

CREDIT INFORMATION REVIEW



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BANKING

Package for Exporters

Interest Rate

The Reserve Bank of India reduced interest rates for export credit by 1.0 percentage point across the board. This reduction will apply to both, pre-shipment and post-shipment credits.

The maximum rate that the bank should charge to exporters will be 2.5 percentage points below its prime lending rate for pre-shipment credit up to 180 days and for post-shipment credit up to 90 days. Earlier, the ceiling rate was 1.5 percentage point below the prime lending rate. This further concession will apply to all export credit granted by banks effective September 26, 2001 and up to March 31, 2002.

In addition to the above facility for rupee credit, exporters would continue to have the facility of foreign currency loans in the currency of their choice at highly internationally competitive rates. The rate for foreign currency loans to exporters will continue to be LIBOR plus a maximum of 1.0 percentage point. Thus, currently dollar - denominated foreign currency loans can be availed by exporters at no higher than 3.0 per cent (LIBOR rate) + 1.0 per cent i.e., 4.0 per cent.

Large Value Exports

The Reserve Bank of India in consultation with the Government of India also announced a special financial package for large value exports of six select products, viz., pharmaceuticals, agro chemicals, transport equipment, cement, iron and steel and electrical machinery. Manufacturer exporters of these products with export contracts of Rs.100 crore and above in value term in one year would be eligible for the special financial package. The validity period of the package will be one year from October 1, 2001.

Exporters covered under the special financial package will be extended credit at concessional rate of interest for an extended period upto 365 days at pre-shipment as well as post-shipment stages as against the maximum periods of 270 days and 180 days, respectively, applicable for normal export credits. Further, the rate of interest of export credit for period beyond 270 days and upto 365 days at pre-shipment stage will be the same as those for normal pre-shipment credit for period beyond 180 days and upto 270 days. Post-shipment

credit will also be extended for periods beyond 180 days and upto 365 days at the same rate of interest as applicable for normal post-shipment credit for the period beyond 90 days and upto 180 days.

Under this dispensation, the rates of interest for the extended period of pre-shipment and post-shipment credit would stand reduced to a maximum of PLR + 0.5 per cent. Currently, these interest rates are decided by the banks on a commercial basis. The rate generally is upto a maximum of PLR + 4 per cent. This measure applicable for large value exports in select products is in addition to the across the board reduction of one percentage point in ceiling interest rates on export credit.

Further, Exim Bank will be permitted to extend buyers' credit of Rs.200 crore without reference to the Reserve Bank of India. Similar permission will also be granted to the participating banks. Exim Bank while approving export contracts will have freedom to decide minimum advance/down payment, security and availability of ECGC cover subject to post facto report to the Reserve Bank. Indian exporters will also be permitted to import raw material on credit terms for period beyond 180 days at the rate of interest upto LIBOR + 1 per cent under the special financial package, as against the current stipulation of LIBOR + 0.75 per cent (ceiling).

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Bank Finance for Margin Trading | The RBI-SEBI Technical Committee examined the issues involved in introducing margin trading. Keeping in view the present circumstances in the capital market and the economy, the Committee recommended that financing of margin trading by banks should be permitted in India.

Based on the recommendations of the RBI-SEBI Technical Committee, on an experimental basis, it has been decided to permit banks to extend finance to stockbrokers for margin trading within the overall ceiling of 5 per cent prescribed by the Reserve Bank in May 2001 for exposure of banks to capital market. Banks may accordingly provide finance to brokers for margin trading in actively traded scrips forming part of the NSE Nifty and the BSE Sensex, subject to certain guidelines.

The guidelines would be valid for a period of 60 days, (i.e., up to November 22, 2001). The working of the guidelines would be reviewed in the light of experience gained and fresh instructions will be issued thereafter.

Banks desirous of extending finance to stockbrokers for margin trading should observe the following guidelines :

- (a) **Minimum Margin**
A minimum margin of 40 per cent should be maintained by banks on funds lent for margin trading.
- (b) **Risk Management**
 - (i) The shares to be purchased with margin should be in dematerialised mode, under pledge to the lending bank.
 - (ii) The banks should put in place appropriate systems for monitoring the margin (40 per cent). If the stockbroker / client fails to meet the margin calls, the lending bank should liquidate the collateral / shares purchased immediately and adjust the loan.
 - (iii) The bank's Board should prescribe necessary safeguards to ensure that no "nexus" develops between inter-connected stock broking entities / stockbrokers and the bank in respect of margin trading. Margin trading should be spread out by a bank among a reasonable number of stockbrokers and stock broking entities. Stockbrokers, availing of margin trading facilities from a bank should be prohibited from lending, directly or indirectly, to their own connected entities, relatives or business associates or those of the promoters / directors of the bank through this facility. Banks should also put in place appropriate systems to ensure end-use of funds lent under margin trading.

Valuation and Disclosure

In addition to the disclosure requirements prescribed earlier in May 2001 by the Reserve Bank banks should disclose the total finance extended for margin trading in the "Notes on Account" to their balance sheets.

Other conditions

In other respects, the terms and conditions set out earlier by the Reserve Bank remain unchanged and would also apply.

Credit Facilities to Minority Communities | The Reserve Bank of India has advised Indian scheduled commercial banks other than Regional Rural Banks (RRBs) to issue suitable instructions to all their controlling offices and branches to effectively implement the guidelines regarding granting of loans to minority communities. These instructions have been issued on the backdrop of a study conducted by the Reserve Bank with a view to assessing the progress made by banks in granting loans to minority communities and in implementation of its instructions on this subject. The study was conducted in pursuance of the recommendations of the National Commission for Minorities to have a wider assessment of economic problems of minorities.

The Reserve Bank in its guidelines instructed that the Lead Banks in minority concentration districts should give a special thrust to accelerate the flow of credit to minority communities. Monitoring and review of the credit flow to minority communities should also be strengthened. These issues should be taken up for discussion in SLBC/DLRC/DCC meetings especially in the districts identified as having a concentration of minority population and flow of credit should be vigorously monitored. Suitable lecture sessions may be included in the relevant training programmes for staff to make them more receptive to the credit needs of the minority communities. The Lead Banks of the minority concentration districts should make concerted efforts to ensure that the minority communities have access to bank credit for taking up productive activities by providing publicity to anti-poverty programmes of the Government and organising Entrepreneur Development Programmes.

The Lead Bank in each of the 44 districts identified as having a concentration of minority population should have an officer to exclusively look after the problems regarding credit flow to minority communities. Also, the names of designated officers in these districts should be furnished to the National Commission for Minorities.

Conflict Diamonds from Liberia | The Reserve Bank of India has advised all banks to obtain a fresh modified undertaking from all their clients who are given credit facility for diamond export including conflict diamonds received from Liberia. This is in the wake of the UN Security Council further imposing ban on direct or indirect import of all rough diamonds from Liberia whether originated in Liberia or not.

The UN Security Council Resolutions adopted so far on conflict diamonds require that any violation of the ban / prohibition imposed should be reported to the UN immediately. In view of this, all the commercial banks should report to the Reserve Bank promptly any violation of provisions of UN Regulations as and when noticed.

No Ration Cards for Identity | At the instance of the Government, banks have been advised to instruct their branches not to insist upon ration cards for the purposes of verifying identity of individual or proof of residence. Instead, other valid documents such as passport, driving licence, voter's identity card, identity card issued by income tax authorities can be considered for verifying address / identity of individuals.

Penal Interest for PSLs | It has been decided that banks should not charge penal interest for loans under priority sector (PSL) up to Rs.25,000. Banks will, however, be free to levy penal interest for loans exceeding Rs.25,000 as per the policy formulated by them for charging of penal interest. Boards of banks have already been authorised to formulate such a policy for charging penal interest for default in repayment, non-submission of financial statements, etc., governed by well accepted principles of transparency, fairness, incentive to service the debt and due regard to difficulties of customers.

Issue of Payment Instruments | The Reserve Bank has cautioned the primary (urban) co-operative banks that they should not issue banker's cheques/pay orders/demand drafts against instruments presented for clearing unless their proceeds are collected and credited to the account of the parties concerned. The Reserve Bank has observed that some banks had issued banker's cheques/pay orders for large sums against instruments presented for clearing without realising the proceedings. The Reserve Bank has also advised that banker's cheques/pay orders/demand drafts should not be issued by debit to cash credit /overdraft accounts which are already overdrawn beyond the limit sanctioned or likely to be overdrawn with the issue of such instruments as applied for by the parties.

EXCHANGE CONTROL

FII Investment | The Reserve Bank of India in consultation with the Government of India has decided that Foreign Institutional Investors (FIIs) in Indian companies can now be increased beyond 24 per cent upto the sectoral cap/statutory ceiling, as applicable, provided this has the approval of the Indian company's board of directors as also its general body.

POLICY

Prime Minister's Rojgar Yojana | The Reserve Bank has advised all Indian scheduled commercial banks to urgently review the progress in the implementation of the Prime Minister's Rojgar Yojana (PMRY) scheme and issue necessary instructions to their controlling offices/branches to ensure that the target set for them is achieved. Steps taken by the banks in achieving the target under the scheme should be advised to the Reserve Bank at an early date.

As per the decision taken in the 11th High Powered Committee on the PMRY held on February 6, 2001, the banks having less than 5 branches should not be allocated targets under PMRY if total targets of all the branches of a bank having less than 5 branches constitute 2 per cent or less of the total target of the state.

Provision for Inter-branch Accounts | It has been decided to reduce the period allowed for making 100 per cent provision for the net debit position in their inter-branch accounts from two years to one year from the year ending March 31, 2002. It may be recalled that as per the Reserve Bank's instructions of 1993, banks are required to reconcile their inter - branch entries within a period of six months. To provide urgency to the efforts needed to be made by banks to comply with these instructions, the Reserve Bank in 1999 advised banks to make 100 per cent provision for unreconciled entries (both debit and credit) outstanding for more than three years as on March 31 every year. The period was brought down to two years from the year ended March 31, 2001. Accordingly, the Reserve Bank has advised all commercial banks other than Regional Rural Banks and local area banks to arrive at the category-wise net position of unreconciled entries outstanding in the inter-branch accounts for more than one year as on March 31, 2002 and make a provision equivalent to 100 percent of the aggregate net debit under all categories. The banks are further advised to ensure that:

- (i) the credit balance in the blocked account is also taken into account and
- (ii) the net debit in one category is not set-off against net credit in another category.

Reconciliation of Nostro Accounts | The Reserve Bank of India has advised all commercial banks, except Regional Rural Banks and Local Area Banks, to transfer balances in the sundry creditors / unclaimed deposits accounts appearing in the books of the banks as on September 30, 2001 to distinct Blocked Accounts under "Other Liabilities and Provisions - Others" in the balance sheet. The balances in the Blocked Accounts will be reckoned for the purpose of maintenance of cash reserve ratio / statutory liquidity ratio. It has been further clarified that these balances in the sundry creditors / unclaimed deposits accounts need to represent the net credit balance arising out of the netting of entries pertaining to the period prior to April 1996 and the credit entries originated on or after April 01, 1996 and remaining unreconciled in nostro / mirror accounts for more than three years.

The Reserve Bank has also advised that banks should earnestly pursue reconciliation of the entries transferred to the blocked accounts and any adjustment from the blocked accounts should be permitted only with the authorisation of two officials, one of whom should be from outside the branch concerned, preferably from the controlling / head office if the amount exceeds Rs. one lakh.

It may be recalled that the Reserve Bank, in an earlier circular, had advised the banks to:

- (a) net off the credit /debit entries in each of their nostro accounts pertaining to the period up to March 31, 1996 which were remaining unreconciled as on March 31, 2000, against the debit/credit entries in the respective mirror account,
- (b) arrive at the aggregate net debit and aggregate net credit positions, taking care not to set off the net debit position in one account with the net credit position in another account and vice-versa,
- (c) transfer the aggregate net debit to profit & loss account and the aggregate net credit to Sundry Creditors Account in the banks' accounts for the year ended March 31, 2000,
- (d) make 100 per cent provision each year in respect of unreconciled debit entries in the nostro and mirror accounts which were originated on or after April 01, 1996 and are outstanding for more than 3 years and transfer each year unreconciled credit entries in the nostro and mirror accounts which were originated on or after April 01, 1996 and are outstanding for more than 3 years to an account like unclaimed deposit account. As the balances carried in the sundry creditors /unclaimed deposits accounts represent unreconciled entries which could be large in a few cases and therefore susceptible for fraud, the Bank examined the issue subsequent to the banks seeking guidance on the treatment of balances carried.

Corporate Debt Restructuring | The Reserve Bank of India has finalised a corporate debt restructuring (CDR) scheme based on the extensive discussions the Government of India and the Bank had with banks and financial institutions. The CDR scheme is to be implemented by all commercial banks, excluding Regional Rural Banks (RRBs) and Local Area Banks (LABs) .

CDR will be a non-statutory, voluntary system based on debtor-creditor agreement and inter-creditor agreement. It will be applicable to only to standard and sub-standard accounts. The objective of the scheme is to ensure a timely and transparent mechanism for restructuring of corporate debts of viable corporate entities affected by internal or external factors. Such entities should be outside the purview of Board for Industrial and Financial Restructuring (BIFR), Debt Recovery Tribunal (DRT) and other legal proceedings. The scheme would be applicable only to multiple banking accounts / syndicates / consortium accounts with outstanding exposure of Rs.20 crore and above with the banks and financial institutions.

All standard and sub-standard accounts subjected to the CDR process would continue to be eligible for fresh financing of funding requirements by the lenders as per their normal policy parameters and eligibility criteria.

There would be no requirement of the account / company being sick, non-performing assets (NPA) or being in default for a specified period before reference to the CDR Group. However, potentially viable cases of NPAs will get priority. In no case, the requests of any corporate indulging in willful default or misfeasance will be considered for restructuring under CDR.

Structural Framework

The CDR scheme will have a three-tier structure consisting of CDR Standing Forum, CDR Empowered Group and CDR Cell. The viability and rehabilitation potential of the corporate would be examined by the CDR empowered group constituted to consider individual cases of corporate debt restructuring.

DISCUSSION

Creation and Enforcement of Security Interest

A Working Group under the chairmanship of Shri M.R. Umarji, Executive Director

appointed by the Government of India recently submitted a bill mainly for the purpose of empowering the banks and financial institutions to take possession of securities and sell them in the event of default. The salient features of the Bill are:

- * The Bill defines security interest as any charge or interest created over any property to secure any financial assistance granted to the borrower. The definition includes mortgage, charge, hypothecation assignment, lien and other transfer of interest in property to secure a loan.
- * Property is defined to include both, movable and immovable property.
- * Secured creditor is defined as any bank or financial institution, non-banking financial companies registered with the Reserve Bank of India, any debenture trustee or other entity holding securities on behalf of banks and financial institutions.
- * In terms of the Bill, default means default in payment of principal or interest or any other dues which result in classification of the concerned account as a non-performing asset.
- * The draft Bill also provides for setting up of a central computerised registry for the purpose of registration of security interest created over movable and immovable properties and proposes to make available the right of enforcement only in cases where there is registration.
- * Under the existing law, there are no specific provisions for certain types of security interest like hypothecation. The security by way of hypothecation is one of the major security interest taken by the banks and financial institutions but there is no law governing it. The draft Bill provides that any type of security interest, including, hypothecation which is created for securing repayment of a loan should be treated as security interest.

Corporate Debt Restructuring

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This group will also approve the restructuring package. The banks representatives in the empowered group should be senior level executives with authorisations from their boards to make commitments on behalf of the banks towards debt restructuring.

The standing forum will lay down policies and guidelines and guide and monitor the progress of CDR. The standing forum will be assisted by a CDR core group in conducting the meetings and taking decisions relating to policy. Individual cases of CDR will be decided by a CDR empowered group. This group would be mandated to look into each case of debt restructuring, examine the viability and rehabilitation potential of the company and approve the restructuring package within a specified time frame of 90 days or at best 180 days of reference to the empowered group. The CDR standing forum and the CDR empowered group will be assisted by a CDR Cell in all their functions. The CDR cell will make the initial scrutiny of the proposals received from borrowers / lenders by calling for proposed rehabilitation plan and other information and put up the matter before the CDR empowered group within one month to decide whether rehabilitation is prima facie feasible. If so, the CDR cell will proceed to prepare detailed rehabilitation plan with the help of lenders and if necessary, experts to be engaged from outside. If not feasible, the lenders may start recovery of dues.

The scheme has also detailed accounting treatment of accounts restructured under CDR.

- * If such security interest is registered under the central computerised registry, in the event of default, secured creditors would have a right to take possession of the securities after giving notice of 90 days and sell the securities for recovery of the loan.
- * Provision has been made for appointing a receiver after taking possession of the securities pending their sale.
- * If there is any resistance from the borrower in handing over possession, the secured creditor can approach the Chief Metropolitan Magistrate or District Magistrate for assistance in taking possession.
- * Any appeal against the action of the bank/financial institution in taking possession of securities can be filed before the Debt Recovery Tribunal after the sale of securities. In other words, the borrowers cannot object to conversion of securities by sale into money.
- * Since the Bill seeks to give drastic powers to the banks and financial institutions it also provides for the rights of the borrowers. It provides that the borrowers should get a copy of the security agreement and periodical statements of accounts with rates of interest charged. The Bill also provides that the central government should prescribe by rules, the procedure for taking possession and sale of securities.
- * Except in case of English mortgage, under the provisions of the Transfer of Property Act, mortgagees do not have power to sell the mortgaged property without the intervention of court. The draft law recognises all kinds of mortgages, including mortgage by deposit of title deeds, as a security interest. It provides for registration of notice of such mortgage with the central computerised registry. By virtue of these provisions, banks and financial institutions would have power to take possession of mortgaged properties and sell them after following the procedure prescribed by the proposed law.
- * A provision has also been made for the purpose of registration of existing security interests under the proposed law within a period of six months.
- * The Bill has suggested that the new computerised central registry system should be operated concurrently with existing registration systems under the Registration Act, Companies Act, Motor Vehicles Act, Merchant Shipping Act, etc. In other words, under the proposed law the rights, obligations and priorities of parties would be governed by the existing provisions relating to registration, the right to take possession and sell the securities would be available under the new law.
- * It is expected that the new computerised central registry system would stabilise in due course and at a later date, the other registration systems can be integrated with the new registry.
- * All actions under the proposed law would be subject to general law of limitation and hence no provision has been made prescribing limitation periods for the action under the proposed law.
- * Provisions of proposed law will not be mandatory and it will be permissible for the banks not to register the secured loan transactions under the new registry.
- * It is not proposed to apply the new law to small value transactions below rupees one lakh. Other exemptions from the applicability of the law are stated in the schedule to the Act. The Central Government has been given power to add or delete any entry in the schedule.

The draft Bill has been placed on the website of the Reserve Bank (www.rbi.org.in) for views/comments of organisations and interested persons.