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Policy

Fair Practices Code for Lenders

The Reserve Bank has advised banks/financial institutions (FIs) to adopt the following broad guidelines and frame the Fair Practices

Code and get it duly approved by their board of directors. The Reserve Bank had in consultation with the government, select banks and financial institutions, examined the feasibility of introducing the fair practices code for lenders on the basis of the recommendations of the Working Group on Lenders' Liability Laws constituted by the Government of India.

Guidelines

Processing of loan applications

(a) Loan application forms for priority sector advances up to Rs. two lakh should be comprehensive. They should include information about the fees/charges, if any, payable for processing, the amount of fees refundable if the application is not accepted, prepayment options and any other matter which affects the interest of the borrower.

(b) Banks and FIs should acknowledge receipt of all loan applications. The acknowledgement slip should indicate the time frame within which loan applications up to Rs. two lakh would be disposed off.

(c) Banks/FIs should verify the loan applications within a reasonable period of time. If additional details/documents are required, they should immediately intimate the borrowers.

(d) If loan applications of small borrowers seeking loans up to Rs. two lakh have been rejected by banks/FIs, they should convey in writing to the applicant the main reason/reasons which led to rejection of the application within the stipulated time.

Loan appraisal

(a) Banks/FIs should ensure that credit applications are properly assessed by borrowers. They should not use margin and security stipulation as a substitute for due diligence on creditworthiness of the borrower.

(b) Banks/FIs should convey to the borrower the credit limit along with the terms and conditions of sanction of loan. They should also keep on record the borrower's acceptance of these terms and conditions.

(c) Terms, conditions and other caveats governing credit facilities given by banks/FIs arrived at after negotiation with the borrower should be written down and duly certified by the authorised official. A copy of the loan agreement along with a copy each of all enclosures quoted in the loan agreement should be furnished to the borrower.

(d) The loan agreement should clearly stipulate credit facilities that are solely at the discretion of

the bank/FI. These may include approval or disallowance of facilities, such as, drawings beyond the sanctioned limits, honouring cheques issued for the purpose other than specifically agreed to in the credit sanction, and disallowing drawing on a borrowal account upon its classification as a non-performing asset or on account of non-compliance with the terms of sanction. It may also be specifically stated that the bank/FI does not have an obligation to meet further requirements of the borrower on account of growth in business, etc., without proper review of credit limits.

(e) In case of lending under consortium arrangement, the participating lenders should evolve procedures to complete appraisal of proposals in a time bound manner to the extent feasible and communicate their decisions on financing or otherwise within a reasonable time.

Loan disbursement

Banks/FIs should ensure timely disbursement of loans sanctioned. Changes in the terms and conditions including interest rates, service charges, etc., should be intimated to the borrowers. Banks/FIs should also ensure that changes in interest rates and charges are only prospectively effected.

Post disbursement

(a) Post disbursement supervision by banks/FIs, particularly in respect of loans upto Rs. two lakh, should be constructive with a view to taking care of any "lender-related" genuine difficulty that the borrower may face.

(b) Before taking a decision to recall/accelerate payment or performance under the agreement or seeking additional securities, lenders should give notice to borrowers, as specified in the loan agreement or a reasonable period if no such condition exists in the loan agreement.

(c) Banks/FIs should release all securities on receiving payment of loan or realisation of loan subject to any legitimate right or lien for any other claim they may have against the borrower.

Borrowers should be given notice if any right of set off is to be exercised, with full particulars about the remaining claims and the documents under which lenders are entitled to retain the securities till the claim is settled/paid.

General

(a) Banks/FIs should restrain from interference in the affairs of the borrowers except for what is provided in the terms and conditions of the loan sanction documents (unless new information, not earlier disclosed by the borrower, has come to the notice of the lender).

(b) While lending, banks/FIs should not discriminate on grounds of sex, caste and religion. This, however, does not preclude lenders from participating in credit-linked schemes framed for weaker sections of the society.

(c) While recovering loans, banks/FIs should not resort to undue harassment viz., persistently bothering the borrowers at odd hours, use of muscle power for recovery of loans, etc.

(d) If request for transfer of borrowal account is received either from the borrower or from a bank/FI, which proposes to take over the account, the consent or objection, if any, should be conveyed within 21 days from the date of receipt of request.

Code to be in place by August 1

Based on these guidelines, banks/FIs should be put in place a Fair Practices Code for all lending prospectively, but not later than August 1, 2003. They have the freedom of drafting the Fair Practices Code, enhancing the scope of the guidelines but in no way sacrificing the spirit underlying these guidelines. For this purpose, the boards of banks and FIs should lay down a clear policy.

Banks/FIs have been further advised that the adoption of the Code, printing of loan application forms and their circulation among the branches and controlling offices should be completed

latest by end of June 2003. The Fair Practices Code, which would be adopted by banks/FIs, should also be put on their website and given wide publicity. A copy may also be forwarded to the Reserve Bank.

Grievance redressal

The board of directors should also set up an appropriate grievance redressal mechanism within the organisation to resolve disputes arising in this regard. Such a mechanism should ensure that all disputes arising out of the decisions of lending institutions' functionaries are heard and disposed of at least at the next higher level. The board of directors should also provide for periodical review of the compliance of the Fair Practices Code and the functioning of the grievances redressal mechanism at various levels of controlling offices. A consolidated report of such reviews may be submitted to the board at regular intervals, as prescribed by it.

Monetary and Credit Policy for the year 2003-2004

The Reserve Bank announced the Monetary and Credit Policy for 2003-04 on April 29, 2003 (URL: www.cpolicy.rbi.org.in). To operationalise the decisions announced in the Policy, the Reserve Bank issued the following notifications during May.

Prime Lending Rate

In order to enhance transparency in banks' pricing of their loan products as also to ensure that the prime lending rate (PLR) truly reflects the actual costs, the Reserve Bank has advised banks that while determining their benchmark PLR they may consider the following suggestions :

(a) Banks should take into account their (i) actual cost of funds, (ii) operating expenses, and (iii) a minimum margin to cover regulatory requirement of provisioning/capital charge and profit margin, while arriving at the benchmark PLR. The benchmark PLR should be announced with the approval of their boards.

(b) The benchmark PLR would continue to be the ceiling rate for credit limit up to Rs. two lakh.

(c) Since all other lending rates can be determined with reference to the benchmark PLR arrived at as above by taking into account term premia and/or risk premia, the system of tenor-linked PLR deserves to be discontinued. These premia can be factored in the spread over or below the PLR.

The decision regarding the date for discontinuation of the tenor-linked PLR would be announced separately after discussion with banks.

In the interest of customer protection and to have greater degree of transparency regarding actual interest rates charged to borrowers, banks have been advised to continue to provide information on maximum and minimum interest rates charged together with the benchmark PLR.

The system of determination of benchmark PLR by banks and the actual prevailing spreads around the benchmark PLR is proposed to be reviewed in September 2003. Banks may, therefore, advise the Reserve Bank of the action taken on the above suggestions as early as possible.

Commercial Paper

In order to provide further flexibility to both issuers and investors in the commercial paper (CP) market, it has been decided that non-bank entities including corporates may provide unconditional and irrevocable guarantee for credit enhancement for CP issue provided :

- the issuer fulfils the eligibility criteria prescribed for issuance of CP;
- the guarantor has a credit rating at least one notch higher than the issuer by an approved credit rating agency; and

- the offer document for CP properly discloses the networth of the guarantor company, the names of the companies to which the guarantor has issued similar guarantees, the extent of the guarantees offered by the guarantor company, and the conditions under which the guarantee will be invoked.

Banks are allowed to invest in CPs guaranteed by non-bank entities provided their exposure remains within the regulatory ceiling as prescribed by the Reserve Bank for unsecured exposures.

Investment Fluctuation Reserve

It has been decided that while investment fluctuation reserve (IFR) would continue to be treated as Tier II capital, it would not be subject to the ceiling of 1.25 per cent of the total risk weighted assets. For the purpose of compliance, with the capital adequacy norms, however, Tier II capital including IFR, would be considered up to a maximum of 100 per cent of total Tier I capital. This is effective from March 31, 2003.

Provisioning for NPAs

The Reserve Bank had, in April 2003 circulated guidelines on sale of financial assets to securitisation/reconstruction companies by banks/financial institutions. Banks/FIs have now been advised that if the sale of assets to securitisation/reconstruction companies is at a price below the net book value (i.e., book value less provisions held), the shortfall should be debited to the profit and loss account of that year. It is envisaged that banks would be able to sell their NPAs to securitisation/reconstruction companies at considerable discount. To enable banks to meet the resultant shortfall, if any, the Reserve Bank has advised them to build up provisions significantly above the minimum regulatory requirements for their NPAs, particularly for those assets which they propose to sell to securitisation/reconstruction companies.

Placement of Deposits - Non-scheduled UCBs

It has been decided to permit non-scheduled urban co-operative banks (UCBs) to place deposits with strong scheduled UCBs, subject to the following conditions :

(a) The strong scheduled UCB with which the non-scheduled UCB desires to place the deposits, should comply with the following norms :

(i) Prescribed level of CRAR.

(ii) Net non-performing assets of less than 7 per cent.

(iii) No default in the maintenance of cash reserve ratio/statutory liquidity requirements for the last two years.

(iv) Net profits for the last three consecutive years.

(v) 'A' rating from co-operative auditors for the last three consecutive years.

(vi) Compliance with prudential norms on income recognition, asset classification and provisioning, exposure ceilings and loans and advances to directors.

(b) Acceptance of deposits by scheduled UCBs from non-scheduled UCBs would be subject to the following conditions :

(i) The total inter-UCB deposits accepted by a scheduled UCB should not exceed 10 per cent of its deposit liabilities as on March 31 of the previous financial year.

(ii). The rate of interest offered on such deposits should be market related.

(iii). The total amount of deposits placed by a non-scheduled UCB with a scheduled UCB should not exceed 20 per cent of its capital funds, so as to be in consonance with the extant exposure norms.

Scheduled UCBs, however, should not place deposits with other scheduled/ non-scheduled urban

co-operative banks.

Earlier in April 2001, UCBs were prohibited from placing any fresh deposits with other UCBs except by way of balances in current accounts for meeting their clearing and remittance requirements. Further, those UCBs which maintained funds in the form of fixed deposits or term deposits with other UCBs were asked to unwind the outstanding deposits before the end of June 2002. In pursuance of the recommendations made by the Geete Committee set up by the Government of India and in view of the difficulties expressed by UCBs in managing their short-term surplus funds, the matter was reviewed and non-scheduled UCBs were allowed to place deposits with strong scheduled UCBs as announced in the Monetary and Credit Policy for 2003-04.

Reporting Call Money Deals on NDS

From the fortnight beginning May 3, 2003, it is mandatory for all negotiated dealing system (NDS) members including all scheduled primary (urban) co-operative banks (UCBs) to report all their call/ notice money market deals on NDS. Deals done outside NDS should be reported within 15 minutes on NDS, irrespective of the size of the deal or whether the counterparty is a member of the NDS or not.

The Reserve Bank would, in September 2003, review whether UCBs are reporting all their deals on NDS. In case of repeated non-reporting of deals by an NDS member, it would be considered whether non-reported deals should be treated as invalid with effect from a future date.

Priority Sector Advances

Indirect Finance to Agriculture

It has been decided that dealers in drip irrigation/sprinkler irrigation system/agricultural machinery would be eligible for finance up to Rs. 20 lakh under priority sector lending for agriculture, irrespective of their location.

Earlier, such finance, classified as 'indirect finance to agriculture' was available provided the dealer was located in the rural/semi-urban area.

Housing Loans

In view of increasing demand for housing in rural and semi-urban areas, and to improve financing to housing sector in these areas, it has been decided that banks, with the approval of their boards, would be free to extend direct finance to the housing sector up to Rs. ten lakh in rural and semi-urban areas as part of priority sector lending.

Highlights

Review

- Inflationary situation on an average basis remained low except in the fourth quarter during 2002-03 despite drought.
- Lower increase in reserve money despite sharp increase in RBI's foreign currency assets.
- Money Supply (M₃) remained within projected trajectory during 2002-03.
- Sustained increase in credit flow during 2002-03;
- Sharp reduction in interest rates of banks and in government and corporate papers.
- Government borrowing programme completed at lower interest cost with longer maturity. Interest rates on corporate paper are all time low.
- Reserves build up at a low effective cost without adding to external debt.
- Low interest rates and strong forex position prompts prepayment of external debt.

Stance

- RBI to provide adequate liquidity to meet credit growth and support investment demand.
- Preference for a soft and flexible interest rate environment to continue.

Some Measures

- Bank Rate reduced by 0.25 percentage point.
- CRR reduced by 0.25 percentage point.
- Export credit refinance facility to continue.
- Interest rate on back-stop facility reduced.
- Transparent system to determine PLR of banks.
- Uniformity in maturity structure of repatriable foreign currency as well as rupee NRI deposits.
- Overseas investments liberalised and flexibility allowed to overseas investors for flow of FDI.
- Further measure to improve credit delivery mechanism to priority sector.
- Changes in prudential measures for UCBs in line with JPC recommendations.

SGSY: Financing of Groups having Defaulters

The Government of India has advised that willful defaulters should not be financed under the Swarnjayanti Gram Swarozgar Yojana (SGSY). Further, in case willful defaulters are members of a group, they might be allowed to benefit from the thrift and credit activities of the group including the corpus built up with the assistance of revolving fund. At the stage of assistance for economic activities, however, the willful defaulters should not be given further assistance until

the outstanding loans are repaid. Willful defaulters of the group should not get benefits under the SGSY scheme and the group may be financed excluding such defaulters while documenting the loan. Further, non-willful defaulters may be certified by a team comprising the block development officer or his representative, bank manager and the sarpanch.

It is also clarified that a household having two kitchens and two ration cards should be treated as two families. Mere declaration by the loan applicant that he has separated from the family may not be considered as sufficient document for separate household. While defining the terms, ration card may not be insisted upon, due to various difficulties faced in its procurement. Banks may advise their branch managers to devise their own ways of verifying the facts by inspecting/visiting the villages in doubtful cases.

RRBs - Concurrent Audit of Treasury

The Reserve Bank has advised all regional rural banks (RRBs)/ sponsor banks of RRBs that their treasury transactions should be separately subjected to a concurrent audit by internal auditors and the results of their audit reports should be placed before their chief executives once every month. The audit reports should be forwarded to the concerned regional office of the National Bank for Agriculture and Rural Development (NABARD).

The concurrent auditors should also certify that investments held by the RRB as on the last reporting Friday of each quarter and as reported to the Reserve Bank are actually owned/held by it as evidenced by physical securities or the custodian's statement. A copy of the certificate should be submitted to the concerned regional office of NABARD within 30 days from the end of the relative quarter. The first such certificate for the last reporting Friday of the quarter ending March 31, 2003 should be submitted to the concerned regional office of NABARD before April 30, 2003.

Time for OTS extended

The Reserve Bank has, in consultation with the Government of India, extended the time period for receipt of applications from borrowers for compromise settlements of loans up to Rs. 10 crore, under the one-time settlement scheme (OTS) from April 30, 2003 to September 30, 2003. The last date by which banks have to process the applications has also been extended from October 31, 2003 to December 31, 2003.

The Government of India and the Reserve Bank had been receiving requests from banks for extending the time limit for operation of the guidelines.

CO-OP Banks

UCBs to Disclose details of Insurance Premia

UCBs have been advised to disclose in their balance sheets, information regarding payment of insurance premia to the Deposit Insurance and Credit Guarantee Corporation (DICGC). Accordingly, all UCBs should disclose in their directors' report whether the insurance premium has been paid up-to-date to DICGC, indicating arrears, if any, effective from the year ended March 31, 2003.

Forex

Residents can obtain International Credit Cards

Resident individuals maintaining a foreign currency account with an authorised dealer (AD) in India or a bank abroad, as permissible under extant foreign exchange regulations, are now free to obtain international credit cards (ICCs) issued by overseas banks and other reputed agencies. The charges incurred against the card either in India or abroad, can be met out of funds held in such foreign currency account/s of the cardholder or through remittances, if any, from India only through a bank where the cardholder has a current or savings account. The remittance for this

purpose, should be made directly to the card-issuing agency abroad, and not to a third party. The Reserve Bank has clarified that it has not fixed any monetary ceiling for remittances, if any, under this facility and that the applicable credit limit would be the limit fixed by the card issuing banks.

The Reserve Bank has also advised that the restriction applicable for use of ICCs by residents would apply. The ICC cannot be used for purchase of prohibited items, such as, lottery tickets, banned or proscribed magazines, participation in sweepstakes, payment for call back services, etc.

Exports to Warehouses Abroad

ADs have been advised to grant permission to exporters for opening/hiring of warehouses abroad subject to :

- a) Applicant's export outstanding does not exceed 5 per cent of exports made during the previous year.
- b) Applicant has a minimum export turnover of USD 1,00,000 during the last year.
- c) Period of realisation should be 180 days for non-status holder exporters and 365 days for status holder exporters.
- d) All transactions should be routed through the designated branch of the AD.

ADs may grant such permissions initially for one year and renewal may be considered subject to the condition that the applicant's export outstanding does not exceed 5 per cent of exports made during the previous year. ADs granting the permission should maintain a proper record of the approvals granted.

Export of Goods for Promotion

It has been decided that ADs may now consider requests received from exporters for export of goods free of cost to the overseas buyer for export promotion. Such exports could be up to two per cent of average annual exports of the applicant during the preceding three years, subject to a ceiling of Rs. five lakh. ADs should maintain a record of permissions issued by them.

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