Contents

Policy
Exchange Control

Policy

Consolidated Supervision

The Reserve Bank has advised all scheduled commercial banks excluding regional rural banks (RRBs) and local area banks (LABs) to implement the revised guidelines on consolidated accounting and other quantitative methods to facilitate consolidated supervision.

Scope

Initially, consolidated supervision would be mandated for all groups where the controlling entity is a bank. In due course, banks in mixed conglomerates would be brought under consolidated supervision, where :

(a) the parents may be non-financial entities, or

(b) the parents may be financial entities falling under the jurisdiction of other regulators like Insurance Regulatory and Development Authority (IRDA) or Securities and Exchange Board of India (SEBI), or

(c) the supervised institution may not constitute a substantial or significant part of the group.

Components

(a) Consolidated financial statements which are intended for public disclosure.

(b) Consolidated prudential reports for supervisory assessment of risks, which may be transmitted to banks (or other supervised entities) by other group members.

(c) Application of certain prudential regulations like capital adequacy, large exposures/risk concentration, etc., on group basis.

Banks are required to put in place an appropriate management information system (MIS) to support their compliance with the consolidated accounting and reporting requirements.

Consolidated Financial Statements

All banks coming under the purview of consolidated supervision of the Reserve Bank, whether listed or unlisted, should prepare and disclose Consolidated Financial Statements (CFS) from the financial year commencing from April 1, 2002 in addition to solo financial statements.

CFS is required to be prepared in terms of Accounting Standard (AS) 21 and other related Accounting Standards prescribed by the Institute of Chartered Accountants of India (ICAI), viz., AS 23 and AS 27. For the purpose, the terms ‘parent’, ‘subsidiary’, ‘associate’, ‘joint venture’, ‘control’ and ‘group’ would have the same meaning as ascribed to them in the Accounting Standards of the ICAI.

A parent presenting CFS should consolidate all subsidiaries – domestic as well as foreign, except those specifically permitted to be excluded under AS 21. The reasons for not consolidating a subsidiary should be disclosed in the CFS. The responsibility of determining whether a particular entity should be included or not for consolidation would be that of the Management of the parent entity and the statutory auditors should comment in this regard if they are of the opinion that an entity which ought to have been consolidated had been omitted.

Components of CFS

CFS should normally include consolidated balance sheet, consolidated statement of profit and loss, principal accounting policies, notes on accounts, etc.

Reference Date

The financial statements used in the consolidation should be drawn up to the same reporting date. If it is not possible, AS 21 allows adoption of six month old balance sheet of subsidiaries and prescribes that adjustments should be made for the effects of significant transactions or other events that have occurred during the intervening period. In case the balance sheet dates of parent and subsidiaries are different, inter-group netting may be done as on the balance sheet date of the parent entity. In cases where the balance sheet date coincides with that of the bank, nationalised banks may publish their CFS without waiting for the Comptroller and Auditor General's audit of the accounts of their subsidiaries. However, banks have to ensure completion of statutory audit of the accounts of such subsidiaries before consolidation with the parent's accounts.

Accounting Policies

CFS should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to do so, that fact should be disclosed together with the proportions of the items in the CFS to which the different accounting policies have been applied.

For the purpose of preparing CFS using uniform accounting policies, banks may rely on a 'statement of adjustments' for nonuniform accounting policies, furnished by the statutory auditors of the subsidiaries.

If different entities in a group are governed by different accounting norms laid down by the concerned regulator for different businesses then, where banking is the dominant activity, accounting norms applicable to a bank should be used for consolidation purposes in respect of like transactions and other events in similar circumstances. In situations where no accounting norms have been prescribed by the regulatory authority and different accounting policies are followed by different entities of the group, balance of business may be used as a deciding factor for application of accounting norms. For dissimilar items and circumstances, different accounting policies would have to be followed.

For the purpose of valuation, the investments in associates other than those specifically excluded under AS 23 should be accounted for under the "Equity Method" of accounting in accordance with AS 23. Investment in RRBs sponsored by banks would also be treated as investments in associates for the purpose of CFS and accounted by "Equity Method" as prescribed under AS 23.

The valuation of investments in subsidiaries which are not consolidated and associates which are excluded under AS 23, should be as per the relevant valuation norm issued by the Reserve Bank.

The valuation of investments in joint ventures should be accounted for under the 'proportionate consolidation' method as per AS 27 on "Investments in Joint Ventures" issued by ICAI.

As regards disclosures in the 'notes on accounts' to the CFS, banks may be guided by general clarifications issued by ICAI from time to time.

The CFS has to be submitted to the Reserve Bank within one month from the publication of the bank's annual accounts.

Consolidated Prudential Reports

In addition to the CFS, banks coming under the purview of consolidated supervision of the Bank should also prepare Consolidated Prudential Reports (CPR). Consolidated Prudential Reports would be initially introduced on half-yearly basis from March 31, 2003 as part of off-site

reporting system on the lines of the existing DSB returns for the entities. The frequency of reporting would be subsequently reviewed and may be increased.

CPR for half-year ended March has to be submitted by end June. If audited results of entities under the CPR are not available, banks should submit the provisional CPR with unaudited results of such entities, by end June. However, CPR for the half-year ended March with audited results has to be submitted by end September and for half-year ended September has to be submitted by end of December. Banks should develop software for auto consolidation of CPR at their end.

The Reserve Bank confines CPR to all groups where the controlling entity is a bank. If the bank is a parent company within a group, the bank should submit CPR for the entities under its control.

CPR for a consolidated bank should include information and accounts of related entities, viz., subsidiaries, associates and joint ventures of the bank, which carry on activities of banking or financial nature. Banks should justify the exclusion of any entity for the purpose of CPR. All related entities of the bank may be consolidated with the parent on the lines prescribed in the various Accounting Standards issued by the ICAI, viz., subsidiaries should be consolidated on a line by line basis (AS 21), associates should be consolidated by the equity method (AS 23) and joint ventures should be consolidated by the proportionate consolidation method (AS 27).

For the purpose of preparation of CPR, the consolidation may exclude group companies which are engaged in (a) insurance business and (b) businesses not pertaining to financial services. The valuation of investment in related entities which are not consolidated should be as per the relevant valuation norm issued by the Reserve Bank.

In respect of related entities which operate under severe long term restrictions which significantly impair their ability to transfer funds to the parent, banks should disclose separately the book value of the amounts due from such related entities and the net amounts recoverable from them. Banks may also consider making appropriate provisions for the shortfall.

Application of Prudential Norms

For the purpose of application of prudential norms on a group wide basis, a 'consolidated bank' is defined as a group of entities which include a licensed bank, which may or may not have subsidiaries. A consolidated bank is required to follow the prescribed prudential norms/limits as indicated below :

(a) Capital adequacy

(b) Large exposures

(c) Liquidity ratios, mismatches, statutory liquidity ratio (SLR), cash reserve ratio (CRR) (where applicable).

Capital Adequacy

Banks have already been advised to voluntarily build into their own balance sheet, on a notional basis, the risk weighted components of their subsidiaries at par with the risk weights applicable to the bank's own assets. Banks were also advised to provide for capital shortfall in the subsidiary in their own books in a phased manner beginning from the year ending March 2001 to rectify the impairment to their net worth on switch over to consolidated accounting.

A consolidated bank should maintain a minimum Capital to Risk-weighted Assets Ratio (CRAR) as applicable to the parent bank on an ongoing basis from the year ending March 31, 2003. While computing capital funds, parent bank may consider the following points : (a) Banks are required to maintain a minimum CRAR of 9 per cent.

Non-bank subsidiaries are required to maintain the capital adequacy ratio prescribed by their respective regulators. In case of any shortfall in the capital adequacy ratio of any of the

subsidiaries, the parent should maintain capital in addition to its own regulatory requirements to cover the shortfall.

Statement about ownership and other particulars concerning
Credit Information Review

FORM IV

1. Place of publication	:	Mumbai
2. Periodicity of publication	:	Monthly
3. Editor, publisher and printer's name, nationality and address	:	Alpana Killawala, Indian Reserve Bank of India Press Relations Division, Shahid Bhagat Singh Road, Mumbai - 400 001.
4. Names and addresses of individuals who own the publication	:	Reserve Bank of India Press Relations Division, Shahid Bhagat Singh Road, Mumbai - 400 001.

I, Alpana Killawala, hereby declare that the particulars given above are true to the best of my knowledge and belief.

sd/-
Alpana Killawala
Date : March 1, 2003 Signature of Publisher

(b) Risks inherent in deconsolidated entities (i.e., entities which are not consolidated in the CPR) in the group need to be assessed and any shortfall in the regulatory capital in the deconsolidated entities should be deducted (in equal proportion from Tier 1 and Tier 2 capital) from the consolidated bank's capital in the proportion of its equity stake in the entity.

Large Exposures

As a prudential measure aimed at better risk management and avoidance of concentration of credit risks, in addition to adherence to prudential limits on exposures assumed by banks, consolidated banks should also adhere to the following prudential limits on :

(a) Single and group borrower exposures,
(b) Capital market exposures, and
(c) Exposures by way of unsecured guarantees and unsecured advances.

The operational details in this regard are -

(i) The consolidated bank's exposure to a single borrower/debtor should not exceed 15 per cent of its capital funds. The consolidated bank's exposure to a borrower/debtor group should not exceed 40 per cent of its capital funds. The aggregate exposure on a borrower/debtor group can exceed the exposure norm of 40 per cent by an additional 10 per cent (i.e., up to 50 per cent) provided the additional exposure is for the purpose of financing infrastructure projects. Computation of capital funds, exposure, etc, would be on par with the methodology adopted for banks.

Special Schemes for Financing Women

Some public sector banks have formulated special schemes for extending finance to women. The following table narrates the salient features of some of these schemes :

Name of the Bank	Scheme	Salient Features
Bank of India	Priyadarshini	Under this scheme, women are assisted for setting up small scale industries, village and cottage industry including purchase of machinery, public transport vehicles, etc. The bank offers 1 per cent concession in rate of interest to limits over Rs.2 lakh for women.
Bank of Baroda	Special Scheme	Under this scheme, the bank encourages rural women for dairy pursuit in Gujarat.
Central Bank of India	Kalyani	This scheme was introduced by the bank in 1995-96 for betterment of women enterpreneurs and for catering to the requirements of women engaged in different activities.
Oriental Bank of Commerce	Oriental Mahila Vikas Yojana	Under this scheme, the bank offers concessional credit to women entrepreneurs. Loans above Rs.2 lakh and up to Rs.10 lakh are offered at a 2 per cent concession in interest rate and loans above Rs.10 lakh at 1 per cent concession in interest rate.
State Bank of India	Stree Shakti Package	Under this scheme, the bank extends credit exclusively to women entrepreneurs. Concessions are offered in promoters' margin and rate of interest. The scheme aims at imparting entrepreneurial skills to inspire women and offers a credit package on concessional terms.
Syndicate Bank	Pigmy Deposit	A daily saving scheme, which caters to a large section of women entrepreneurs.

Union Bank of India	Viklang Mahila Vikas Yojana	This scheme envisage financing handicapped women for starting their own vocations. Physically handicapped women are identified and their aptitude ascertained for starting suitable vocation in the locality. Finance of Rs.25,000 is provided for starting any productive venture.

Source : Parliament Questions, February 2003

(ii) The consolidated bank's aggregate exposure to capital markets should not exceed 2 per cent of its total on-balance-sheet assets (excluding intangible assets and accumulated losses) as on March 31 of the previous year. This ceiling will apply to the consolidated bank's exposure to capital market in all forms, including both fund-based and non-fund based, similar to the computation for the parent bank. Within the total limit, investment in shares, convertible bonds and debentures and units of equity-oriented mutual funds should not exceed 10 per cent of consolidated bank's net worth.

(iii) The norms relating to unsecured guarantees and unsecured funded exposures on the lines of the guidelines already issued and as amended from time to time, are also extended to the consolidated bank.

Liquidity Ratios

CRR and SLR requirements : The existing liquidity requirements applicable to banks on a solo basis are extended to the consolidated bank as well. If the related entities in the consolidated bank are banks, liquidity position, i.e., cash reserve ratio (CRR) and statutory liquidity ratio (SLR) would be monitored on a consolidated basis after netting out intra-group transactions and exposures. If the related entities in the consolidated bank are heterogeneous comprising non-banking entities, compliance with the CRR/SLR norms would be restricted to the banking entities on a consolidated basis. In respect of non-banking financial entities within bank groups, they should comply with the liquidity requirements prescribed at solo level.

Asset Liability Management : Maturity wise distribution/analysis of assets and liabilities should be disclosed on a consolidated basis in the CPR. Tolerance limits for near-term and short-term deficits/ mismatches in the first two time bands of 1-14 days and 15-28 days would be monitored at the consolidated level. Intra-group transactions and exposures should be excluded from this consolidation.

In view of the increased focus on empowering supervisors to undertake consolidated supervision of bank groups and the Core Principles for Effective Banking Supervision issued by the Basel Committee on Banking Supervision, the Reserve Bank had set up a multi-disciplinary working group in November 2000 under the Chairmanship of Shri Vipin Malik, Director on the Central Board of the Reserve Bank. The Working Group identified three components of consolidated supervision :

(a) consolidated financial statements,

(b) consolidated prudential reports, and

(c) application of prudential regulations like capital adequacy and large exposures/risk

concentration on group basis.

The draft guidelines were issued to banks for their comments. On the basis of the feedback received from banks and the deliberations with the officials of banks and financial institutions (FIs) the guidelines have been issued.

Bills Discounting/Rediscounting

It has been decided that banks should adhere to the following guidelines while purchasing/discounting/ negotiating/rediscounting of genuine commercial/trade bills:

(a) Since banks have already been given freedom to decide their own guidelines for assessing/ sanctioning working capital limits of borrowers, they may sanction working capital limit as also bills limit to borrowers after proper appraisal of their credit needs and in accordance with the loan policy as approved by their board of directors.

(b) Banks should clearly lay down bills discounting policy approved by their board of directors, which should be consistent with their policy of sanctioning of working capital limits. The procedure for board approval should include banks' core operating process from the time the bills are tendered till these are realised. Banks should review their core operating processes and simplify the procedure for bills financing. In order to address the oft-cited problem of delay in realisation of bills, banks may take advantage of improved computer/communication network like Structured Financial Messaging System (SFMS) and adopt the system of 'value dating' of their clients' accounts.

(c) Banks should open letters of credit (LCs) and purchase/discount/ negotiate bills under LCs only in respect of genuine commercial and trade transactions of their borrower constituents who have been sanctioned regular credit facilities by the banks. Banks should not, therefore, extend fund based (including bills financing) or non-fund based facilities like opening of LCs, providing guarantees and acceptances to non-constituent borrower or/and non-constituent member of a consortium/multiple banking arrangement.

(d) For the purpose of credit exposure, bills purchased/discounted/ negotiated under LCs or otherwise should be reckoned on the bank's borrower constituent. Accordingly, the exposure should attract a risk weight appropriate to the borrower constituent (*viz*., 100 per cent for firms, individuals, corporates, etc.) for capital adequacy purposes.

(e) While purchasing/discounting/negotiating bills under LCs or otherwise, banks should establish genuineness of underlying transactions/documents.

(f) Banks should ensure that blank LC forms are kept in safe custody as in case of security items like blank cheques, demand drafts etc., and verified/balanced on daily basis. LC forms should be issued to customers under joint signatures of the bank's authorised officials.

(g) The practice of drawing bills of exchange claused 'without recourse' and issuing letters of credit bearing the legend 'without recourse' should be discouraged because such notations deprive the negotiating bank of the right of recourse it has against the drawer under the Negotiable Instruments Act. Banks should not, therefore, open LCs and purchase/discount/negotiate bills bearing the 'without recourse' clause.

(h) Banks should not purchase/discount/negotiate accommodation bills. The underlying trade transactions should be clearly identified and a proper record thereof maintained at the branches conducting the bills business.

(i) Banks should be circumspect while discounting bills drawn by front finance companies set up by large industrial groups on other group companies.

(j) Bills rediscounts should be restricted to usance bills held by other banks. Banks should not rediscount bills earlier discounted by non-bank financial companies (NBFCs) except bills arising

from sale of light commercial vehicles and two/three wheelers.

(k) Banks may exercise their commercial judgement in discounting of bills of services sector. However, while discounting such bills, banks should ensure that actual services are rendered and accommodation bills are not discounted. Services sector bills should not be rediscounted. Further, providing finance against discounting of services sector bills may be treated as unsecured advance and therefore, subject to the condition that 20 per cent of a bank's unsecured guarantees plus the total of its outstanding unsecured advances do not exceed 15 per cent of its total outstanding advances.

(l) In order to promote payment discipline which would to a certain extent encourage acceptance of bills, all corporates and other constituent borrowers having turnover above threshold level as fixed by the bank's board of directors should be mandated to disclose 'aging schedule' of their overdue payables in their periodical returns submitted to banks.

(m)Banks should not enter into repo transactions using bills discounted/rediscounted as collateral.

The guidelines have been issued after considering the recommendations of a Working Group on Discounting of Bills by Banks constituted by the Reserve Bank under the Chairmanship of Shri K.R. Ramamoorthy, Chairman, Vysya Bank submitted its report.

Interest Rates

Savings Bank Deposits

The interest rate on domestic and ordinary non-resident savings deposits as well as savings deposits under non-resident (external) accounts scheme has been reduced by 0.5 percentage point from 4.0 per cent to 3.5 per cent per annum from March 1, 2003.

Repo

The repo rate under the liquidity adjustment facility (LAF) of the Reserve Bank of India has been reduced by 0.5 percentage point from 5.5 per cent to 5.0 per cent from March 3, 2003.

NBFC Deposits

Taking into account the market conditions and changes in other interest rates in the entire financial system, the maximum rate of interest that non-banking finance companies (NBFCs) can pay on their public deposits, has been revised to 11 per cent per annum. The revision is effective from March 4, 2003. The new rates will be applicable only to fresh deposits and renewal of existing deposits.

The Reserve Bank has clarified that this is the maximum permissible rate NBFCs can pay on their public deposits and they are free to offer lower rates.

The new ceiling of 11 per cent on interest rate has also been extended to the deposits accepted by miscellaneous non-banking companies (chit fund companies) under the directions prescribed by the Reserve Bank.

Exchange Control

Capital Account Transactions Further liberalised

The Honourable Finance Minister announced, among other things, relaxations relating to certain capital account transactions in the Union Budget for the year 2003-04 as follows. These are :

Investment in Overseas JVs/WOSs

The automatic route of investments up to US$ 100 million is now available to Indian corporates with a proven track record for investments in overseas joint ventures (JVs) or wholly owned subsidiaries (WOSs) even where the investment is not in the same core activity they are engaged in. They are also permitted to invest in such ventures up to 100 per cent of their net worth.

Indian corporates were so far permitted to invest under the automatic route in overseas

JVs/WOSs engaged in the same core activity and up to 50 per cent of their net worth. Core activity means activity carried on by an Indian entity, which constitutes at least 50 per cent of its average turnover.

Pre-payment of ECBs

Pre-payment of external commercial borrowings (ECBs) under the automatic route would be permitted without any limit by removing the current ceiling of US$100 million. Earlier, any pre-payment out of market purchases beyond US$ 100 million required the Reserve Bank's prior approval. This facility would be available until further notice, subject to review.

These relaxations will be effective from March 1, 2003.

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 **Printrite,** 16, Sassoon Dock, Colaba, Mumbai - 400 005. **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), DEAP, 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