died leaving no tangible Assets, (c) where the members have left the area of operation of the society leaving no property

and their sureties have also no means to pay the dues, (d) where the Loan is fictitious or when gross misutilisation is noticed, and (e) amounts which can not be recovered in case of liquidated societies.

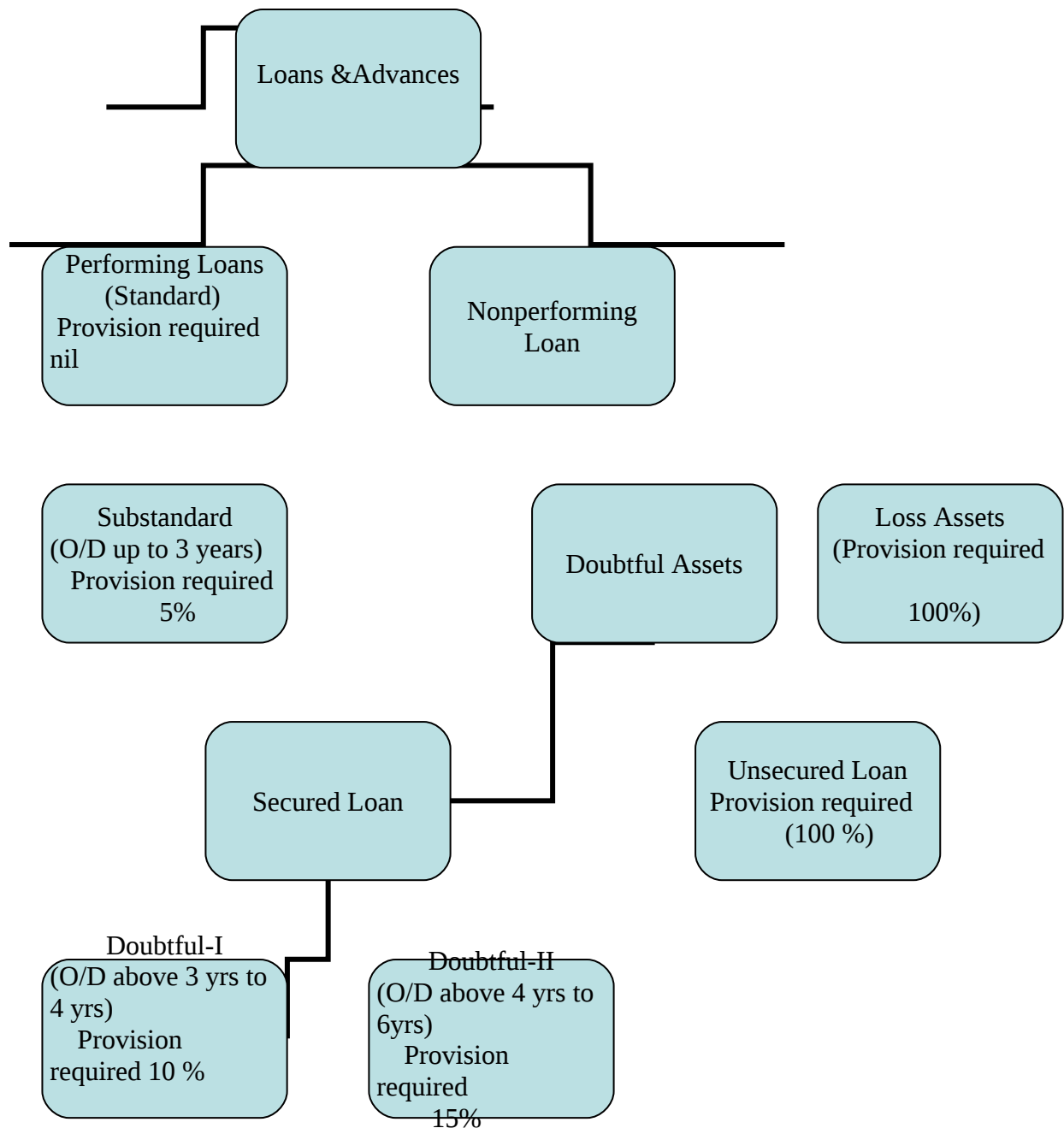
**4. Provisioning norms :-** provisioning is necessary considering the erosion in the value of security charged to the Banks/ P.A.C.S over a period of time. Therefore, after the Assets of Banks /P.A.C.S are classified into various categories (viz., standard, substandard, Doubtful and Loss Assets) necessary provision has to be made for the same. The details of provisioning requirements in respect of various categories of Assets are mentioned below:-

<b>Sln.</b>	<b>Name of Assets</b>	<b>Rate of provisioning In respect of PACS</b>	<b>Rate of provisioning In respect of Bank</b>
1.	Standard Assets	Nil	0.40 %
2.	Sub standard „	5 %	10 %
3.	Doubtful –I „	10 %	20%
.	Doubtful -II „	15 %	30 %
5.	Doubtful –III „	50 %	50 %
6.	Unsecured Doubtful Assets	100 %	100 %
.	Loss Assets	100 %	100 %

Note -: (i) In the case of Loans outstanding under the back end subsidy schemes, provision may be made only on net of subsidy basis.

(iii) All Agricultural Loans to be treated as fully secured as the same are disbursed against charge on land.

Graphically presentation of Assets classification & provisioning norms:-



Doubtful-III  
(O/D above 6 yrs)  
Provision required  
50%

### **Calculation of N.P.A. on Agricultural and non Agricultural Loan Of BANKS / P.A.C.S**

The Loan portfolio of a Bank/P.A.C.S is mainly divided in to two groups; one group is” Agricultural Loan” and other group is” non Agricultural Loan “as per details below:-

**1. Non Agricultural Loan -:** Loans granted for non Agricultural activities are called as non Agricultural Loans. Business Loan, housing Loan, Loan to service holders etc are the examples of non Agricultural Loans. All Loans granted for non Agricultural purposes should be treated as N.P.A if amounts of installments of principal or interest remain over due for a period of 90 days from the due date.

An example is given here;

A Loan amounting to Rs 72000.00 was given to a shop keeper on 01.8.2009. for 36 months with repayment schedule of monthly installment Rs2000.00 along with interest. Suppose no installment was paid up to 31.3.2010. The calculation of N.P.A. of this Loan will be as follows;

Date of issue and Purpose of Loan	Amount of Loan	Due date of 1 <sup>st</sup> installment	Date after 90 days since due date	Date of NPA	Date of Balance sheet 31.3.10
01.8.2009. Business(nonAgril)	Rs72000	31.8.09	29.11.09	29.11.09	Substandard (O/D up to 3 years)

The total Loan Rs72000 will be treated as NPA under “substandard category” as on 31.3.10.

<sup>2nd</sup> example-:

Further, suppose that the shop keeper has repaid 7<sup>th</sup> installments along with interest on regular basis as per terms & conditions and he has stopped payment from 8<sup>th</sup> installments. In the above cases the date of NPA will be calculated as under-:

Date of issue and purpose of Loan	Amount of Loan	Due date of payment of installment	Amount of installment paid	Balance outstanding	Date after 90 days since due date	Date of NPA	Date of Balance sheet.
01.8.09 Business (nonAgril)	Rs72000			72000			
		1 <sup>st</sup> installment	2000	70000			
		2 <sup>nd</sup> „	2000	68000			
		3 <sup>rd</sup> „	2000	66000			
		4 <sup>th</sup> „	2000	64000			
		5 <sup>th</sup> „	2000	62000			
		6 <sup>th</sup> „	2000	60000			
		7 <sup>th</sup> „	2000	58000			
		8th(31.3.10 )	Nil	58000	29.6.10	29.6.10	31.3.11 substandard ( O/D up to 3 years)

From 8<sup>th</sup> installment, the payment was stopped. The due date of 8<sup>th</sup> installment was on 31.3.10. so after 90 days from due date i.e. on 29.6.10., the total outstanding amount Rs 58000 will be treated as N.P.A and on the very next date of Balance i.e. on 31.3.11, it will be treated as N.P.A under sub standard category (O/D up to 3 years).

**2. Agricultural Loan -:** The Loans granted for Agricultural activities are called as “Agricultural Loan” and the Agricultural Loan granted for raising crops are called as “crops Loan”. There are two types of crops in our country; one is short duration crops and other is Long duration crops as per details below -:

**(a) Short duration crops -:** “short duration’ crops would be crops with crop season not longer than one year. Kharif paddy, boro paddy, potato, jute, wheat etc are the examples of “short duration crops”.

**b) Long duration crops -:** “Long duration” crops would be crops with crop season longer than one year. Sugarcane, pine Apple etc are the examples of “Long duration crops”.

- (c) **Crop season -:** The “Crop season” for each crop which means the period from seed to harvesting of the crop raised.
- (d) **Due date- :** Due date means the date on which installments of principals/ interests have to be paid.
- (e) Some crops seasons and Due date of repayment of crops Loans are mentioned below -:

Sl no.	Name of crop	Type of crop	Crop season (seed to harvesting period)	Due date Of repayment of crop Loan
1.	Kharif paddy	Short duration crop	April to December	31 <sup>st</sup> march
2.	Potato	Do	Mid October to February	31 <sup>st</sup> may.
3.	Boro paddy	Do	Mid November to April	31 <sup>st</sup> July.
4.	Sugarcane	Long duration crop	November to next November	

During the time of calculation of N.P.A of crops Loans, due date of repayment of Loan and crop season should be considered vividly. The calculation of N.P.A. of short duration crops and Long duration crops are mentioned below-:

**(a) N.P.A. of short duration crops-;** A Loan granted for short duration crops will be treated as N.P.A,if the installment of principal or interest remain unpaid for two crop seasons beyond the due date.

**(b) N.P.A. of Long duration crops:-** A Loan granted for Long duration crops will be treated as N.P.A, if the installment of principal or interest remain unpaid for one crop season beyond the due date.

Some examples for calculation of N.P.A. are given here.

Date of issue of Loan.	Amount of Loan	Type of Loan	Due date of repayment	1 <sup>st</sup> crop season	2 <sup>nd</sup> crop season	Date of N.P.A .	Date of Balance sheet	Classification of Assets
10.4.07	20000.	Kharif paddy	31.3.08	31.12.08	31.12.09	31.12.09	31.3.10 (O/D up to 3yrs)	Sub standard
28.10.08	50000	potato	31.8.09	28.2.10	28.2.11	28.2.11	31.3.11	Substandard.
15.1.10	25000	Boro paddy	31.9.10	30.4.11	30.4.12	30.4.12	31.3.13	substandard

Note-I:- If the above kharif, potato and boro Loans referred in the Table are not realized subsequently, then

- The above kharif Loan shall be classified as substandard up to 31.3.10 & 11 and Doubtful-I as on 31.3.12 and Doubtful-II as on 31.3.13 & 14 and Doubtful-III as on 31.3.15 and onwards.
- The above potato Loan shall be classified as substandard up to 31.3.11 & 12 and Doubtful-I as on 31.3.13 and Doubtful-II as on 31.3.14&15 and Doubtful-III as on 31.3.16. and onwards
- The above boro Loan shall be classified as substandard up to 31.3.13 and Doubtful-I as on 31.3.14 and Doubtful-II as on 31.3.15&16 and Doubtful-III as on 31.3.17 and onwards.

**Note-II:- Direct Agricultural Loans ----:** Short term Loan for raising crops (including K.C.C), M.T.Agricultural Loan for purchase of Tractor, Power tiller, construction of Mini deep tube well, deep tube well, Shallow etc and Loan to small and marginal farmers to purchase of Agricultural land and traditional/ non traditional plantations and horticulture are Direct Agriculture Loans. The norms of N.P.A. for crop Loans should be made applicable to all Direct Agricultural Loans as per the guide lines of R.B.I/NABARD.

**Note -: III -: Allied and non farm Loan-** Loans for other allied agricultural activities and non farm sector activities will be treated as NPA if the amount of installment of principal / interest remains over due for 90 days from the due date.

**Note-iv:- out of order status -:** In respect of cash credit/over draft facility an account should be treated as out of order (N.P.A), if the out standing balance remains continuously in excess of the sanctioned limit/drawing power, in cases where the outstanding balance in the principal operating account is less than the sanctioned limit / drawing power, but there are no credits continuously for 90 days or credits are not enough to cover the interest debited during the same period, these cash credit / over draft accounts should be treated as out of order (N.P.A).

**Note-v:-Treatment of N.P.A. Borrower wise and not facility wise-;** In respect of a borrower having more than one facility with a P.A.C.S, all the facilities granted by the P.A.C.S will have to be treated as N.P.A and not the particular facility or part there of which has become N.P.A.

**Note –vi-: Agricultural Loans –default in payment due to natural calamities-:**

Where ever due to natural calamities conversion of the short term production Loan into medium or long term Loan or re-schedulement of the repayment period is allowed, the converted / rescheduled Loan as well as fresh Loan granted has to be treated as current dues (standard Loan) and need not be classified as N.P.A.

In the case of all other rescheduled Loans, the accounts which have been subjected to restructuring etc, whether in respect of principal installment or interest amount, will be eligible to be up graded to the standard category only after one year of satisfactory performance in regard to repayment of installment / interest.

**Note-vii-: staff Loan- :** In the case of housing Loan or similar advances granted to staff members where interest is payable after recovery of principal, interest need not be considered as overdue from the first quarter onwards. Such Loans / Advances should be classified as NPA only When there is a default in repayment of installment of principal or payment of interest on the respective due dates.

**Note –viii-: Loans & Advances exempted from NPA norms -:** Advance against term deposit, NSC, KVP and life insurance policy need not be classified as NPA. But Advance against gold and other ornament to be classified as NPA based on the period of overdue and purpose for which Loan disbursed i.e. whether for agriculture or non-agriculture.

**Note-ix-: Provision for other Assets /outstanding Liabilities -:** Loss in respect of cash balances /deposits with Banks, amounts in Branch adjustment accounts, frauds and embezzlements and depreciation on building, furniture and vehicles etc may be assessed and fully provided for as per the existing practice. With a view to ensuring full disclosure on the profitability and net worth of the PACS, items not provided for or items of liabilities where inadequate provisions have been made (e.g. Gratuity, provident fund, income tax, interest accrued on deposits /borrowings, etc), Auditors or inspecting officers should specify the same to arrive at the un provided for expenditure and treat them as actual expenditure for the purpose of arriving at the correct profitability and net worth of the PACS.

In the case of Assets other than Loans and Advances, the provisioning norms may be as under;-

- (1) **Cash in hand - :** The shortage in cash, if any observed on verification either by the Auditor/inspector or by the society officials may be provided for , if the society is holding any soiled /mutilated notes on the date of Balance sheet, provisions may be made for the value of such notes held.
- (2) **Balances with Banks (cash at Banks)-:** The general ledger /Bank book may be reconciled on a periodical basis with the pass book or certificates / statement



of account issued by the Bank. Provision may be made in respect of the entries not reconciled and outstanding more than one year.

- (3) **Investments -:** PACS, normally, would have investments in fixed deposits with DCCB / Commercial banks, NSC /KVP with post office and shares of DCCB and other institutions. Investments in fixed deposits with banks and pos office may be considered as fully realizable and no provision need be made. In the case of fixed deposits with other institutions no provision may be made if the interest is received regularly and the institution is functioning properly. If not, the realisability of the amount may be assessed and provision may be made for the unrealizable portion. The value of fixed deposit / share etc with institutions which under liquidation / winding up procedure may be treated as loss assets and provision may be made. The government and other trustee securities, if held with PACS may be valued at book value. When securities are purchased at a price higher than the face value, the difference between the purchase value and the face value may be depreciated in equal proportion every year over the remaining maturity period of the security.
- (4) **Sundry debtors & other receivables-:** If the amount is not realized within one year from the date of claiming (due date), it can naturally be assumed that there are some problems in realization of the amount. Therefore, for such amount 10% provision may be made, if not received within one year, 50% provision if not received within above 1 year to 3 years and 100% provision for more than 3 years. In case of frauds and embezzlement etc, full provision may be made.
- (5) **Non credit business -:** PACS under take business of fertilizer, clothes, consumers' goods etc. The physical verification of stock of each item should be done as on 31<sup>st</sup> march in every year and if any shortage of stock degraded stock and unsaleable stock is found provision may be made. For shortage of stock, full provision may be made. Any item which remains unsold after the period indicated may be treated as unsaleable and full provision may be made there against. The items having no expiry period may be treated as unsaleable if remaining unsold for more than 3 years and full provision may be made. The cloths in stock up to 1 year may be valued at purchase price, above 1 year to 2 years may be valued at 80% of purchase rate and above 2 years to 3 years at 50% and 3 years at nil and provision for diminution in value may be made accordingly.
- (6) **Fixed Assets -:** Yearly depreciation should be provided to each of the fixed Assets as per the existing practice. In the case of land no depreciation is required. In case of lease hold land, amount in proportion to expiry of the lease period may be provided.
- (7) **Conclusion-:** The income recognition, Assets classification and provisioning norms which have to be adopted by the PACS from the year 2009-10 as per the instruction of the NABARD have been discussed here in details. The above norms should be adopted to reflect true and fair picture of financial status of the PACS. The staff and board members of PACS need extensive training and time to assimilate the new concepts involved in the prudential norms.

