Master Circular – Housing Finance

A. Purpose
To consolidate framework of rules/regulations and clarification on Housing Finance issued by Reserve Bank of India from time to time.
B. Classification
A statutory directive issued by the Reserve Bank in exercise of the powers conferred by Sections 21 and 35 A of the Banking Regulation Act, 1949.
C. Previous instructions consolidated
This Master Circular consolidates and updates all the instructions contained in Circulars listed in the appendix and clarifications issued during the year.
D. Scope of Application
Applicable to all Scheduled Commercial Banks, excluding Regional Rural Banks.

1. INTRODUCTION

Banks, with their vast branch network throughout the length and breadth of the country, occupy a very strategic position in the financial system and have an important role to play in providing credit to the housing sector.

Keeping in view the objectives of the National Housing Finance Policy of the Central Government, RBI had introduced a scheme of Housing Finance Allocation wherein every year, banks were required to achieve the prescribed target of 'Housing Finance' announced annually. The banks could deploy their funds under the housing finance allocation in any of the three categories, viz. direct finance, indirect finance, or investment in bonds of NHB/HUDCO, or combination thereof.

The allocation under the scheme was last announced for the year 2002-2003 and the scheme has since been discontinued.

Presently, banks have the freedom to evolve their own guidelines on various aspects of granting housing finance with the approval of their Boards.

2. VARIOUS REGULATIONS

While formulating their policies, banks have to take into account the following RBI guidelines and ensure that bank credit is used for production, constructions activities and not for activities connected with speculation in real estate.

(a) ACQUISITION OF LAND

Bank finance granted only for purchase of a plot, provided a declaration is obtained from the borrower that he intends to construct a house on the said plot, with the help of bank finance or otherwise, within such period as may be laid down by the banks themselves.

(b) CONSTRUCTION OF BUILDING / READY-BUILT HOUSE

(i) Banks may grant loans to individuals for purchase/construction of dwelling unit per family and loans given for repairs to the damaged dwelling units of families.

(ii) Bank may extend finance to a person who already owns a house in town/village where he resides, for buying/ constructing a second house in the same or other town/ village for the purpose of self occupation.

(iii) Bank may extend finance for purchase of a house by a borrower who proposes to let it out on rental basis on account of his posting outside the headquarters or because he has been provided accommodation by his employer.

(iv) Bank may extend finance to a person who proposes to buy an old house where he is presently residing as a tenant.

(v) Banks may finance for construction meant for improving the conditions in slum areas for which credit may be extended directly to the slum-dwellers on the guarantee of the Government, or indirectly to them through the State Governments.

(vi) Bank may provide credit for slum improvement schemes to be implemented by Slum Clearance Boards and other public agencies.

(vii) Banks are advised to also adhere to the following conditions, in the light of the observations of Delhi High Court on unauthorized construction:

(a) In cases where the applicant owns a plot/land and approaches the banks/FIs for a credit facility to construct a house, a copy of the sanctioned plan by competent authority in the name of a person applying for such credit facility must be obtained by the Banks/FIs before sanctioning the home loan.

(b) An affidavit-cum-undertaking must be obtained from the person applying for such credit facility that he shall not violate the sanctioned plan, construction shall be strictly as per the sanctioned plan and it shall be the sole responsibility of the executants to obtain completion certificate within 3 months of completion of construction, failing which the bank shall have the power and the authority to recall the entire loan with interest, costs and other usual bank charges.

(c) An Architect appointed by the bank must also certify at various stages of construction of building that the construction of the building is strictly as per sanctioned plan and shall also certify at a particular point of time that the completion certificate of the building issued by the competent authority has been obtained.

(d) In cases where the applicant approaches the bank/FIs for a credit facility to purchase the built up house/flat, it should be mandatory for him to declare by way of an affidavit-cum-undertaking that the built up property has been constructed as per the sanctioned plan and/or building bye-laws and as far as possible has a completion certificate also.

(e) An Architect appointed by the bank must also certify before disbursement of the loan that the built up property is strictly as per sanctioned plan and/or building bye-laws.

(f) No loan should be given in respect of those properties which fall in the category of unauthorized colonies unless and until they have been regularized and development and other charges paid.

(g) No loan should also be given in respect of properties meant for residential use but which the applicant intends to use for commercial purposes and declares so while applying for loan.

(viii) **Supplementary Finance**

(a) Banks may consider requests for additional finance within the overall ceiling for carrying out alterations/ additions/repairs to the house/flat already financed by them.

(b) In the case of individuals who might have raised funds for construction/ acquisition of accommodation from other sources and need supplementary finance, banks may extend such finance after obtaining *paripassu* or second mortgage charge over the property mortgaged in favour of other lenders and/or against such other security, as they may deem appropriate.

(c) Banks may consider for grant of finance to –
(i) the bodies constituted for undertaking repairs to houses, and

(ii) the owners of building/house/flat, whether occupied by themselves or by tenants, to meet the need-based requirements for their repairs/additions, after satisfying themselves regarding the estimated cost (for which requisite certificate should be obtained from an Engineer / Architect, wherever necessary) and obtaining such security as deemed appropriate.

(ix) **Bank finance should, however, not be granted for the following:**
(a) Banks should not grant finance for construction of buildings meant purely for Government/Semi-Government offices, including Municipal and Panchayat offices. However, banks may grant loans for activities, which will be refinanced by institutions like NABARD.

(b) Projects undertaken by public sector entities which are not corporate bodies (i.e. public sector undertakings which are not registered under Companies Act or which are not Corporations established under the relevant statute) may not be financed by banks. Even in respect of projects undertaken by corporate bodies, as defined above, banks should satisfy themselves that the project is run on commercial lines and that bank finance is not in lieu of or to substitute budgetary resources envisaged for the project. The loan could, however, supplement budgetary resources if such supplementing was contemplated in the project design. Thus, in the case of a housing project, where the project is run on commercial lines, and the Government is interested in promoting the project either for the benefit of the weaker sections of the society or otherwise, and a part of the project cost is met by the Government through subsidies made available and/or contributions to the capital of the institutions taking up the project, the bank finance should be restricted to an amount arrived at after reducing from the total project cost the amount of subsidy/capital contribution receivable from the Government and any other resources proposed to be made available by the Government.

(c) Banks had, in the past, sanctioned term loans to Corporations set up by Government like State Police Housing Corporation, for construction of residential quarters for allotment to employees where the loans were envisaged to be repaid out of budgetary allocations. As these projects cannot be considered to be run on commercial lines, it would not be in order for banks to grant loans to such projects.

(C) LENDING TO HOUSING INTERMEDIARY AGENCIES
(i) Financing of Land Acquisition
(a) In view of the need to increase the availability of land and house sites for increasing the housing stock in the country, banks may extend finance to public agencies and not private builders for acquisition and development of land, provided it is a part of the complete project, including development of infrastructure such as water systems, drainage, roads, provision of electricity, etc. Such credit may be extended by way of term loans. The project should be completed as early as possible and, in any case, within three years, so as to ensure quick re-cycling of bank funds for optimum results. If the project covers construction of houses, credit extended therefore in respect of individual beneficiaries should be on the same terms and conditions as stipulated for financing the beneficiary directly.
(b) Banks should have a Board approved policy in place for valuation of properties including collaterals accepted for their exposures and that valuation should be done by professionally qualified independent valuers.

(c) As regards the valuation of land for the purpose of financing of land acquisition as also land secured as collateral, banks may be guided as under:

(i) Banks may extend finance to public agencies and not to private builders for acquisition and development of land, provided it is a part of the complete project, including development of infrastructure such as water systems, drainage, roads, provision of electricity, etc. In such limited cases where land acquisition can be financed, the finance is to be limited to the acquisition price (current price) plus development cost. The valuation of such land as prime security should be limited to the current market price.

(ii) Wherever land is accepted as collateral, valuation of such land should be at the current market price only.

(ii) Lending to Housing Finance Institutions

Banks may grant term loans to housing finance institutions taking into account (long-term) debt-equity ratio, track record, recovery performance and other relevant factors including the other applicable regulatory guidelines.

(iii) Lending to Housing Boards and Other Agencies

Banks may extend term loans to state level housing boards and other public agencies. However, in order to develop a healthy housing finance system, while doing so, the banks must not only keep in view the past performance of these agencies in the matter of recovery from the beneficiaries but they should also stipulate that the Boards will ensure prompt and regular recovery of loan installments from the beneficiaries.

(iv) Term Loans to Private Builders

(a) In view of the important role played by professional builders as providers of construction services in the housing field, especially where land is acquired and developed by State Housing Boards and other public agencies, commercial banks may extend credit to private builders on commercial terms by way of loans linked to each specific project.

(b) Banks however, are not permitted to extend fund based or non-fund based facilities to private builders for acquisition of land even as part of a housing project.

(c) The period of credit for loans extended by banks to private builders may be decided by banks themselves based on their commercial judgment subject to usual safeguards and after obtaining such security, as banks may deem appropriate.

(d) Such credit may be extended to builders of repute, employing professionally qualified personnel. It should be ensured, through close monitoring, that no part of such funds is used for any speculation in land.

(e) Care should also be taken to see that prices charged from the ultimate beneficiaries do not include any speculative element, that is, prices should be based only on the documented price of land, the actual cost of construction and a reasonable profit margin.

(v) Terms and Conditions for Lending to Housing Intermediary Agencies

(a) In order to enhance the flow of resources to housing sector, term loans may be granted by banks to housing intermediary agencies against the direct loans sanctioned/ proposed to be sanctioned by the latter, irrespective of the per borrower size of the loan extended by these agencies.

(b) Banks can grant term loans to housing intermediary agencies against the direct loans sanctioned/proposed to be sanctioned by them to Non-Resident Indians also. However, banks should ensure that housing finance intermediary agencies being financed by them are authorised by RBI to grant housing loans to NRIs as all housing finance intermediaries are not authorised by RBI to provide housing finance to NRIs.

(c) Banks have freedom to charge interest rates to housing intermediary agencies without reference to Benchmark Prime Lending Rates (BPLR) upto June 30, 2010. Under the Base Rate System effective from July 1, 2010, all categories of loans will be priced with reference to Base Rate which is the minimum interest rate for all loans.

(vi) Adherence to guidelines on Commercial Real Estate (CRE) exposure

Lending to housing intermediary agencies will be subject to the guidelines on commercial real estate exposure.

3. QUANTUM OF LOAN

(a) While deciding the quantum of loan to be granted as housing finance, banks should ensure that the LTV ratio for loans is as under:

Category of Loan	LTV Ratio (%)
(a) Individual Housing Loans	
Upto ` 20 lakh	90
Above ` 20 lakh & upto ` 75 lakh	80
Above ` 75 lakh	75
(b) CRE – RH	NA

(b) In order to have uniformity in the practices adopted for deciding the value of the house property while sanctioning housing loans, banks should not include stamp duty, registration and other documentation charges in the cost of the housing property they finance so that the effectiveness of LTV norms is not diluted.
(c) However, in cases where the cost of the house/dwelling units does not exceed Rs.10 lakh, bank may add stamp duty, registration and other documentation charges to the cost of the house/dwelling unit for the purpose of calculating LTV ratio.
(d) It has been observed that some banks have introduced certain innovative Housing Loan Schemes in association with developers / builders, e.g. upfront disbursal of sanctioned individual housing loans to the builders without linking the disbursals to various stages of construction of housing project, Interest/EMI on the housing loan availed of by the individual borrower being serviced by the builders during the construction period/ specified period, etc. This might include signing of tripartite agreement between the bank, the builder and the buyer of the housing unit. These loans products are popularly known by various names like 80:20, 75:25 schemes.

(e) Such housing loan products are likely to expose the banks as well as their home loan borrowers to additional risks e.g. in case of dispute between individual borrowers and developers/builders, default/ delayed payment of interest/ EMI by the developer/ builder during the agreed period on behalf of the borrower, non-completion of the project on time etc. Further, any delayed payments by developers/ builders on behalf of individual borrowers to banks may lead to lower credit rating/ scoring of such borrowers by credit information companies (CICs) as information about servicing of loans get passed on to the CICs on a regular basis. In cases, where bank loans are also disbursed upfront on behalf of their individual borrowers in a lump-sum to builders/ developers without any linkage to stages of constructions, banks run disproportionately higher exposures with concomitant risks of diversion of funds.

(f) Banks are advised that disbursal of housing loans sanctioned to individuals should be closely linked to the stages of construction of the housing project / houses and upfront disbursal should not be made in cases of incomplete / under-construction / green field housing projects.

(g) However, in cases of projects sponsored by Government/Statutory Authorities, banks may disburse the loans as per the payment stages prescribed by such authorities, even where payments sought from house buyers are not linked to the stages of constructions, provided such authorities have no past history of non-completion of projects.

(h) It is emphasized that banks while introducing any kind of product should take into account the customer suitability and appropriateness issues and also ensure that the borrowers/ customers are made fully aware of the risks and liabilities under such products.

4. RATE OF INTEREST

Banks should charge interest on housing finance granted by them in accordance with the directives on “Interest Rates on Advances” issued by Reserve Bank of India from time to time.

5. APPROVALS FROM STATUTORY/ REGULATORY AUTHORITIES

While appraising loan proposals involving real estate, banks should ensure that the borrowers should have obtained prior permission from government / local governments / other statutory authorities for the project, wherever required. In order that the loan approval process is not hampered on account of this, while the proposals could be sanctioned in normal course, the disbursements should be made only after the borrower has obtained requisite clearances from the government authorities.

6. DISCLOSURE REQUIREMENTS

In view of the observations of Hon’ble High Court of Judicature at Bombay, while granting finance to specific housing / development projects, banks are advised to stipulate as a part of the terms and conditions that:

(a) the builder / developer / company would disclose in the Pamphlets / Brochures etc., the name(s) of the bank(s) to which the property is mortgaged.

(b) the builder / developer / company would append the information relating to mortgage while publishing advertisement of a particular scheme in newspapers / magazines etc.

(c) the builder / developer / company would indicate in their pamphlets / brochures, that they would provide No Objection Certificate (NOC) / permission of the mortgagee bank for sale of flats / property, if required.

(d) Banks are advised to ensure compliance of the above terms and conditions and funds should not be released unless the builder/developer/company fulfils the above requirements.

(e) The above mentioned provisions will be mutatis-mutandis, applicable to Commercial Real Estate also.

7. EXPOSURE TO REAL ESTATE

Banks are well advised to frame comprehensive prudential norms relating to the ceiling on the total amount of real estate loans, single/group exposure limit for such loans, margins, security, repayment schedule and availability of supplementary finance and the policy should be approved by the bank’s board. While framing the bank’s policy the guidelines issued by the Reserve Bank should be taken into account.

8. HOUSING LOANS UNDER PRIORITY SECTOR

The grant of housing loan for the purpose of the priority sector lending targets including reporting requirements will be subject to the instructions on “Priority Sector Lending” as amended from time to time.

9. FINANCING OF AFFORDABLE HOUSING-ISSUE OF LONG TERM BONDS BY BANKS

Banks can issue long-term bonds with a minimum maturity of seven years to raise resources for lending to affordable housing subject to the conditions mentioned in circular DBR.BP.BC.No.25/08.12.014/2014-15 dated July 15, 2014 on “ Issue of Long term Bonds by Banks- Financing of Infrastructure and Affordable Housing”.

10. ADDITIONAL GUIDELINES

It is advised that banks should adhere to the National Building Code (NBC) formulated by the Bureau of Indian Standards (BIS) in view of the importance of safety of buildings especially against natural disasters. Banks may consider this aspect for incorporation in their loan policies. Banks should also adopt the National Disaster Management Authority (NDMA) guidelines and suitably incorporate them as part of their loan policies, procedures and documentation.