Indian Banks' Association

REVISED GUIDANCE NOTES ON MODEL EDUCATIONAL LOAN SCHEME FOR PURSUING HIGHER EDUCATION IN INDIA AND ABROAD (2015).

I. Introduction

Educational Loan Scheme is a socially and economically relevant loan scheme from the Indian banking industry. Rightly, the RBI has included education loans as part of the priority sector lending of banks. It aims to provide need-based finance to meritorious student for taking up higher education.

In any commercial lending decision, credit worthiness of the borrower and the viability of the scheme are important. The student borrower has no credit history and as such he is assumed to be creditworthy as this is a futuristic loan. However, it is likely that the joint borrower for the loan has a credit history and any adverse features could have a bearing on the assessment of credit risk. If the joint borrower has a loan account with the bank and the loan is treated as non-performing asset, the bank runs the risk of having to consider the student loan also as NPA ab-initio. To overcome this, the bank may, as a prudent measure insists on a joint borrower acceptable to the bank, in case of adverse credit history of the parent/guardian of the student.

II. Objectives of the scheme

The educational loan scheme is meant to provide need-based assistance to meritorious students in pursuing higher education. Since the word "meritorious" is a relative term it would be necessary for banks to specify parameters for defining the term meritorious. The following approach is suggested:

If the student has obtained admission to an eligible course through a merit based selection process, he/she could be considered a meritorious student. Generally, admission to professional and technical courses are through common entrance tests and those who get admission through this process could be considered meritorious. Where the admission is purely based on the marks scored in qualifying examinations, the bank may fix cut-off marks (percentage) for loan eligibility.

Very often enquiries are made whether the model scheme covers students who are getting admission against management quota. Management seats or management quota refers to the seats in private education institutions for which the management has discretion to give admission on factors other than merit. Usually, out of permitted seats for the batch, a certain percentage is earmarked to be filled from State level merit list and the rest are allowed to be filled by the management at their discretion.

Usually for the management seats the only requirement would be passing of the qualifying examination with certain minimum stipulated marks. It is logical to interpret that these seats do not qualify for being called "meritorious"

Banks have reported certain cases where the employment potential would not justify the fee structure for management seats from the point of repayment of the loan being sought. Hence, any loan considered by banks for students getting admission under management quota would be outside the model scheme. Banks may fix appropriate terms and conditions for such loans. However, a student getting admission offer under merit quota may choose to take up a course under management quota as a personal preference. Such students may be sanctioned loans under this Model Scheme.

III. <u>Applicability of the Scheme</u>

The Model Scheme has been developed for the benefit of the member banks of the Association. However, other banks and financial institutions can also adopt the model without reference to the Association.

IV. <u>Eligibility Criteria</u>

IV.i. Student Eligibility

For the purpose of this scheme higher education is defined as studies taken up after completion of higher secondary school i.e. ten plus two stage. The need for bank loan scheme came for discussion in the country for meeting higher levels of fees charged by private managements for technical and professional courses consequent to ban on capitation fee. However, in the model scheme a generalized definition has been adopted for higher studies for wider coverage. It is expected that the banks will decide on the courses for which they will be giving student loans based on employability and consequent ability to repay the loan.

References are often made about the eligibility of students pursuing employment oriented courses like teachers training courses and 3-year technical diploma courses in polytechnic institutions after completion of 10^{th} standard. It is clarified that banks are free to include such employment-oriented courses as eligible course provided they are offered by approved/recognized colleges/institutions. The 3 year diploma courses are also covered as eligible courses under 'IBA Model Loan Scheme for Vocational Education and Training'.

It need to be noted that while the Central Sector Interest Subsidy Scheme of MoHRD is based on 'IBA Model Educational Loan Scheme', the subsidy is applicable only for loans given for Professional and Technical courses (after 12^{th} standard) in India.

IV.ii. Courses eligible

a. Studies in India

The list of courses given in the model scheme is purely indicative in nature. The important thing is that the course is approved / recognized by the designated academic authority/regulatory body for the stream of study concerned.

Links to the web sites of the University Grants Commission (UGC), All India Council for Technical Education (AICTE) and the Ministry of HRD (MoHRD) have been provided in the model scheme to serve as guidance on courses and approving authorities for various courses, which fall within the definition of higher studies.

Banks may prepare and publish a list of eligible courses they would consider for sanctioning of student loans. Since employability of students on the completion of the course is an important consideration for loan approval, banks may consider introducing a system of assessing the employability of students through the campus placements system. Details such as percentage of final year students getting job offers through campus placement, average salary offers etc. may be collected in respect of colleges / institutions from which most loan applications were received in the past for evaluation of employability of students. This exercise should be done on an on going basis to reflect the current status.

Since employability is the main criteria for decision making, it would be in order for banks to consider financing for studying part-time courses (evening classes or otherwise).

Job oriented specialized programmes like maritime courses which are offered in collaboration with foreign institutions may not be having recognition in India. However, if the placement record of such institution gives confidence about employability, banks may, at their discretion consider financing such courses.

Similarly, financial assistance for pursuing research work could also be considered for financing on merit.

Note:

While evaluating employability and repayment possibilities, banks should take into consideration, availability of interest subsidy under the MoHRD Central Sector Scheme introduced w.e.f. 1.4.2009. Under the scheme, the Central Govt.

subsidises 100% of the loan’s interest during the study period and subsequent moratorium period before commencement of repayment. It is expected that the interest subsidy could bring the EMI for repayment by as much as 30 to 40%. The student hailing from economically weaker section family would benefit from this scheme.

b. Studies Abroad

Diploma courses and certificate courses have not been included as eligible courses for the scheme. Post graduate studies leading to PG degrees and PG diplomas offered by reputed institutes/universities only will be covered by the scheme. Assessment of employment potential or future prospects is very important criterion considering the higher cost of studies involved. The web link given in the scheme is for guidance and there could be other links/sources giving such useful information.

c. Expenses considered

The Model scheme is aimed at meeting all genuine study expenses of a student required to complete the study undertaken. It needs to be noted that sometimes, the fee structure varies with type of college/institution within the same State for a given course. The fees charged by the government colleges/institutes are generally the lowest, with higher fees permitted in aided private colleges/institutions; fee structure being highest in unaided private colleges/institutes. Sometimes the difference between the lowest and highest fee structure levied for the same course by different colleges/institutions is too high to give comfort to a banker in taking credit decision as employment prospects remain same. A practical approach would be to consider approved fee structure for merit quota seats in all colleges/institutions, provided banks are satisfied about repayment prospects on employment.

d. Rating as an assessment tool

Banks could use rating of education institutions and student as a tool for targeting students borrowers and improving asset quality. External data on rating of various education institutions may be available in public domain. The track record of the institution in terms of percentage placement and average emoluments offered to passing out student would be useful information in creating rating matrix. Similarly, along with the rating of institutions, banks could also attempt rating of students. Academic record and ranking in the selection test would be core for the initial rating. To this, the academic record during the study period could be added to revise the students rating from year to year. Students getting admission to highly rated institutions and students who have high rating for themselves could be offered loans with lower rate of interest.

Besides weightage to ranking of institute and merit of students ranking of courses offered by the educational institution be done on the basis of placements record of the institution concerned.

IV.iii **Design elements for classification of education loans**

Rating of education institutions is recognized as an assessment tool. As detailed in IV ii (d) banks could use rating of education loan institutions and student as a tool for targeting student borrowers and improving asset quality. For meritorious students taking up education in rated institutions there is a case for ensuring hassle free sanction of loan with improved terms and conditions considering better employability and probability of prompt repayment. Keeping this in view banks are advised to classify the student loans in the three categories viz. a) Loans to students admitted to top rated institutions b) Loans to students admitted to other domestic institutions c) Loans to students seeking studies abroad.
The top rated institutions could consist of institutions given A rating by NAAC, institutions / courses similarly rated by other recognized agencies and institutions identified as top ranking by the banks based on reputation, employability and track record of *aluminous* in repaying student loans. Banks could consider relaxed security norms and interest rates for the students. 50% cut-off mark is suggested for students getting admission in these institutions.

For students getting admission in institutions other than rated institutions the standard norms suggested in the model education loan scheme may be applied. The loans given to students who take up studies abroad are classified separately . The assessment norms and trems of sanction cold be different for these loans. Also these loans are normally collateralized.

V. **Quantum of finance**

While assessing the quantum of finance, banks should ensure that a student is neither over financed or under financed. It would be necessary to take into account Scholarships / concessions etc., if the student is entitled to, before fixing the limit for sanction. At the same time, if some of the genuine expenses are left out or remains uncovered, the student will find difficulty in completing the course with consequent stress on repayment.

Banks should ensure that the government scholarships or scholarships from any source are credited to the loan account, if the scholarship amount was not netted off while fixing quantum of finance.

VI. Margin

VII. Security **--**

VIII. Rate of interest

In the past, interest rates were linked to the BPLR of banks. With effect from 1st July 2010, the banking system has switched over to base rate linked product pricing for loans and advances. The new system is more transparent and expected to result in better risk based pricing of loans in the country. Also, market competition is expected to bring down interest spreads. Hence it is proposed to leave the interest rates free for banks to decide at their end. However, it is proposed to retain 1% interest concession for servicing of interest during study/moratorium period. It is also expected that the banks will charge relatively lower rates for loans up to ₹ 4 lakhs and continue concessions hitherto being given to girl students**.** It will also be open to banks to offer differential interest rates based on rating of courses/institutions or even students**.**

IX. Appraisal/Sanction/Disbursement

The model scheme does not look at the financial position of parents while evaluating loan to a meritorious student. Repayment possibilities have to be based on projected future earnings of the student on employment after education. To avoid subjectivity in assessment, it is suggested that the banks may fix from time to time earning potential for various courses, percentage of income to be considered for repayment etc. A well laid appraisal procedure will ensure that the decision to sanction an education loan is based on sound commercial logic, besides serving a noble social cause.

The suggestion that bank branches nearest to the residence of parents to consider the loan application was given for better tracking of students during and after study period. Banks are, however, free to adopt different norms to suit their business plans.

X. Repayment

Repayment period has been increased to give greater comfort to the student borrowers to repay the loan out of their future earnings. Prepayment options are also provided for persons who would like to clear the loan faster out of better than anticipated earnings. No prepayment charges are to be levied in such cases.

XI. Insurance

Insurance policy should be obtained only with the prior consent of the student borrower. This is more so relevant in case of loans up to ₹ 4 lakhs where the bank loans are without any security. The clause regarding insurance has been included in the scheme to provide a life cover to the student**.**

XII. Follow Up/Monitoring

Monitoring academic progress of the student is necessary for the success of the Scheme. Considering that all banks are now on CBS, it is suggested that irrespective of the branch where loan is sanctioned, monitoring of loans during the study period may be entrusted to the branch dealing with the institution or the one located nearer to the educational institution. Generally, college authorities will provide progress report after every semester / year.

Member banks may note that professional colleges allow students to move to the higher class even if they fail in a few subjects in the examination for previous year/semester. The disbursement of subsequent installments should not be stopped for the reason that the student has failed in one or two subjects in the examination provided he has been allowed to keep terms.

The Banks may also explore the possibility of sending payment towards the fees to the institutions through electronic channels. Progress reports may also be received electronically wherever possible.

XIII. Tracking of students

It is found that banks will be able to track the student after completion of the course effectively if co-ordinated with the education institutions. Educational institutions will be able to provide placement details and in some cases changes in the initial years after education. The alumni forums of educational institutions can also give valuable feedback.

Many banks obtain Permanent Account Number (PAN) for its value in future tracking. However, as most of the students may not require PAN during education period, submission of PAN details should not be made a pre-condition for loan sanction. However, considering the ease of registering PAN, the students may be asked to submit PAN during the course of studies.

Aadhaar Card issued by the Unique Identification Authority of India is also seen as a unique identifier for future tracking. While Aadhaar registration should not be made a pre-condition for loan sanction, it is suggested that banks may obtain the Aadhaar for their record before the student completes the full course of studies. Accordingly, suitable clause may be included in the sanctioned letter.

XIV. Processing Charges --

XV. Capability Certificate --

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