

GOVERNMENT OF INDIA  
MINISTRY OF FINANCE  
**LOK SABHA**  
**UNSTARRED QUESTION NO-577**  
ANSWERED ON- 24/07/2023

**FIRST LOSS DEFAULT GUARANTEE PROGRAMME**

577. SHRI RITESH PANDEY

Will the Minister of FINANCE be pleased to state:-

- (a) the safeguards and monitoring mechanisms established by the RBI to ensure that the First Loss Default Guarantee Programme effectively mitigates default risks and protects the interests of all stakeholders involved, including borrowers, fintech firms, banks, and non-banking finance companies;
- (b) the factors that influenced the RBI's decision to set the cooling off period for non-farm credit at a minimum of 12 months and whether the RBI has considered any potential challenges or unintended consequence associated with this period;
- (c) the process by which the cooling off period for farm credit will be determined and approved by the lender's board;
- (d) whether the RBI intends to regulate compromise settlements for loan accounts classified as fraud or belonging to wilful defaulters;
- (e) whether the measures proposed to be implemented to ensure that compromise settlements are fair and equitable for both lenders and borrowers; and
- (f) if so, the details thereof?

**ANSWER**

THE MINISTER OF STATE IN THE MINISTRY OF FINANCE

(DR. BHAGWAT KARAD)

- (a): The Reserve Bank of India (RBI) has issued the Guidelines on Default Loss Guarantee (DLG) in Digital Lending, *vide* its Circular dated 8.6.2023. Safeguards and monitoring mechanisms are provided in the said guidelines, which include, *inter alia*, the following:
- (i) Regulated entities (REs) are required to put in place a Board-approved policy before entering into any DLG arrangement.
  - (ii) REs, at the time of entering into or renewing a DLG arrangement, are required to obtain adequate information that entity extending DLG would be able to honor it. Such information includes, *inter alia*, a declaration from the DLG provider, certified by the statutory auditor, on the aggregate DLG amount outstanding. The declaration is also required to contain past default rates on similar portfolios.
  - (iii) REs shall accept DLG only in the form of cash, fixed deposits or bank guarantee.
  - (iv) The total amount of DLG cover on any outstanding portfolio which is specified upfront shall not exceed five per cent of the amount of that loan portfolio.

- (v) REs are required put in place a mechanism to ensure that loan service providers, with whom they have a DLG arrangement, publish on their website the total number of portfolios and the respective amount of each portfolio on which DLG has been offered.
- (vi) DLG arrangement shall not act as a substitute for credit appraisal requirements.

(b) to (f): With a view to provide further impetus to resolution of stressed assets in the system, RBI, *vide* its circular dated 8.6.2023, has issued comprehensive regulatory framework governing compromise settlements and technical write-offs covering all the REs. The framework prescribes minimum cooling off period of 12 months as a general prescription for normal cases of compromise settlements during which the REs undertaking settlement or write off shall not take any fresh exposure to the borrower entity. The same has been introduced as a disincentive to both the Regulated Entity and the borrower entering into compromise settlement. The framework provides that the cooling off period for farm credit exposures is to be determined by the REs as per their respective Board approved policies.

However, the compromise settlement is not available to borrowers as a matter of right; rather it is a discretion to be exercised by the lenders based on their commercial judgement. The guidelines seeks to ensure transparency of the whole process. The penal measures currently applicable to borrowers classified as fraud or wilful defaulter in terms of extant guidelines remain unchanged and shall continue to be applicable in cases where the banks enter into compromise settlement with such borrowers. Such penal measures entail, *inter alia*, that no additional facilities should be granted by any bank/ FI to borrowers listed as wilful defaulters, and that such companies (including their entrepreneurs/ promoters) get debarred from institutional finance for floating new ventures for a period of five years from the date of removal of their name from the list of wilful defaulters. In addition, borrowers classified as fraud are debarred from availing bank finance for a period of five years from the date of full payment of the defrauded amount.

Further, the prudential guidelines provide sufficient safeguards with regard to such settlements so as to ensure, *inter alia* fair treatment of all parties involved:

- (i) All decisions on compromise settlements are required to be taken by lenders as per their Board approved policies, instead of adopting an ad-hoc approach on a case to case basis;
- (ii) The circular further strengthens the regulatory guidance by mandating that all such cases of compromise settlement involving borrowers classified as fraud or wilful defaulter must be approved by the Board;
- (iii) Such settlements shall be without prejudice to the criminal proceeding underway or to be initiated, if under consideration of the lenders against such borrowers;
- (iv) The extant penal provisions continue to remain applicable in such cases.
- (v) Wherever recovery proceedings are pending before a judicial forum, and settlement arrived at with the borrower shall be subject to obtaining a consent decree from the concerned judicial authorities.
- (vi) The Boards of lenders have been entrusted with the oversight of the overall trends in approvals of all compromise settlements, including specifically the breakup of accounts classified as fraud, red-flagged, wilful defaulter and quick mortality accounts.

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