

Fair Practice Code

Interest rates and approach for gradation of risks

(1) Background:

RBI vide its notification no: DNBS.204/CGM (ASR)-2009 dated January 2, 2009 notified the following and the same is reproduced below:

“The Board of each NBFC shall adopt an interest rate model taking into account relevant factors such as, cost of funds, margin, risk premium, etc and determine the rate of interest to be charged for loans and advances. The rate of interest and the approach for gradations shall be disclosed to the borrower or customer in the application form and communicated explicitly in the sanction letter

The rates of interest and the approach of gradation of risk shall also be made available on the web site of the Companies, or published in the relevant newspapers. The information published in the website or otherwise should be updated whenever there is a change in the rates of interest.

The rate of interest should be annualized and the borrower is made aware of the exact rate that would be charged to the account ”

(2) Methodology Proposed for appraising & grading clients:

IL&FS Financial Services Ltd (IFIN) for its retail portfolio (ticket size upto Rs 250 Mn) and having a diversified basket proposes to grade the clients based on the following factors :

- a. Income \ Asset Base\ Net worth
- b. Amount of Loan requested
- c. Type of Loan Facility \ Committed Draw downs
- d. Collateral offered
- e. Reputation \ Parentage \ Risk Profile of customer
- f. Conduct of Past Relationships \ Scope of Existing Relationships:
- g. Management Perception \ Discretion \ Future Relationships

Loans above this ticket size may be sanctioned as an exception with approval of the credit committee

- (3) The loans would be appraised on quantitative factors on a scale of 1 to 3 (for most factors) The Loan scores would be assigned for each of the factors considering the following framework:

a. Income \ Asset Base\ Net worth:

For appraisal of a loan, Income tax returns for the 2 immediate preceding years would be collected. Net worth certificate would be collected to quantify the asset base of the customer & guarantors (if available).

Leverage vis a vis Annual Income	Leverage vis a vis Network	Score
Upto 4 times income	Upto 1 time the net worth	3
> 4 upto 10 times income	> 1 and = < 2.5 times net worth	2
> 10 times income	> 2.5 times	1

Incase the net worth certificate is available along with Income tax statement, then preference would be given to the net worth certificate for assigning scores for this factor

Incase the loan is guaranteed, the overall network strength of the borrower & guarantor would be considered for giving a rating

b. Amount of Loan requested:

ROI requested is inversely related to the amount of loan requested in the capital market segment business. Bigger borrowers with good credit standing would get loans at cheaper rates.

Category of Client	Score Range
Big ticket clients: Where loan proposal value is equal to \ greater than 50 Mn	2
Medium Clients : Where loan value is upto 50 Mn	1

c. Type of Loan Facility \ Committed Draw downs:

ROI is also dependent on the type of loan facility, sanctioned amount and extent of draw-downs. Fixed loan proposals guarantees stability of corpus & interest income due to committed draw-downs over a defined period & hence may be approved at lower ROI. Conversely, Line of Credit loans require higher levels of

treasury management skills and consequently command higher ROI. Hence appropriate grading scores would be assigned to the type of loan facility proposed.

Type of Loan Facility	Score Range
Fixed Loans	2
Line of credit Loans	1

d. Collateral Offered

Clients offering diversified basket of collateral (atleast 3 scrips or more) would be given a higher rating. Clients offering single scrip loans may be given a lower rating. However, as an exception, single scrips loans backed by collateral which are part of the BSE 100 index may be treated on par with diversified scrip basket due to the quality of the collateral and therefore assigned a higher rating. Similarly mutual fund units offered as collateral would be considered as a diversified collateral. As per the product specifications, most of the loans are supposed to be diversified except single scrip loans.

Collateral Offered	Score Range
Diversified Collateral \ Mutual Fund Units	2
Single Scrip loans	1

e. Reputation \ Parentage \ Risk Profile of the customer:

Customers are categorized into high risk, low risk and medium risk customers. Brokers, NBFCs, ESOP customers are categorized as low risk customers since they are either regulated entities \ referred by company. Similarly employees working with PSUs or good private limited companies are categorized as low risk customers

Corporates unless forming part of a broking group\ without strong parentage may be referred at medium risk client

Borrowers who have pending SEBI cases, politically exposed persons may be categorized as high risk clients and charged a higher ROI

The rating provided by credit agencies (Experien etc) would also be considered for categorizing a client

Category of Client	Score Range
Low Risk	3
Medium Risk	2
High Risk	1

f. Conduct of Past Relationships \ Scope of Existing Relationships:

The depth & tenure of existing business relationship IL&FS group has with the client has a bearing on the final ROI. Higher the client’s engagement with IL&FS group, lower is the possibility of his defaulting or not rectifying shortfall, which greatly reduces risk perception. Besides the conduct of a client during his past relationships would have a bearing on the ranking and indirectly interest rates

Extent of Relationship	Score Range
Is a existing customer of IL&FS group / Conduct during past relationships is good	2
Does not have any dealing with IL&FS Group	1

g. Management Perception and Discretion

Lending to appropriate borrowers or fledging business or a great innovating strategy adopted by a borrower is an art. It may not be possible to quantify the benefit arising out of such client relationship Keeping in view that primary objective of IFIN being an NBFC is to encourage lending and facilitate funding, the discretion of the management plays an important role in determining whether the proposal from a prospective customer is worthy of funding.

IFIN believes in catching the client in its younger stages of growth, thus ensuring that it grows with the client. Smaller but aggressive clients may get a longer rope from IFIN who would then remain loyal to IFIN. IFIN, in such cases may assign a higher rating to ensure continuous flow of new business to IL&FS group

The range would vary between -2 to 2 and needs no corroborative evidence to assign the score

(4) Grading of Client & Determination of Applicable ROI :

All the factor scores have been given a standard weightage of 1. IFIN would sum up the scores across all factors to arrive at the final Proposal Score. Based on the score, clients would be categorized into A, B and C category clients. Assuming that the interest band moves in a range difference of 50 bps, the interest rate is also defined herewith. For eg : If the ROI range band is 13.50 – 15 % (indicative), the Lower limit (LL) would be 13.50% while the Higher Limit (HL)would be 15%. IFIN may review the band at every monthly interval if reqd.

The maximum possible score as per the mandatory appraising factors is 14 and lowest possible is 6

Client categories	Final Proposal Score (Sum of Factor score)	Minimum Limit ROI	Maximum Limit ROI	Rationale for ranking proposals
A	Above 10	Lower Limit	Lower Limit + 50 Bps	> 70% of total factor score
B	8 to 10	Lower Limit + 50 Bps	Lower Limit +100 Bps	> 50% and < 70% of total factor score
C	Less than 7	Lower Limit + 100 Bps	Higher Limit	< 50% of total factor score

(5) Appraisal Process :

HO would appraise the loan based on the parameters, information received from the branches and analysis of the statements and assign relevant score for each factor.

Encl: (1) Rating Score Card

Annexure A :

Rating Score Card:

Client Name			
Loan Amt Applied	Rs.		
Date of Appraisal	/ /		
Factors Considered	Rating Range Band	Scores Assigned	Remarks
Income \ Asset Base\ Net worth	1 – 3		
Amount of Loan requested	1 – 2		
Type of Loan Facility \ Committed Draw downs	1 – 2		
Reputation \ Parentage \ Risk Profile of customer	1 – 2		
Conduct of Past Relationships \ Scope of Existing Relationships:	1- 2		
Management Perception \ Discretion \ Future Relationships	-2 – 2		
Total			
Grade (A / B / C)			
ROI Offered			%

Notes :

Grade	Score Range	Minimum Limit ROI	Maximum Limit ROI
A	10 and above	Lower Limit	Lower Limit + 50 Bps
B	8 to 9	Lower Limit + 50 Bps	Lower Limit +100 Bps
C	Less than 7	Lower Limit + 100 Bps	Higher Limit