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Declaration of Dividend

The Reserve Bank has revised its guidelines on dividends payable by banks as under :

Eligibility Criteria

- Only those banks, which comply with the following minimum prudential requirements, would be eligible to declare dividends without the Reserve Bank's prior approval :

  The bank should -

  (a) have capital to risk-weighted assets ratio (CRAR) of at least 11 per cent for preceding two completed years and the accounting year for which it proposes to declare dividend. (b) have net non-performing assets (NPA) of less than 3 per cent.

  (c) comply with the provisions of Sections 15 and 17 of the Banking Regulation Act, 1949.

  (d) comply with the Reserve Bank's prevailing regulations/ guidelines, including creating adequate provisions for impairment of assets and staff retirement benefits, transfer of profits to statutory reserves and investment fluctuation reserve, etc.

- The Reserve Bank should not have placed any explicit restrictions on the bank for declaration of dividends.

Quantum of Dividend

Banks which qualify to declare dividends would be eligible to pay dividends without obtaining the Reserve Bank's prior approval provided -(i) The dividend payout ratio does not exceed 33. 33 per cent. (ii) The proposed dividend should be payable out of the current year's profit.

(iii) The dividend payout ratio is calculated as a percentage of 'dividend payable in a year' (excluding dividend tax) to 'net profit during the year'.

(iv) In case the profit for the relevant period includes any extraordinary profits/income, the payout ratio should be computed after excluding such extra-ordinary items for reckoning compliance with the prudential payout ratio ceiling of 33.33 per cent.

(v) The financial statements pertaining to the financial year for which the dividend is declared, should be free of any qualifications by the statutory auditors, which have an adverse bearing on the profit during that year. In case of any qualification to that effect, the net profit should be suitably adjusted while computing the dividend payout ratio.

Banks desirous of declaring dividend higher than the specified limit, should obtain the Reserve Bank's prior approval. The Reserve Bank would consider requests received from banks on a case-to-case basis.

Interim Dividend

Banks which qualify for declaring dividend and satisfy the other requirements mentioned above, may also declare and pay interim dividends out of the relevant accounting period's profit without the Reserve Bank's prior approval provided, the cumulative interim dividend(s) are within the prudential cap on dividend payout ratio (33.33 per cent) computed for the relevant accounting period. Declaration and payment of interim dividends beyond this ceiling would, however, require the Reserve Bank's prior approval.

Banks which do not meet the Eligibility Criteria

Banks which do not meet the eligibility criteria prescribed above, should obtain the Reserve Bank 's prior approval before declaring any dividend. Requests received from such banks would be considered by the Reserve Bank on a case-to-case basis.

Highlights of the Annual Policy Statement for the year

Domestic Developments

- GDP growth for 2004-05 projected at 6.5-7.0 per cent.
- Assuming no significant supply shocks and appropriate management of liquidity, the inflation rate projected for policy purposes at around 5.0 per cent during 2004-05.
- Growth in reserve money and Money supply(M3) were higher during 2003-04 reflecting capital inflows; the expansionary impact of foreign currency assets, however, was neutralised to a large extent by substantial open market operation (OMO) including sustained repo operations under LAF.
- Sustained pick-up in non-food credit since September; total flow of resources to the commercial sector was higher than last year.
- Government market borrowing programme in 2003-04 completed at a much lower cost; while noting reduction in fiscal deficit, need to step up capital expenditure stressed.
- Further reduction in interest rates in money and government securities markets observed in 2003-04.
- Public sector banks have reduced their BPLR in the range of 25-100 basis points.
- RBI to continue with its policy of active liquidity management; Market Stabilisation Scheme (MSS), is an additional tool.

External Developments

- lThe exchange rate of the rupee appreciated *vis-à-vis* US dollar but depreciated against the Euro, Pound sterling and Japanese yen in 2003-04.
- India's foreign exchange reserves increased by US $ 37.6 billion during fiscal 2003-04 and are at US $ 118.6 billion by May 7, 2004.

- India’s exports in US dollar terms increased by 17.1 per cent while imports by 25.3 per cent; the current account expected to register surplus during 2003-04 for the third year in succession.
- The most distinguishing feature of the external sector during 2003-04 relates to the large capital flows with its inevitable implications for the conduct of domestic monetary policy and exchange rate management.

Overall Assessment

- Despite uncertainties, India’s position among the top performers globally in terms of GDP growth is expected to continue during 2004-05.
- As regards prices, despite overhang of problems on account of oil prices and large domestic liquidity, price situation unlikely to cause concern to macro stability during 2004-05.
- Need to overcome the bottlenecks in flow of bank credit to agriculture and small & medium enterprises emphasised.
- Restructuring of rural banking sector stressed for enhancing the quality, purposiveness and reach of banking in India.

Stance of Monetary Policy

- Projected expansion of money supply(M3) at 14.0 per cent with credit growth by 16.0-16.5 per cent during 2004-05.
- The overall stance of monetary policy for 2004-05 will be:

    (i) provision of adequate liquidity to meet credit growth and support investment and export demand while keeping a very close watch on the movements in the price level.

    (ii) Consistent with the above, while continuing with *status quo*, RBI to pursue an interest rate environment that is conducive to maintaining momentum of growth and, macroeconomic and price stability.

Measures

- Bank Rate kept stable at 6.0 per cent. l Repo Rate unchanged at 4.5 per cent. l Revised LAF scheme operationalised.
- Entire export credit refinance made available at reverse repo rate.
- Almost all banks adopted the new system of BPLR and the rates are lower from their earlier PLRs.
- Banks are encouraged to align the pricing of credit to assessment of credit risk to improve credit delivery and credit culture.
- RBI accepted some recommendations of the interim Report of Vyas Committee for implementation, e.g., loans for storage facilities under priority sector, securitised agricultural loans as priority sector lending, waiving margin/security requirements for certain agricultural loans up to a limit, NPA norms for crop loans aligned to crop seasons.
- Development of mechanism for debt restructuring for medium enterprises on the lines of corporate debt restructuring.
- Definition of infrastrucutre lending broadened.
- Working Group constituted on Credit Enhancement by State Governments for financing infrastructure.
- A Gold Card Scheme for creditworthy exporters drawn up.
- Various restructuring options being considered by the government and other stakeholders for rationalising the structure of RRBs - Vyas Committee is also looking into restructuring of RRBs.

- Limit on the lending of non-bank participants in the call/notice money market reduced to 45 percent effective June 26, 2004.
- Automated value-free transfer of securities proposed between market participants and the CCIL under CBLO.
- RBI constituted Working Group to review the performance of negotiated dealing system (NDS).
- Clearing of OTC derivatives through CCIL being considered.
- CCIL to work out arrangement for settlement of trades in non-SLR debt instruments for NDS members.
- Discussion paper on Capital Indexed Bonds being put in public domain.
- The ECB limit already enhanced to US $ 500 million under the automatic route for investment in the real sector.
- Resident individuals already permitted to remit freely up to US $ 25,000 per calendar year.
- Indian corporates and partnership firms allowed to invest overseas upto 100 per cent of their net worth.
- Banks allowed to raise long-term bonds to finance infrastructure.
- The extant limit on unsecured exposures for banks withdrawn.
- Exposures on all public financial institutions (PFIs) to attract a risk weight of 100 per cent.
- Banks required to maintain capital charge for market risk in a phased manner.
- Banks to draw a road map for migration to Basel II.
- Banks to make higher provisioning according to the age of NPAs.
- Banks/FIs to provide credit information to CIBIL.
- Banks to fully adhere to the KYC policy for opening new accounts.
- Report of the Working Group on Financial Conglomerates being put in public domain.
- Risk based supervision extended to more banks.
- Fresh licences to UCBs only after a comprehensive policy.
- Report of the Working Group on Development Finance Institutions being put in public domain.
- Technical Group to evaluate the regulatory and supervisory systems deployed by refinancing institutions (RFIs).
- Waiver of service charges on banks for electronic funds transfer and electronic clearing services.
- RBI sets up a Board for Payment and Settlement Systems.
- RBI expects most commercial banks to join the RTGS system by June 2004.
- A Working Group on Electronic Funds Transfer for Capital Market constituted.
- Single window services for all transactions in RBI cash department.
- Operationalisation of On-line Tax Accounting System by June 2004.
- Standing Committee on Procedures and Performance Audit on Public Services has submitted four Reports, being put in the public domain.
- Recommendations of the Advisory/Technical Groups on International Financial Standards and Codes being pursued.

Reporting

Banks should report details of dividend declared during the accounting year within a fortnight of payment of the dividend(s).

These revised guidelines would be applicable to the dividends declared for the accounting year ended March 31, 2004 onwards. Banks should place a copy of these guidelines before their Board at its next meeting.

Banks are further advised that violation of these guidelines would be viewed very seriously and would attract penal action under Section 46 of the Banking Regulation Act, 1949. The Reserve Bank had, in consultation with the Standing Technical Advisory Committee on Financial Regulation, reviewed the policy approach regarding payment of dividends by banks. It was decided that the regulatory focus with regard to payment of dividend by banks should shift from ‘quantum of dividend’ to ‘dividend payout ratio’.

Information System Audit

With a view to ensuring uniformity in the Information System (IS) audit being followed by banks, the Reserve Bank has advised all scheduled commercial banks to -(i) Adopt an IS audit policy (if not already done) appropriate to their level of computerisation and review the same at regular intervals in tune with the industry best practices and guidelines issued by the Reserve Bank from time to time ii) Adopt appropriate system and practices for conducting IS audit on an annual basis covering all the critically important branches (in terms of nature and volume of business) iii) Undertake such audits preferably prior to the statutory audit so that the IS audit reports are available to the statutory auditors well in time for examination and for incorporating comments, if any, in the audit reports iv) Place the IS audit reports before their top management and ensure compliance within the time frame as outlined in the audit policy.

Banks have been advised to place these instructions before their board in its next meeting and implement them during the current financial year.

The Reserve Bank had, in the past, taken many initiatives in sensitising banks to the risks and concerns that emerge from adoption of information technology. Various committee reports, instructions and circulars were issued from time to time towards assisting banks in adopting sound IS audit policy framework and practices.

The Reserve Bank had recently conducted a study to assess the current practices being followed by banks vis-à-vis IS audit.

The study revealed that though banks have put in place a mechanism for conducting IS/EDP audit, the practices differ from bank to bank depending upon the level of adoption of technology. Further, many banks are in the process of implementing IS audit system in place of computer/EDP audit.

Margins for Bank Financing against Shares Reduced

On the recommendation made by the Task Force constituted for monitoring developments in the financial markets, it has been decided to restore, with immediate effect, the status quo ante on margins that banks have to maintain for financing against shares/ IPOs/issue of guarantees. The margins would now be 40 per cent against the earlier 50 per cent. Furthermore, the minimum cash margin of 25 per cent (within the margin of 50 per cent) stands reduced to 20 per cent.

It may be recalled that the margins against shares were increased from the level of 40 per cent to 50 per cent in January 2004.

CUSTOMER SERVICE

Opening of Current Accounts

The Reserve Bank has reiterated its earlier instructions to banks to scrupulously ensure that their branches do not open current accounts of entities which enjoy credit facilities (fund based or non-fund based) from the banking system without specifically obtaining a no-objection certificate from the lending bank(s). Banks have also been advised that non-compliance of these instructions would be perceived as abetting the siphoning of funds and such violations, reported to the Reserve Bank or noticed during its inspection would render the concerned banks liable for penalty under the Banking Regulation Act, 1949.

In January 2000 banks were advised that at the time of opening current accounts, they should insist on a declaration from the account-holder stating that he is not enjoying any credit facility with any other bank or obtain a declaration giving particulars of credit facilities enjoyed by the intending customer with any other bank(s). Concerned lending bank(s) were required to be duly informed so that they could take suitable precautionary measures, where necessary.

Customer Information

The Reserve Bank has advised all commercial banks that information collected from customer while opening an account is confidential and divulging any details thereof for cross selling or any other purpose would be in breach of customer confidentiality obligations. Banks are, therefore, advised to instruct all the branches to strictly ensure compliance with their obligations to the customer in this regard.

The Reserve Bank has further advised banks that if they desire to collect any information about their customer for a purpose other than “Know Your Customer” (KYC) requirements, it should not form part of the account opening form. Such information may be collected separately, purely on a voluntary basis, after explaining the objectives to the customer and taking his express approval for the specific uses to which such information could be put.

Banks have also been advised to get their existing practices in this regard examined by the Ad hoc Committee/Board and issue suitable instructions to their branches and ensure compliance.

The Committee on Procedures and Performance Audit on Public Services had observed that banks are using information collected from their customers for cross selling of services of various products by their subsidiaries and affiliates. Sometimes, such information is also provided to other agencies.

Minimum Balance

Banks have been advised to inform, at least one month in advance, their existing account holders any change in the prescribed minimum balance and the charges that would be levied if the prescribed minimum balance is not maintained.

Earlier, in August 2003, banks were advised that at the time of opening savings bank accounts, they should inform their customers about the requirement of maintaining minimum balance and levying of charges if such minimum balance is not maintained. Any subsequent change in this regard should be informed to the account holders.

The Committee on Procedure and Performance Audit on Public Services had observed that banks added charges without informing the existing depositors. The Committee had recommended that any charge levied subsequently should be transparently made known to all depositors with one month’s advance notice.

Joint Accounts

The Reserve Bank has clarified that non-resident ordinary (NRO) accounts may be held by non-residents jointly with residents.

In August 2003, banks were advised that non-resident (external) (NRE) deposits should be held jointly with non-residents only. Some banks had interpreted that these instructions were equally applicable to NRO accounts and that NRO accounts could not be held jointly with residents.

Processing Charges for EFT/ECS

In order to give further fillip to other types of electronic modes of funds transfer, it has been decided to waive the service charges on banks for Electronic Funds Transfer (EFT) and Electronic Clearing Service (ECS) transactions up to March 31, 2006. The details in this regard are :

- The Reserve Bank would not levy ECS/EFT processing charges. The waiver would be applicable to ECS (credit and debit clearing), centralised ECS, the normal EFT as well as to the special EFT schemes.
- The waiver would be effective from June 1, 2004, i.e., in respect of data submitted by banks from June 1, 2004 and would be in vogue up to March 31, 2006.
- Banks should required to pass on this benefit to the customers in the form of a reduction in the charges being levied for such transactions.

It may be recalled that in December 2003, the Reserve Bank had waived the processing charges for EFT transactions for two years. This measure was undertaken to encourage electronic mode of payments which is fast and efficient.

Banks have been further advised to inform the Reserve Bank of the steps taken by them to pass on the benefit in terms of the change in tariff along with details of pre and post waiver charges.

RRBs

Valuation of Investment

The Reserve Bank has advised all regional rural banks (RRBs)/ sponsor banks that the exemption granted to RRBs from 'mark to market' norms in respect of stautory liquidity ratio (SLR) securities has been extended for one more year i.e., for the financial year 2004-05. Accordingly, RRBs should classify the entire investment portfolio of SLR securities under 'held to maturity' for the financial year 2004-05 with valuation on book value basis and amortisation of premium, if any, over the remaining life of securities.

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