SARASWATI COMMERCIAL (INDIA) LIMITED

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EXPECTED CREDIT LOSSES POLICY

Effective From	30.01.2019
1st Review	11.11.2022
2nd Review	12.08.2024
3rd Review	13.08.2025

Introduction

In line with the RBI's requirement for the Board of Directors to approve sound methodologies for computation of Expected Credit Losses (ECL), that address policies, procedures and controls for assessing and measuring credit risk on all lending exposures, commensurate with the size, complexity and risk profile specific to the NBFC, the Company has formulated this ECL policy.

Objective

Policy's objective is to guide Saraswati Commercial (India) Limited ["The Company"] for ensuring adherence with RBI guidance for application of Indian Accounting Standards placed via notification dated 13th March 2020 i.e. assess the appropriateness of ECL computation (as per IND AS 109) as well as enable making appropriate provision and reserves. The Policy gives an overview of how to determine the impairment stage of a Loan Facility extended by company as well as explains how to compute appropriate provision (IRAC norms or ECL) for the different stages.

Applicability

Expected Credit Losses shall be applicable to following items in company's Financial Statements

(a) Cash equivalent based on Amortized Cost Principles
(b) Fixed Deposits with banks
(c) Loans and Advances
(d) Trade receivables
(e) Investment in unlisted securities
(f) Other financial assets (whether recurring or not)

(only on-balancesheet items shall be considered for this purpose, however appropriate disclosure of impairment of contingent asset shall be made in financial statements (if any), in conjunction with the prescribed regulatory guidelines)

Roles and Responsibility

1. **Board of Directors**

   As the highest decision-making body within the organization, the Board of Directors determines the strategy for lending for the company. The strategy shall be guided by the oversight of the Expected Credit Losses Computed for different clients across different sectors. Apart from oversight of the computation of Expected Credit Losses, the board shall have following responsibilities:

   - Appropriate Mechanism to bring down the Expected Credit Losses
   - Suggest changes and appropriate methodologies and inputs to compute ECL figures
   - Determine, in consultation with the Risk Management Committee, clients / industry that pose material risks to the Company's business strategy, or reputation
   - Reviewing and, as requested, approving exceptions to ECL Policy
   - Suggest reporting mechanism, to ensure quarterly comparison of ECL figures as well as to review upward / downward trends in asset quality.

- Authorize the rebuttable presumption of 30 days as suggested by IND AS 109 and ensure maintenance of appropriate records thereof.
- Ensure implementing the recommendation of the Internal as well as statutory Auditor.

2. Accounting Team

- Determines Stage 1 & Stage 2 provisions upon deliberation with the Credit Team as well as Risk Team, but within the limits prescribed by board of directors
- Implement actions for recovery of amount as laid down in company's recovery / credit policy
- Ensure appropriate provision is created in books of the company and appropriately reported to the regulatory authorities
- Ensure appropriateness of figures disclosed in financial statements / website.

Methodology

Company is mainly engaged in Investment in Shares and Securities. Company also engaged in short term lending facilities in the forms of revolving Loan facilities and short term Loan, where tenure of Loan is 12 months of less. Considering the same company has decided to Compute ECL as follows: -

Data Input and Criteria

Expected credit losses are a probability weighted estimate of credit losses. Credit losses are measured as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the Company in accordance with the contract and the cash flows which the Company expects to receive).
The Company continuously monitors all financial assets subject to ECLs. In order to determine whether an instrument is subject to 12-month ECL (12m ECL) or life time ECL (LTECL), the Company assesses whether there has been a significant increase in credit risk or the asset has become credit impaired since initial recognition. The Company will apply following quantitative and qualitative criteria to assess whether there is significant increase in credit risk or the credit quality of the asset has impaired:

(a) Historical trend of collection from counterparty;
(b) Company's contractual rights with respect to recovery of dues from counterparty;
(c) Credit rating of counterparty and any relevant information available in public domain;
(d) Formula for the computation of ECL shall be as determined by the board based on guiding parameters in the policy

Measurement of expected credit loss

IND AS 109 requires all financial instruments other than those recognized as FVTPL and equity instruments to be classified into one of the three stages (Stage 1, Stage 2 or Stage 3) based on the assessed credit risk of the instrument/facility.
There are three stages:
• Stage 1 would include all facilities which have not undergone a significant increase credit risk
• Stage 2 would include facilities meeting the criteria for Significant Increase in Credit Risk and facilities with DPD 30 or more. The Company may rebut this presumption based on behavioral pattern of financial instruments.
• The stage 3 will have facilities classified as NPA and facilities with DPD 90 or more

The determination of the IND AS 109 provision results from a two-step approach.

As step 1, the facilities will have to be allocated to one of the three stages by determining whether a significant increase in credit risk has occurred since initial recognition or whether the facility has defaulted. The following diagram provides a general overview of the approach in determining significant increase in credit risk.

As step 2, the expected credit loss is calculated i.e., 12-month expected loss for all facilities in stage 1 and lifetime expected credit loss for all facilities in stage 2. The facilities in stage 3 are covered by specific provisions as detailed in specific write-off policy.

- To determine if the risk of default of a financial instrument has increased significantly since initial recognition, the current risk of default at the reporting date should be compared with the risk of default at initial recognition.
- Assessment of whether there has been a significant increase in credit risk is required to be carried out at each reporting date.

Stagging Mechanism

Stage 1: As soon as a financial instrument is originated or purchased, 12-month expected credit losses are recognized in profit or loss and a loss allowance is established. This is applicable across all the instruments the Company deals in.
Stage 2: Determining Significant Increase in Credit Risk (SICR)
IND AS 109 presumes 30 DPD criteria for Stage 2 classification. This presumption is subject to rebuttal. This measure of Stage 2 shall be further assessed through forward and backward flow rates to rebut the 30 DPD criteria. However, in any case, this should not exceed 90 days as a back-stop measure. Accordingly, in line with IND AS 109, any financial asset with DPD of 30 days or more shall be classified as stage 2.
Additionally, following criteria shall also be for investments:

- Facilities with rating grade AAA and AA (including modifiers) are considered as highly rated facilities with no history of defaults. Accordingly, for rating grades AAA, **a three notch** down (without modifiers) shall be taken as stage 1
- Facilities with rating A (including modifiers) to BB (including modifiers) are considered as highly rated facilities with low probability default. Accordingly, for rating grade A (including modifiers), BBB (including modifiers) and BB (including modifiers) **a two notch** down (without modifiers) shall be taken as stage 2 assets
- Facilities with rating grade B (including modifiers) are represent high credit risk with higher probability of default. Accordingly, for rating grades B (including modifiers), **one notch** down shall be considered as stage 2 assets.
- Any financial instrument with **rating grade CCC or below** shall be classified as stage 2 at origination.

- **Asset Classification and Provisioning**

Loan asset classification and requisite provision made under RBI prudential norms, as applicable to company, are given below:

Particulars	Criteria	Provision
Standard asset	The asset in respect of which, no default in repayment of principal or payment of interest is perceived and which does not disclose any problem nor carry more than normal risk attached to the business.	0.40% of the outstanding loan portfolio of standard assets
Sub-standard assets	An asset for which, interest/principal payment has remained overdue for more than 3 months and less than 12 months.	10% of the outstanding loan portfolio of sub-standard assets
Loss assets	An asset for which, interest/principal payment has remained overdue for a period of 12 months or more	100% of the outstanding loan portfolio of loss assets.

Provision in books and Disclosure

After applying above criteria, Management will decide to make minimum ECL provision. However, if the ECL provisioning calculated based of above criteria is lesser than provisioning required by RBI prudential norms (as given in above table) then company will make provision as per RBI rates & if ECL provisioning required as per above criteria is higher than RBI rates then higher provisioning as per above criteria will be made. So, in all the cases provision made by the company will be equal to or at higher than RBI required rates.

Company shall provide a comparison between provisions required under IRACP and impairment allowances made under Ind AS 109 by way of disclosure in the notes to their financial statements to provide a benchmark to their Boards, RBI supervisors and other stakeholders, on the adequacy of provisioning for credit losses.

Policy Review and Updation

This policy will be reviewed at least annually or more frequently if required and approved as per the usual review process applicable. The review would incorporate changes in regulatory guidelines on ECL, new methodologies in the area of ECL, due to changes in the Company's business, changes in the organisation structure or as required.