



SME FINANCE DEPARTMENT

STANDARD OPERATING PROCEDURES

of

CREDIT GUARANTEE SCHEME
FOR SMALL & RURAL ENTERPRISES

Table of Contents

<u>PART A: ROLES AND RESPONSIBILITIES</u>	<u>3</u>
Organization and Role of the Technical Committee on Credit Guarantee	<u>3</u>
The Role of SME Finance Department	<u>3</u>
Organization and Role of the Credit Guarantee Office – Unit (DFSD (CGO unit))	<u>4</u>
Roles and responsibilities of Banking Inspection Department	<u>5</u>
Roles and responsibilities of Agricultural Credit Department	<u>5</u>
<u>PART B: GUIDELINES FOR PROCESSES AND PROCEDURES UNDER THE GUARANTEE SCHEME</u>	<u>6</u>
I. Selection of the PFIs	<u>6</u>
II. Target Market for the CGS	<u>7</u>
III. The Maintenance of PFI Records of Guarantee Limits and Claims	<u>7</u>
IV. Guaranteeing	<u>7</u>
V. Claims	<u>10</u>
VI. Recoveries	<u>11</u>
VII. Management Information System (MIS)	<u>12</u>
<u>PART C: SUPREMACY AND PRECEDENCE OF THE APPROVED CREDIT GUARANTEE SCHEME/ TECHNICAL COMMITTEE ON CREDIT GUARANTEE</u>	<u>12</u>
<u>Appendix: IMPORTANT TERMS & ACRONYMS</u>	
<u>DRAFT LETTERS for the DFSD (CGO Office)</u>	
<u>DRAFT REPORTING FORMATS FOR THE PFIs</u>	<u>13</u>

Standard Operating Procedures (SOPs) of the Credit Guarantee Scheme

PART A: ROLES AND RESPONSIBILITIES

1. Organization and Role of the Technical Committee on Credit Guarantee:

The **Technical Committee on Credit Guarantee (TCCG)** is the apex body (headed by DG (BPR & DF) or ED (DFG)) and responsible for taking all policy decisions regarding the operations/functioning of the CGS. The apex body also reviews performance of Credit Guarantee Scheme (CGS) and approve changes/modifications in the Scheme.

TCCG comprises of representatives from:

- UK's Department for International Development (UKAID),
- Pakistan Banking Council (PBA) and
- State Bank of Pakistan (SBP) – SME Finance Department
- SBP, BSC – Development Finance Department (DFSD)

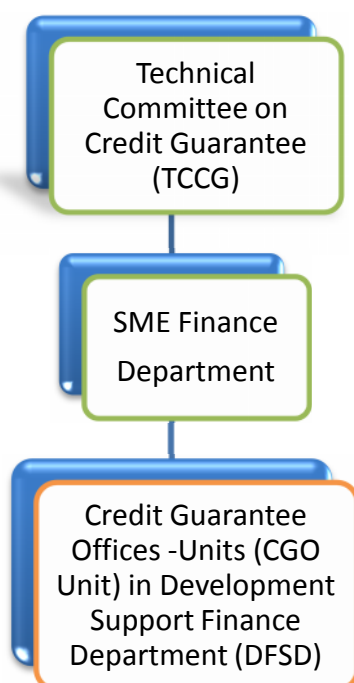
2. Role of SME Finance Department

- Serve as secretariat of TCCG and provide administrative support for organizing its meetings and ensuring implementation of its decisions
- Liaise among all stakeholders including PFIs, DFSD (CGO unit), PBA, donor agencies, government and Small Enterprises.
- Take part in policy decision making process as a representative of State Bank of Pakistan in the Technical Committee on Credit Guarantee (TCCG).
- Undertake the process of calling expression of interest from banks and evaluate the qualifying banks as per laid down criteria, along with providing support to ACD for rating banks for rural/agr. financing. Then, finalize recommendations for selection of banks to serve as Participating Financial Institutions (PFIs) and allocation of Credit Guarantee Limits (CGLs) for formal approval of the TCCG.
- SMEFD may consult ACD for selection of PFIs and finalization of their CGLs. *The guarantee limits of each PFI will be formally approved by TCCG which will be conveyed by SMEFD to PFIs and DFSD (CGO).*
- Hold awareness seminars/ road-shows etc under the supervision and direction of TCCG.
- Liaise with SMEs, PFIs, DFSD (CGO) and other stakeholders to assess the efficiency and effectiveness of scheme. SMEFD will take measures/ initiatives for improvements in the operational and policy matters of the scheme. In case of major policy changes in the Scheme, SMEFD will approach TCCG for its formal approval. DFSD (CGO unit) and the PFIs owing to their first hand experience in operational matters of the Scheme may also submit their recommendations to SMEFD for further improvements.
- Review performance of existing PFIs, select new PFIs for the next year and prepare recommendations of limit allocation to each PFI as envisioned above.

- Monitor performance of the PFIs on quarterly basis and review their guarantee limits based on their performance during the previous quarters.

3. Organization and Role of Credit Guarantee Office – Unit (DFSD (CGO unit)):

A Credit Guarantee Office (CGO), established under the supervision of Development Finance Support Department (DFSD) of SBP BSC (Bank), serves as operational arm of CGS. The DFSD (CGO) is responsible for handling all operational matters of CGS and oversee performance of PFIs. DFSD (CGO) also maintains proper MIS of CGS and reports to SMEFD about operations of CGS. The CGO is organized in a pattern similar to customary Units of SBP BSC under the administrative supervision of Director DFSD. Further, the DFSD (CGO) may also carry out surprise verification visits to the PFIs for ensuring compliance with the instructions of the scheme.

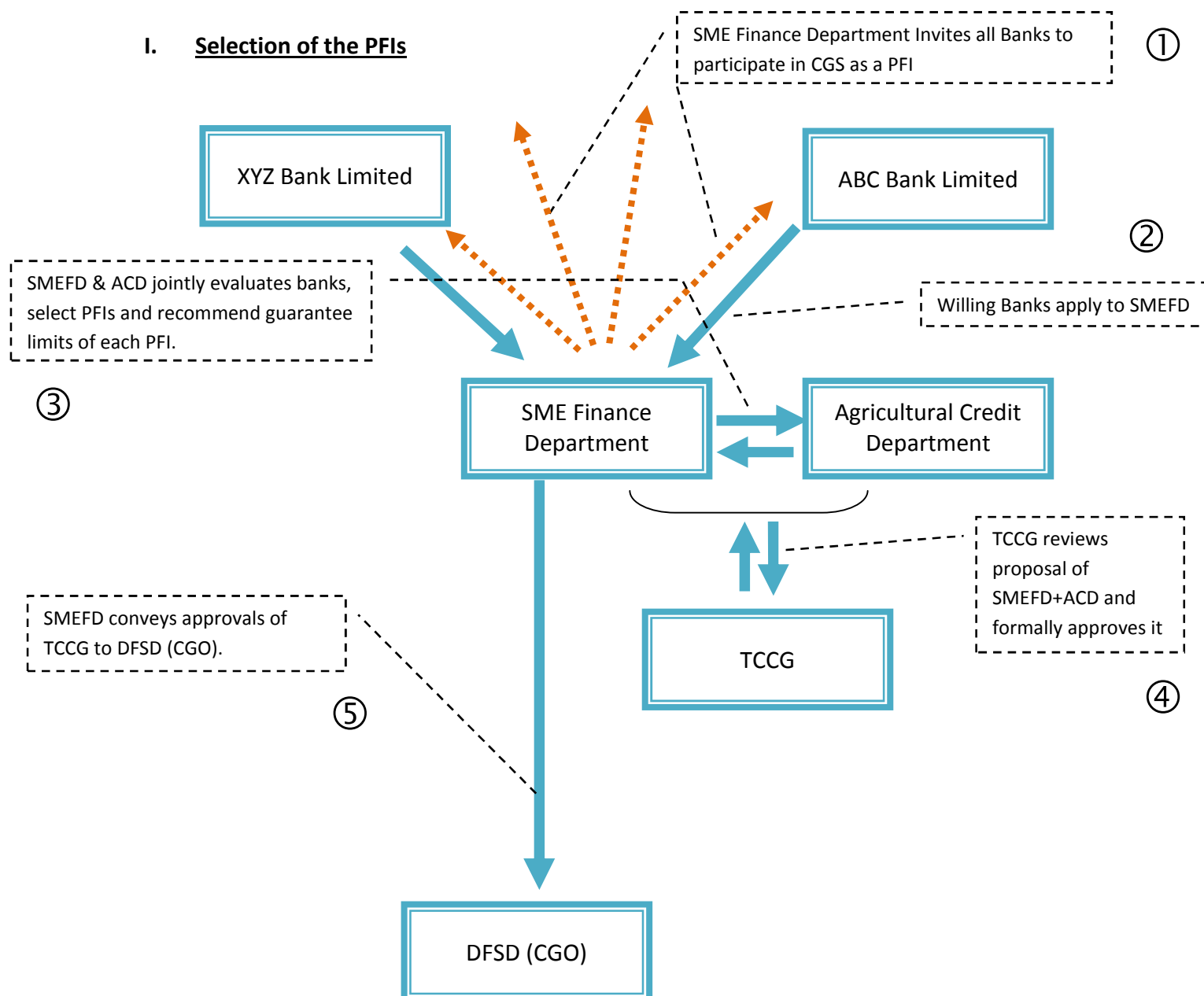


4. Roles and responsibilities of Banking Inspection Department

- Regular Inspection: BID conducts inspection of the guarantee portfolio on sampling basis using its own sampling techniques during regular inspection of the banks. The Report of the inspection is then provided to the SMEFD for necessary action – using it as an important input for reviewing the Scheme and assessing its effectiveness.
- Claims Inspection: DFSD (CGO unit) forwards all approved claim requests of PFIs to SMEFD which advises BID to carry out inspection of ***preferably all*** claim requests during their regular inspection and forward a report of inspection to the DFSD (CGO) for necessary action under intimation to SMEFD. On the basis of this report, the DFSD may cancel those claims that were made by PFIs in violation of the approved criteria and call back the funds by debiting accounts of the concerned bank.

5. Roles and responsibilities of Agricultural Credit Department

The ACD have its role in selection of PFIs and finalization of proposal for their CGLs. The department coordinates with SMEFD and the later takes responsibility for submission of the consolidated proposals for perusal/approval of TCCG.

PART B: PROCESSES UNDER THE GUARANTEE SCHEME**I. Selection of the PFIs**

The banks are selected to serve as the Participating Financial Institutions (PFIs) and Credit Guarantee Limits (CGLs) are allocated to each PFI. The selection of PFIs and allocation of CGLs is approved by the TCCG and only PFIs are eligible to apply for the Guarantee Facility to the extent of their allocated CGLs from SBP/SBP (BSC) for their eligible borrowers. The Procedure for selection of PFIs is as outlined below:

- At the start of the guarantee scheme, SMEFD invites banks to participate under the Scheme as PFIs.
- The banks are given a period of 1-2 week(s) to show their willingness for participation in the guarantee scheme and provide desired data to the SMEFD (as envisaged in the CG Scheme).
- The SMEFD coordinates with the Agricultural Credit Department for evaluation of data / information of the banks regarding the agri. Loans
- SMEFD forwards joint recommendations of at least 5-7 PFIs along-with their proposals of their respective CGLs to the TCCG for its final approval.
- After selection, SMEFD informs the CGLs to the DFSD (CGO unit) and respective PFIs giving a signal to the PFIs to approach SBP for availing the facility.
- The TCCG may, based on performance of a PFI, frequency and size of claims of all PFIs etc, revise allocated CGL and/or stop/ restrict utilization of the same by any one or all PFIs in its own discretion.

II. Target Market for the CGS

- The TCCG is the right forum for any review of the broader guidelines of target market given in the approved credit guarantee scheme.

III. Maintenance of PFI Records of Guarantee Limits and Claims

1. The Credit Guarantee Limits (CGL) of each PFI are conveyed by SMEFD to DFSD (CGO). The DFSD (CGO) maintains separate record of guaranteed loans of PFIs and the claims against those guarantees.
2. Any subsequent revisions in the allocated guarantee limits are incorporated in the records of the DFSD (CGO).

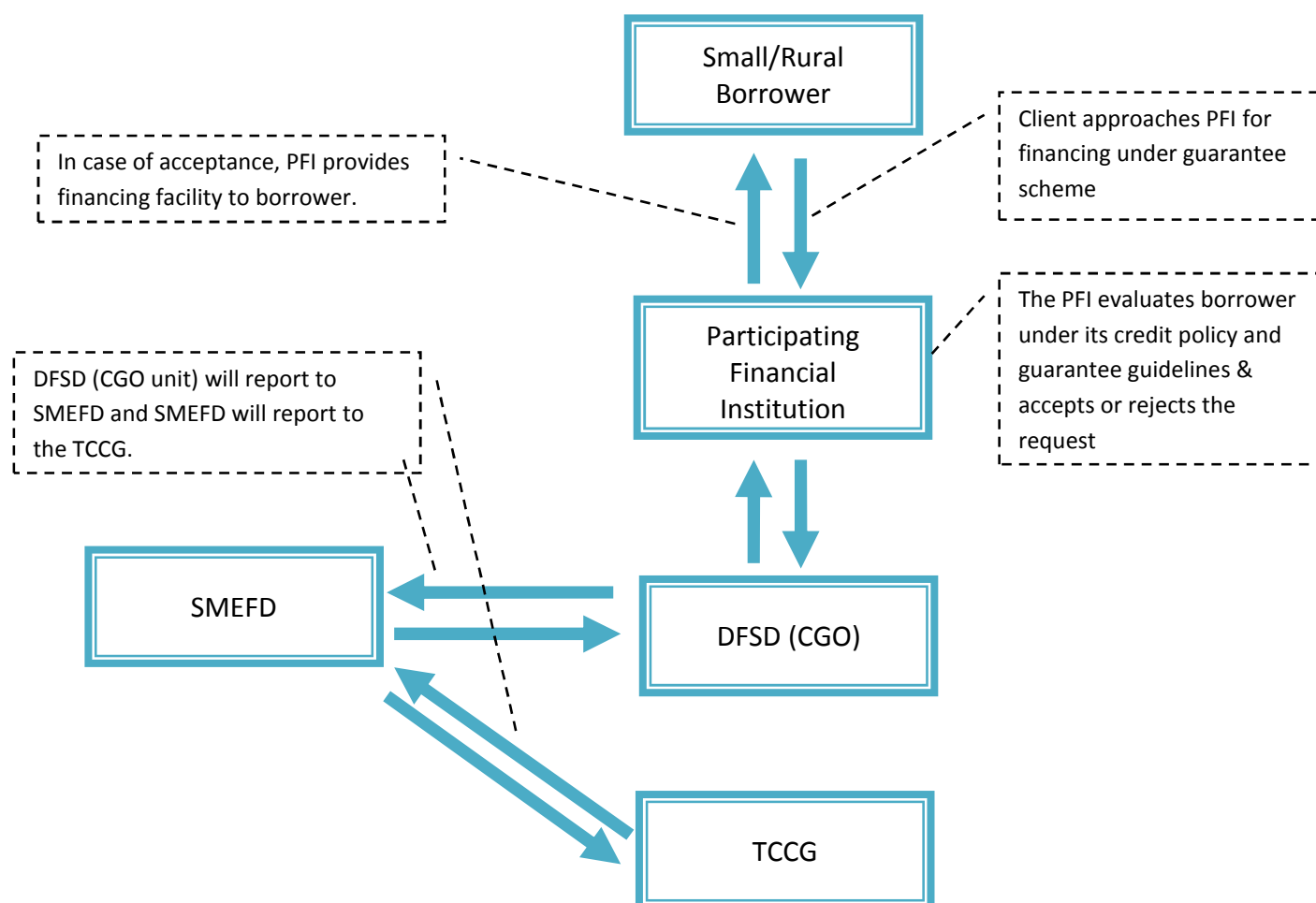
IV. Guaranteeing:

1. The selected PFIs shall be evaluating the borrowers eligible for lending under the Credit Guarantee Scheme in the light of following **Evaluation Criteria**.
 - i. The borrower is a Small Enterprise or a farmer with economic landholding
 - ii. The borrower has clean e-CIB record
 - iii. The borrower is eligible under the applicable PRs
 - iv. The borrower has regular and estimable positive cash flows
 - v. The borrower is eligible under Credit Policy of Bank.

- vi. The borrower is preferably a fresh customer; however an existing borrower can also be extended additional lending facility under the Scheme.
 - vii. The repayment tenure of the loan shall be up-to a maximum of 3 years.
 - viii. The loan limit for single Small Enterprise shall be Rs 15 million which may be utilized by the borrower for meeting working capital and/or medium term needs.
 - ix. The loan limit under the Scheme to the farmers shall not exceed Rs 2.0 million.
2. The SME Finance Department may introduce/ suggest further improvements in the general criteria and also develop sector specific criteria based on its experiences. However, any improvements/ changes in the **Borrower Evaluation Criteria** shall have to be approved by TCCG.
 3. The loan applicant shall preferably present a business plan, showing adequate cash flows and ability of debt servicing.
 4. The bank shall evaluate the individual proposals and if the bank feels the case meets the criteria, it will extend loan to the borrower, and the borrower shall become eligible for a credit guarantee facility.
 5. Since the system places primary responsibility on the PFIs and does not require evaluation on part of DFSD (CGO) prior to disbursement of the loan amount, the credit guarantee shall automatically stand issued for a customer which the bank has evaluated to be eligible and the PFI shall extend lending facility to the borrower treating him/her as a guaranteed customer under the Scheme.
 6. This Tacit Consent for a partial guarantee of maximum 40% to borrowers evaluated as eligible by the PFIs shall be subject to compliance with Borrower Evaluation Criteria. Each PFI shall ensure that the outstanding guarantee amount does not exceed its allocated guarantee limit at any time. The DFSD (CGO) shall have the right to withdraw its approval of guarantee if it is identified through inspection/ verification that the borrower was not eligible for financing under the guarantee scheme at the time of extension of the loan facility. In such an event, the PFI shall bear 100% of the credit risk of such borrower.
 7. **Authorized Contact Officials:** Each PFI shall nominate at least two senior officials in their head offices as Authorized Contact Officials/ Signatories (ACOs) to communicate with the Development Finance Support Department-CGO Office, SBP BSC (Bank), Karachi and State Bank of Pakistan, Karachi. The PFIs shall convey the duly verified signatures along-with names, designations and contact address (phone, mobile, fax, email) of nominated ACOs to both State Bank of Pakistan and CGO-Office. Only those guarantee/ claim etc requests of banks which are signed by at least two ACOs shall be entertained by CGO

Office. Branches/ regional offices and other officials of the banks are strictly prohibited to approach for the Guarantee Facility under the scheme.

8. **Customer Identification Number:** Each bank shall issue a unique Customer Identification Number (CIN) in the format of ABC-xxxx-yyy where ABC is the abbreviated/acronym reference of the bank 'ABC Bank Limited', xxxx is four digit number issued to each successive customer in ascending order and the yyy is the three digit loan number for the customer bearing number xxxx (e.g. XYZ Bank Limited may issue Identification Number XYZ-0158-005 for the 5th guaranteed loan to its 158th customer).
9. The PFIs shall on monthly basis (i.e. within first 5 days of every month) apply for the guarantee facilities for their borrowers who were extended lending facilities during the previous month. The applications for guarantee facility shall accompany a covering letter requesting for the facility and duly filled-in format CG-1 (attached as Appendix II). Both the Covering Letter and duly filled in format shall be signed by at least two Authorized Contact Persons of the bank. Each PFI shall have the primary responsibility of ensuring that its total Guaranteed Loans does not exceed its allocated CGL at any point in time.

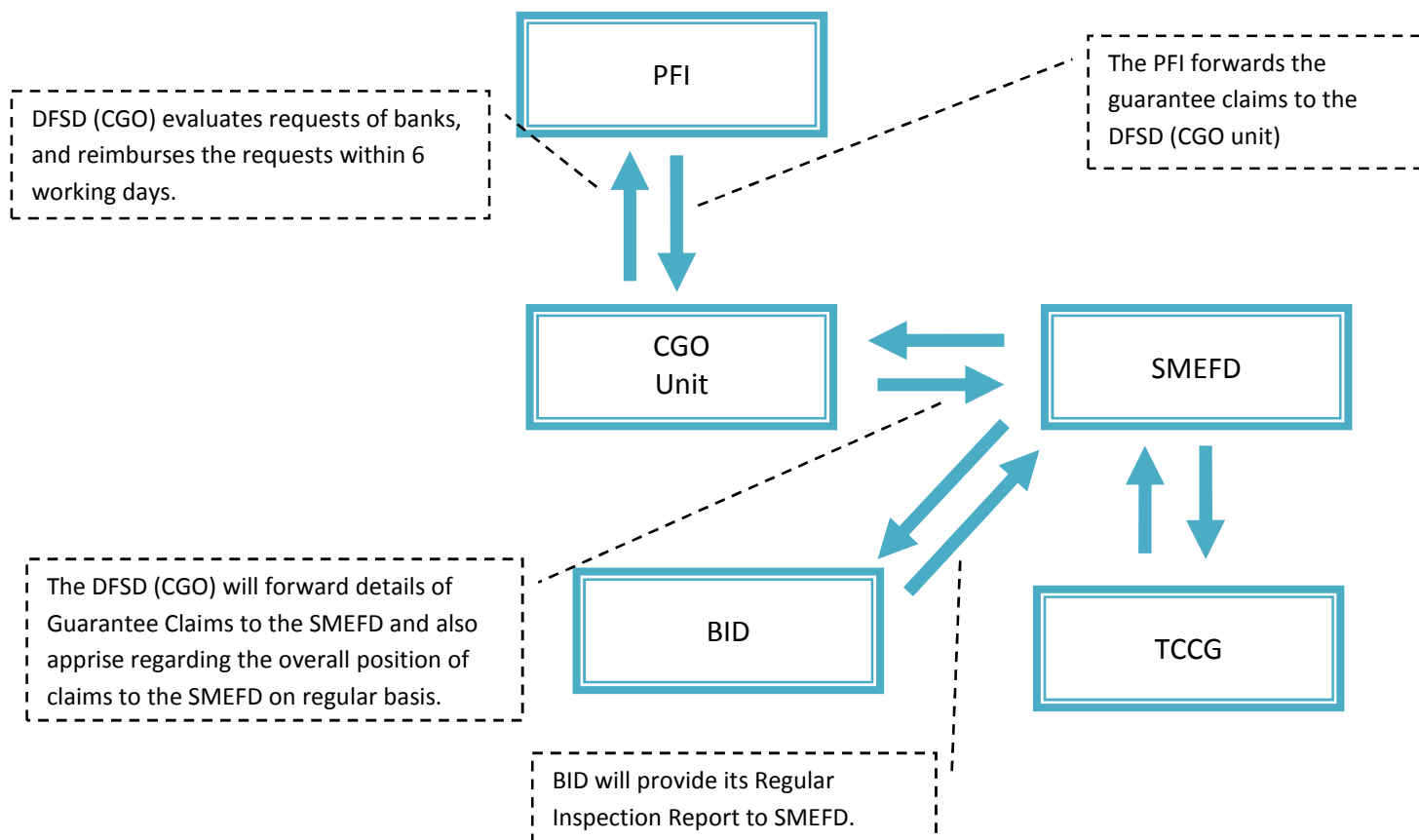


10. Each PFI shall report its outstanding position of all previously guaranteed loans on monthly basis as per the format CG-2 (attached as Appendix III).
11. The DFSD (CGO unit) shall ensure that the outstanding guaranteed amount of any PFI does not exceed its allocated limit as conveyed to it by SMEFD.
12. DFSD (CGO unit) shall consolidate the position of fresh issuance and existing position of guarantee facility, status of claims and recoveries etc of all the PFIs and shall forward the report to SMEFD (on monthly basis) for review and presentation to the TCCG (in its regular/special meetings).
13. The DFSD (CGO) shall intimate the concerned bank regarding acceptance of their Request of Guarantee through Issuance of Guarantee Letter (Appendix VI).

V. Claims:

1. Under the scheme borrowers shall preferably be those who fail to provide required collaterals to the banks. In the absence of collaterals, the ***internal controls and monitoring mechanism*** of the banks under the scheme should be strong enough to cater the adverse selection issues.
2. In the event that a particular borrower falls under the category of Loss as per the relevant PRs, the bank shall have the right to lodge a claim of the guaranteed amount. The PFIs shall lodge claims on quarterly basis (i.e. within first 10 days of every quarter) against all loans falling under the Loss category in the previous quarter as per the format CG-3 duly audited and authenticated by their Internal Audit Department.
3. After receipt of claim, the DFSD (CGO) shall internally scrutinize the claim request in the light of information submitted by bank to assess any deviation and seek clarification from the PFI, if so required. In case the claim is as per the instructions of the Guarantee Scheme, the DFSD (CGO) shall reimburse the guaranteed amount as per the request of the PFI within 6 working days after receipt of complete information relating to the claim request. However, DFSD (CGO) shall intimate the requesting PFI (Appendix IX) that the reimbursement of the guarantee claim is subject to final clearance by Banking Inspection Department based on their on-site inspection of the guarantee claims during regular inspection of the bank.
4. Separately DFSD (CGO) Unit shall send an intimation summary regarding approval of the claim to SMEFD for inspection of individual claims of each PFI through BID.
5. **Claims Inspection:** BID shall pay special attention to the claims lodged by PFIs under the scheme during their regular inspection of the bank in order to ensure that the lodged claims were genuine.

Banking Inspection Department shall submit report of guarantee claims to CGO for necessary action. In case any deviation in the reimbursed claims of PFI is found in the inspection report, the amounts of such claims shall be debited from the account of the concerned PFI maintained with the SBP BSC (Bank) with intimation to the PFI (Appendix VIII). DFSD (CGO) shall seek guidance from SMEFD in cases where clear violation by the PFIs cannot be determined.



Note: Each Claims Request (Covering Letter and accompanied filled in format) shall bear authorized signatures of at least two ACOs of the PFI and will also accompany Audit Verification Certificate issued by the Internal Audit Department of the PFI.

VI. Recoveries

The re-imbursements of the claim(s) by State Bank shall not obviate lending bank from right of recovery of the defaulted amount. The banks shall continue with their regular procedure for recovery of loan and status shall be reported to the CGO on yearly basis. In the event of recoveries from delinquent borrowers, all such recoveries shall be treated as the recovery of principal and the concerned bank shall remit proportionate share of the Guarantee Scheme to State Bank immediately (within two working days) along-with duly filled-in format CG-4, delaying which may attract penal action from State Bank. The costs incurred on recovery efforts shall be borne by the concerned PFI and shall not be passed on to the Guarantee Fund.

VII. Management Information System (MIS):

1. The PFIs shall report their outstanding position of guaranteed limits as per the format CG-2 to the DFSD (CGO) on monthly basis (i.e. within first 5 days of every month).
2. In addition to the regular reporting, the DFSD (CGO) shall have the right to call information from the PFIs for its own monitoring and reporting to the SMEFD/TCCG. DFSD (CGO unit) shall also issue instructions to the PFIs for submission of data as per the requirements of SMEFD/ TCCG.
3. The DFSD (CGO) shall maintain proper records of guarantee portfolio and submit periodic monthly reports of total outstanding guarantees, claims approved, reimbursements against recoveries by the PFIs and the new guarantees issued to the SMEFD.

PART C: SUPREMACY AND PRECEDENCE OF THE APPROVED CREDIT GUARANTEE SCHEME/TECHNICAL COMMITTEE ON CREDIT GUARANTEE

It is pertinent to mention here that objective of these operating procedures is to facilitate smooth functioning of the credit guarantee Scheme. The duly approved Credit Guarantee Scheme and improvements/ modifications thereon by the Technical Committee on Credit Guarantee/SMEFD will have precedence/supremacy in events of any confusion/ contradiction. SMEFD will bear responsibility in case any interpretation/ clarification is required in the guarantee Scheme, SOPs and the instructions of the TCCG.

Important Terms & Acronyms

Credit Guarantee Scheme for Small & Rural Enterprises has been alternatively referred to as “Credit Guarantee Scheme”, “the Scheme” and “CGS” in the main Guarantee Scheme Document and the accompanied Standard Operating Procedures.

Credit Guarantee Fund: The seed money of the Credit Guarantee Scheme has been alternatively referred to as “the CG Fund”, “the Guarantee Fund” and “the Fund” in the main Guarantee Scheme Document and the accompanied Standard Operating Procedures

A Small Enterprise (SE) is a business entity which meets both the following parameters:

Number of Employees	Annual Sales Turnover
*Upto 20	Upto Rs. 75 million

**including contract employees.*

Participating Financial Institution: The Banks which have been selected and allocated Credit Guarantee Limits for extension of Guaranteed Loans under the Scheme are referred to as Participating Financial Institutions or PFIs.

Authorized Contact Officials (ACOs) are the Officials of a PFI who have been authorized to communicate with SBP / SBP BSC (Bank) for availing Credit Guarantee Facility, lodging claims against delinquent borrowers, explanations/ clarifications etc.

Credit Guarantee Limits: State Bank of Pakistan allocates Credit Guarantee Limits (CGLs) to each Participating Financial Institution for availing Credit Guarantee facility against the loans extended to the borrowers eligible under the Scheme.

Customer Identification Number (CIN) is a unique number issued by a PFI to its borrower under the scheme. The format of CIN is ABC-xxxx-yyy where ABC is the abbreviated/acronym reference of the bank ‘ABC Bank Limited’, xxxx is four digit number issued to each successive customer in ascending order and yyy (e.g. XYZ Bank Limited may issue Identification Number XYZ-0158-005 to its 5th loan extended to 158th customer).

Acronyms:

- DFSD = Development Finance Support Department in the SBP BSC (Bank).
- SMEFD = SME Finance Department of SBP
- BID =Banking Inspection Department of SBP
- ACD=Agriculture Credit Department of SBP
- PRs = Prudential Regulations
- TCCG = Technical Committee on Credit Guarantee.

- CGO = Credit Guarantee Office established in the DFSD.
- PBA = Pakistan Banks Association
- PFI = Participating Financial Institution
- UKAID= UK's Department for International Development
- ACO = Authorized Contact Officials
- CIN = Customer Identification Number
- CGL = Credit Guarantee Limit