

Underwriting Guidelines for Commercial Vehicle Loans

Definition of a Commercial Vehicle

All those vehicles which are used by businesses (transporters and non-transporters) for transporting goods or passengers

Definition of a Commercial Vehicle Loans

For the purpose of these underwriting guidelines, Commercial Vehicle Loans are defined as loans that are made based on the following criteria

As loans that are provided

1. By way of refinancing based on hypothecation of a commercial vehicle owned by the borrower, or
2. For the purpose of purchase of a commercial vehicle which would be used by the borrower for either transporting goods or passengers for her own business (non- transporter/captive users) or for generating revenue by transporting goods or passengers for other businesses (transporters).
 - Age of old vehicles should not more than 10 years
 - Total tenor should be between one year to seven years
 - Loans are repayable in monthly instalments

Eligibility Criteria

Criteria	Standard
Governance, Strategy	<ul style="list-style-type: none"> • The promoters must <ul style="list-style-type: none"> – Have a credible reputation – Have a past track record proving their ability to raise financial resources in the form of equity, subordinated debt and senior debt from the market – Track record in lending/ financing of at least 5 years with at least 3 years' experience in lending for commercial vehicles
	The originator should have a Board consisting of members with relevant experience and should have at least one independent Director. The Board should play an active role in guiding the management
	Audited financial statements must be available within three months of audit. Audit must have been conducted by a reputed firm
Legal documentation and loan Data Collection	<ul style="list-style-type: none"> • Client information and supporting proof filed and/or recorded in the system • Proof of identity and residential address must be collected from every client and this must be admissible under the RBI "Know Your Clients" guidelines. The relevant guidelines are available at http://rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=4354 • Details on each loan be recorded in the system of the originator • Name and address of the borrower • Unique client identification number • Address proof for residence stability • Details of the co applicant borrower and guarantor • Initial Loan amount • Current outstanding balance • Interest Rate • Loan to value • Underlying Commercial Vehicle • Any other fees and charges collected • Due and actual instalment payment and dates • Amortization type/term to maturity • Copy of bank statements, where available • Collection of KYC documents • Collection of a copy of documents related with vehicle: vehicle insurance, vehicle age and fitness certificate original RC book and permit validity. • CIBIL report of borrower and guarantor • Valuation report along with photographs of the vehicle and chassis number print • Collection of Form 34 B extract from the RTO after endorsement of hypothecation

	<ul style="list-style-type: none"> All loans must require at least one a/c payee post-dated cheque, preferably of the borrower's main operative bank account drawn in favour of the originator, to aid in the process of recovery of loans as per provisions under Indian law and legal precedents.
<p>Customer protection</p>	<p>The Originator should have clearly stated processes and policies to protect customer interests</p> <p>The originator must have put in place systems for grievance redressal providing for inter alia:</p> <ol style="list-style-type: none"> 1. Direct, independent access to higher authorities within the organization, for clients to share their grievances and feedback; 2. Independent team that complies and reports on grievances/feedback to the senior management 3. Policies for redressal of grievances within reasonable time 4. System for internal audit/monitoring department to check on grievance redressal 5. A summary of this should be reported to the board on a periodic basis <p>The product features, rules and regulations, including those related to the effective interest rate, upfront fees and other charges, any security or pledge against the loan, penalties for delay in repayment or for prepayment/pre-closure, must be clearly mentioned in the loan agreement and/or sanction letter, as per RBI's Fair Practices Code for NBFCs.</p> <p>Proof of identity and residential address must be collected from every client and this must be admissible under the RBI "Know Your Clients" guidelines.</p> <p>The originator should not use or encourage strong arm tactics for collections of payment of overdue amounts</p> <p>The originator must clearly communicate to borrowers regarding:</p> <ol style="list-style-type: none"> 1. Interest and other charges associated with the loan product 2. Interest provided (in any) on security deposits or other deposits 3. Returns, lock-in periods, surrender/pre-closure charge, administrative charges and other deduction, cheque default charges and any other penal charges 4. Premium paid to insurance companies, in case of credit-linked life insurance or other insurance products offered to the borrower 5. Confirmation of repayments and balance loan outstanding <p>The loan agreement should clearly mention the Financiers right and the process to repossess in case of default and this should be explained to the borrower before disbursement</p>

	<p>To ensure transparency, the terms and conditions of the contract/loan agreement should also contain provisions regarding: (a) notice period before taking possession; (b) circumstances under which the notice period can be waived; (c) the procedure for taking possession of the security; (d) a provision regarding final chance to be given to the borrower for repayment of loan before the sale / auction of the commercial vehicle; (e) the procedure for giving repossession to the borrower and (f) the procedure for sale / auction of the property</p>
Legal form	<p>NBFCs or (NBFC MFIs) providing commercial vehicle loans are eligible</p>
Second line and Organisation aspects	<p>The Business/Sales, Field investigation, Credit and credit-Operations/Back-office functions must be clearly separated, both in terms of the organisation structure and operations</p> <p>The originator must have a strong second line of leadership. Specifically, the heads of key functions – Business/Sales, Finance, HR, MIS, Operations and Internal Audit/Risk – must have at least five years’ experience in their respective functions, preferably in financial services</p> <p>In addition, the head of the Credit function must have at least five years of specific experience of having appraised loan/investment proposals of commercial vehicle-based loans/ financing activities with ticket sizes and type similar to the proposed line of business</p> <p>Adequate training must be provided to the Business/Sales team staff as well as to the Credit team staff. Training to Credit staff must cover in sufficient detail, modules related to business assessment for transporters and non-transporters, risk assessment and cash-flow analysis. In addition, Credit staff must be provided training on commercial vehicle types/ segments that the originator is financing covering the LTV for used vehicles and different type of borrowers. The credit policy and the related staff training should differ for heavy, medium and light weight commercial vehicles. Where the Originator does commercial vehicle financing in different states, the credit policy should be tailored to each state based on underlying credit characteristics of the buyers and the vehicle sustainability based on the types of end use and expected cash flow and should be reflected in the vehicle grid used for lending</p> <p>The loan origination process must have sufficient “maker-checker” arrangements, to ensure that the Sales/Sourcing team’s activities are checked at the branch level and the branch level activities (especially, preparation of loan forms and collection of KYC documents) are also checked centrally by the credit team and specialized team of under writers.</p> <p>Maker checker arrangement should also be in place so that origination/ sourcing and field investigation is not done by the same person.</p> <p>The company can do the Field investigation in-house or appoint specialized FI agency</p>

<p>Operating process and performance</p>	<p>Operating Efficiency: Each Relationship officer must be responsible for a reasonable number of clients. This must be in keeping with the business model of the originator, the lending model, collection methodology, disbursement methodology, time required for the field officer to travel and conduct business.</p> <p>Optimum level of operating efficiency should be reflected in the loan outstanding per branch, loan outstanding per field staff and loan outstanding per borrower</p>
	<p>Each new staff must be adequately informed and trained to know the company, the loan product, and their risks and responsibilities under the loan.</p> <p>A different field investigation staff must physically verify each client’s details by visiting their home, supported by interviews with, family members and neighbours. They must verify and collect the following information on these visits</p> <ol style="list-style-type: none"> 1. Name and address 2. Occupation, Income and debt of the household 3. KYC documents provided <p>The financier should use the services of an experienced and specialised external valuator to verify the physical existence of the vehicle and assess the condition of vehicle and its market value. Ideally, the financier should pay the valuator to avoid any conflict of interest.</p> <p>The valuator should be empanelled by the company Clients must be made aware of the stipulation under any power of attorney that they sign.</p>
	<p>Each borrower should sign a demand promissory note to endorse the loan</p>
	<p>The product features, rules and regulations, including those related to effective interest rates, upfront fees and other charges, any security or pledge against the loan, penalties for delays in repayment or for prepayment/pre-closure, must be clearly mentioned in the loan agreement and/or sanction letter, as per RBI’s Fair Practices Code for NBFCs.</p>
	<p>Systems</p>
<p>The originator must have a clear process for collecting & collating accounting information from the branches and preparing consolidated accounting statements. Consolidated financial statements should be ideally prepared at least on a monthly basis</p>	
<p>All the customer level and loan level information must be stored in an electronic format</p>	

	<p>The system should have the capability to generate a unique client identification number and a unique loan number. The system should have capabilities to track multiple loans under the same client ID.</p> <p>The MIS must provide for a clear process for checking the demand-collection-balance (DCB) and any balance must be reported to the HO immediately.</p> <p>The system should have the capability to track co-borrowers and guarantors in the system.</p> <p>The MIS must be capable of ‘flagging’ of loans to different funding sources. MIS should also provide the ability to change the ‘flagging’ from one source to another. This should only be done by an administrator.</p> <p>The system must be able to correctly report on pre-payments, default and other exceptions (including dropout, transfer of client accounts) as well as PAR and ageing PAR.</p>
<p>Risk Management</p>	<p>Credit Risk:</p> <p>The originator should have:</p> <ul style="list-style-type: none"> • Identified specific commercial vehicle models and the borrower types that it will cater to and those that are in the exclusion list (exclusion list should also mention the purposes for which the commercial vehicles will not be financed) • Documented estimated price of each of these commercial vehicle models - for purchase of new vehicle and an old vehicle. This list should be updated on a periodic basis. • Documented allowable loan to value for different models of commercial vehicle and borrower types. <p>This information should form an input to credit decision making.</p> <p>Credit policy should have clearly defined limits on exposure (value and number of loans) to clients (borrower, co borrower and guarantors).</p> <ul style="list-style-type: none"> • The originator should be a member of a Credit Bureau and utilise its services in credit decision making • The Originator should have a process of cash flow analysis of the vehicle and borrower and validation of the same by the credit team. • The Originator should use existing payment track record information from the credit bureau report and/or as confirmed by existing lenders to assess the credit quality of a potential borrower. • The Originator should require each borrower to provide a guarantor with the guarantor preferably being an existing client

	<p>Operational Risk</p> <p>The originator must have an internal audit system, which is designed with a focus on operational risk management. The audit system must especially check for the possibility of ‘ghost’ loans, loans disbursed without proper KYC or without proper analysis of viability of commercial vehicle, or without proper verification of the vehicle and documents, adequate reference check.</p>
	<p>Cash Management</p> <p>The originators must have robust systems for storage of cash in branches and the same must be regularly monitored centrally and also be subject to frequent physical checks by the audit/risk management team.</p> <p>Cash at branches beyond pre-specified retention limits must be deposited in bank the same day or the next day, so as to minimise overnight balance of cash.</p> <p>Cash and assets (as applicable) as well as all documents and data must be transported in a secure manner</p> <p>The Originator must have a process of daily reconciliation of cash balances at the branch centrally.</p> <p>The originator must have availed of adequate insurance of cash-in-transit and cash-in-premises.</p>
	<p>The originator must have a well- defined process to handle defaults; this should be reflected in a low volatility of default rates, measured quarterly as PAR 90, for the life of the originator</p>
	<p>Regulatory Risk</p> <p>The originator must operate in compliance with the law of the land including regulations mandated by the RBI such as those pertaining to deposit taking, insurance and customer protection</p>
	<p>Reputation Risk</p> <ul style="list-style-type: none"> • The loan agreement should clearly mention the Financiers right to repossess the underlying vehicle in case of default and this should be explained to the borrower. • To ensure transparency, the terms and conditions of the contract/loan agreement should also contain provisions regarding: <ul style="list-style-type: none"> (a) notice period before taking possession; (b) circumstances under which the notice period can be waived; (c) the procedure for taking possession of the security; (d) a provision regarding final chance to be given to the borrower for repayment of loan before the sale / auction of the commercial vehicle; (e) the procedure for giving repossession to the borrower and (f) the procedure for sale / auction of the property

	<ul style="list-style-type: none"> • The originator should clearly differentiate between regular collection team and repossession team. The originator should have clear policy on appointing recovery agents deployed to repossess the vehicle for defaulting customers and must not in any case use strong arm tactics for these purposes. • The originator must have clearly defined recovery policies and partnerships with garages where vehicles repossessed can be held • The financier should have a documented policy for repossession of vehicles and disposal of these vehicles to avoid any conflict of interest
Financial performance	The originator must regularly map its Asset-Liability Mismatch (ALM) and must have means of financing negative mismatches (i.e., liquidity gaps).

Guidelines for Evaluation

In addition to the Eligibility Criteria laid out above, Northern Arc Capital will undertake a more detailed study of the originators business as per the underwriting guidelines below:

Criteria	Standard
Legal form	<p>The legal structure of the originator should preferably be an NBFC or NBFC MFI registered with the RBI and following all regulatory norms.</p> <p>If the company is listed on a stock exchange it should have always complied with the rules and regulations thereof and should have never been disqualified</p> <p>Originator should take a trade certificate from all the different RTOs under whose jurisdictions it is operating</p>
Governance and Strategy	<p>The Originator should have a Board with relevant experience and with at least one independent director.</p> <p>The board should play an active role in guiding the management</p> <p>The Originator should have a business plan for at least three years approved by the board including financial projections. The projections should be supported by (for a period of at least 6 months):</p> <ol style="list-style-type: none"> Details of new geographies for expansion, including branch locations Details of geographies for exit, including branch locations Details of product based/ asset class-based expansion plan Fund raising plans – debt and equity Assessment of their competitive position and comparative advantage <p>Promoters Background: promoters should be reputed professionals with at least 5 years of experience in financing commercial vehicles. Should have demonstrated ability of raising debt and equity funds</p>

	<p>The Originator should have created a strong level of management below the promoters and the chief executive officer ensuring that the business is not overtly dependent on a few key people</p> <p>The Originator must have clear delegation of authority, and oversight mechanism to ensure these are properly adhered to</p> <p>The CEO has at least five years of experience in lending/ financing for commercial vehicles</p> <p>The originator should have support functions such as finance, accounting, HR, IT, Internal Audit apart from credit and operations. Heads of these functions should have more than 5 years of experience in their respective function.</p> <p>The entity should have a mechanism in place to retain talent specially at key positions of responsibility</p> <p>Client Protection: The Originator should have clearly stated processes and policies to protect customer interests</p> <p>The originator must have put in place systems for grievance redressal providing for inter alia:</p> <ol style="list-style-type: none"> 1. Direct, independent access to higher authorities within the organization, for clients to share their grievances and feedback 2. Independent team that complies and reports on grievances/feedback to the senior management 3. Policies for redressal of grievances within reasonable time 4. System for internal audit/monitoring department to check on grievance redressal <p>The product features, rules and regulations, including those related to the effective interest rate, upfront fees and other charges, any security or pledge against the loan, penalties for delay in repayment or for prepayment/pre-closure, must be clearly mentioned in the loan agreement and/or sanction letter, as per RBI's Fair Practices Code for NBFCs.</p> <p>Proof of identity and residential address must be collected from every client and this must be admissible under the RBI "Know Your Clients" guidelines.</p> <p>The originator should not use or encourage strong arm tactics for collections of payment of overdue amounts</p> <p>The originator must clearly communicate to borrowers regarding:</p> <ol style="list-style-type: none"> 1. Interest and other charges associated with the loan product 2. Interest provided (in any) on security deposits or other deposits
--	--

	<p>3. Returns, lock-in periods, surrender/pre-closure charge, administrative charges and other deduction, cheque default charges and any other penal charges</p> <p>4. Premium paid to insurance companies, in case of credit-linked life insurance or other insurance products offered to the borrower</p> <p>The loan agreement should clearly mention the Financiers right to repossess in case of default and this should be explained to the borrower.</p> <p>To ensure transparency, the terms and conditions of the contract/loan agreement should also contain provisions regarding: (a) notice period before taking possession; (b) circumstances under which the notice period can be waived; (c) the procedure for taking possession of the security; (d) a provision regarding final chance to be given to the borrower for repayment of loan before the sale / auction of the commercial vehicle; (e) the procedure for giving repossession to the borrower and (f) the procedure for sale / auction of the property</p>
<p>Human Resource Management</p>	<p>The originator should have a clearly defined recruitment policy for field staff and staff at other levels. This policy should be followed, with the involvement of senior HO staff & regional level field staff. Professional reference check should be a part of the recruitment process. Recruitment should be planned and structured based on the business needs of the entity</p>
	<p>The Originator should have appropriate/adequate training for sales officer and middle management staff and the credit team staff. Originator could have certification programs for branch managers and credit staff. Regular refresher training should be done at the Head office and branch level</p>
	<p>The training for credit officer should consist of adequate field level and classroom training with focus on grid of vehicles being financed, process of FI</p>
	<p>The originator should have put in place a proper process for hand-over of customer relationships and job responsibilities in case of change in front-line staff on account of transfer, termination or general attrition. Specific cases of such hand-over should be checked by the internal audit or risk management team of the originator at least on a sample basis.</p>
<p>Origination process</p>	<p>The Originator should have a defined process for new branch opening which captures information on economic activity, credit culture and history of political/ administrative interference</p>
	<p>Negative areas identified by the originator should be listed. Reasons and record of the same should be maintained</p>
	<p>Maker-checker arrangement should be in place to ensure that the sourcing and field investigation is not done by the same staff</p>
	<p>The origination process should consist of the following steps:</p> <ol style="list-style-type: none"> i. Sourcing of potential clients ii. Credit Bureau Check iii. De Dupe

	<ul style="list-style-type: none"> iv. Collection of information and KYC documents, v. Collection of a copy of documents related with vehicle: vehicle insurance, vehicle age and fitness certificate, original RC book and permit validity. vi. Assessment of business strength and borrower's creditworthiness, House and business visit by field investigation personnel vii. Verification of the vehicle by an external valuator viii. Preparation of loan application form and "Health check" of application form by Operations/Back-office ix. Credit appraisal of loan application by credit department personnel. This should include an analysis to identify the fit between borrower profile and the vehicle being financed x. Cross-checking of business and entrepreneur's household information through tele-verification/ site verification/house visit by credit department personnel (including visit to guarantor, if any) xi. Reference check: Triangulation of information and evaluation of "willingness to pay" through interviews of relatives, neighbours, traders, suppliers etc. xii. Final credit decision-making (should ideally be centralised at region or HO level), supported by a tele-call with the customer by senior credit department staff xiii. Collection of documents/cash/FD/Post-dated cheques or any valuables as pledge or security, if applicable xiv. Execution of loan agreement xv. Issue of sanction letter to client xvi. Disbursement, preferably into client's operative bank account and Endorsement of hypothecation in the RC book of vehicle. Collection of Form 34 B extract from the RTO
	<p>Loans should be disbursed through cheque preferably to the seller of the commercial vehicle when the loan is taken for purchase of a vehicle</p>
	<p>Collection of repayments:</p> <p>The originator must have a clearly defined policy for follow-up on overdue accounts, which should ideally consist of the following steps in accordance with the number of days of delay in payment:</p> <ul style="list-style-type: none"> i. Follow-up visit to client's house and business site by staff ii. Make contact with guarantor(s) iii. Written intimation of default (with copy to guarantor), including therein, the penalties and charges due as well as notice of placing post-dated cheques (if any) iv. Placing of post-dated cheque (if any) v. Legal notice for bouncing of cheque, as required under relevant legal provisions

	<ul style="list-style-type: none"> vi. Initiation of arbitration process, if applicable vii. Legal notice for filing of suit for recovery of all dues, including penalties and charges <p>While following the above steps, regular personal contact must be maintained with the borrower and the guarantor(s).</p> <p>Sufficient escalation mechanisms to either more senior sales staff or the credit/recovery/delinquency management team must be in place during each step of the above process.</p> <p>The originator may allow for out-of-court settlement of cases of delinquency and rescheduling/restructuring of the loan. The process for such settlement or restructuring of loan should be clearly laid out and must involve a recommendation from the customer relationship management team, approval from senior credit department staff as well as from senior staff of the recovery/collections department.</p>
	<p>The Originator should not encourage the use of strong-arm tactics and clearly separate collection team from the repossession of the vehicle in case of default</p> <p>Credit Function should be separate from sourcing and collection (only at PAR 60 and above). The head of the Credit function must have at least five years of specific experience of having appraised loan/investment proposals of commercial vehicle-based loans/ financing activities with ticket sizes and type similar to the proposed line of business.</p> <p>Credit staff should not be eligible for any incentives based on business numbers</p> <p>The originator should have (state wise if it operates in multiple states):</p> <ul style="list-style-type: none"> i. Identified specific commercial vehicle models and the borrower types that it will finance ii. A clearly defined exclusion list that mentions the purposes for which the commercial vehicles will not be financed, it also details area-wise 'exclusion list', which is updated from time to time based on portfolio performance iii. Documented estimated price of each of these commercial vehicle models - for purchase of a new vehicle and an old vehicle. This list should be updated on a periodic basis. iv. Documented allowable loan to value for different models of commercial vehicle and borrower types. Specific policies on the type of registrations that it will finance. E.g.: financing of outside-state vehicles may not be done by the originator i.e. branches will finance vehicles registered with state RTO only.

	Management should have developed templates for doing a viability analysis of commercial vehicle it finances. This analysis should capture the free cash flow available with the borrower after paying the EMI. The cash flow analysis training and templates should capture details of household expenses and other obligations of the borrower and guarantor, if applicable.
Internal audit	The originator must have an internal audit system, which is designed with a focus on operational risk and legal risk. The audit system should specifically check for possibility of loans captured without sufficient documentation, instances of fraud and improper valuation of vehicle.
	The head of the internal audit team should have at least five years of audit experience
	The team should have members with experience in operations, accounts, finance and MIS
	The strength of the internal audit team should be adequate to ensure regular audit of all branches and Head Office
	A comprehensive audit must be conducted on all branches, periodically with mix of planned as well as surprise audit
	Originator should have an internal audit score model and the frequency of audit should linked to the branch performance
	Issues highlighted during the audit should be shared with the branch and action report should be filed at the branch
	The head of internal audit should directly report to the board via the audit committee
Systems	All customer level and loan level information should be stored in an electronic format with periodic backups, and should be regularly updated to a centralized location (i.e. up to date regional data should be available at HQ)
	The System should be able to retrieve accurate information in a timely manner and have restricted access as per the company hierarchy, i.e. employees at each level mist have access to only the information that they need
	The system should be able to track historical loan information on each individual client
	All data such as client asset information, late payment, defaults, additional deposit amounts should be recorded in the centralized electronic system
	Adequate process controls should be in place to ensure data integrity during transfer of data from manual to electronic format
	The system should have the capability to provide data to Credit Bureau in the required format
	The system should have the capability to perform a client level “de dupe” for loan disbursement to the same client
	The system should be able to monitor and track portfolios to manage credit risk

	<p>The system should be able to generate reports such as collections, disbursements by branch/hub, client history, product summaries, hypothecated portfolio, portfolio by loan purpose/tenor/clients profile/loan officer, portfolio at risk, defaults, repossessed vehicles etc. Timely access to such reports should be facilitate business and operational Decisions</p>
	<p>The originator must have systems in place for safe storage of loan files, original documents and security cheques, giving due consideration to:</p> <ol style="list-style-type: none"> a. Traceability of cheques to customer’s loan account b. Filing of cheques in accordance with cheque date or in accordance with customer loan file number c. Maintaining a stock of cheques based on cheque number, so as to enable audit of cheques d. Ensuring restricted and controlled access to cheques and other important documents e. Protection of storage vault from fire or other natural disasters
	<p>The Originator should be a member of credit bureau and loan disbursement should only be done after processing client information available through credit bureau.</p>
	<p>Interest Rate Risk: The originator should use appropriate interest rate risk management technique, including interest rate hedge as needed. The originator should maintain a low equity duration which is a measure of interest rate risk/sensitivity and is calculated as the ratio of the weighted average duration of assets and the weighted average duration of liabilities</p>
	<p>Liquidity Risk: The originator should maintain a robust liquidity position, as assessed by the analysis of static liquidity (projected month on month cash outflow and inflow in terms of maturity of assets and repayment of existing liability, assuming no further inflow of external funds and no further disbursement of new loans</p>
	<p>Credit Risk: The originator should have:</p> <ol style="list-style-type: none"> i. Identified specific commercial vehicle models and the borrower types that will be catered to and those that are in the exclusion list (exclusion list should also mention the purposes for which the commercial vehicles will not be financed) ii. Documented estimated price of each of these commercial vehicle models - for purchase of new vehicle and an old vehicle. This list should be updated on a periodic basis iii. Documented allowable loan to value for different models of commercial vehicle and borrower types. <p>This information should form an input to credit decision making.</p>

- The Originator should be a member of credit bureau and loan disbursement should only be done after processing client information available through credit bureau
- The Originator should use repayment track record information available from other existing lenders as well.
- **Risk of adverse client selection:** Originators should give high weightage to reference of an existing client.
 - Some originators ensure that borrower owns a property

Default risk - capacity of borrower:

Following process should be followed:

- i. Assessment is done by discussing with the operators, Field investigation, Trade reference checks
- ii. Credit Bureau checks
- iii. Asset usage: average capacity utilisation rates etc.
- iv. Free Cash flow analysis: taking into account the fleet size of the client, the routes he plies on, freight rate, driver expenses if applicable, other obligations and household expenses etc.
- v. Client and vehicle wise exposure limits
- vi. Margin requirement ensure check for early default

Risk of over valuation of the collateral (vehicle)

Originator should maintain a valuation grid which gives details financing of estimated market value of the CVs

LTVs are based on borrower profile and asset financed (assets with high resale value and better market reputation financed at higher LTVs)

- New CV: on road price (MHCV – different LTV for chassis and body, LCV
- Used CV: LTV based on valuation as per grid
 - Documentation: Standard legal documentation should be followed
Endorsement of hypothecation in the RC book
 - Risk Containment unit checks a sample % of documents

The Originator must have a process of reviewing the valuation grid at a minimum of once in _three months and more often based on market conditions prevailing in particular segments.

Monitoring of portfolio, delinquency management:

- i. Strong relationship management practices
- ii. Bad debt management is considered as a key function;

	<ul style="list-style-type: none"> iii. Bad debt classification is automatic, based on delinquency buckets, according to credit policy rules; iv. Bucket wise collection teams ensure concentrated collection effort v. Well-defined incentive plan for field officers, branch manager and credit manager to ensure low default rates vi. Detailed process for repossession along with a strong legal team and approval for repossession from senior management
	<p>Operational risk: Risk of fraud by employees: Entity should avail of fidelity insurance, to protect itself from staff fraud The originator should develop of Standard Operating Procedures (SOP) of all activities of the business. The originator should have a strong internal audit team to ensure compliance</p>
	<p>Reputation Risk: The originator should have a process in place for customer grievance in a timely manner. The originator should have clearly laid down policies for its staff to interact with clients at the time of origination, collections and follow up with delinquent clients. Repossession: as defined in client protection</p>
<p>Cash Management</p>	<ul style="list-style-type: none"> • The originators must have robust systems for storage of cash in branches and the same must be regularly monitored centrally and also be subject to frequent physical checks by the audit/risk management team. • Cash at branches beyond pre-specified retention limits must be deposited in bank the same day or the next day, so as to minimise overnight balance of cash. • Entity should have clearly-defined policies for management and storage of cheques (including security cheques) • Cheque number and other details of all cheques should be entered in the MIS and placement, bounce, cancellation of cheques should be tracked • The originator must have availed of adequate insurance of cash-in-transit and cash-in-premises.
<p>Financial and operational performance</p>	<p>The promoter should have adequate stake and control in the company</p> <p>The originator should maintain multiple sources of funding</p> <p>The originator must have a capital adequacy ratio of at least 15%, measured as defined under the Prudential Norms prescribed for NBFCs by the Reserve Bank of India.</p> <p>The originator must regularly map its Asset-Liability Mismatch (ALM) and must have means of financing negative mismatches (i.e., liquidity gaps)</p> <p>The volatility of PAR, as measured by the maximum historical PAR (>30 days) on loans originated at different points of time and the variation between the PAR from different origination periods and different geographies must not be significantly different or high</p>

	The Originator should have minimum loan loss provisions as stipulated by the RBI for its type of NBFCs
	The originator should maintain a robust liquidity position, as assessed by the analysis of static liquidity (projected month-on-month cash outflows and inflows in terms of maturity of assets and repayment of existing liabilities, assuming no further inflow of external funds and no further disbursement of new loans).
	Entity has clearly-defined policies for management and storage of cheques (including security cheques)

Definition

Capital Adequacy	Ratio of tangible net worth (less retained first loss default guarantee and investment in related or subsidiary entity) to risk weighted assets
De Dupe	Process that uses matching logic to eliminate file records that are duplicate in the system
Default	A loan is considered in default if the borrower has not made any payment for that loan for a period greater than 30 days for weekly and fortnightly and 90 days for monthly instalment
Equity Duration	Ratio of the weighted average duration of assets and the weighted average duration of liabilities
Portfolio at Risk	Ratio of loan amounts overdue to total loan balance outstanding
Promoters	Initial equity investors who continue to remain whole time executive directors on the Board of the Company
Volatility of Default	Annualised standard deviation of default measured using weekly, fortnightly or monthly data since inception, or using default data for the 3 years
Weighted Average Annual Default Rate	Combined outstanding balance at time of default for all loans that has fallen into default at any time during the fiscal year (excluding loans that were already in default at the start of the fiscal year) divided by the sum of all scheduled principal payment due during the fiscal year
Valuation grid	A table that documents estimated price of each of the identified specific commercial vehicle models and the borrower types that will be catered commercial vehicle models - for purchase of new vehicle and an old vehicle. This table should be updated on a periodic basis.

Issued on: 15th July 2013