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POLICY

Rehabilitation of Sick SSI Units

Several internal and external factors have put considerable pressure on the performance of small scale industries (SSIs), resulting in a number of them becoming sick. Of late, the incidence of sickness in SSI sector is showing an increasing trend and a large number of SSI units, identified as sick, were not found to be potentially viable.

To address this, and other allied issues, the Reserve Bank constituted a Working Group on Rehabilitation of Sick SSI in November 2000 with Shri S.S.Kohli, Chairman, Indian Banks' Association, as its Chairman. The Group submitted its report in June 2001. The Reserve Bank has accepted all the major recommendations made by the Group, including a change in the criteria for identification and classification of sick units in the SSI sector. Based on the recommendations of the Working Group, revised guidelines for rehabilitation of sick and potentially viable SSI units have been drawn up as under :

Incipient Sickness

The branch officials should keep a close watch on the operations in the account and take adequate measures to achieve this objective. The managements of the units financed should be advised about their primary responsibility to inform the banks if they face problems which could lead to sickness and to restore the units to normal health. The organisational arrangements at branch level should also be fully geared up for early detection of sickness and prompt remedial

action. Banks/financial institutions (FIs) should identify the units showing symptoms of sickness by effective monitoring and provide additional finance, if warranted, so as to bring back the units to a healthy track. An illustrative list of warning signals of incipient sickness that are thrown up during the scrutiny of borrowal accounts and other related records e.g. periodical financial data, stock statements, reports on inspection of factory premises and godowns, etc., is given in the box which will serve as a useful guide to the operating personnel. Further, the system of asset classification introduced in banks will be useful for detecting advances, which are deteriorating in quality well in time. When an advance slips into the sub-standard category, as per norms, the branch should make full enquiry into the financial health of the unit, its operations, etc., and take remedial action. The branch officials who are familiar with the day-to-day operations in the borrowal accounts should be under obligation to identify the early warning signals and initiate corrective steps promptly. Such steps may include providing timely financial assistance depending on established need, if it is within the powers of the branch manager and an early reference to the controlling office where the relief required are beyond his delegated powers. The branch manager may also help the unit, in sorting out difficulties which are non-financial in nature and require assistance from outside agencies like government departments/undertakings, electricity boards, etc. The branch manager should also keep the term lending institutions informed about the position of the units wherever they are also involved.

Definition of Sick SSI Unit

A SSI unit should be considered '**sick**' if -

- (a) Any of the borrowal accounts of the unit remains substandard for more than six months, i.e., principal or interest, in respect of any of its borrowal accounts has remained overdue for a period exceeding one year. The requirement of overdue period exceeding one year will remain unchanged even if the present period for classification of an account as sub-standard, is reduced in due course; or
- (b) There is erosion in the net worth due to accumulated cash losses to the extent of 50 per cent of its net worth during the previous accounting year; and
- (c) The unit has been in commercial production for at least two years.

While the above definition of a SSI unit may be adopted for the purpose of reporting the data for the half-year ending March 31, 2002, for the purpose of formulating nursing programme, banks should go by the above definition with immediate effect.

Illustrative Warning Signals of Incipient Sickness in SSI Units

- ? Continuous irregularities in cash credit/overdraft accounts such as inability to maintain stipulated margin on continuous basis or drawings frequently exceeding sanctioned limits, periodical interest debited remaining unrealised.
- ? Outstanding balance in cash credit account remaining continuously at the maximum.
- ? Failure to make timely payment of instalments of principal and interest on term loans.
- ? Complaints from suppliers of raw materials, water, power, etc., about non- payment of bills.
- ? Non-submission or undue delay in submission or submission of incorrect stock statements and other control statements.

- ? Attempts to divert sale proceeds through accounts with other banks.
- ? Downward trend in credit summations.
- ? Frequent return of cheques or bills.
- ? Steep decline in production figures.
- ? Downward trends in sales and fall in profits.
- ? Rising level of inventories, which may include large proportion of slow or non-moving items.
- ? Larger and longer outstandings in bill accounts.
- ? Longer period of credit allowed on sale documents negotiated through the bank and frequent return by the customers of the same as also allowing large discount on sales.
- ? Failure to pay statutory liabilities.
- ? Utilisation of funds for purposes other than running the units.
- ? Not furnishing required information/data on operations in time.
- ? Unreasonable/wide variations in sales/receivables levels vis-à-vis level of operation of the unit.
- ? Non co-operation for stock inspections, etc.
- ? Delay in meeting commitments towards payments of instalments due, crystallised liabilities under Letter of Credit/Bank Guarantees, etc.
- ? Diverting/routing of receivables through non-lending banks.

Viability

A unit may be regarded as potentially viable if it would be in a position, after implementing a relief package spread over a period not exceeding five years from the commencement of the package, from banks/financial institutions (FIs), government (central/state) and other concerned agencies, 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 five-year period. The repayment period for restructured (past) debts should not exceed seven years from the date of implementation of the package. In the case of tiny/decentralised sector units, the period of reliefs/concessions and repayment period of restructured debts which were hitherto, two years and three years respectively, have been revised, so as not to exceed five and seven years respectively, as in the case of other SSI units. Based on these norms, banks/ FIs may decide whether a sick SSI unit is potentially viable or not. Viability of a unit identified as sick, should be decided quickly and made known to the unit and others concerned at the earliest. The rehabilitation package should be fully implemented within six months from the date the unit is declared as 'potentially viable'/'viable'. While identifying and implementing the rehabilitation package, banks/FIs are advised to do 'holding operation' for a period of six months. This will allow SSI units to draw funds from the cash credit account at least to the extent of their deposit of sale proceeds during the period of such 'holding operation'.

Delegation of Powers

One of the factors contributing to delay in the implementation of agreed rehabilitation packages was found to be the time taken for obtaining clearance from the controlling office for the relief and concessions. Banks/FIs may, therefore, delegate sufficient powers to senior officers at various levels, such as, district, divisional, regional, zonal and also at head office to sanction the bank's/FI's commitment to its share in the rehabilitation package.

Reliefs and Concessions

Only those units which are considered to be potentially viable should be taken up for

rehabilitation. Reliefs and concessions are not to be given in a routine manner and have to be decided by the concerned bank/FI based on the commercial judgment and merits of each case. Banks have the freedom to extend reliefs and concessions beyond the parameters in deserving cases. Only in exceptional cases, concessions/reliefs beyond the parameters should be considered. In fact, the viability study itself should contain a sensitivity analysis in respect of the risks involved that in turn will enable firming up of the corrective action matrix.

Units becoming sick on account of wilful mismanagement, wilful default, unauthorised diversion of funds, disputes among partners/promoters, etc., should not be considered for rehabilitation and steps should be taken for recovery of bank's dues. The definition of wilful default, broadly covers the following:

- (a) Deliberate non-payment of dues despite adequate cash flow and good networth.
- (b) Siphoning off of funds to the detriment of the defaulting unit.
- (c) Assets financed have either not been purchased or have been sold and proceeds have been misutilised.
- (d) Misrepresentation/falsification of records.
- (e) Disposal/removal of securities without bank's knowledge.
- (f) Fraudulent transactions by the borrower.

The views of the lending FI/bank in regard to wilful mismanagement of funds/defaults will be treated as final.

As the viability and the rehabilitation of a sick SSI unit would depend primarily on the unit's ability to continue to service its repayment obligations, including the past restructured debts, it may be ensured that there is no write-off or scaling down of debt, such as, by reduction in rate of interest with retrospective effect except in cases as under :

Interest Dues on Cash Credit and Term Loan

If penal rates of interest or damages have been charged, such charges should be waived from the accounting year of the unit in which it started incurring cash losses continuously. After this is done, the unpaid interest on term loans and cash credit during this period should be segregated from the total liability and funded. No interest may be charged on funded interest and repayment of such funded interest should be made within a period not exceeding three years from the date of commencement of implementation of the rehabilitation programme. Unadjusted interest dues such as interest charged between the date up to which the rehabilitation package is prepared and the date from which it is actually implemented, may also be funded as indicated above.

The rate of interest on term loans may be reduced, where considered necessary, by not more than three per cent in the case of tiny/decentralised sector units and by not more than two per cent for other SSI units, below the document rate.

Working Capital Term Loan (WCTL)

After the unadjusted interest portion of the cash credit account is segregated as indicated above,

the balance representing principal dues may be treated as irregular to the extent it exceeds drawing power. This amount may be funded as WCTL with a repayment schedule not exceeding 5 years. The rate of interest applicable may be 1.5 per cent to 3 per cent points below the prevailing fixed rate/ prime lending rate (PLR), wherever applicable, to all sick SSI units including tiny and decentralised units.

Cash Losses

Cash losses are likely to be incurred in the initial stages of the rehabilitation programme till the unit reaches the break-even level. Such cash losses excluding interest as may be incurred during the nursing programme may also be financed by the bank/FI, if only one of them is the financier. But if both are involved in the rehabilitation package, the FI concerned should finance such cash losses. Interest may be charged on the funded amount at the rates prescribed by Small Industries Development Bank of India (SIDBI) under its scheme for rehabilitation assistance.

Future cash losses in this context will refer to losses from the time of implementation of the package up to the point of cash break-even as projected. Such future cash losses should be worked out before interest (i.e., after excluding interest) on working capital etc., due to the banks and should be financed by the FI if it is one of the financiers of the unit. In other words, FIs should not be asked to provide for interest due to the banks in the computation of future cash losses and this should be taken care of by future cash accruals.

The interest due to the bank should be funded by it separately. Where, however, a commercial bank alone is the financier, the future cash losses including interest will be financed by it.

The interest on the funded amounts of cash losses/interest will be at the rates prescribed by SIDBI under its scheme for rehabilitation assistance.

Working Capital

Interest on working capital may be charged at 1.5 per cent below the prevailing fixed/prime lending rate wherever applicable. Additional working capital limits may be extended at a rate not exceeding the PLR.

Contingency Loan Assistance

For meeting escalations in capital expenditure to be incurred under the rehabilitation programme, banks/FIs may provide, where considered necessary, appropriate additional financial assistance up to 15 per cent of the estimated cost of rehabilitation by way of contingency loan assistance. Interest on this contingency assistance may be charged at the concessional rate allowed for working capital assistance.

Start-up Expenses and Margin for Working Capital

Units under rehabilitation may be provided with funds for start-up expenses (including payment of pressing creditors) or margin money for working capital in the form of long-term loans.

Where a FI is not involved, banks may provide the loan for start-up expenses. Margin money may either be provided by SIDBI under its refinance scheme for rehabilitation or by state government where it is operating a margin money scheme. Interest on fresh rehabilitation term loan may be charged at a rate 1.5 per cent below the prevailing fixed rate/PLR, wherever applicable, or as prescribed by SIDBI/NABARD where refinance is obtained from them.

All interest rate concessions would be subject to annual review depending on the performance of the units.

Promoters' Contribution

As per the extant guidelines of the Bank, promoter's contribution towards the rehabilitation package is fixed at a minimum of 10 per cent of the additional long-term requirements under the rehabilitation package in the case of tiny sector units and at 20 per cent of such requirements for other units. In the case of units in the decentralised sector, promoter's contribution is not insisted upon.

A need is felt for increasing the promoters' contribution towards rehabilitation from the present limits. It is, therefore, open to banks/FIs to stipulate a higher promoters' contribution where warranted. At least 50 per cent of the promoters' contribution should be brought in immediately and the balance within six months. For arriving at the promoters' contribution, the monetary value of the sacrifices from banks, FIs and government may be taken into account, in addition to the long - term requirement of funds under the rehabilitation package.

While evolving packages, it should be made a precondition that the promoters should bring in their contribution within the stipulated time frame. Further, banks should incorporate a 'Right of Recompense' clause in the sanction letter and other documents that, when the sick unit turns the corner and rehabilitation is successfully completed, the sacrifices undertaken by the FIs and banks would be recouped from the units out of their future profits/ cash accruals.

Advertisement on ATMs

The Reserve Bank has advised all scheduled commercial banks not to display products and services of manufacturers, dealers and vendors on their automated teller machine (ATM) screens for a fee. This amounts to advertising, which is not a permitted activity in which a bank can engage under section 6 (1) of the Banking Regulation Act, 1949. Banks may, however, utilise the ATM screens for displaying their own products.

Branch Banking

Period of Realisation of Export Proceeds Extended

Authorised Dealers (ADs) have been permitted to extend, without any reference to the Reserve Bank, the period of realisation of export proceeds beyond six months from the date of export. This relaxation in procedure would be applicable where the invoice value does not exceed US\$ 1,00,000. ADs may, however, grant such extension after obtaining an application from the

exporter and subject to the following conditions :

- (i) The AD is satisfied that the exporter has not been able to realise export proceeds for reasons beyond his control;
- (ii) The exporter submits a declaration that he will realise the export proceeds during the extended period; and
- (iii) The extension may be granted up to a period of three months at a time and while considering the extension beyond one year from the date of export, the total export outstandings of the exporter should not be more than 10 per cent of the average of export realisations during the preceding three financial years.

The ceiling of US \$ 1,00,000 would not apply where the exporter has filed a suit against the importer abroad. In such cases extension may be granted up to six months at a time, irrespective of the amount involved.

Cases which do not fall in the above category as well as those mentioned below, would require the prior approval of the regional office of the Reserve Bank.

- (a) Where the export invoices are under investigation by the Enforcement Directorate/Central Bureau of Investigation or other investigating agencies.
- (b) Where the invoice value exceeds US \$ 1,00,000.

ADs have been advised to report all the export bills outstanding beyond six months from the date of export in XOS statement as usual. Where the AD grants extension of time, he should indicate the date up to which extension has been granted in the 'Remarks' column.

Collateral Exemption Limit for SSI

To improve flow of credit to the small scale industries sector (SSI), the Reserve Bank has raised the exemption limit of borrowal accounts for obtaining collateral securities. The exemption limit has been raised to Rs. 5 lakh from Rs. 1 lakh for all SSI units. The exemption limit of borrowal accounts for obtention of collateral securities was raised in March 2000 from Rs.1 lakh to Rs.5 lakh for the tiny sector.

Assets of Deceased Customers

The Reserve Bank has advised all commercial banks not to insist upon legal representation for release of either the amount to the credit of the deceased depositor or his other assets. Other assets would include articles kept in safe custody, securities held against advances, etc. Banks may, however, call for succession certificate from legal heirs as a safeguard in cases where there are disputes and all legal heirs do not join in indemnifying the bank; or when the bank has reasonable doubt about the genuineness of the claimant/s being the only legal heir/s of the deceased customer.

Exchange Control

Two-Way Fungibility of ADRs/GDRs

The Reserve Bank has operationalised the guidelines for the limited two-way fungibility of American Depository Receipts/ Global Depository Receipts (ADRs/GDRs) as approved by the Government of India. Under the guidelines, re-issuance of ADRs/ GDRs would be permitted to the extent of ADRs/GDRs that have been redeemed into underlying shares and sold in the domestic market. No specific permission of the Reserve Bank would be required for re-conversion. The re-conversion of shares into ADRs/GDRs under this scheme would be distinct from portfolio investment by foreign institutional investors (FIIs). The transactions would be demand driven and, as such, would not require company involvement or fresh permissions. The custodian will monitor the re-issuance of ADRs/GDRs within the sectoral cap fixed by the Government of India. Further, each purchase transaction will be only against delivery and payment received in foreign exchange through banking channels.

Brokers registered with the Securities and Exchange Board of India (SEBI) would act as intermediaries in the two-way fungibility of ADRs/GDRs. Earlier, the Reserve Bank had given general permission to brokers to buy shares on behalf of overseas investors through its notification of March 2, 2001. As secondary market transactions, the acquisition of shares on behalf of overseas investors through the intermediary would fall within the regulatory purview of SEBI. Since the demand for re-conversion of shares into ADRs/GDRs would be from overseas investors and not the company, the expenses involved in the transaction would be borne by the investor. These transactions would be governed by the Income Tax Act, 1961.

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