CHARTERED FINANCE & LEASING LIMITED

RISK MANAGEMENT POLICY

CHARTERED FINANCE & LEASING LIMITED

RISK MANAGEMENT POLICY

POLICY VERSION CONTROL:

VERSION NO.	APPROVED BY BOARD ON	REMARKS
1.0	07-Apr-2022	Policy adopted by the Board

Chartered Finance & Leasing Limited

Approving Authority	Board of Directors
Reviewing Authority	Audit Committee
Original Issue Date	07-Apr-2022
Last Review Date	07-Apr-2022
Policy Making Body	Audit Committee
Effective Date	07-Apr-2022

Contents

1. Background

The Board of Directors ('Board') of Chartered Finance & Leasing Limited ('Company'), acknowledges and identifies that the Company is prone to certain inherent risks, while operating as a Non-Banking Financial Company ('NBFC') in the financial sector. The Company realizes the importance of having in place a Board approved policy to clearly lay down the process of risk management within and at each level of operation and function in the Company. Considering this, the following Risk Management Policy ('Policy') has been adopted by the Board of the Company.

2. Objective and Purpose

2.1. To have in place an effective risk management system, within and at each level of operation and function in the Company;

2.2. To identify, assess, strategize and report the types of risks that are associated with the nature of business activities and the associated operations of the Company;

2.3. To provide for measures to be taken by the Company, in order to analyze, prioritize and handle foreseen or unforeseen events which may have a material impact on the working of the business of the Company, whether directly or indirectly, and take further measures to minimize the losses, if any occurring on account of such event;

2.4. To review and revise the existing system in place, by identifying new risks, likelihood of their impact and the measures to mitigate them in future;

2.5. To monitor the existing systems and revise the Policy as and when the need arises, so that the system remains robust and effective to deal with all types of risks in the Company;

2.6. To identify the authority, who shall be primarily responsible for the management of risks and suggest measures thereon to the Board of the Company.

3. Principles

For risk management to be effective, all operations/departments of the Company must apply the following principles to the context of the business and its objectives:

- Risk management must create and protect value
- Risk management is integrated into organisational processes.
- Explicit risk management helps decision-makers make informed choices.
- Risk management is focused on the sources of uncertainty around the achievement of objectives
- Risk management must be tailored to the context and fit for purpose
- Risk management is dynamic, iterative and responsive to change.

4. Risk Management

Figure 1: Process of Risk Management

4.1. Investment Risk management**:**

4.1.1. "Investment Risk" is associated with the erosion in the value of investment owing to the poor performance of the investee entities or due to non-financial reasons including but not limited to governance, compliances, external market factors, government policies, etc. resulting in de-rating of the securities issued by the entities.

4.1.2. The Company shall carry out a detailed appraisal of the investee company, including financial appraisal, quality of governance, compliances, sectoral outlook, its competitive positioning and right to exist and then conduct periodical reviews of such indicators to continue or disinvest to ensure preservation of investment amount and earn appropriate returns.

4.2. **Credit Risk Management**

4.2.1. 'Credit Risk' is typically the risk of default on account of non-payment of any contractual obligation on part of investee/debtor companies, as per the agreed terms. Largely, credit risk is indirectly proportional to the credit worthiness of the investee;

4.2.2. It is pertinent to identify such risks by means of effective credit appraisal of a potential investee.

4.2.3. The Company shall carry on a detailed credit appraisal of the investee/debtor entities with the help of supporting financial statements, repayment track record, borrowing trends, any past records of default, tenure of default, credit ratings etc.

4.2.4. While carrying out the credit appraisal of an investee, the Company shall verify as to whether the names of any of the directors of the companies appear in the list of defaulters by way of reference to DIN/PAN, etc.

4.2.5. The Company shall also use tools to manage credit risk, including but not limited to following:

4.2.5.1. Credit evaluation models: It denotes financial appraisal of the business operations meant to identify the major factors which affects/ have the potential to affect the ability of the investee to repay and arrive at overall scoring of the entity.

4.2.5.2. Credit scoring– In the above-mentioned model, for rated securities, the Company shall rely upon credit ratings allotted to securities of the Company by SEBI registered credit rating agency.

4.3. **Market Risk Management** – Being a financial sector entity, the Company has a variety of market risks. The Company shall deal with each of these risks in the following manner:

4.3.1. Interest Rate Risk – Interest Rate Risk can be defined as the risk of change in interest rates in the market which may have a material impact on the Company's activities. The immediate impact of changes in interest rate is on the Company's earnings (i.e., reported profits) by changing its Net Interest Income (NII). Further, such change has a long-term impact on Market Value of Equity (MVE) or Net Worth as the economic value of the assets, liabilities and off-balance sheet positions get affected due to variation in market interest rates. Liquidity Risk – Liquidity Risk is the risk of inability of the Company to meet the financial obligations in accordance with the agreed terms. The Board shall analyze the liquidity position of the Company on an on-going basis, to ensure that the Company has adequate funds to dispose of its obligations and any cash outflow requirement. Excess funds may be invested into such securities or market, which offers ease of redemption and high liquidity, based on the maturity and future requirements. For measuring and managing net funding requirements, the use of a maturity ladder and calculation of cumulative surplus or deficit of funds at selected maturity dates shall be adopted as a standard tool.

4.4. **Operational Risks** – The Company shall identify risks associated with the operational activities, including but not limited to:

4.4.1. Risk of IT system failure (*refer IT Policy for detailed procedures*);

4.4.2. Risk of physical infrastructure failure;

4.4.3. Risks relating to business support activities, including business disruptions;

4.4.4. Procedural lapses / non-adherence to laid down guidelines or processes;

4.4.5. Loss of documents;

4.4.6. Collusion/Fraud;

4.4.7. Any other risk which may have a direct bearing on people, technology, infrastructure, etc. in relation to the Company;

The benefit of efficiently managing operational risks includes alignment of all functions and verticals towards identifying the key risks in the underlying process. Each functional vertical shall conduct transaction testing to evaluate internal compliance and thereby lay down processes for further improvement.

4.5. **Regulatory Risks**

Risks arising out of any change in any applicable law, rules, regulations, which may adversely affect the business operations of the Company, whether directly or indirectly, are termed as 'Regulatory Risks'. The Board of the Company, along with and on regular recommendations of various departments of the Company, is responsible to ensure timely modifications in the policies and strategies of the Company in accordance with any amendment in law.

4.6. **Reputation Risk**

Reputation risk is the risk to earnings and capital arising from adverse perception of the image of the company, on the part of customers, counterparties, shareholders, investors, vendors and regulators. It refers to the potential adverse effects, which can arise from the Company's reputation getting tarnished due to factors such as unethical practices, regulatory actions, customer dissatisfaction and complaints leading to negative publicity.

Presence in a regulated and socially sensitive industry can result in significant impact on Company's reputation and brand equity as perceived by multiple entities like the RBI, Central/State/Local authorities, banking industry and last but not least, Company's customers. The risk can emanate from:

- Political activism
- Non-Compliance with Regulations
- Customer Dissatisfaction

4.7. Compliance Risk:

The Company is present in an industry where the Company has to ensure compliance with regulatory and statutory requirements. Non-Compliance can result in stringent actions and penalties from the Regulator and/or Statutory Authorities and which also poses a risk to the Company's reputation. These risks can take the form of:

- Non-Compliance with RBI Regulations
- Non-Compliance with Statutory Regulations

5. Identification and Assessment of Risks & Control

5.1 Identification:

Risk identification will be done by involving personnel at the senior and middle management level of all key functions to achieve a holistic view of risks. The purpose is to identify the risks that will have an impact on the operations of the Company.

After the key risks have been identified, they will be assessed in terms of their 'consequence' and 'likelihood'. Also, in order for risks to be assessed objectively, there shall be a common approach or methodology for measuring risks. It is critical for the process owners and management to define and agree on the quantitative and qualitative descriptors for consequence and likelihood scale in identifying and assessing risks.

5.2 Prioritization of Risk Treatment

Risk prioritization is the process of rating the risks in order to identify those risks which may have the most significant impact on the achievement of the stated goals and objectives of the business

Identified risk shall be rated based on the nature of the risk and likelihood of its occurrence. Risks that are characterized with high inherent risks (gross risk in absence of any controls) or high residual risks (risk assessed to be higher than the 'targeted' level after considering existing controls) shall be prioritized for treatment.

Detailed action plans (include responsible parties and target dates) are to be developed and documented.

6. Risk Mitigation

Risk mitigation is the process of initiating responsive action for managing the RTMs ('Risk That Matter') and restricts their impact to a tolerable level. The process of Risk

Mitigation involves development of mitigation plans with defined ownership and implementation timelines.

The identified risks shall be mapped by the senior management, to the respective person / authority ('Risk Owners'), in-charge, who shall identify the process/controls in place to mitigate the respective identified risk. All such Risk Owners shall report the compliance statement to the Director responsible for handling the operations of the Company at such intervals as the Director may deem fit.

Monitoring of the process activities shall be done to ensure their timely and appropriate execution. Further reporting to the Board and the AC on the risk profile and effectiveness of the implementation plan shall be done.

7. Risk Management System

7.1. The entire risk management system in the Company is based upon the following essential components:

7.1.1. Board of Directors,

7.1.2. Audit Committee (AC)

7.2. The AC, which shall be delegated with the overall responsibility of implementation and monitoring of this Policy and recommending any change or review of the same, as and when required. The AC shall ensure that all steps are taken for the correct implementation and mitigation of risks, as per the prescribed procedures.

7.3. The AC shall consist of such a number of members, as appointed by the Board.

7.4. The AC shall meet at such intervals as may be required under the applicable laws and as decided by the Board of Directors. (Other detailed procedures in respect of the Committee have been laid down in its terms of reference).

8. Roles and Responsibilities of the Board

The principal roles and responsibilities of Board, in the overall risk structure are as follows:

i. To set/approve overall risk appetite and risk tolerance limit of the Company that aligns with the stakeholder expectations;

ii. Review and approve risk management strategies, policies and procedures proposed by AC/Senior Management;

iii. Ensure that the company has in place adequate internal audit coverage to satisfy itself that policies and procedures have been implemented effectively;

iv. Provide senior management with clear guidance and direction for risk management initiatives for items reported by AC/Senior Management;

v. Regular monitoring of and response to executive summary risk reporting by AC/ Senior Management;

9. Constitution, Roles & Responsibilities of Audit Committee or Senior Management

The AC, if any, or the Senior Management, is responsible to establish policies and minimum process standards of risk management across the Company.

i. Monitor and ensure that appropriate risk management framework is in place;

ii. Review the risk profile, understand future changes and threats, and prioritize action steps on a periodic basis;

iii. Review and approve the development, implementation of risk methodologies and tools, including assessments and reporting;

iv. Review periodical risk assessment results;

v. Review the critical risks and their drivers identified as a result of the risk assessment exercise;

vi. Nominate Risk Owners for developing and implementing mitigation plans for critical risks that are prioritized during risk prioritization workshop;

vii. Discuss and recommend suitable controls/ mitigations for gaps identified during risk assessment exercise;

viii. Review and manage potential risks which may arise from regulatory changes/ or changes in economic / political environment in order to keep ahead;

ix. Guide the risk team in developing the risk appetite statements;

x. Encourage the risk team to develop an MIS framework commensurate to the strategy of the company and also expectations of Board and Top management;

Further, the AC/Senior Management shall meet at such intervals as may be required to review the significant risk issues. Major changes proposed by AC will be discussed at BoD meetings.

10. Policy Review

The contents of this Policy shall be reviewed by the Board of the Company/ Audit Committee, on such intervals but not later than once in a year as may be necessary for smooth and robust business operations of the Company.