Restructuring Policy for MSME 2016-17

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1. Introduction

Micro, Small & Medium Enterprises sector constitute the growth engine of the country's economy. The MSMEs lead to entrepreneurial development and diversification of the industrial sector, and also provide depth to industrial base of the economy. More employment opportunities are generated and the capital cost per employee is low. With the Services sector dominating the MSME, and MNCs outsourcing their various requirements to Indian service providers, the scope for MSME finance has increased even further. With the deregulation of the financial sector, the general ability of the banks to service the credit requirements of the MSME sector depends on the underlying transaction costs, efficient recovery processes and available security. Thus, there is an immediate need for the banks generally to focus on credit and finance requirements of MSMEs. Accordingly, an MSME Policy has been framed to cater the needs of the eligible borrowers. However, due to various internal and external factors, lack of expertise, financial discipline etc. the industries faces the losses and become unviable in the long run.

2. Objective

Thus, the objective of this Policy is an embodiment of the bank's approach to understand, measure, approach towards the MSME sector and to ensure timely and transparent Debt Restructuring Mechanism (DRM) for restructuring the debts of viable MSMEs facing problems, outside the purview of BIFR, DRT, CDR and other legal proceedings. This policy takes the cognizance of preserving viable MSMEs that are affected by certain internal and external factors and minimize the losses to the creditors (the Bank) and other stakeholders through an orderly and coordinated debt restructuring mechanism or rehabilitation package.

3. Scope & Applicability

This policy will cover and be applicable to the industries as defined under The Micro, Small & Medium Enterprises Development (MSMED) Act, 2006.

3.1 Definition of Micro and Small Enterprises

3.1.1 Enterprises engaged in the manufacture or production, processing or preservation of goods:

I. A micro enterprise is an enterprise where investment in plant and machinery does not exceed Rs. 25 lakhs;

II. A small enterprise is an enterprise where the investment in plant and machinery is more than Rs. 25 lakhs but does not exceed Rs. 5 crores;

In case of the above enterprises, investment in plant and machinery is the original cost excluding land and building and the items specified by the Ministry of Small Scale Industries vide its notification No. S.O.1722(E) dated October 5, 2006.

3.1.2 Enterprises engaged in providing or rendering of services and whose investment in equipment (original cost excluding land and building and furniture, fittings and other items not directly related to the service rendered or as may be notified under the MSMED Act, 2006).

I. A micro enterprise is an enterprise where the investment in equipment does not exceed Rs. 10 lakh;

II. A small enterprise is an enterprise where the investment in equipment is more than Rs.10 lakh but does not exceed Rs. 2 crore;

3.2 MSEs (Direct and indirect finance)

In addition to the above categories, direct finance to MSEs to include small road & water transport operators, small business, professional & self-employed persons, retail trader i.e. advances granted to retail traders dealing in essential commodities (fair price shops), consumer
Co-operative stores and advances granted to private retail traders with credit limits not exceeding Rs.20 lacs and all other service enterprises as per the definition of MSEs based on investment in plant and machinery and equipment.
Indirect finance to MSEs to include –

- Finance to persons involved in assisting the decentralised sector in the supply of inputs and marketing of outputs of artisans, village and cottage industries.
- Advances to co-operatives of producers in the decentralized sector viz. artisans village and cottage industries.
- Loans granted to Micro Finance Institutions (MFI), on or after April 1, 2011 for on lending to MSEs, provided not less than 85% of total assets of MFI (other than cash, balances with banks and financial institutions, government securities and money market transactions) are in the nature of “qualifying assets”. In addition aggregate amount of loan extended for income generating activity is not less than 75% of the total loans given by MFIs.
- A “qualifying asset” is a loan disbursed by MFI which satisfies the following criteria:
    - The loan extended to a borrower whose household annual income in rural areas does not exceed Rs.60,000/- while for non-rural areas it should not exceed Rs.1,20,000/-
    - Loan does not exceed Rs.35, 000/- in the first cycle and Rs.50, 000/- in the subsequent cycles.
    - Total indebtedness of the borrower does not exceed Rs.50, 000/-.

- Tenure of loan is not less than 24 months when loan amount exceeds Rs.15, 000/- with right to borrower of prepayment without penalty.
- The loan is without collateral.
- Loan is repayable by weekly, fortnightly or monthly instalments at the choice of the borrower.
- The loans which has been sanctioned under MUDRA schemes also.

3.3 Definition of sick unit/enterprise

Credit facilities sanctioned by banks may turn out to be out of order / irregular due to various reasons which may be minor or major, temporary or of a more lasting nature, internal & external etc. Depending upon the type of irregularity, necessary remedial measures are to be taken.
In broad terms the irregularity may be due to:

- Unsatisfactory conduct of the account like non-submission of stock statements, non-payment of instalments and interest on due dates etc.
- Sticky tendencies like suspended operations in the account, lack of periodic
  Intimations/ submissions to the Bank, lack of financial discipline, etc.

As per the revised definition, a Micro or Small Enterprise (as defined in the MSMED Act 2006) may be said to have become **'Sick'** if –

1. Any of the borrower account of the enterprise remains NPA for three months or more
OR
2. There is erosion in the net worth due to accumulated losses to the extent of 50% of its net worth during the previous accounting year.

Causes of Sickness

The causes of sickness in an Industrial Unit can be broadly classified into two categories:

a. Internal causes
b. External causes

- While "Internal causes" are those causes which can be attributed to the management of the unit,
- The "External causes" are those which are attributed to factors outside the purview / control of the Promoters / management / banks etc.

4. Handholding Stage

Timely and adequate assistance to MSEs and rehabilitation efforts would be provided on proactive basis when early signs of sickness are detected so that sickness is arrested at an early stage. This stage which is called "Handholding stage" is defined if any of the following events are triggered –

1. There is delay in commencement of commercial production as proposed or by more than six months for reasons beyond the control of the promoters;
2. The company incurs losses for two years or cash loss for one year, beyond the accepted time frame.
3. The capacity utilization is less than 50% of the projected level in terms of quantity or the sales are less than 50% of the projected level in terms of value during a year.

This will ensure intervention by banks immediately after detecting early symptoms of sickness so that sickness can be arrested at an early stage.

Timely remedial action like enquiring into the operations of the unit and proper scrutiny of the accounts, providing guidance/counselling services, timely financial assistance as per established need and helping the unit in sorting out difficulties which are non-financial in nature are to be taken up on immediate basis.

The handholding support to units should be undertaken within a maximum period of two months of identification of such units. The review of business activities and assistance wherever required will be provided by the branch. Units which could not be revived after intervention by the bank at the "handholding stage" are to be classified as sick subject to compliance with any of the two conditions as mentioned above.

5. Viability study

A unit or enterprise would be regarded as viable if it would be in a position, after implementing a relief package spread over a period of maximum 5 years from the commencement of the package, to continue to service its repayment obligations as agreed without the help of concessions after the aforesaid period. The repayment period for restructured (past) debts should not exceed 7 years from the date of implementation of the package.

In the case of non-performing loans / stress cases where settlement or exit is not possible immediately, handholding could be provided subject to long term viability of the Company and possibility to retain the loan as earning assets. The handholding could also include incremental exposure, wherever needed. However, such instances in exposure to be covered, as far as possible, by collateral / corporate guarantees of a good company / escrow or securitization of cash flows.

The scheme includes giving appropriate reliefs and concessions such as reduction in interest rate, funding of interest, re schedule of principal, waiver of interest etc under RBI guidelines, as a tool to improve the long term viability of the borrower. Rehabilitation shall however be used selectively and without diluting the Bank's focus on collections / remedial action.

The Bank would undertake the restructuring of credit facilities to micro and small enterprises within a maximum period of 60 days subject to the eligible borrower agreeing for the restructuring and submitting a formal request to that effect to the Bank.

On receiving a borrower request, a viability study would be done covering the following aspects, depending upon the availability of inputs:

- The proposed restructuring would be based on the realistic projections for the borrower including the estimated future cash flows
- Promoters & their background: Objective assessment of promoters and their background based on their experience, existing operations and professional qualifications etc. to be done. Relevance of these to the proposed venture in case of new units to be brought out.
- As far as possible, efforts would be made to ensure commensurate sacrifices from all the stakeholders including existing promoters
- Wherever considered necessary, the bank would insist on change of management and / or pledge of promoter's stake subject to extant regulatory stipulations
- Efforts to be made, wherever possible, to include the following covenants / conditions in rehabilitation package:
    - Enhancement in security package and payment security mechanism e.g. escrow of cash flow of the borrower
    - Up-front trigger conditions, non-compliance of which would result into automatic change of management
    - Personal Guarantee of the promoters
    - Appointment of professionals on the board
    - Appointment of concurrent auditors

The above list is illustrative and not exhaustive. The sanctioning authority may decide on additions / deletions to the above list, on case to case basis and depending on the nature of the project and purpose of the report i.e. new finance or restructuring.

Units / enterprises becoming sick on account of wilful mismanagement, wilful default, unauthorized diversion of funds, disputes among partners / promoters, etc. would not be considered for rehabilitation and steps would be taken for recovery of bank's dues.

Branch Manager or empanelled vendor will carry out first level credit assessment of the proposal. Branch Manager would take appropriate request letter and commitment from the eligible borrower. Before processing the request, concerned branch manager of the bank would carry out preliminary checks / assessment of viability / restructuring before detailed scrutinizing by the bank. The rehabilitation package will be approved by the next sanctioning authority but not below the rank of GM Committee.

6. Viability of Units

The viability and the rehabilitation of a sick unit would depend on unit"s ability to service its repayment obligations including the past restructured debts. There may not be any write off or scaling down of debt such as by reduction in interest rate with retrospective effect.

Reliefs and concessions under rehabilitation to include funding of unpaid interest on cash credit/term loans, sanction of WCTL, reduction of interest, contingency loan assistance. The viability of any sick unit would be reviewed and examined by Credit Review authority as well as Credit Department or TEV study being done by the empanelled vendor for approval.

Under any circumstances, the decision on viability of the unit to be taken at the earliest but not later than 3 months of the unit becoming sick.

The following procedure is to be adopted before declaring any unit as unviable -

(i) Units becoming sick on account of wilful mismanagement, wilful default, unauthorized diversion of funds, disputes among partners / promoters, etc. should not be considered for rehabilitation

(ii) A unit is to be declared unviable only if the viability status is evidenced by a viability study.

(iii) In case of very small units viz micro (manufacturing) enterprises, having investment in plant and machinery up to Rs.5 lakh and micro (service) enterprises having investment in equipment up to Rs.2 lakh, the Branch Manager in consultation with Credit Department will take a decision on viability and record the same along with justification.

(iv) The declaration of the unit as unviable, as evidenced by the viability study, is to have the recommendation of the Branch Manager and to be evaluated by a Committee comprises of General Manager (Credit), Functional heads of Operation, Credit, Risk, Credit Review, and Accounts.

(v) The next authority is to take decision only after giving an opportunity to the promoters of the unit to present their case.

(vi) For sick units declared unviable, with credit facilities of Rs.1 crore and above, a committee comprising of Business Head, Product Risk Head / Functional Head – Credit and Head – DFSO is to examine such proposals and final decision to be taken. The decision is to be informed to the promoters in writing.

If any of the units is found non-viable, settlement under OTS scheme or recovery by initiating legal action to be undertaken expeditiously.

7. Eligibility criteria for restructuring

As per the RBI circular DBOD.BP.BC.No.34/21.04.132/2005-06 dated 8th September 2005, the following entities which are viable or potentially viable are eligible for restructuring.

- All non-corporate MSEs irrespective of the level of dues to the bank.
- All corporate MSEs, which are enjoying facilities from the bank as sole lender, irrespective of the level of dues to the bank.
- All corporate MSEs, which have funded and non-funded outstanding up to Rs.10 crore under multiple/consortium banking arrangement.
- Accounts involving wilful default, fraud and malfeasance will **not** be eligible for restructuring.
- Accounts classified by bank as "Loss Assets" will **not** be eligible for restructuring.

8. Rehabilitation of Sick MSEs

The rehabilitation package to be fully implemented within six months from the date the unit is declared as potentially viable/viable. During this six months period of identifying and implementing rehabilitation package, handholding of the units to draw funds from the cash credit account at least to the extent of deposit of sale proceeds is to be allowed.

The relief and concessions is to be given for revival of potentially viable sick MSE units, broadly as under. However, reliefs and concessions beyond these parameters are to be decided on case to case basis and only in exceptional cases.

- Interest on Working capital : Interest at the base rate/MCLR, wherever applicable
- Funded Interest Term Loan : Interest free
- Working Capital Term Loan : Interest to be charged at base rate /MCLR wherever applicable
- Term Loan : Concessions in the interest to be given not more than 2% (not more than 3% in the case of

tiny/decentralized sector units) below the document rate or base rate/ MCLR whichever is higher.

- Contingency loan assistance: The concessional rate allowed for working capital. (Temporary limits)

As per extant RBI guidelines, promoter's contribution towards rehabilitation package is to be at a minimum of 10% of the additional long term requirements for micro units and 20% of such requirements for small units. Higher promoter's contribution, wherever possible and warranted, should be insisted upon. At least 50% of the promoter's contribution should be brought in immediately and the balance within six months. It should be a pre-condition that the promoters should bring in their contribution within the stipulated time frame.

Further, with regard to the concessions and relief made available to sick units, the sanction letter and other documents would incorporate a "Right of Recompense" clause that when such units turn the corner and rehabilitation is successfully completed, the sacrifices undertaken by the Bank would be recouped from the units of their future profits/cash accruals.

A suitable evaluation process will be designed by Credit Department to conduct preliminary viability study. If Branch Unit is convinced that the unit is viable, a detailed Credit Appraisal will be submitted to Credit Department for assessment.

9. Asset Classification norms of restructured MSEs

As per extant guidelines for MSME Debt Restructuring, the accounts of borrowers engaged in industrial and non-industrial activities would continue to be classified in the existing asset classification on restructuring and slip into further lower asset classification categories as per extant asset classification norms with reference to the pre-restructuring repayment schedule.

All restructured accounts which have been classified as non-performing assets upon restructuring, would be eligible for up-gradation to the "standard" category after observation of "Satisfactory performance" during the "specified period".

The terms "Specified period" and "Satisfactory performance" are defined as under –

- "Satisfactory performance" means during the specified period means adherence to the following conditions during that period.

    - Non-agricultural Cash credit accounts – In these types of accounts, the account should not be out of order any time during the specified period, for duration of more than 90 days. In addition, there should not be any over dues at the end of the specified period.

- Non-agricultural Term loan accounts – In such accounts, no payment should remain overdue for a period of more than 90 days. In addition there should not be any over dues at the end of the specified period.
- All agricultural accounts – In case of such accounts, at the end of the specified periods the account should be regular.

- Specified period means a period of one year from the date when the first payment of interest or instalment of principal falls due under the terms of restructuring package.

In case, satisfactory performance after the specified period is not evidenced, the asset classification of the restructured account is to be governed as per the applicable prudential norms with reference to the pre-restructuring payment schedule.

10. Delegation of Powers

Such proposals are to be initiated by the concerned branch where the borrowal account is maintained in consultation with Credit Department based on the guidelines mentioned above. The rehabilitation proposal would be approved by the next sanctioning authority under whose power it falls but not the below the rank of General Manager Credit Committee.

11. Monitoring the Progress in rehabilitation of sick MSE units

Credit Review Department will adhere to the guidelines relating sick MSEs and submit the concerned statements to RBI and other regulators and authorities from time to time as per the requirement.

Credit Department will publish the progress in rehabilitation of sick MSE units on a quarterly basis as per extant guidelines.