CREDIT INFORMATION REVIEW

268
NOVEMBER
2001

Policy

Apropos the mid-term review of the Monetary and Credit Policy for 2001-02 on October 22, 2001, the Reserve Bank of India has taken the following actions :

Unhedged Forex Exposures of Corporates

The Reserve Bank of India has advised all scheduled commercial banks, excluding the regional rural banks and local area banks, that the banks with large exposures to corporates should monitor and review on a monthly basis, through a suitable reporting system, the unhedged portion of the foreign currency exposures of those corporates whose total foreign currency exposure is relatively large (say, above US$ 25 million or its equivalent). Earlier, banks were advised to evolve a suitable framework for regularly monitoring the market risks, especially forex risk exposure of corporates that had no natural hedges.

Over a period, considerable flexibility has been given to the corporates to hedge their forex exposure in the market. Instruments available to the corporates for hedging their exchange risks include forward cover, currency options, foreign currency-rupee swaps, hedging of the loan exposures, etc. Banks are also allowed to hedge their asset-liability portfolio, after obtaining necessary policy approval in this regard from their top management. The Reserve Bank had, however, observed that sometimes a noticeable portion of the corporate foreign currency commitments tend to remain unhedged by the corporates on the basis of their perceptions of the market and these could impact the overall financial status of the corporates under severe uncertainties.

Balance Sheet Disclosures

In a communication to all scheduled commercial banks, other than regional rural banks, the Reserve Bank of India has advised the following :

The banks should furnish the following disclosures in the 'Notes on Accounts' in their balance sheets. This additional information should be furnished in the prescribed proforma from the year ending March 2002 showing (i) movement of provisions held towards NPAs and (ii) movement of provisions held towards depreciation on investments. These would be in addition to the disclosures already being made in the 'Notes on Accounts' in the balance sheet, the details of the maturity pattern of loans and advances, investments, deposits and borrowings, movements in non-performing assets (NPAs), exposure to sensitive sectors, etc.

Settlement of NPAs

The Reserve Bank guideline is to ensure transparency and credibility of financial positions of banks. The Reserve Bank of India has advised all commercial banks that the broad framework for compromise or negotiated settlement of Non-performing assets (NPAs) outlined July 1995 will continue to be in place.

The Reserve Bank had, in July 2000 circulated simplified, non-discretionary and non-discriminatory guidelines to provide a one-time impetus to reduction of the stock of chronic NPAs by recovery of dues relating to public sector banks. The guidelines covered accounts upto Rs. 5 crore in all sectors including the small scale sector, but excluded cases of willful default, fraud or malfeasance. The settlement scheme laid out by these guidelines was operative till June 2001 and all applications received upto this date were to be processed by September 2001. Some representations had been received for further extension of the scheme.

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Given that the purpose of the guidelines on settlement of NPAs was to provide an opportunity for "one-time settlement" within a specified time period, and that sufficient time was already provided, the Reserve Bank decided not to extend this scheme. Banks are free to design and implement their own policies for recovery and write-off incorporating compromise and negotiated settlements with the approval of their boards, particularly for old and unresolved cases falling under the NPA category. In this respect, banks can also take the experience with the one-time settlement scheme into account. It is important to ensure that any scheme formulated by bank boards is simple, non-discriminatory and transparent so that all eligible cases are given equal treatment.

Compromise through Lok Adalats

The Reserve Bank has advised all scheduled commercial banks and all India financial institutions that they can take up matters where outstandings are Rs 10 lakh and above with lok adalats organised by the Debt Recovery Tribunals / Debt Recovery Appellate Tribunals. The advice was issued to clarify the doubt raised by banks whether, in view of the limitation of ceiling of Rs. 5 lakh for disposal by Lok Adalats, they should participate in the Lok Adalats convened by various DRTs/ DRATs for resolving cases involving Rs. 10 lakh and above.

Prudential Norms

Treatment of restructured accounts

The Reserve Bank has clarified that its instructions issued in April and May 2001 regarding regulatory treatment of restructured standard and sub-standard loans would be applicable to all type of credit facilities including working capital limits, extended by commercial banks to industrial units, provided they are fully covered by tangible securities.

Further, trading involves only buying and selling of commodities and the problems associated with manufacturing units such as bottleneck in commercial production, time and cost escalation, etc., are not applicable to them, these guidelines should not be applied to restructuring / rescheduling of credit facilities extended to traders.

While assessing the extent of security cover available to the credit facilities, which are being restructured / rescheduled, collateral security would also be reckoned, provided such collateral is a tangible security properly charged to the bank and is not in the intangible form like guarantee, etc., of the promoter/ others.

These instructions were issued after discussing the existing guidelines on prudential norms relating to income recognition, asset classification and provisioning, etc. with the Bank Audit Committee.

Accounting of Broken Period Interest

The Reserve Bank has further advised the banks to strictly follow the guidelines for accounting of broken period interest. It has advised that the banks should not capitalise the broken period interest paid to seller as part of cost, but treat it as an item of expenditure under Profit and Loss Account.

Income Recognition

The investments are also subject to the prudential norms on income recognition. Therefore, banks should not book income on accrual basis in respect of any security, irrespective of the category in which it is included, where the interest / principal is in arrears for more than 180 days. With effect from March 31, 2004, banks should not book income on accrual basis if the interest / principal is in arrears for more than 90 days.

Interest on Matured Deposits

Banks may devise their own policy in making provisions or otherwise for interest payable on matured deposits based on the past trend / experience and follow the same policy consistently.

Credit Card Outstandings

Banks should show all dues from credit card operations including the dues from other banks / organisations under "Advances". They should, however, not include any item, which is in the nature of 'Revenue' under 'Advances'.

Issue of Debit Cards

The Reserve Bank of India has removed the stipulation of minimum net worth of Rs.100 crore for introduction of on-line debit cards where straight through processing (STP) is done. Banks now need not seek prior approval of the Reserve Bank for introducing on-line debit cards. In a circular to all scheduled commercial banks, the Reserve Bank has stated that banks may launch the debit card product with the approval of their respective boards and should only send a copy of the board agenda note and board resolution to the Reserve Bank. The banks, however, need to adhere to the minimum net worth criterion of Rs.100 crore for introducing off-line mode of operation of debit cards and in such cases they can not issue smart/debit cards in tie-up with other non-bank entities.

It may be recalled that the Reserve Bank had in October 2000 advised that only commercial banks with minimum networth of Rs.100 crore should issue debit cards; whereas the condition of taking prior approval of the Reserve Bank was removed in November 1999.

The Reserve Bank in its circular to commercial banks, has further reiterated that for introducing debit cards where authorisation and settlement are off-line or where either authorisation or settlement is off-line, banks should obtain prior approval of the Reserve Bank. For this purpose, they should submit to the Reserve Bank details on mode of authorisation and settlement, authentication method employed, technology used, tie-ups with other agencies/service providers, if any, together with board note/resolution. Further, the banks should also adhere to the stipulation of the minimum networth of Rs 100 crore for introducing off-line mode of operation of debit cards.

Note on Credit Risk Management

As a step towards enhancing and fine-tuning the existing risk management practices in banks, a Working Group on Credit Risk was constituted in the the Reserve Bank drawing experts from select banks and financial institutions for preparing detailed guidance notes on credit risk management by banks. The working group has identified further steps, which should be taken by banks for improving their existing risk management framework, suiting the Indian conditions. The draft guidance note on credit risk is available on the Reserve Bank's web site http://www.rbi.org.in

Branch Banking

Loan System for Delivery of Bank Credit

The Reserve Bank of India has reviewed its guidelines relating to the 'Loan System' against the backdrop of the current environment of short-term investment opportunities available to both corporates and banks. It has decided that banks can, if they so desire, change the composition of working capital by increasing the cash credit component beyond 20 per cent or by increasing the 'loan component' beyond 80 per cent, for working capital limits of Rs. 10 crore and above. Banks are, however, expected to appropriately price each of the two components of working capital finance, taking into account the impact of such decisions on their cash and liquidity management.

The guidelines on loan system are:

(i) *Loan and Cash Credit*

(a) In the case of borrowers enjoying working capital credit limits of Rs.10 crore and above from the banking system, loan component should normally be 80 per cent. Banks, however, have the freedom to change the composition of working capital by increasing the cash credit component beyond 20 per cent or to increase the loan component beyond 80 per cent, if they so desire. Banks are, however, expected to appropriately price each of the two components of working capital finance, taking into account the impact of such decisions on their cash and liquidity management.

(b) In the case of borrowers enjoying working capital credit limit of less than Rs.10 crore, banks may persuade them to go in for the loan system by offering an incentive in the form of lower rate of interest on the loan component, as compared to the cash credit component. The actual percentage of 'loan component' in these cases may be settled by the bank with its borrower clients.

(c) Strict application of loan system may create difficulties for the borrowers with cyclical and seasonal business activities or activities that have inherent volatility. Banks may, with the approval of their respective boards, identify such business activities, which may be exempt from the loan system of delivery.

(ii) *Ad hoc Credit Limit*

As at present, ad hoc / additional credit for meeting temporary requirements can be considered by the financing bank only after the borrower has fully utilised / exhausted the existing limit.

(iii) *Sharing of Working Capital Finance*

The ground rules for sharing of cash credit and loan components may be laid down by the consortium, wherever formed, subject to guidelines on bifurcation between loan and cash credit components. The level of individual bank's share would continue to be governed by the norm for single borrower / group exposure.

(iv) *Rate of Interest*

Banks are allowed to prescribe Prime Lending Rates and spreads over Prime Lending Rates separately for 'loan component' and 'cash credit component'.

(v) *Period of Loan*

The minimum period of loan for working capital purposes may be fixed by banks in consultation with borrowers. Banks may decide to split the loan component according to the need of the borrower with different maturity bases for each segment and allow roll over.

(vi) *Security*

Banks may themselves decide on the requirement of security, sharing of charge, documentation, etc. if necessary, in consultation with the other participant banks.

(vii) *Export Credit*

Bifurcation of working capital limit into loan and cash credit components, would be effected after excluding the export credit limits (pre-shipment and post-shipment). Export credit limit would continue to be allowed in the form granted so far.

(viii) *Bills*

Bills limit for inland sales may be fully carved out of the 'loan' component' . Bills limit also includes limits for purchase of third party (outstation) cheques/bank drafts. Banks must satisfy themselves that bills limit is not misultilised.

(ix) *Renewal*

The 'loan component' may be renewed/rolled over at the request of the borrower.

(x) *Investment of Short-Term Surplus Funds*

The banks, at their discretion, may permit the borrowers to invest their short-term/temporary surplus in short-term money market instruments such as, commercial paper (CP). certificates of deposit (CD) and in term deposit with banks, etc.

(xi) *Applicability*

The loan system would be applicable to borrowal accounts classified as 'standard' or 'sub-standard'.

Financing for Purchase of Land

It has been decided that finance granted by banks under the scheme of financing farmers for purchase of land for agricultural purpose would be eligible for classification under "Direct-Agriculture" under "Priority Sector Advances ". This would be subject to following conditions:

(a) The loans are granted to share croppers, tenant farmers, small and marginal farmers, i.e., who own maximum of 5 acres of non-irrigated land or 2.5 acres of irrigated land including proposed area of land to be purchased.

(b) The purchase of land should not be in fragmented holdings and there should be resultant increase in production / productivity.

(c) The purchase of land should be for cultivation / development of agricultural as well as fallow land or for establishing / diversifying into other allied activities. Banks should ascertain the end use of funds.

The Reserve Bank has advised all scheduled commercial banks to classify such advances under "Direct Agricultural Advances" in the half-yearly statements on priority sector lending.

R. No. 35646/79 Licensed to post without prepayment - Licence No. 193 Regd. No. TECH/47-505/MBI-2001
Posted on 29th and 30th November 2001 at BYCULLA SORTING POST OFFICE

Foreign Exchange

Certification of SOFTEX Forms

The Reserve Bank of India has advised all authorised dealers (ADs) that designated officials of Ministry of Information Technology, Government of India at the Software Technology Parks of India (STPIs) or at Free Trade Zones (FTZs) or Export Processing Zones (EPZs) or Special Economic Zones (SEZs) have been authorised to certify exports declared on SOFTEX forms by the units located in STPIs / EPZs / SEZs. In terms of the Exim Policy designated officials of STPIs /EPZs /SEZs may also certify the SOFTEX forms in respect of export oriented units (EOUs) which are registered with them. Accordingly, EOU software exporters may approach the designated officials of STPIs/EPZs/SEZs where they are registered, for certification of software exports on SOFTEX Forms.

Realisation of Export Proceeds

The Reserve Bank of India has on September 24, 2001 decided to relax the period of realisation and repatriation of full value of exports of select products up to 365 days from the date of shipment as a temporary measure. However, the relaxation in the period of realisation will be available to the manufacturer exporters of the specified products as:

- Pharmaceuticals (including drugs, fine chemicals).
- Agro-chemicals (including inorganic and organic chemicals).
- Transport equipment (including commercial vehicles, two and three wheelers, tractors, railway wagons, locomotives).
- Cement (including glass, glassware, ceramics and refractories).
- Iron & Steel (including iron & steel bars/rods and primary and semi-finished iron & steel) and
- Electrical machinery (including transmission line towers, gear, transformers),

They should also have export contracts of Rs.100 crore and above in value term in one year for exports to be made on or after October 1, 2001 for a period of one year subject to review. Earlier, the period for realisation and repatriation of exports of goods was six months within which the amount representing full export value of the goods needed to be realised and repatriated to India.

Settlement of Insurance Claims in Forex

The Reserve Bank has advised all authorised dealers in foreign exchange that settlement of claims in foreign currency in respect of general insurance policies in foreign currency other than those covered by the provisions of General Insurance Manual can now be permitted by insurance companies subject to the following conditions:

(i) The policy has been issued in foreign currency with specific approval of the Reserve Bank;

(ii) The claim has been made for the loss occurred during the policy period;

(iii) The claim has been admitted by the competent authority of the insurance company;

(iv) The claim has been settled as per the surveyors' report and other substantiating documents;

(v) Claims on account of reinsurance are being lodged with the reinsurers and would be received as per reinsurance agreement;

(vi) The remittances are being made to the non-resident beneficiary under the policy. For resident beneficiaries the claim may be settled in Rupee equivalent of foreign currency due. Under no circumstances payment in foreign currency be made to a resident beneficiary; and

(vii) While reporting the transaction in R-Returns, the Reserve Bank approval for issue of policy may be quoted.

Authorised Dealers may accordingly allow remittances towards settlement of claims subject to compliance of the conditions stipulated by the Indian insurance companies.

Earlier such requests were referred to the Reserve Bank and approvals were granted by the Reserve Bank on merits of each case and insurance companies were permitted to issue policies denominated in foreign currency and receive premium in foreign currency.

No Stapling of Note packets

The Reserve Bank has directed all commercial banks including regional rural banks and local area banks that with immediate effect :

(a) They should do away with stapling of any note packet and instead secure note packets with paper bands;

(b) They should sort notes into re-issuables and non-issuables, and issue only clean notes to public. Soiled notes in unstapled condition may be tendered at the Reserve Bank in inward remittances through currency chests; and

(c) They should forthwith stop writing of any kind on watermark window of bank notes.

It was observed that banks still continue to follow the practice of stapling fresh note packets and multiple stapling of re-issuable note packets which reduces life span of the notes. It also enables unscrupulous persons to insert half notes pasted on papers into note packets.

FOREX Notes and Coins for Travellers Abroad

Authorised dealers and Full Fledged Money Changers are now permitted to release foreign exchange in the form of foreign currency notes and coins to travellers abroad upto US dollars 2000 or its equivalent without permission of the Reserve Bank of India. The Reserve Bank of India has amended its instructions to this effect with a view to simplifying procedures. The existing limit for releasing foreign exchange in the form of foreign currency notes and coins is US dollar 500 or its equivalent.

This instruction will be applicable to travellers to countries other than Iraq, Libya, Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States. The Reserve Bank of India has clarified that travellers to Iraq and Libya are already allowed to take US$5,000 or its equivalent; whereas travellers to Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States are allowed to take the entire foreign exchange in foreign currency notes and coins.

Edited and published by **Alpana Killawala** for the **Reserve Bank of India,** Press Relations Division, Central Office, Shahid Bhagat Singh Marg, Mumbai-400 001 and printed by her at **Alco Corporation**, A-2, 331, Shah & Nahar Ind. Estate, Lower Parel (West), Mumbai - 400 013. **Annual Subscription : Rs. 12, Readers desirous of subscribing may remit the subscription, by way of cheque/DD payable at Mumbai to the Director, DRRP (Sales Section), DRRP, Reserve Bank of India, Amar Building, Sir P. M. Road, P. B. No. 1036, Mumbai - 400 001. Also Available on Internet at www.cir.rbi.org.in**