

## India Rating's Default Recognition and Post-Default Curing Period Policy

Ratings revision to default rating (IND D), the lowest rating on the long-term and short-term rating scale, is governed by India Ratings and Research's (Ind-Ra) default recognition policy outlined in this document. Ind-Ra's default recognition policy adheres to the guidelines issued by Securities and Exchange Board of India (SEBI) and Reserve Bank of India (RBI) and is consistent with the Standard Operating Procedure for CRAs for Monitoring and Recognition of Defaults. The policy is consistently applied across instrument classes for capital market and bank loan instruments. The framework also ensures that Ind-Ra's default studies provide an accurate metric for investors to rely on the rating performance.

The document outlines Ind-Ra's default recognition policy and also provides the curing period required for upgrading ratings post-default recognition.

### A. Default recognition policy

Ind-Ra considers the first instance of a missed payment as an 'event of default' for instruments with pre-defined repayments such as Debentures, Bonds, Commercial Paper or Term Loans. Default is recognised irrespective of the magnitude and period of delay and can be summarized as not meeting the 'one-day-one-rupee' condition.

Default recognition on working capital bank loan facilities without a pre-defined repayment schedule, such as Cash Credit or Overdraft, is after the facility remains continuously overdrawn for more than 30 days. A similar default definition of 30 days of the facilities being overdue is considered for other working capital facilities such as Packing Credit and Letter of Credit. Instrument-wise definition of default is provided at Figure 1.

Upon recognition of a default, as determined by Ind-Ra's policy, the outstanding ratings will be downgraded to 'IND D'.

The default recognition policy is consistent with the regulatory guidelines/prescriptions i.e.

- a) SEBI guidelines ([SEBI/HO/MIRSD/MIRSD4/CIR/P/2016/119](#) dated 01 November, 2016 - Enhanced Standards for Credit Rating Agencies) lays down the principal and has provided instrument-wise default recognition to be adhered to by all credit rating agencies.
- b) Standard Operating Procedure for CRAs for Monitoring and Recognition of Defaults as prescribed by SEBI
- c) RBI circular ([DBR.No.BP.BC.4./21.06.001/2015-16 dated 01 July 2015](#)- Master Circular - Prudential Guidelines on Capital Adequacy and Market Discipline-New Capital Adequacy Framework (NCAF)) states that external credit "assessment must fully take into account and reflect the credit risk associated with timely repayment of both principal and interest"
- d) RBI has prescribed uniform default definition for bank loan ratings as below:
  - i. For bank facilities having a predefined repayment date/due date, the definition of 'one day one rupee' may be adhered to;
  - ii. For revolving facilities like cash credit, CRAs may allow, as of now, grace period upto the maximum of 30 days from the date of overdraw, beyond which an activity would be considered as 'default';

**Figure 1- Instrument-wise definition of default ([SEBI/HO/MIRSD/MIRSD4/CIR/P/2016/119](#) dated 01 November, 2016)**

Facilities	Rating Scale	Proposed Definition of Default
<b><i>Fund-based facilities &amp; Facilities with pre-defined repayment schedule</i></b>		
Term Loan	Long Term	A delay of 1 day even of 1 rupee (of principal or interest) from the scheduled repayment date.
Working Capital Term Loan		
Working Capital Demand Loan (WC DL)		
Debentures/Bonds		
Certificate of Deposits (CD)/ Fixed Deposits (FD)	Short Term/ Long Term	
Commercial Paper	Short Term	
Packing Credit (pre-shipment credit)	Short Term	Overdue/unpaid for more than 30 days.
Buyer's Credit	Short Term	Continuously overdrawn for more than 30 days.
Bill Purchase/Bill discounting/Foreign bill discounting /Negotiation (BP/BD/FBP/FBDN)	Short Term	Overdue/unpaid for more than 30 days.
<b><i>Fund-based facilities &amp; No Pre Defined Repayment Schedule</i></b>		
Cash Credit	Long Term	Continuously overdrawn for more than 30 days.
Overdraft	Short Term	Continuously overdrawn for more than 30 days.
<b><i>Non fund-based facilities</i></b>		
Letter of credit (LC)	Short Term	Overdue for more than 30 days from the day of devolvement.
Bank Guarantee (BG)(Performance/ Financial)	Short Term	Amount remaining unpaid from 30 days from invocation of the facility.
<b><i>Other Scenarios</i></b>		
When rated instrument is rescheduled:		Non-servicing of the debt (principal as well as interest) as per the existing repayment terms in anticipation of a favourable response from the Banks of accepting their restructuring application/proposal shall be considered as a default. Rescheduling of the debt instrument by the lenders prior to the due date of payment will not be treated as default, unless the same is done to avoid default or bankruptcy
Curing Period		90 Days - for Default to Speculative Grade and generally 365 Days for Default to Investment Grade

## B. Curing Period Policy

Rating upgrade following a default requires a curing period. This is the period over which the issuer will demonstrate a track-record of timely debt servicing. Over this period Ind-Ra determines if the operational changes and liquidity management is sustainable for upgrading the rating. This is inline with curing period guidelines of SEBI vide circular no. [SEBI/HO/MIRSD/MIRSD4/CIR/P/2016/119](#) dated November 1, 2016 and RBI's prescription to rating agencies.

Default rating will be considered for an upgrade to a sub-investment grade rating once all the instruments under default rating with similar seniority have demonstrated a track-record of timely payment for atleast 90 consecutive days.

Ratings may be further upgraded to investment grade, usually after 365 days of continuous timely repayment track-record from the date of regularization and Ind-Ra's view that the measures adopted by the issuer will sustain their credit profile at the assigned investment grade level.

While, Ind-Ra shall generally apply the curing period as mentioned above, it can deviate on a case-to-case basis in accordance with SEBI circular no. [SEBI/ HO/ MIRSD/ CRADT/ CIR/ P/ 2020/ 87](#) dated May 21, 2020. The circular states that "CRAs may deviate from the said period of 90 days on a case to case basis, subject to the CRAs framing a detailed policy in this regard.". Further, "The CRA shall frame a policy in respect of upgrade of default rating to investment grade rating and place it on its website." Ind-Ra may deviate from the said curing period policy after the defaults have been regularized, and on a case-to-case basis it is of the view that the underlying credit profile has structurally improved and the circumstances leading to the default is unlikely in the near to medium term. These should fundamentally alter the credit risk profile of the defaulting company. Further, all claims from existing lenders should be comprehensively settled, prior to an upgrade being considered. Some of the likely instances for deviation include, but not limited to, the following:

- Defaults that have occurred on account of procedural or system issues or human errors (often termed as technical defaults) and that have been rectified by the issuer to ensure no recurrence
- Change in management leading to expectation of significant improvement in the credit profile of the issuer
- Acquisition by another firm
- Sizeable inflow of long-term funds alleviating liquidity stress
- Benefits arising out of a regulatory action, which immediately improves the adequacy and stability of cashflows
- Refinancing of instruments in default eliminates cashflow mismatches for e.g. replacement of the current facilities with longer tenure instruments; so long as business profile of the issuer is robust
- Force majeure event i.e. events which are outside the reasonable control of the issuer leading to default and have now been rectified; so long as business profile of the issuer continues to remain viable

Ind-Ra may use an accelerated curing period upon occurrence of events stated above and there being no overdue payments. The rationale for all such accelerated curing period for rating upgrade will be provided in the Ratings Action Commentary.

Clearing overdues from ongoing business and financial improvements will not be considered as an exceptional event for accelerated curing period.

## C. Standard Operating Procedure for Monitoring and Recognition of Defaults

In order to standardize the operating process for monitoring and recognition of defaults, SEBI's Circular "[Guidelines for Enhanced Disclosures by Credit Rating Agencies \(CRAs\)](#)" dated June 13, 2019 has required that "CRAs, in consultation with SEBI, shall frame a uniform Standard Operating Procedure (SOP) in respect of tracking and timely recognition of default, which shall be disclosed on the website of each CRA".

SEBI in its Circular dated June 30, 2017 on "[Monitoring and Review of Ratings by Credit Rating Agencies \(CRAs\)](#)" had also noted that "CRAs have to be proactive in early detection of defaults/delays in making payments." SEBI had further stated, "As responsible institutions, CRAs are expected to proactively track all important changes relating to the client companies in order to yield timely and accurate ratings. It is reiterated that CRAs are required to ensure prompt and accurate rating action".

In line with these regulatory guidelines, we have put together an SOP for tracking and timely recognition of default. Recognition of defaults in a timely and consistent manner helps achieve the following objectives:

1. Present accurate performance statistics like default rates
2. Help investors and other stakeholders compare performance of CRAs using objective metrics and consistent default monitoring/recognition practices

Following practices shall be consistently adopted by all CRAs towards ensuring consistency and uniformity in tracking and recognition of defaults.

1. **Communication with bankers:** Every CRA shall write to the bankers to take feedback at the time of initial rating and at periodic intervals (at least once every quarter) to ascertain timeliness in debt servicing. In cases where bankers do not respond in writing, the discussions shall be documented (through email/ letter to the banker).
2. **No default statement (NDS)** to be sought on a monthly basis from the Issuer in line with SEBI regulations.
3. **Tracking confirmation from debenture trustee** on timely debt servicing on specific ISINs rated by the CRA in line with SEBI regulations. For securities, the withdrawn rating shall be included in the computation of default rates till the completion of the 3-year cohort or the maturity of the instrument, whichever is earlier. Accordingly, the CRAs shall continue to track the confirmation received from the debenture trustees on the status of debt servicing on securities even after rating withdrawal, where applicable.
4. **Monitoring of Exchange website:** The CRA shall also monitor the Exchange website for disclosures made by issuers with listed securities (either debt or equity) in respect of timely debt servicing.
5. **Publishing of press release in case of payment default:** In case of confirmation of any delay in servicing of the debt obligation, press release shall be published within timelines as prescribed under regulations.
6. **Disclosure in case of non-confirmation of timely debt servicing:** In case no confirmation regarding servicing of debt obligation on the listed security is received by the CRA from the Debenture Trustee within 1 day post the due date, the CRA shall immediately follow up with the Issuer for confirmation of payment. In case no response is received from the Issuer within 2 days of such communication, the CRA shall publish a Press

Release as per SEBI prescribed format on its website and send to all stock exchanges where the security is listed.

7. **Rating agreements shall be suitably modified** to incorporate Issuers responsibility to provide consent to the CRA to obtain details of the existing and/ or future borrowing of the issuer, its repayment and any delay or default in servicing of such borrowing, either from the lender or any other statutory/non - statutory organisation maintaining any such information. Such right to access to information shall be made clear to the said external parties while seeking information.
8. **Factoring in past defaults:** In rare circumstances, if a CRA becomes aware of the delays that have occurred in the past and have not been recognized by way of a 'D' rating, the delay shall be recognised by downgrading the rating to 'D'. The rating can be simultaneously upgraded to a non-D rating, in line with the SEBI guidelines on curing period and the SOP on curing period mentioned below.
9. **Default on instruments not rated by CRA:** In case an issuer defaults on an unrated instrument which has same seniority as the rated instrument by the CRA,
  - a. The CRA shall recognise the default in its default statistics from the rating level of the rated instrument. The rating of the rated instrument which has not defaulted may be appropriately reviewed by the CRA.
  - b. For the sake of ample clarity, it is highlighted that a default on an unrated instrument may not mean and shall not be construed as a default for computation of default statistics, if the rated instrument is credit enhanced or there is a structure around the cash flows.
  - c. The CRA in its default studies shall also give out a list of all companies where ratings may not have been downgraded 'D', but issuer has been included in the default study due to default on unrated debt.
10. **Curing period post defaults:**
  - a. The curing period principle for default category ratings should apply to fresh rating assignment as well as surveillance assignments and usually at an issuer level. For the sake of ample clarity, if a CRA is rating an issuer afresh, a non-default rating would not be assigned if the curing period post an earlier default on any instrument of similar seniority has not lapsed.
  - b. However, for ratings on subordinated or hybrid bonds, since a default on such instruments may not necessarily imply a default by the issuer for senior instruments, curing period should apply at instrument level. In case of default on subordinated or hybrid instruments, ratings on senior instruments may not be upgraded during the curing period for subordinated and hybrid instruments.
  - c. If rated instruments is credit enhanced or there is a structure around the cash flows, the curing period will apply at instrument level, as default by issuer on other instruments may not imply or lead to default on such instrument.

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