
Policy on Debt Restructuring Mechanism for Small and Medium Enterprises

1. Introduction

With a view to improve flow of credit and to ensure restructuring of viable and potentially viable debts of SMEs, the Reserve Bank of India has issued guidelines for implementation by the Banks. Accordingly the policy has been prepared which is detailed in the following paragraphs.

2. Eligibility criteria:

2. a. Definition of SME

Units in Small and Medium Enterprises (SME) Sector will include all units in tiny and Small Scale industrial (SSI) sector and also those industrial units whose investment in plant and machinery is up to INR 100 million. Accordingly, only those units in the SME sector as per definition of RBI (defined in RPCD Circular No. RPCD.PLFNS.BC. 31/06.02.31/2005-06 dated August 19, 2005) will be considered for restructuring under the Debt Restructuring Mechanism for SMEs.

2. b. Criteria

The following entities, which are viable or potentially viable, are eligible: -

- i. All non-corporate SMEs banking with us irrespective of the level of dues.
- ii. All corporate SMEs, which are enjoying banking facilities only from our bank, irrespective of the level of the dues to the Bank.
- iii. All corporate SMEs, which have funded and non-funded outstanding up to INR 100 million under multiple/consortium banking arrangement.
- iv. In respect of BIFR cases, branches will ensure completion of all formalities in seeking approval from BIFR before implementing the package.

Exclusions:

- i. Accounts involving willful default, fraud and malfeasance will not be eligible for restructuring under these guidelines. The identification of accounts involving willful default and fraud should be on the basis of guidelines issued by RBI.
- ii. Accounts classified by our Bank as "Loss Assets" will not be eligible for restructuring.

3. Viability criteria

A unit under SME sector may be regarded as potentially viable if it would be in a position to continue to service its repayment obligations as agreed upon including those forming part of the package, without the help of the concessions after the said period, after implementing a Debt Restructuring Package spread over a period not exceeding seven years from the commencement of the package from Banks / financial institutions and other concerned agencies, as may be necessary. The repayment period for restructured (past) debts should not exceed ten years from the date of implementation of the package. For the purpose, all eligible units will comply with the following:

- a. Debt Service Coverage Ratio (DSCR): Should have average DSCR of more than 1.25, and more than 1.10 in any year. DSCR is defined as $[(EBITDA - Tax) / (\text{Term loan Installments due during the year} + \text{Interest})]$. EBITDA is defined as Earnings Before Interest, Tax, Depreciation and Amortization and excludes any non operating income.
- b. Current Ratio: Current Ratio is to be maintained at the minimum level of 1.20 to satisfy under 1st method of lending during seven years of operation after implementation of the package which is expected to improve at minimum level of 1.33 in the subsequent years. Current liabilities to also include short term working capital finance and long term loans maturing within 1 year.
- c. Variation to the extent of 10% benchmark parameters at (a) & (b) above may be considered on merit.
- d. The company's past performance for 3-5 years and future projections for the period of proposed repayment would be examined.
- e. After restructuring of the existing liabilities and providing of the need based additional finance, the unit should be in a position to generate cash profit from the 2nd year of implementation of the restructuring scheme.
- f. The break-even analysis should be carried out, and operating and cash breakeven points should be worked out.
- g. Promoters to bring in a minimum of 20% of the additional long term requirements under the restructuring package. However, a higher promoters' contribution may be insisted upon where warranted. While evolving packages for restructuring, it should be made a pre condition that the promoters should bring in at least 50% of their contribution immediately and the balance in stages during implementation of the package.

4. Prudential Norms for restructured accounts

i. Treatment of 'standard' accounts subjected to restructuring:

- (a) A rescheduling of the installments of principal alone would not cause a standard asset to be classified in the sub-standard category, provided the borrower's outstanding is fully covered by tangible security. However, the condition of tangible security may not be made applicable in cases where outstanding is up to INR 0.50 million, since the collateral requirement for loans up to INR 0.50 million has been dispensed with for SSI/tiny sector.
- (b) A rescheduling of interest element would not cause an asset to be downgraded to sub-standard category subject to the condition that the amount of sacrifice, if any, in the element of interest, measured in present value terms is either written off or provision is made to the extent of sacrifice involved.
- (c) In cases there is a sacrifice involved in the amount of interest in present value terms, as at (b) above, the amount of sacrifice should either be written off or provision made to the extent of the sacrifice involved.

ii. Treatment of 'sub-standard' / 'doubtful' accounts subjected to restructuring:

- (a) A rescheduling of the installments of principal alone, would render a 'sub-standard' / 'doubtful' asset eligible to continue in the 'sub-standard' / 'doubtful' category for specified period (i.e. a period of one year after the date when first payment of interest or of principal, whichever is earlier, falls due under the rescheduled terms, subject to satisfactory performance during the period.) provided the borrower's outstanding is fully covered by tangible security. However, the condition of tangible security may not be made applicable in cases where outstanding is up to INR 0.50 million, since the collateral requirement for loans up to INR 0.50 million has been dispensed with for SSI/tiny sector.
- (b) A rescheduling of interest element would render a 'sub-standard' / 'doubtful' asset eligible to be continued to be classified in the 'sub-standard' / 'doubtful' category for the specified period subject to the condition

that the amount of sacrifice, if any, in the element of interest, measured in present value terms is either written off or provision is made to the extent of sacrifice involved.

- (c) Even in cases where the sacrifice is by way of write off of the past interest dues, the asset should continue to be treated as 'sub-standard' / 'doubtful'.

iii. Treatment of Provision:

- (a) Provision made towards interest sacrifice should be created by debit to Profit & Loss account and held in a distinct account. For this purpose, the future interest due as per the current BPLR in respect of an account should be discounted to the present value at a rate appropriate to the risk category of the borrower (i.e., current BPLR + the appropriate term premium and credit risk premium for the borrower category) and compared with the present value of the dues expected to be received under the restructuring package, discounted on the same basis.
- (b) Sacrifice may be re-computed on each balance sheet date till satisfactory completion of all repayment obligations and full repayment of the outstanding in the account, so as to capture the changes in the fair value on account of changes in BPLR, term premium and the credit category of the borrower. Consequently, banks may provide for the shortfall in provision or reverse the amount of excess provision held in the distinct account.
- (c) The amount of provision made for NPA, may be reversed when the account is re-classified as a 'standard asset'.

5. Additional Finance

The rehabilitation package will comprise restructuring of present dues to the Bank and sanction of additional credit facilities, if required. Such additional finance will be treated as 'standard asset' in all accounts one year after the date when first payment of interest or of principal, whichever is earlier, falls due under the approved restructuring package. If the restructured asset does not qualify for upgradation at the end of the above period, additional finance shall be placed in the same asset classification category as the restructured debt.

6. Upgradation of restructured accounts

The sub-standard/doubtful accounts, which have been subjected to restructuring (refer Para 4.ii. (a) & (b)), whether in respect of principal installment or interest, by whatever modality, would be eligible to be upgraded to the standard category after the specified period, i.e., a period of one year after the date when first payment of interest or of principal, whichever is earlier, falls due under the rescheduled terms, subject to satisfactory performance during the period.

7. Asset Classification status

During the specified one-year period, the asset classification status of rescheduled accounts will not deteriorate if satisfactory performance of the account is demonstrated during the period. In case, however, the satisfactory performance during the one year period is not evidenced, the asset classification of the restructured account would be governed as per the applicable prudential norms with reference to the pre-restructuring payment schedule. The asset classification would be bank-specific based on record of recovery of each bank as per the existing prudential norms applicable to banks.

8. Repeated restructuring

The special dispensation for asset classification as available in terms of paragraphs 4, 5 and 6 above, shall be available only when the account is restructured for the first time.

9. Procedure and Time Frame

- i. The borrower shall submit a request to the Relationship Manager (RM), responsible for the borrower, for restructuring his account.
- ii. In case of eligible SMEs which are under consortium / multiple banking arrangements, the borrower will submit his request to the bank having the maximum outstanding. However, the restructuring package will be worked out with the consent of the bank having the second largest share.
- iii. If other banks have worked out the restructuring package, we may accept the package if it is in accordance with this policy.
- iv. All requests received by the RM will be scrutinized by them to ensure that these are prima facie in order and are eligible for consideration as per the prescribed criteria. RM shall seek requisite approvals from the Country Credit Officer (CCO). Suitable action shall be suggested by the CCO, where considered necessary including assessment of viability by engaging external consultants, wherever required, for working out detailed restructuring package.
- v. After receipt of sanctions, the Bank will complete documentation with the borrower and implement the restructuring package.
- vi. The whole process will have to be completed within 60 days of the receipt of the application, provided the unit has submitted all information and terms of sanction are complied with.

10. Monitoring & Review

The progress in rehabilitation and restructuring of SME accounts will be reviewed on a quarterly basis and the India Country Credit Committee (ICCC) will be kept informed by CCO.

11. Disclosure Requirements

The Debt Restructuring Scheme for SMEs is being displayed on the Bank's website under "Regulatory and Policy Guidelines" and a copy of scheme is also being forwarded to SIDBI for placing on their website.

The necessary disclosures in the published annual Balance Sheet of the Bank, under "Notes on Accounts", will be done, as under: -

- a) Total amount of assets of SMEs subjected to restructuring. [(a) = (b) + (c) + (d)]
- b) The amount of standard assets of SMEs subjected to restructuring.
- c) The amount of sub-standard assets of SMEs subjected to restructuring.
- d) The amount of doubtful assets of SMEs subjected.

Financial Controller will include the above reporting requirements in the Circular on Annual Closing. Consolidation work in respect of above will be done by CCO.