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MONETARY AND CREDIT INFORMATION REVIEW

Important Financial Developments in 2004

January

- The Reserve Bank announced Know Your Customer (KYC) guidelines for non-banking financial institutions (NBFCs).
- Banks advised to constitute an *ad hoc* committee to undertake procedures and performance audit on public services rendered by them.
- The uniform margin to be applied on all advances against shares/financing of initial public offerings/issues of guarantees raised from 40 per cent to 50 per cent.
- Banks advised to constitute a Special Committee to monitor and follow up fraud cases involving amounts of Rs.1 crore and above.
- General permission granted to foreign companies to establish branch offices/units in special economic zones to undertake manufacturing and service activities.
- The limit for foreign exchange remittance for miscellaneous purposes without documentation formalities raised from USD 500 to USD 5000
- Indian students studying abroad to be treated as NRIs.
- Final guidelines on investment by financial institutions (FIs) in debt securities issued. FIs prohibited from investing in unrated debt securities and in debt securities of original maturity of less than one year other than commercial paper (CP) and Certificates of Deposit (CDs).
- Time limit for receipt of applications for one time settlement of chronic non-performing assets (NPAs) of public sector banks up to Rs. 10 crore, extended up to July 31, 2004. Consequently, the last date for processing applications also extended up to October 31, 2004.

February

- Banks given the freedom to decide all aspects concerning renewal of overdue deposits. Banks' board, however, to lay down a non-discretionary and non-discriminatory transparent policy in this regard.
- Quantum of margin on advance against term deposit left to the discretion of banks.
- Interest payable on maturity proceeds of the deposit account of a deceased depositor now to be decided by individual banks subject to their board laying down a transparent policy in this regard.
- Non-banking financial institutions (NBFCs) registered with the Reserve Bank permitted to take up insurance agency business on fee basis and without risk participation, without the Reserve Bank's prior permission.
- As a step towards further simplification and liberalization of foreign exchange facilities available to residents, resident individuals permitted to freely remit up to USD 25,000 per calendar year for any purpose. The facility is, however, not available to corporates, partnership firms, HUFs, trusts, etc.
- Urban co-operative banks (UCBs) advised not to open constituent subsidiary general ledger (CSGL) accounts of other UCBs. If any already opened, should be closed immediately.

March

- To bring about a certain level of uniformity regarding the content and coverage of the Best Practices Code (BPC), the Reserve Bank prepared guidelines for banks to keep in view while preparing the BPC.
- Urban co-operative banks (UCBs) advised to exercise caution while sanctioning loans against relief bonds/certificates.
- Indian and foreign banks, including those not having operational presence in India, advised to seek the Reserve Bank's prior approval for the schemes marketed by them in India to residents either for soliciting foreign currency deposits for their foreign/overseas branches or for acting as agents for overseas mutual funds or any other foreign financial services company.
- The Real Time Gross Settlement (RTGS) System put in live operations for settling inter-bank transactions on transaction by transaction (i.e., gross) basis, in an online at real time mode.
- As a step towards further liberalization, residents allowed to freely remit money, without the Reserve Bank's prior approval towards health insurance, commission for sale of property, short term credit to overseas offices of Indian companies, advertisement on foreign TV, royalty/lump-sum fee, use of trademark/franchise, hiring charges of transponders.
- The limit for export of goods by way of gift raised from rupees one lakh to rupees five lakh per annum.
- Authorised dealers (ADs) permitted to make remittances up to USD 100,000 for import bills/documents which are received directly by importers from their overseas suppliers.
- ADs permitted to grant rupee loans to non-resident Indians (NRIs) as per policy laid down by the bank's board of directors. The rupee loans are, however, not to be utilised for business of chit fund, nidhi company, agricultural/plantation activities,

real estate business, construction of farm houses, trading in transferable development rights (TDRs) and investment in capital market including margin trading and derivatives. The quantum of loan, rate of interest, margins, etc., on such loans to be decided by ADs.

- General permission granted to Indian companies in India to grant loans in foreign currency to the employees of their branches outside India for personal purposes in accordance with their staff welfare scheme/loan rules and other terms and conditions as applicable to their staff resident in India and abroad.
- The Foreign Inward Remittance Payment System was withdrawn as it was no longer used by banks in the wake of electronic credits and online transfer of funds.
- The Reserve Bank operationalised the revised LAF scheme from March 29, 2004. Normal facility and backstop facility merged in to a single facility to be made available at a single rate.
- Reverse repo rate reduced to 6.0 per cent.

April

- It was decided that the interest rates on non-resident (external) rupee (NRE) deposits for one to three years contracted effective close of business in India on April 17, 2004, should not exceed the LIBOR/SWAP rates for US dollar of corresponding maturity. Revised rate also to be applicable is case the maturity period of the deposit exceeds three years.
- Interest rates on NRE savings deposits linked to LIBOR/SWAP rates with effect from the close of business on April 17, 2004. The interest rates on NRE savings deposits not to exceed the LIBOR/SWAP rates for six-month maturity on US dollar deposits.
- As account holders of NRE savings deposits can withdraw savings deposits at any time, banks advised not to mark any type of lien, direct or indirect, against these deposits.
- Following the recommendations of the Committee on Procedures and Performance Audit on Public Services (Chairman:Shri S.S.Tarapore) revised norms were issued regarding cheque drop box facility, delivery of cheque books over the counter and statement of accounts/pass book.
- Banks advised to issue an acknowledgement receipt when a currency note tendered at the their branch counter is found to be forged and is impounded.
- Scheduled commercial banks advised not to allow offshore banking units (OBUs) set up in special economic zones (SEZs) to open foreign currency accounts of residents.
- ADs permitted to allow remittance of net salary (after deduction of taxes, contribution to provident fund and other contributions) of Indian national employed by overseas companies on deputation to the office or branch or subsidiary or joint venture in India of such overseas company for the maintainance of close relatives residing abroad.
- Guidelines relating to trade credits for imports into India revised.
- Comprehensive guidelines issued for investment in non-SLR securities by UCBs.

May

- The Reserve Bank revised its guidelines on dividend payable by banks. According to the revised guidelines, only those banks which comply with certain minimum prudential requirements would be eligible to declare dividends without the Reserve Bank's prior approval.
- Series of measures announced for improving flow of credit to agriculture, such as, rescheduling/restructuring debts of farmers who have suffered production and income loss on account of natural calamities, formulating guidelines for one-time settlement for small and marginal farmers, waiver of margin/security for agricultural loans up to Rs. 50,000 and Rs. 5 lakh in case of agri-business and agri-clinics, loans to storage units designed to store agricultural produce/products irrespective of their location, to be treated as indirect agricultural finance under priority sector, etc.
- Banks advised 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).
- The Reserve Bank announced the Gold Card Scheme for exporters. The Scheme envisages certain additional benefits based on the performance record of exporters. The Gold Card holder would enjoy simpler and more efficient credit delivery mechanism in recognition of his good track record.
- Banks advised to inform, at least one month in advance, their account holders any change in the prescribed minimum balance and the charges that would be levied if the prescribed minimum balance is not maintained.
- The Reserve Bank clarified that non-resident ordinary (NRO) counts may be held by NRIs jointly with residents.
- In order to give fillip to other types of electronic modes of transfer, the Reserve Bank decided to waive the service charges applicable for Electronic Funds Transfer (EFT) and Electronic Clearing Service (ECS) from June 1, 2004 to March 31, 2006.
- Banks advised to align the pricing of credit to assessment of credit risk by putting in place comprehensive and rigorous risk assessment procedures for borrowers.
- The Reserve Bank reiterated that micro finance institutions cannot accept public deposits unless they comply with the extant regulatory framework.
- Automated value-free transfer of securities between market participants and the Clearing Corporation of India Ltd. enabled for collateralised borrowing and lending operations (CBLO).
- The Reserve Bank clarified to banks that NRO accounts may be held by NRIs jointly with residents.
- NBFCs advised not to accept fresh NRI deposits from April 24, 2004 but allowed to renew the deposits already accepted.
- Banks advised that the subsidy under the Swarna Jayanti Swarozgar Yojana (SJSRY) would be a back-ended subsidy with a lock-in period of two years.
- The margin requirement on all advances against shares/ financing of IPOs/issue of guarantees by banks reduced from 50 per cent to 40 per cent. Further, banks advised to take minimum cash margin of 20 per cent (within the margin of 40 per cent) in respect of guarantees issued by them for capital market operations.
- Exemption granted to regional rural banks (RRBs) from 'mark to market' norms in respect of SLR securities extended for one more year, i.e., up to 2004-2005.
- UCBs advised to exercise due caution with regard to valuation while sanctioning loans and advances against mortgage of house property.

- The off-site surveillance system already in place for scheduled UCBs extended to all non-scheduled UCBs having deposit size of Rs. 100 crore and above.

June

- Graded higher provisioning to be introduced according to the age of NPAs in 'doubtful for more than three years' category with effect from March 31, 2005.
- In order to extend further flexibility to banks on their loan policies, Reserve Bank advised banks to formulate their own policies on unsecured exposures. Unsecured exposures redefined and it was clarified that unsecured sub-standard assets would attract 20 per cent provisioning.
- With a view to providing a boost to infrastructure lending, banks allowed to raise long term bonds with a minimum maturity of five years.
- Banks advised to draw a road map for migration to Basel II by the end of 2004 and make a quarterly review of the progress made.
- The Reserve Bank clarified that the process of identifying willful defaulters and the mechanism relating to redressal of grievances were two distinct processes. The borrower should be suitable advised before being classified as a willful defaulter.
- Banks' boards allowed to raise single or group exposure limit by 5 per cent of capital funds under exceptional circumstances.

July

- The Reserve Bank placed in public domain a draft policy framework for ownership and governance in private sector banks for discussion before finalization.
- Pursuant to the recommendations of the Ganguly Group Report, the Reserve Bank advised that persons to be appointed as directors in private sector banks would have to fulfill specific criteria prior to their appointment.
- With a view to ensuring smooth transition to Basel II norms, The Reserve Bank advised banks to phase the implementation of capital charge for market risk over a two year period.
- With a view to ensuring that existing small account holders are not inconvenienced and the Know Your Customer (KYC) guidelines procedure is completed in time, the Reserve Bank advised banks to limit the application of KYC procedures to existing accounts where the credit or debit summation for the financial year ended March 31, 2003 is more than Rs. 10 lakh or where unusual transactions are suspected.
- In an attempt at job consolidation, the Reserve Bank merged the functions handled by its Industrial and Export Credit Department with those of the other departments.

August

- The Reserve Bank circulated amongst banks a list of deficiencies noticed in the sanctioning/monitoring of borrowal accounts and suggestions for minimising frauds.
- The Reserve Bank clarified that where due diligence is carried out on the request of a prospective customer who is a corporate or large borrower enjoying credit facilities from more than one bank, banks should inform the consortium leader, if under consortium, and the concerned banks, if under multiple banking arrangements.
- To make the Prime Minister's Rozgar Yojana (PMRY) more effective, self help groups have been included for assistance under the scheme.
- The Reserve Bank clarified that directors of primary urban co-operative banks (UCBs) and their relatives cannot stand as surety/guarantor to the loans and advances (both secured and unsecured) sanctioned by the UCBs.
- Keeping in view the importance of credit discipline for reduction in NPA level, UCBs advised that at the time of opening of current accounts they should insist on a declaration from the account holder stating that he is not enjoying any credit facility with any other commercial bank.
- UCBs advised that from the year ending March 31, 2005, they would be required to classify an asset as non-performing if interest and/or instalment of principal remain overdue for a period of more than 90 days.

September

- The cash reserve ratio (CRR) to be maintained by SCBs increased by one-half of one percentage point of their net demand and time liabilities (NDTL) in two stages. CRR increased to 4.75 per cent from September 18, 2004 and to 5.00 per cent from October 2, 2004. The effective CRR to be maintained by SCBs on total NDTL should, however, not be less than 3.00 per cent.
- SCBs to be paid interest at the rate of 3.5 per cent per annum with effect from the fortnight beginning September 18, 2004 on eligible cash balances maintained with the Reserve Bank under the CRR requirement.
- Taking into account the changes brought in due to the introduction of technology and the need to cut down operational costs while enhancing customer service, banks permitted to open central processing centres/back offices. These would be branches which would attend exclusively to data processing, verification and processing of documents, issuance of cheque books, demand drafts, etc. and other functions incidental to banking business having no interface with customers.
- A Sub-Committee of SLBC for Export Promotion set up to take up exporters' problems relating to export finance and other related issues.
- Banks advised that they may exceed the limit of 25 per cent of their total investments under held to maturity (HTM) category provided, the excess comprises only of SLR securities and the total SLR securities held in the HTM category is not more than 25 per cent of their NDTL as on the last Friday of the second preceding fortnight.
- SCBS advised to arrange for a special review/scrutiny of the computation of their DTL/NDTL as well as verification of the integrity of the software used by them for this purpose by internal or external auditors.
- Banks advised to link the interest/instalment payable on rural housing advances granted to agriculturists under the Indira Awas Yojana and Golden Jubilee Rural Housing Finance Scheme, to crop cycles, while fixing the repayment schedule.
- The facility for realisation and repatriation of full value of goods/ software exported to Latin American within a period of 360 days from the date of shipment, discontinued from September 1, 2004. Accordingly, exporters exporting to the Latin American countries on or after September 1, 2004, would be under obligation to realise full export proceeds within the prescribed period of six months from the date of export.
- UCBs advised to apply the 90 day impairment norm to gold loans and small loans up to rupees one lakh with effect from the financial year ending March 31, 2005 for the purpose of asset classification, income recognition and provisioning.

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October

- The Model KCC Scheme revised to include investment credit requirements of farmers, viz., allied and non-farm activities. The Scheme to be referred to as the 'Scheme to cover term loans for agriculture and allied activities under Kisan Credit Card Scheme'.
- The Reserve Bank finalised the guidelines relating to issue of subordinated debt Instruments under Tier II and Tier III capital for primary dealers.
- With a view to providing an option to issuers to raise short-term resources through commercial paper (CP) as also an avenue to investors to invest in quality short-term papers, the minimum maturity period of CP reduced from 15 days to 7 days.
- Banks permitted to extend finance to non-banking finance companies (NBFCs) against second hand assets financed by them. Banks also permitted to extend financial assistance to customers directly for purchase of second hand assets.
- With a view to bringing in the urban poor into the formal financial system, banks advise to advance loans to distressed urban poor to prepay their debt to non-institutional lenders, against appropriate collateral or group security. Urban poor to include families in the urban areas who are below the poverty line.
- The composite loan limit for small scale industries (SSIs), enhanced from Rs.50 lakh to Rs.1 crore.
- Banks' investments in securitised assets representing direct lending to the SSI sector, to be treated as their direct lending to SSI sector under priority sector provided, the pooled assets represent direct loans to SSI sector which are reckoned under priority sector; and the securitised loans are originated by banks/financial institutions.
- In order to further improve flow of credit to the housing sector, banks permitted to extend direct finance to housing sector up to Rs. 15 lakh irrespective of location, as part of their priority sector lending.

November

- SCBs advised to formulate a comprehensive and transparent policy covering issues relating to (i) immediate credit of local/ outstation cheques (ii) time frame for collection of local/ outstation cheques and (iii) interest payment for delayed collection.
- To bring consistency in the procedure of fixing interest rates on non-resident (external) rupee (NRE) and foreign currency non-resident (banks) FCNR (B) deposits, banks advised to fix the interest rates on FCNR (B) deposits on the basis of LIBOR/SWAP rates as prevailing on the last working day of the preceding month, effective from November 1, 2004.
- It was decided that the interest rates on NRE deposits for one to three years maturity contracted with effect from November 1, 2004 should not exceed the LIBOR/SWAP rates, as on the last working day of the previous month, for US dollar of corresponding maturity plus 50 basis points. The revised interest rates for three year deposits also to be applicable in case the maturity period exceeds three years and to NRE deposits renewed after their present maturity period.
- In order to provide uniformity in the tenor of term deposits, banks permitted to reduce the minimum tenor of domestic/ ordinary non-resident (NRO) term deposits, even those below Rs.15 lakh, from 15 days to 7 days.
- Units set up in electronics hardware technology parks (EHTPs), software technology parks (STPs) and bio-technology parks (BTPs) and 100 per cent export oriented units (EOUs) allowed to realise and repatriate the full value of export proceeds within a period of twelve months from the date of export. The relaxation is available for exports made on or after September 1, 2004.
- The limit on advances under priority sector for dealers in agricultural machinery, including drip/sprinkler irrigation systems, raised from Rs. 20 lakh to Rs.30 lakh and for distribution of inputs for allied activities from Rs.25 lakh to Rs.40 lakh.
- The Reserve Bank issued detailed guidelines based on the Recommendations of the Financial Action Task Force and the paper issued on Customer Due Diligence for banks by the Basel Committee on Banking Supervision. Banks advised to ensure that a proper policy framework on 'Know Your Customer' and Anti-Money Laundering measures is formulated and put in place with their board's approval within three months.

December

- In order to further improve flow of credit to the housing sector, banks permitted, with the approval of their boards, to extend direct finance to housing sector up to Rs.15 lakh, irrespective of location, as part of their priority sector lending.
- With a view to rationalising banks' investments under priority sector lending and encouraging banks to increasingly lend directly to the farmers/other priority sector borrowers, it was been decided that the extant guidelines in respect of classifying the investments by banks in the bonds issued by the specified institutions as under priority sector lending should continue up to March 31, 2005.
- With the stabilisation of reporting of call/notice money transactions over negotiated dealing system (NDS) as also to reduce reporting burden, the practice of reporting of call/notice/ term money transactions to the Reserve Bank discontinued from December 11, 2004. Deals between non-NDS members should, however, continue to be reported to the Reserve Bank.
- Foreign banks advised that the amount of shortfall in their priority sector obligation should be placed with the Small Industries Development Bank of India (SIDBI) for a tenor of three years. The funds placed with SIDBI would have a graded interest rate structure linked to the Bank Rate.

MONETARY AND CREDIT INFORMATION REVIEW
Wishes its Readers
A Happy and A Prosperous New Year

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