

Policy for Treatment of Wilful Defaulters and Large Defaulters

Company: ART Climate Finance (India) Private Ltd

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1. Background

The Reserve Bank of India (RBI), through its guidelines on Wilful Defaulters, has mandated NBFCs to adopt a Board-approved policy to identify, classify, and report wilful defaulters. In line with these directions, ART Climate Finance (India) Private Limited (“the Company”) has formulated this policy to ensure a fair, transparent, and consistent approach in dealing with wilful defaulters. The primary objective of the policy is to provide for a non-discriminatory and transparent procedure, having regard to the principles of natural justice, for classifying a borrower as a wilful defaulter.

This policy is designed in line with RBI Master Direction on Treatment of Wilful Defaulters and Large Defaulters, RBI/DoR/2024-25/122 DoR.FIN.REC.No.31/20.16.003/2024-25 dated July 30, 2024.

2. Objectives

- To define “Wilful Default” in accordance with RBI guidelines.
- To establish a structured framework for identification, examination, and declaration of wilful defaulters.
- To ensure reporting of wilful defaulters to RBI/credit information companies.
- To implement penal measures for wilful defaulters and restrict further credit exposure.
- To safeguard the integrity of the lending process.

3. Definitions

1. **“Borrower”** means one who has availed credit facility from the Company.
2. **“Credit facility”** means any fund based or non-fund-based facility, including off balance sheet items like derivatives, guarantees and letters of credit, which the company has extended to the borrower
3. **“Director”** means the director of a company which was classified as a large defaulter/wilful defaulter and who was associated with the company at the time when the acts of omission or commission by the company/ its directors led to the default.
4. **“Diversion of funds”** means and includes the under- noted occurrences:
 - a. Utilization of short-term working capital funds for long-term purposes not in conformity with the terms of sanction of credit facility;
 - b. deploying funds availed using credit facility for the creation of assets other than those for which the credit was sanctioned.
 - c. Transferring funds availed using credit facility to the subsidiaries/group companies or other entities, by whatever modality, without approval of the lender/ all the lenders in the consortium.
 - d. Routing of funds through any lender other than the lender or members of consortium without prior written permission of the lender or all the lenders of consortium.
 - e. investing funds availed using credit facility in other companies/entities by way of acquiring equities/debt instruments without the approval of lender or all the lenders of consortium; and
 - f. Shortfall in the deployment of funds vis-à-vis the amounts disbursed/ drawn under the credit facility and the difference not being accounted for.

5. **“Guarantor”** is a person / entity who has guaranteed the credit facility
6. **“Large defaulter”** means a defaulter with an outstanding amount of ₹1 crore and above, and –
 - a. where suit has been filed; or
 - b. whose account has been classified as doubtful or loss (in accordance with the instructions issued by the Reserve Bank from time to time).
7. **“Promoter”** means a person who has been named as such in a prospectus or is identified by the company in the annual return, and has (i) control over the affairs of the company, directly or indirectly, whether as a shareholder, director or otherwise; and/or (ii) in accordance with whose advice, directions or instructions, the Board of Directors of the company is accustomed to act.
8. **“Siphoning of funds”** shall be construed to have occurred if any funds availed using credit facility from lenders are utilized for purposes unrelated to the operations of the borrower.

9. Wilful Default (As per RBI Guidelines)

A borrower shall be deemed to have committed wilful default if he/she/it:

- i. Deliberate Non-payment – Defaults in repayment obligations to the Company despite having capacity to pay.
- ii. Diversion of Funds – Utilizes borrowed funds for purposes other than those sanctioned.
- iii. Siphoning of Funds – Utilizes funds in a manner that cannot be traced to the sanctioned purpose and assets are not available in the borrower’s unit.
- iv. Disposal of Secured Assets – Disposes/removes secured assets without the lender’s knowledge/consent.
- v. Non-infusion of Equity – The borrower or the promoter has failed in its commitment to the company to infuse equity despite having the ability to infuse the equity, although the lender has provided loans or certain concessions to the borrower based on this commitment and other covenants and conditions.

A guarantor shall be deemed to have committed wilful default if the guarantor does not honor the guarantee when invoked by the lender, despite having sufficient means to make payment of the dues or has disposed of immovable or movable assets provided for the purpose of securing the credit facility, without the approval of the lender or has failed in commitment to the lender to infuse equity despite having the ability to infuse the equity, although the lender has provided loans or certain concessions to the borrower based on this commitment.

4. Scope & Applicability

This policy shall apply to all credit exposures (fund-based and non-fund-based) of the Company. The framework covers borrowers, guarantors, and promoter directors associated with the borrowing entity.

5. Governance Structure

5.1 Wilful Defaulter Identification Committee (WDIC)

Composition:

- Chief Risk Officer (Chairperson)
- Head – Credit/Business
- Head – Legal & Compliance

Role:

- Examine evidence of wilful default.
- Provide the borrower an opportunity to be heard.
- Record findings and recommend classification as wilful defaulter.

5.2 Review Committee**Composition:**

- Managing Director/CEO (Chairperson)
- Independent Director of the Board
- Senior Executive not part of WDIC

Role:

- Review WDIC recommendations
- Take final decision on classification as wilful defaulter

6. Criteria for Identification of Wilful Defaulters and Large Defaulters:

S.no	Norm / criteria	Interpretation
1	Applicability	Borrower, Co-borrowers and Guarantors
2	Exclusions	A director other than whole-time director, including an independent director/ nominee director, shall not be considered as wilful defaulter unless it is conclusively established that: the wilful default by the borrower or the guarantor has taken place with their consent or connivance or he/ she was aware of the fact of wilful default by the borrower or the guarantor, as revealed from the proceedings recorded in the minutes of the meeting of the Board or a Committee of the Board, but has not recorded his/ her objections to the same.
3	Loan level/ borrower level	Borrower level
4	Defaulter	NPA (90+ DPD)
5	If one loan is defaulting and others are performing	All non-performing borrower accounts with aggregate fund / non-fund outstanding of ₹25 lacs or more shall be considered.

7. Procedure for Declaration of Wilful Default

The identification of the wilful default should be made keeping in view the track record of the borrowers and should not be decided based on isolated transactions/ incidents. The default to be categorized as wilful must be intentional, deliberate, calculated and meeting the conditions defined under “Wilful Default”. Identification of wilful default will be solely at the discretion of the Company fulfilling the “criteria” mentioned above.

- (i) Cases observed as ‘wilful default’ in the preliminary screening along with its evidence will be examined by an Identification committee as defined above.
- (ii) The Identification Committee, if satisfied that an event of wilful default has occurred, will issue a show-cause notice to the borrower/ guarantor/ promoter/ director/ persons who are in charge and responsible for the management of the affairs of the entity and call for the submissions from them within 21 days of issuance of show cause notice. All materials and information on which show- cause notice is based shall be disclosed to them.
- (iii) After considering the submissions and where satisfied, the Identification Committee shall make a proposal to the Review Committee as defined above for classification as a wilful defaulter by explaining the reasons in writing.
- (iv) The borrower/ guarantor/ promoter/ director/ persons who are in charge and responsible for the management of the affairs of the entity is to be advised about the proposal to classify them as ‘wilful defaulter’ along with the reasons therefor.
- (v) An opportunity shall be provided to borrower/ guarantor/ promoter/ director/persons who are in charge and responsible for the management of the affairs of the entity for making a written representation to Review Committee within 15 days of such a proposal from the Identification Committee.
- (vi) The proposal of the Identification Committee along with the written representation received shall be considered by the Review Committee.
- (vii) The Review Committee shall provide an opportunity for a personal hearing also to the to the borrower/ guarantor/ promoter/ director/ persons who are in charge and responsible for the management of the affairs of the entity. However, if the opportunity is not availed or if the personal hearing is not attended by such persons mentioned above, the Review Committee shall, after assessing the facts or material on record, including written representation, if any, consider the proposal of the Identification Committee and take a decision and pass a reasoned order and the same shall be communicated to the wilful defaulter.
- (viii) Legal Team will issue the show cause notice and serve the written order on behalf of the Identification Committee and the Review Committee respectively. The show-cause notice and the order served shall clearly state that it has the approval of the competent authority, i.e., Identification/ Review Committee and shall identify its members. Measures against Wilful Defaulters.

8. Penal Measures

Once a borrower is declared a wilful defaulter:

8.1 No further funding: The company shall not grant any new facilities/additional facilities to a wilful defaulter or to an entity with which a wilful defaulter is associated. Existing facilities may be recalled.

8.2 No funding for new ventures: Further no additional funding would be done, for floating new ventures/to the new ventures floated by the borrower and companies (including their entrepreneurs, promoters, whole time directors etc. whose name were reported along with the entity in the wilful

defaulters list) where the Company has identified siphoning/diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions. This restriction for funding new ventures shall apply for a period of 5 years or as subsequently amended by the regulator from time to time, from the date of removal of their name from the list of wilful defaulters as published/disseminated by RBI/CICs/regulators as applicable.

8.3 Initiation of Criminal proceedings: Based on the facts and circumstances of each case, it can be examined whether initiation of criminal proceedings against wilful defaulters under the provisions of the applicable law, is warranted. In cases where criminal proceedings have been initiated, removal of the name of a wilful defaulter from the List of Wilful Defaulters (LWD) shall be without prejudice to the continuation of criminal proceedings against the wilful defaulter.

8.4 Incorporation of a Covenant: Loan agreements to include a covenant that

- i. a borrower would not induct a person on its Board or as a person in charge of and responsible for the management of the affairs of the entity, whose name appears in the list of wilful defaulters and if already appointed the borrower to take effective steps for removal of the said person from the board or being in charge of its management.
- ii. under no circumstances shall a renewal/ enhancement/ fresh credit facilities or restructuring of existing facilities be provided to such a borrower so long as the name of its promoter and/or the director (s) and/or the person in charge and responsible for the management of the affairs of the entity remains in the LWD.

8.5 Initiation of Legal Action: Legal Action, wherever warranted, shall be initiated expeditiously against the borrowers/ Guarantors for foreclosure or recovery of dues.

8.6 Associated Entities

- If the wilful defaulter is a company, another company will be deemed to be associated with it, if that company is –
 - a) a ‘subsidiary company’ as defined under clause 2 (87) of the Companies Act, 2013.
 - b) falls within the definition of a ‘joint venture’ or an ‘associate company’ under clause (6) of section 2 of the Companies Act, 2013.
- If the wilful defaulter is a natural person, all entities in which he is associated as promoter, or director, or as one in charge and responsible for the management of the affairs of the entity shall be deemed to be associated.
- The penal provisions mentioned above, shall cease to be applicable on the associated entities when they are no longer associated with the wilful defaulters.
- In cases where the existing promoters are replaced by new promoters in terms of directions contained in circular ‘Prudential Framework for Resolution of Stressed Assets’ dated June 7, 2019 (as amended from time to time) and the borrower company is totally delinked from such erstwhile promoters/ management, the Company may take a view on restructuring such accounts based on their viability, without prejudice to the continuance of criminal proceedings against the erstwhile promoters/ management.

9 Role of Internal Audit

- The internal auditors shall specifically look into the adherence to instructions for classifying a borrower as a wilful defaulter.
- The Audit Committee shall quarterly review the cases of wilful default and recommend steps to be taken to prevent such occurrences and their early detection should these occur. The review shall focus on identifying root causes of wilful default and addressing deficiencies, if

any, in the wilful defaulter classification process.

10 Liability of a Guarantor

- When a default happens in making payment/ repayment by the principal debtor, the Company can proceed against the guarantor even without exhausting the remedies against the principal debtor. Where a claim has been made on the guarantor on account of the default made by the principal debtor, the liability of the guarantor is immediate.
- In case the said guarantor refuses to comply with the demand made by the Company, such guarantor shall also be considered for classification as a wilful defaulter by following the mechanism as set out in point I.2.
- While dealing with the wilful default of a single borrowing company in a Group, the track record of the individual company, with reference to its repayment performance to its lenders shall be considered. In cases where guarantees furnished by the companies within the Group on behalf of the willfully defaulting units are not honoured when invoked by the Company, such Group companies should also be considered for classification as wilful defaulter by following the mechanism set out above.

9. Reporting of Wilful Defaulters and Large Defaulters

9.1 Reporting and Dissemination of Credit Information on Large Defaulters

- i. Information with respect to large defaulters shall be submitted to all credit information companies (CICs) at monthly intervals in the format provided in Annex 1
 - a) A list of suit filed accounts of large defaulters; and
 - b) A list of non-suit filed accounts of large defaulters whose account has been classified as doubtful or loss (in accordance with the instructions issued by the Reserve Bank from time to time).
- ii. For calculating the threshold of ₹1 crore, the unapplied interest, if any, shall also be included. In the case of suit-filed accounts, the threshold shall relate to the amount for which the suits have been filed.
- iii. The term 'suit filed accounts' shall mean those accounts in respect of which all entities regulated by Reserve Bank have approached courts or tribunals (including under Insolvency and Bankruptcy Code, 2016) for recovery of their dues, and proceedings are pending. Accounts shall be treated as suit filed if any application, appeal or execution is pending in continuation of the original recovery proceedings.
- iv. Suit filed accounts shall be deemed to include accounts in which SARFAESI proceedings or any other proceedings for recovery of the dues from the borrower or any other person liable to make payment of a debt under Acts governing co-operative societies are initiated and pending, and shall include the account of a debtor against whom resolution or liquidation proceedings have been initiated and are continuing.

9.2 Reporting and Dissemination of Credit Information on Wilful Defaulters

- i. Information with respect wilful defaulters as defined above that have been transferred shall be submitted at monthly intervals to all CICs
 - a) a list of wilful defaulters (LWD) in respect of suit filed accounts
 - b) a LWD in respect of non-suit filed accounts
- ii. The removal of the name of the wilful defaulter from the LWD shall be informed to all CICs promptly and not later than 30 days, from the date when the outstanding

amount falls below the threshold of ₹25 lakh or as notified by Reserve Bank of India from time to time.

9.3 Treatment of Compromised Settlements

- i. Any account included in LWD, where a compromised settlement is initiated with the borrower, shall be removed from the LWD only when the borrower has fully paid the compromise amount.
- ii. Till such time as only part payment is made, name of the borrower shall not be removed from the LWD even if the outstanding amount becomes less than the threshold of ₹25 lakh or as notified by Reserve Bank of India from time to time.
- iii. The compromise settlement shall be without prejudice to the continuation of criminal proceedings against the wilful defaulter.
- iv. OTS Procedures will be in line with the Corporate Legal Manual approved by the board.

9.4 Treatment of defaulted loans sold to the other lenders and ARCs

- i. Before transferring a defaulted loan with outstanding of ₹25 lakhs and above, irrespective of its classification as NPA, to other transferees, a comprehensive investigation shall be conducted internally from a wilful default perspective.
- ii. In a case where wilful default is observed, the process of classification of the borrower as wilful defaulter as per mechanism set out above, and report it in the LWD to CICs, before selling the asset to other lenders/ ARCs.
- iii. While transferring a Wilful default loan to a lender/ ARC the same is to be communicated to the Lender/ ARC to which the loan is being transferred.

9.5 Treatment of accounts where resolution is done under Insolvency and Bankruptcy Code (IBC)/ Resolution framework guidelines issued by the Reserve Bank

- i. In case an account which is included in LWD and has subsequently undergone liquidation or where the resolution [either under IBC or under the Prudential Framework for Resolution of Stressed Assets dated June 7, 2019 (as amended from time to time) issued by the Reserve Bank] results in a change in the management and control of the entity/ business enterprise, the name of such a borrower or guarantor who were classified as wilful defaulter [which includes in case of a company, its promoters and the director (s), and in case of entity (other than companies), persons who are in charge and responsible for the management of the affairs of the entity], shall be removed from the LWD after implementation of the resolution plan under IBC or aforesaid prudential framework.
- ii. The penal measures as detailed in point 1.2.3 shall not be applicable to such entities/ business enterprises after implementation of the resolution plan under IBC or aforesaid prudential framework.
- iii. The penal measures detailed in point 1.2.3 shall continue to apply to the erstwhile promoter(s)/ director(s)/ guarantor(s)/ persons who were in charge and responsible for the management of the affairs of the entity/ business enterprise, and to the entities they are associated as a promoter or director or as one in charge and responsible for its management.

9.6 Responsibility for Correct Reporting

The Company shall be responsible for reporting correct information and also ensuring the

accuracy of facts and figures to CICs of the particulars of the directors, and wherever possible, by cross-checking with the database maintained by the Registrar of Companies.

9.7 Reporting of Guarantors

The details of guarantors who have failed to honour the commitments thereunder when invoked, as large defaulters/ wilful defaulters, as the case may be, are to be reported to CICs. The details shall be reported as per regulatory requirements.

9.8 Reporting of Directors

- i. In case of business enterprises registered as companies under the Companies Act, 2013, the full names of the directors are also to be reported to facilitate better identity of persons concerned.
- ii. In order to ensure that directors are correctly identified and in no case, persons whose names appear to be similar to the names of directors appearing in the LWD are wrongfully denied credit facilities on such grounds, the Director Identification Number (DIN) is to be included as one of the fields in the data submitted to the CICs.

10. Preventive Measures and Role of Auditors

10.1 Preventive Measures

Credit Appraisal

- While carrying out the credit appraisal, it should be verified as to whether the name of any of the directors of a company/ guarantors/ persons in charge of the management of affairs of the entity appears in the list of large defaulters/ LWD by way of reference to DIN/ PAN, etc.
- In case of any doubt arising on account of identical names, independent sources shall be used for confirmation of the identity of directors rather than seeking a declaration from the borrowing company.

Monitoring End Use of Funds

- The end-use of funds is to be monitored and certificates from the borrowers are to be obtained certifying that the funds have been utilised for the purpose for which they were obtained. In case of the wrong certification by the borrowers, wherever necessary, initiation of appropriate legal proceedings, including criminal proceedings against the borrower can be considered.
- In cases of project financing, end use of funds should be ensured by, inter alia, obtaining certification from the Chartered Accountants for the said purpose.
- With a view to monitoring the end-use of funds, if any specific certification from the borrowers' auditors is desired regarding diversion/siphoning of funds by the borrowers, a separate mandate can be awarded to the auditors for the purpose. To facilitate such certification by the auditors, it shall be ensured that appropriate covenants in the loan agreements are incorporated to enable the award of such a mandate to the auditor.
- In addition to the above and with a view to preventing diversion/ siphoning of funds by the borrowers, engagement of own auditors for such specific certification can be done without relying on certification given by borrowers' auditor.

10.2 Role of Statutory Auditors

- In case any falsification of accounts on the part of the borrowers is observed and the auditors are found to be negligent or deficient in conducting the audit, lodging a formal complaint against the statutory auditors of the borrowers with the National Financial Reporting Authority (NFRA)/ Institute of Chartered Accountants of India (ICAI) can be considered to enable them to examine and fix accountability of the auditor.
- Pending disciplinary action by NFRA/ ICAI, the complaints shall be forwarded to the Reserve Bank (Department of Supervision, Central Office) and Indian Banks' Association (IBA). Before reporting to the Reserve Bank and IBA, the concerned auditors will be provided an opportunity to be heard. In this regard, normal procedures and processes shall be followed, which will be suitably recorded
- Depending upon the nature of the borrowers' acts underlying the wilful default and the quality of evidence available with the company in the normal course, the company shall consider commissioning a forensic audit of the affairs of the borrowers and their books of accounts, in respect of accounts with an outstanding of ₹5 Crores and above

10.3 Role of Third Parties

- As prescribed in para 4.2 of the Master Directions on Frauds Risk Management in Commercial Banks (including RRBs) and AIFIs/ UCBs, State Cooperative Banks, Central Cooperative Banks/ NBFCs (including Housing Finance Companies) dated July 15, 2024 (as updated from time to time), in case of wilful defaults also there should be some accountability for the third parties engaged by the Company, if they have played a vital role in credit sanction/ disbursement and are found negligent or deficient in their work or have facilitated the wilful default by the borrower.
- The Company shall forward the details of these third parties to the Indian Banks' Association (IBA) for records. Before reporting to IBA, the Company shall satisfy itself of the involvement of concerned third parties and provide them with an opportunity of being heard.

11. Borrower Rights & Fair Practices

- No borrower/guarantor shall be classified as wilful defaulter without being given due notice and opportunity to present their case.
- All proceedings shall be recorded and documented for transparency.

12. Policy Review

This policy shall be reviewed annually or earlier, if required by changes in regulatory guidelines. Any modifications shall be subject to approval of the Board of Directors.
