SONATA FINANCE PRIVATE LIMITED

Loan and Interest Rate Determination Policy

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V.1	10-02-2017
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V.3	30-05-2019
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1. Policy Overview:

1.1 Poverty and exclusion continue to dominate socio-economic and political discourse in India as they have done over the last six decades in the post-independence period. Poverty reduction has been an important goal of development policy since the inception of planning in India. Various anti-poverty, employment generation and basic services programmes have been in operation for decades in India. The ongoing reforms attach great importance to removal of poverty and to addressing the wide variations across states and the rural-urban divide. Though the Indian economy recorded impressive growth rates until recently, its impact has not fully percolated to the lowest deciles. Despite being one of the ten fastest growing economies of the world, India is still home to one-third of the world's poor. Further analysis shows that poverty is getting concentrated continuously in the poorer states.

1.2 Over the past five years, Reserve Bank of India, as also other policy makers have resolutely pursed the agenda of financial inclusion and achieved discernible progress in improving access to financial services for the masses. However, the progress is far from satisfactory as evidenced by the World Bank Findex Survey (2012). According to the survey findings, only 35%of Indian adults had access to a formal bank account and 8%borrowed formally in the last 12 months. Only 2% of adults used an account to receive money from a family member living in another area and 4% used an account to receive payment from the Government. The miniscule numbers suggest a need for a further push to the financial inclusion agenda to ensure that the people at the bottom of the pyramid join the formal financial system, reap benefits and improve their financial well-being (Source:Reserve Bank of India).

1.3 The present economic growth of our country is sustainable when primary sector growth picks up. Proper credit flow is required for planning such growth. Since the existing banking structure is not in a position to meet this demand, a quicker and effective outreach is possible through the NBFC-MFIs/Non-Government Organizations (NGOs)/ Self Help Promoting Institutes (SHPIs)/ Other FIswhich would be a better model to achieve the set goal. Hereafter, NBFC-MFIs/ Non-Government Organizations (NGOs)/ Self Help Promoting Institutes (SHPIs)/ Other Financial Institutions (FI) will be called MFI in the policy.

2. Objectives:

2.1 To increase lending under priority sector and directly/indirectly assist underprivileged segments particularly to Women through aggressive micro credit marketing as a part of Financial Inclusion.

2.2 The document addresses the genuine needs of micro credit of the existing & new Women clients and ensures quicker and prompt credit decision.

3. Scope:

3.1 The policy would govern all fund based term loan exposures to JLG, IL and Utility Loan.

3.2 The policy would also govern lending under Business Correspondent Model, Securitization and all other loan including housing loan, sanitization loan etc.

3.3 This Policy lays down the principals and procedures for determination of rate of interests to be charged from the clients, subject to the adherence of RBI circular's in this regard and also the policy be read in concurrence with the existing RBI guidelines, directives, circulars and instructions

3.4 Financial inclusion is gaining importance for promoting inclusive growth. This has created more opportunities for MFIs in rural/semi urban area especially for lending to allied agriculture and micro enterprises.

4. Regulatory Guidelines for Lending:

RBI has created a separate category of NBFCs viz. Non-Banking Financial Company Micro Finance Institutions (NBFC-MFIs). NBFC-MFIsshould be registered with RBI. RBI has stipulated regulatory guidelines/ compliance for NBFC-MFI,which are listed hereafter.

(i) not less than 85% of total assets of MFI (other than cash, balances with banks and financial institutions, government securities and money market instruments) are in the nature of "qualifying assets";

(ii) In addition, aggregate amount of loan, extended for income generating activity, is not less than 50%of the total loans given by MFIs;

(iii) The revised household income limit of the borrowers shall be Rs. 1,60,000 in rural areas and Rs. 2,00,000 in Semi urban and Urban areas, to classify the loan as eligible asset.

(iv) The maximum lending limit shall be Rs.125,000 for being classified as qualifying asset.

(v) The Sonata has to ensure that it comply with the following caps on margin and interest rate as also other 'pricing guidelines' as qualifying asset. The Details are as under:

- Margin cap, cap on the difference between the amount charged to the borrower and the cost of funds to the NBFC-MFI, shall not exceed 10 per cent for large MFIs (loans portfolios exceeding ₹ 100 Crore) and 12 per cent for the others.
- The interest rates charged by an NBFC-MFI to its borrowers shall be the lower of the following:
    a) The cost of funds plus margin as indicated in para (i) above; or
    b) The average base rate of the five largest commercial banks by assets multiplied by 2.75. The average of the base rates of the five largest commercial banks

shall be advised by the Bank on the last working day of the previous quarter, which shall determine interest rates for the ensuing quarter.

- NBFC-MFIs shall ensure that the average interest rate on loans sanctioned during a quarter does not exceed the average borrowing cost during the preceding quarter plus the margin, within the prescribed cap.
- The maximum variance permitted for individual loans between the minimum and maximum interest rate cannot exceed 4 per cent.
- The average interest paid on borrowings and charged by the MFI are to be calculated on average monthly balances of outstanding borrowings and loan portfolio respectively. The figures shall be certified annually by Statutory Auditors and also disclosed in the Balance Sheet.
- Only three components are to be included in pricing of loans viz., (a) a processing fee not exceeding 1% of the gross loan amount, (b) the interest charge and (c) the insurance premium.
- The processing fee is not to be included in the margin cap or the interest cap.
- Only the actual cost of insurance i.e. actual cost of group insurance for life, health and livestock for borrower and spouse can be recovered; (administrative charges may be recovered as per IRDA guidelines).
- There should not be any penalty for delayed payment.
- No Security Deposit/Margin are to be taken.
- Loan to be extended without collateral;
- Loan is repayable on weekly, fortnightly or monthly instalments at the choice of the borrower.

5. Credit Flow to Women Entrepreneurs- Procedure for Selection of Clients:

The process of accelerating credit to women for up-liftment and economic development shall be continued. While extending finance to Joint Liability Groups [JLGs]/ Individuals as beneficiaries, special attention and top priority is to be given to women beneficiaries. Following steps shall be taken in seriatim.

1: SELECTION OF POTENTIAL VILLAGE

- **Selection of potential village**
- **Identification & Motivation of poor women**
- **Identification & Classification of Poor households**
- **Asset verification**

2: CREATING & MAINTAINING CREDIT DISCIPLINE

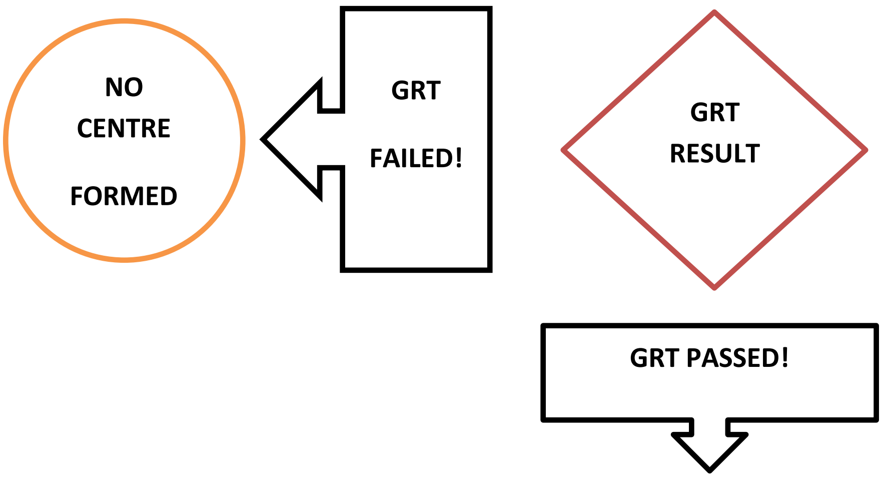
- **Group Formation**
  - ✓ **Village Profile & household survey**
  - ✓ **Introductory meeting**
  - ✓ **Group training**
  - ✓ **Group recognition test(GRT)**

3: CONTINUOUS GROUP TRAINING (CGT)

- **The objective of Continuous Group Training is to create a culture of credit discipline and to ensure a minimum understanding of the credit program amongst all clients**

4: RECOGNITION OF GROUPS

- **GRT are the final stage of quality control in our targeting of the poor. They are a check on the identification of poor households and on the quality client training under CGT. GRT can be carried out only by an authorized officer of the rank of BM or higher.**



5: FILLING OF LOAN PROPOSALS

- **Loan ticket size or loan decision is made through cash flow analysis.**
- **Credit Bureau check for all filled clients proposals prior to disbursal**
- **Confirmation/Acceptance of Loan proposals**

6: LOAN DISBURSEMENT

- **Loan disbursement to clients in one or two tranches.**

7: LOAN UTILIZATION CHECK

- **Once the loan is disbursed the client's loan utilization is checked**

8: LOAN REPAYMENT

Loan repayment to be weekly/fortnightly/monthly as per the convenience of the borrower

6. Areas of lending:

a. Priority areas of Lending:

Trade, Agriculture and Allied activities will continue to drive company's business growth. The Company shall also focus on services, professional and manufacturing sector.

b. Restricted areas of Lending: Lending towards any income generating activity where the par >= 90 days exceeds 3% of total outstanding of such activity.

c. Prohibited areas ofLending:

We do not provide loan for the below mentioned activities:

- Leather industry
- Tobacco, cigarettes and bidi making industry.
- Plastic Industries.
- Alcohol and beverages manufacturing and selling.
- Chemical, Aerosols and other toxic industries.
- Chemically harmful pesticides and insecticides.
- Any other environment hazardous industry.
- Activities barred by law.

d. BC Model:-

Sonata may become the Business Correspondent of banks and can engage itself in lending on service charge basis. The Management may decide the service fees to be taken from bank based on market scenario. In any case it should not be less than NIM(net interest margin) available to Sonata while lending to borrowers from owned funds.

e. Securitisation:-

Sonata can also engage itself in lending under securitisation provided unencumbered portfolio is available.

7. Multiple Lending/Indebtness:

1. As borrower of Sonata, one can be member of only one JLG or borrow as an individual. He /She can thus, borrow from us as a member of JLG or borrow in individual capacity. However, he/she cannot borrow from more than 2 MFI and one other financial institution
2. Recovery of loans given in violation of the regulatory norms shall be deferred till all the prior existing loans of the borrower are fully repaid.
3. The maximum debt of the borrower shall not exceed Rs. 125,000

8. Membership of Credit Information Company:

Sonata has to be a member of Credit Information Company (CIC) established under the Credit Information Company Regulation Act-2005, provide timely and accurate data to the CICs and use the data available with them to ensure compliance with the conditions regarding membership of SHG/JLG level of indebtedness and source of borrowings. While the quality and coverage of data with CICswill take some time to become robust, we may rely on self-certification from the borrowers and their own local enquiries on those aspects as well as annual house hold income. The Self Certification shall be restricted only in respect of KYC documents and all market inquiries will be done by the field staffs.

9. Provisioning Norms:

The provisioning norms pertaining to NBFC-MFIs have been covered RBI's Master Directions – Non-Banking Financial Company-Systemically Important Non-Deposit Taking Company Reserve Bank Directions 2016 bearing circular no. PD.008/03.10.119/2016-17 dated September 01, 2016.

(a) The aggregate loan provision to be maintained by MFI at any point of time shall not be less than the higher of a) 1%of the outstanding loan portfolio or b) 50% of aggregate loan installments which are overdue for more than 90 days and less than 180 days and 100%of the aggregate loan installments which are overdue for 180 days or more.

(b) Standard asset provisioning:

Every Systematically Important NBFC-MFI shall also make additional provisions for standard assets at 0.30 per cent by the end of March 2016; 0.35 per cent by the end of March 2017 and 0.40 per cent by the end of March 2018 and thereafter, of the outstanding, which shall not be reckoned for arriving at net NPAs. The provision towards standard assets need not be netted from gross advances but shall be shown separately as 'Contingent Provisions against Standard Assets' in the balance sheet.

10. Asset Classification Norms:

- Standard asset means 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;
- Non-performing asset means an asset for which, interest/principal payment has remained overdue for a period of 90 days or more.

Asset classifications and provisioning norms are mandatory for NBFC-MFI

11. INTEREST RATE

a. The rate of interest on Micro Loans shall be based on the cost of borrowed funds, matching tenor cost, refinance avenues, market liquidity, cost of capital required, cost of disbursements, RBI policies on credit flow, inherent credit and default risk in the products and customer per se arising from customer segment, profile of the customers, stability in earning and employment, future potential, group strength and value to lender group, past repayment track record of the customers, external ratings of the customers , industry trends, switchover options, canvassed accounts etc.

b. In case of Loans other than the Micro Finance Loans, the company may adopt discreet interest rate model whereby the rate of interest for same product and tenor availed during same period by customers would not be a standardized one but could be different for different customers depending upon consideration of any or combination of a few or all factors listed out above.

c. The annualized rate of interest would be intimated to the customer.

d. The interest rates may be offered on fixed, floating, variable basis.

e. Interest rates shall be intimated to the customers at the time of sanction/ availing of the loan and the equated instalments apportionment towards interest and principal dues shall be made available to the customer.

f. Interest changes would be prospective in effect and intimation of change of interest, if any, or other charges would be communicated to customers.

g. While designing the Interest Rate Model, all the above factors shall be taken into consideration.

12. REVIEW AND REVISION OF INTEREST RATES

The interest rate shall be reviewed periodically and suitable changes shall be made through office orders executed by the Managing Director in this regard.

13. PRICING OF CREDIT ON MICRO FINANCE LOANS

a) Margin cap, cap on the difference between the amount charged to the borrower and the cost of funds to the NBFC-MFI, shall not exceed 10 per cent for large MFIs (loans portfolios exceeding ₹ 100 crore) and 12 per cent for the others.

b) The interest rates charged by an NBFC-MFI to its borrowers shall be the lower of the following:
   - The cost of funds plus margin as indicated as indicated in para (i) above; or
   - The average base rate of the five largest commercial banks by assets multiplied by 2.75. The average of the base rates of the five largest commercial banks shall be advised by the Bank on the last working day of the previous quarter, which shall determine interest rates for the ensuing quarter.

c) NBFC-MFIs shall ensure that the average interest rate on loans sanctioned during a quarter does not exceed the average borrowing cost during the preceding quarter plus the margin, within the prescribed cap.

d) The maximum variance permitted for individual loans between the minimum and maximum interest rate cannot exceed 4 per cent.
e) The average interest paid on borrowings and charged by the MFIare to be calculated on average monthly balances of outstanding borrowings and loan portfolio respectively. The figures will be certified annually by Statutory Auditors and also disclosed in the Balance Sheet.

The above criteria is based on the RBI circulars issued in this regard from time to time and in case of any variance/ amendment in the RBI regulations, the same shall be read in accordance with the guidelines.

Operating Procedure :

On the first working day of the Quarter Interest rate shall be calculated in the format provided hereunder and shall be placed before the Financial Advisory and Asset Liability Management Committee for approval. Subsequently, an office Order shall be issued informing all concerned the rate of Interest for that Quarter. Information and Technology Department shall be simultaneously directed to update Website of the company with the latest Interest Rate as well update its master record file (s) with the latest Interest Rate so that the software for Loan Clients starts calculating Interest on Loans at the Interest Rate valid for the period. Such Interest shall be charged prospectively and not retrospectively, i.e. will not be applicable to previously disbursed loans.

Interest rate shall be calculated as per the following format :

Calculation of yield and cost of borrowings		
		(Rs. in crores)
(I)	Average portfolio (Period)	
(II)	Average borrowing (Period)	
(III)	Interest Income	
(IV)	Interest Expenses	
	Add. processing fee paid	
	Less: accrued interest on collateralised F.Ds (Pledge FD in BC, secuitisation, UIDAI, overdraft, unpledged)	
(V)	Net financial charges	
(VI)	Cost of borrowings V/II (annualized)	
(VII)	Interest cap III/I (Yield)	
(VIII)	NIM-(Yield-cost of borrowings) 7-6	

Pricing as per RBI new guidelines		
A.	Average base rate for Qtr ending _____ as informed by RBI	
B.	Interest rate cap-(A*2.75)	
C.	Cost of funds	
D.	Cost of funds plus margin permitted 10%	
	Company can charge rate of interest lower of B and D	

Since the rate of Interest to be charged from the clients is expected to change every quarter, the company shall, as soon as practicable, stop using pre-printed Interest Rate bearing stationery and instead the rate of interest charged column in loan documents shall be kept blank and the disbursement officer of the company shall fill the Interest Rate to be charged, manually.

14. PENAL INTEREST / LATE PAYMENT CHARGES

a) There shall be no penalty for any delay in repayment of Micro Finance Loan by the borrower to the company.
b) The Company shall not collect any Security Deposit/ Margin from the Micro Finance borrower.

However, the company may collect penal interest / late payment charges for any delay or default in making re-payments of any other loans apart from the Micro Finance Loans. These penal interest / late payment charges for different products or facilities would be decided by the Company from time to time. No claims for refund or waiver of such charges/ penal interest / additional interest would normally be entertained by the company and it is the sole discretion of the company to deal with such requests, if any

15. PROCESSING / DOCUMENTATION AND OTHER CHARGES

a. All processing / documentation and other charges recovered are expressly stated in the Loan documents.

b. Processing charges shall not be more than 1% of gross loan amount. Processing charges need not be included in the margin cap or the interest cap.

c. Service Tax and other applicable taxes shall be charged as per the guidelines issued by the Government from time to time.

The Company shall recover only the actual cost of insurance for group, or livestock, life, health for borrower and spouse. Administrative charges where recovered, shall be as per IRDA guidelines.

However, in case of borrowers other than the Micro Finance Borrowers the processing/ documentation charges may vary based on the loan product, geographical location, market competitors and their practices, customer segment and generally represent the cost incurred in rendering the services to the customers.

16. Exposure Limits:

The Company has in place duly approved General Risk Management policy wherein to avoid concentration risk exposure limit have been fixed for difference segments as under:

Indicators	**Limits**
Geographical Concentration	
Portfolio per State	<=50% (Should gradually reduce to 45% over the period of 2 years i.e. by March, 21)
Portfolio per District	<=8%
Portfolio per Branch	<=Rs.15 crores
Line of Business/Product Concentration	
Income Generation Loan	>=75%
Non- Income Generation Loan	<=25%

Managed Loan Portfolio, Securitisation and BC Model Partnership (all combined)	<=40%
Exposures	
% of exposure to single borrower	<=10 Lacs (here employees should not be included in the definition of borrower)
% of exposure to group/centre borrower	<=0.05% of the total portfolio

17. Formation of Self-Regulatory Organization:

NBFC-MFIs will have to become member of at least one Self-Regulatory Organization (SRO)which is recognized by RBI and will also have to comply with the code of conduct prescribed by SRO.

Accordingly Sonata has become the member of M-fin and Sa-dhan at national level and with UPMA at state level.

18. Compliance:

All the functional divisions are expected to comply with the policy guidelines laid down in this document. In case of any doubt about the applicability of any aspect of this policy to any situation, clarification/ approval shall first be sought from Head Office.

19. Modification and Review/Revision:

The policy shall be modified to give effect to the changes in the extant guidelines/directives/instructions that may be advised by the Reserve Bank of India/Government of India from time to timeandreporting and ratification/approval of the Board. The Policy shall also be reviewed/ revised from time to time to adapt to the changing environmental demands and to incorporate and implement any changes in the micro credit strategy of the Bank, with the approval of the Board.

20. Fair practice Code:

All elements of the Fair Practice Codes issued by the RBI vide DNBS.PD.CC.No.286/03.10.04212012·13 dated July 2, 2012 as amended from time to time will need to be adhered by the MFI. MFI must also ensure that greater resources are devoted to professional inputs information of JLG/IL and appropriate training and skill development activities for capacity building and empowerment after formation of the groups.

21. Fair Practice in Lending by Sonata:

1. **Transparency in Interest Rates:**

a. There shall be only three components in the pricing of the loan viz., the interest charge, processing charge and the insurance premium' (which includes the administrative chargesin respect thereof).

b. There will be no penalty charged on delayed payment.

c. MFIs shall not collect any Security Deposit/Margin from the borrower.

d. There should be a standard form of loan agreement.

e. Every MFIshould provide to the borrower a loan card reflecting

- the effective rate of interest charged
- all other terms and conditions attached to the loan
- information which adequately identifies the borrower and
- acknowledgements by the MFIof all repayments including installments received and the final discharge.
- All entries in the Loan Card should be in the vernacular language.

f. The effective rate of interest charged by the MFI should be prominently displayed in all its offices and in the literature issued by it and on its website.

2. **Multiple-lending, Over-borrowing and Ghost-borrowers:**

a) MFIs can lend to individual borrowers who are not member of Joint Liability Group(JLG) or to borrowers that are members of JLG.

b) b. A borrower cannot be a member of more than one JLG.

a. Not more than two MFIs and maximum one other financial institution should lend to the same borrower. However, the maximum indebtedness shall not exceed Rs. 125,000

b. There must be a minimum period of moratorium between the grant of the loan and the due date of the repayment of the first instalment. The moratorium shall not be less than the frequency of repayment e.g. in the case of weekly repayment, the moratorium shall not be less than one week.

c. Recovery of loan given in violation of the regulations should be deferred till all prior existing loans are fully repaid. All sanctioning and disbursement of loans should be done only at a centrallocation and more than one individual should be involved in this function. Inaddition, there should be close supervision of the disbursement function.

3. **Non- Coercive Methods of Recovery:**

a. NBFC-MFIs shall ensure that a Code of Conduct and systems are in place for recruitment, training and supervision of field staff. The Code of Conduct should also incorporate the

Guidelines on Fair Practices Code issued for NBFCsby RBI vide circular CCNo.80 dated September 28, 2006 as amended from time to time.

b. Recovery should normally be made only at a central designated place. Field staff shall be allowed to make recovery at the place of residence or work of the borrower only if borrower fails to appear at central designated place on two or more successive occasions.

c. All other elements of the Fair Practices Code issued for NBFCs vide CCNo. 80 dated September 28, 2006 as amended from time to time shall be adhered to by NBFCMFIs.

4. **Improvement of Efficiency:**

Sonata shall review their back office operations and make the necessary investments in Information Technology and systems to achieve better control, simplify procedures and reduce costs.

22. Monitoring and Control:

The responsibility for compliance to all regulations prescribed for NBFC MFIslies primarily with the vertical Heads and all controlling offices and branches. The Industry associations/ SROs will also play a key role in ensuring compliance with the regulatory framework.

The SRO formulates specific operational guidelines for member organisation for its implementation and monitors the same based on the various monthly, quarterly & annual returns submitted by the MFIs.

23. Appraisal standards:

1. Sonata has in place a well-defined framework for approving loan limits of different segments. Requests for credit facilities from the prospective beneficiaries shall be on the prescribed format and the full-fledged proposal should be prepared for submission to the competent authority for sanction. Each loan proposal should have cash flow analysis.
2. Presentation of credit proposals shall be done in the prescribed appraisal formats and all the modalities including those mentioned in this policy are to be adhered as per the system in vogue.
3. Proposal should clearly indicate the need-based requirement of the MFI borrower for finance and the rationale for recommendations.

24. Credit Administration:

1. Time norms for disposal of credit proposals and credit refusal to be adhered to:

- For JLG around 7 days
- For other 10 days.

2. The Company shall comply with the guidelines relating to issue of acknowledgement for receipt of proposals and time norms for processing and disposal.

25. Documentation:

25.1 Documents required for lending of Joint Liability Group (JLG) Loans are:

- Loan Application Form.
- KYC
- Demand promissory Note.
- Repayment Schedule Sheet
- Checklist

25.2 The various Documents required for lending of Individual Loans are stipulated hereunder:

- Two Joint Photographs (Client and Spouse)
- Check List
- Loan Application
- Appraisal Sheet
- Guarantor form
- Notary
- Demand Promissory Loan.
- Ins. Receipt
- Repayment Schedule Sheet
- Post Dated Check receiving Sheet
- Client And Guarantor KYC
- Bank Statement.
- Post Dated Cheques (PDC's)

26. Credit Risk

The Company already has Risk Management Policy approved by the Board outlining the entire gamut of risks perceived and their mitigates. Although credit risk is also part of risk management function, only certain functions attributed to credit standards are highlighted in this policy.

27. Delegation of Powers:

Delegated Authority	Authority vested for Advances to IL/JLG
Branch Manager	100,000 (JLG) 35,000 (IL)
Credit Committee at Branch (Hub-In-charge, Branch Manager and Credit Manager)	35,001 – 60,000 (IL)
Credit Committee (DO)	60,001 - 1,00,000 (IL)
Credit Committee (HO)	Upto 5,00,000 (MEL)

Any deviation in the norms is to be approved by Hub In charge for loans falling within the delegation at Branch level.

Delegates will exercise their delegation as per their respective loaning power. No delegated power will be vested at Branch level in regards to advance to IL and others.

28. General

a. Staff should refrain from interference in the affairs of the borrower except for the purposes provided in the terms and conditions of the loan agreement.

b. In case of receipt of request from the borrower for transfer of borrower account, the same may be considered on its merit.

c. In the matter of recovery of loans, the branches should not resort to undue harassment viz. persistently bothering the borrowers at odd hours, use of muscle power for recovery of loans etc. As complaints from customers also include rude behavior from the staff of the companies. we shall ensure that the staff are adequately trained to deal with the customers in an appropriate manner.

d. At the operational level, all branches have to display the name and contact details (Telephone / Mobile nos. as also email address) of the Grievance Redressal Officer who can be approached by the public for resolution of complaints against the Company and also Tol free Numbers, for the benefit of their customers, at their branches / places where business is transacted.

e. The Fair Practice code duly approved by the Board should be put up on their web-site, if any, for the information of various stakeholders.

f. Company should engage themselves in capacity building and empowerment of the groups to the desired extent. The Sonata should not disburse loans to the newly formed groups immediately after their formation but disburse only after nurturing and handholding them so as cohesiveness and a sense of purpose are being built up in the groups formed by the MFIs.

g. The company would ensure that stipulations with regard to lending activities are adhered that no loans/advances shall be granted to those borrowers who are on the existing defaulters list of CIBIL/Highmark/Equifax.

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