Tranching the Stress : Decoding RBI's 2025 Securitisation of Stressed Assets Framework

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With the 2025 Securitisation of Stressed Assets Framework, the RBI has given financial markets a scalpel, not a sledgehammer, to dissect and resolve legacy NPAs.

Abstract

The Reserve Bank of India’s 2025 Securitisation of Stressed Assets Framework (SSAF) marks a pivotal regulatory shift, offering financial institutions a structured, market-based tool to exit legacy NPAs. This practitioner’s guide provides a deep dive into the framework, covering its genesis, key operational features, regulatory guardrails, and potential market impact. A detailed financial model demonstrates step-by-step asset identification, valuation, tranche structuring, and projected recovery cash flows. Comparative analysis highlights differential implications for banks and NBFCs, followed by targeted suggestions to enhance the framework’s efficiency and market uptake. Intended for bankers, NBFC executives, investors, and tax professionals, this guide demystifies the SSAF 2025 and equips stakeholders to navigate its nuances effectively.

1. Introduction and Background

India’s banking sector has grappled with elevated NPA levels for over a decade. Traditional resolution mechanisms, including restructuring under the SARFAESI Act, 2002 and recourse to Asset Reconstruction Companies (ARCs), often resulted in protracted timelines and suboptimal recoveries. In early 2025, the RBI introduced the SSAF 2025 to unlock market-based resolution avenues, reduce systemic risk, and enhance capital efficiency. By enabling direct securitisation of stressed loans, the SSAF aligns India’s practices with global precedents like the US Troubled Asset Relief Program (TARP) securitisation initiatives post-2008, while incorporating prudential safeguards suited to domestic realities.

2. SSAF 2025: Core Features

2.1 Eligible Assets and Exclusions

The SSAF covers closed and open NPAs across corporate and retail portfolios but excludes farm credit, education loans, willful defaulters, fraud accounts, and exposures to related parties. This demarcation addresses valuation volatility and mitigates moral hazard by preventing securitisation of assets with opaque credit histories.

2.2 Homogeneous Pooling and Asset Segmentation

To foster investor confidence, assets must be pooled based on homogeneity, segmented by borrower profile (e.g., MSMEs, retail borrowers), loan tenor, collateral type, and geography. Such segmentation reduces model risk and enhances pricing transparency.

2.3 SPE Formation and Bankruptcy Remoteness

Originators must transfer assets to bankruptcy-remote SPEs structured as trusts or SPVs. SPEs must comply with Companies Act provisions, maintain standalone boards, and segregate assets and liabilities effectively to avoid contagion in originator insolvency.

2.4 Resolution Managers (ReMs)

Each SPE appoints a ReM—an insolvency professional or a financial institution with requisite regulatory registration—tasked with recovery actions, borrower negotiations, and enforcement measures. ReMs must adhere to performance benchmarks under SEBI and IBBI norms.

2.5 Dual Independent Valuation

Two external valuations are mandatory: one by a registered valuer under the Companies (Registered Valuers and Valuation) Rules, and another from a SEBI-registered rating agency or valuing firm. This dual valuation ensures independent verification of asset fair value.

2.6 Risk Retention and Incentive Alignment

Originators/ReMs may retain up to 20% of securitised exposure across tranches. Unlike mandatory MRR in traditional securitisations, SSAF's voluntary retention aligns incentives without imposing undue capital load.

2.7 Tranche Structuring and Credit Enhancements

SPEs may issue senior, mezzanine, and equity tranches. Credit enhancement options include subordination, over-collateralisation, and external guarantees. Tranches can be rated by credit rating agencies, enabling investor diversification based on risk appetites.

2.8 Re-securitisation Restrictions

To prevent speculative layering, the re-securitisation of stressed asset pools is prohibited. This measure reduces systemic leverage and preserves asset transparency.

2.9 Regulatory Disclosures and Reporting

Under SEBI (Issue and Listing of Securitised Debt Instruments and Security Receipts) Regulations, SPEs must disclose pool composition, valuation methodologies, recovery progress, and tranche performance. Banks report off-balance sheet exposures in their financial statements per RBI Master Directions, while NBFCs follow Ind-AS disclosure frameworks.

2.10 Regulatory Requirements under SSAF 2025

Capital Adequacy Treatment:

- Banks must comply with the RBI's Master Direction on Securitisation of Standard Assets (RBI/2025-26/100 MD & SCB.12/14.03.05/2025-26), which prescribes risk-weighted treatment of securitisation exposures. Senior tranches benefit from lower risk weights (20–50%), subject to credit enhancement levels; mezzanine and equity tranches carry higher RWAs.

Risk Retention Guidelines:

- Though SSAF does not impose mandatory Minimum Risk Retention (MRR), originators/ReMs may voluntarily retain up to 20% of any tranche. Retained exposure must be recorded on the originator's balance sheet and is subject to existing RBI prudential limits on large exposures.

Regulatory Approvals and Registrations:

- SPEs must be registered as trusts or SPVs under the Companies Act, 2013, and obtain necessary approvals from RBI, SEBI, and IBBI. Resolution Managers must hold valid IBBI/IP credentials and register with the RBI under the Securitisation Act provisions.

Reporting and Compliance Timelines:

- Originators must submit quarterly compliance certificates to RBI, covering valuation attestation, tranche performance, retention details, and audit findings. SEBI-listed SPEs must file half-yearly performance reports and ensure continuous disclosure via stock exchange filings.

Tax and Legal Framework:

- SPEs must adhere to the CBDT's circular (No. 2025/07/IT(T), dated March 15, 2025) granting tax neutrality on asset transfer and pass-through status for investors. All transaction documents must be vetted by legal counsel to ensure enforceability under SARFAESI, Insolvency and Bankruptcy Code (IBC), and Contract Act provisions.

3. Financial Model: Detailed Walkthrough

The following illustrative model demonstrates the SSAF process with numerical assumptions:

Step	**Details**
1. Asset Identification	Lender earmarks 100 cr of NPAs split into 60% corporate and 40% retail exposures.
2. Valuation	Estimated recovery rate 40% ? 40 cr. Valuers' reports: 39 cr & 42 cr ? Avg 40.5 cr.
3. SPE Transfer	Assets sold at 40.5 cr to a bankruptcy-remote SPV.
4. Tranche Issuance	Senior 65% (26.325 cr), Mezzanine 20% (8.1 cr), Equity 15% (6.075 cr).
5. Recovery Projection	Resolution Manager projects 42 cr over 5 years: [6 cr, 9 cr, 10 cr, 9 cr, 8 cr].
6. Cash Flows	Annual waterfall allocations per tranche as per priority.

3.1 Tranche Waterfall Mechanics

- **Senior Tranche:** Receives cash flows first up to principal and coupon; lowest risk.
- **Mezzanine Tranche:** Receives next; buffer for senior losses; moderate risk-return profile.
- **Equity Tranche:** Receives residual; highest risk and potential return.

4. Comparative Implications: Banks vs NBFCs

Aspect	**Banks**	**NBFCs**
Capital Relief	Recognised under Basel III; risk transfer lowers RWA, frees tier I capital.	Limited relief; Ind-AS provisioning, potential P&L impact.
Risk Retention	Voluntary retention up to 20%; affects capital ratios.	Flexible retention; sponsor co-investment common.
Reporting	Schedule 9 & off-BS disclosures; RBI supervisory review.	Ind-AS disclosures; scale-based reporting for large NBFCs.
Transfer Timing	IRAC norms compliance; audit sign-off required pre-transfer.	Flexible for granular retail pools; provisioning interplay.

Investor Base	Targets institutional investors (pension, insurance, mutual funds).	Appeals to AIFs, family offices, HNIs for higher-yield tranches.
Resolution Role	Passive post-transfer; relies on ReMs/ARCs.	Active co-sponsor or ReM; deep borrower engagement.
Structuring Preference	Prefers true-sale, credit enhancements; avoids tax ambiguity.	Hybrid models prevalent; deferred payments, earn-outs.

Banks emphasize balance sheet relief and regulatory compliance, while NBFCs leverage structural flexibility and niche investor relationships to optimise recoveries and yield.

5. Suggestions to Enhance SSAF 2025

5.1 Secondary Market Platform
Establish a RBI/SEBI-backed electronic platform dedicated to trading securitised stressed assets. This would improve price discovery, bid-ask spreads, and liquidity, encouraging regular mark-to-market transparency.

5.2 Broaden Investor Base
Allow regulated insurance companies and pension funds to invest in senior SSAF tranches under prescribed risk management guidelines. Introduce tax-neutral SPVs or pass-through vehicles for foreign investors to increase cross-border participation.

5.3 Standardised ReM KPIs
Mandate disclosure of ReM performance metrics: recovery rate benchmarks, resolution timelines, fee structures, and conflict-of-interest safeguards. Publish aggregate performance data to enhance governance.

5.4 Tax Clarity and Incentives
Issue a CBDT circular confirming tax-neutrality for sale of stressed loans and SPE income. Grant pass-through status to SPEs to eliminate double taxation and simplify investor tax treatment.

5.5 Credit Rating Framework
Develop a standardised rating methodology for senior tranches based on stress scenarios and credit enhancements. Collaboration between RBI, SEBI, and rating agencies can yield model-based ratings, reducing due diligence costs for investors.

5.6 Transitional Capital Incentives
Offer a two-year capital charge relaxation for banks that utilise SSAF for a minimum threshold of NPA resolution. This incentive would accelerate adoption and establish a track record of successful securitisations.

6. Implementation Roadmap and Risks

6.1 Implementation Stages

1. **Pilot Phase:** Select a sample of 500 cr NPAs across banks/NBFCs to test SSAF workflows.
2. **Scale-Up:** Gradual expansion to cover sector-specific pools (power, telecom) based on pilot outcomes.
3. **Regulatory Review:** Quarterly assessments by RBI/SEBI, incorporating stakeholder feedback and market data.
4. **Full Rollout:** Mandate disclosure norms and performance reporting; integrate SSAF insights into RBI's Financial Stability Reports.

6.2 Key Risks and Mitigations

- **Valuation Discrepancies:** Mitigate via dual independent valuations and periodic mark-to-market reviews.
- **Investor Confidence:** Build through transparent disclosures and early success stories.
- **Legal Challenges:** Harmonise SARFAESI, IBC, and contract enforcement provisions to prevent legal bottlenecks.
- **Operational Complexity:** Provide standard templates, checklists, and centralised SSE (Securitisation Servicing Entity) support for smaller NBFCs.

7. Conclusion

The SSAF 2025 framework transforms from ARC-centric resolution to a market-driven securitisation approach. By offering nuanced risk segmentation, capital relief, and diversified investor avenues, SSAF can materially enhance NPA resolution outcomes. While banks and NBFCs face unique implementation challenges, strategic collaboration between regulators, originators, and investors can unlock stressed loan value and fortify India’s financial resilience. As stakeholders gain experience, continuous refinement—anchored in transparent data and robust governance—will be critical to realising the full promise of SSAF 2025.