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MONETARY AND CREDIT
INFORMATION REVIEW

POLICY

Interest Subvention for Short-term Crop Loans

Pursuant to the announcement made by the Hon'ble Finance Minister in his Budget Speech for 2008-09, the Government will provide interest subvention of 2 per cent to public sector banks in respect of short-term production credit up to Rs.3 lakh provided to farmers. The amount of subvention would be calculated on the amount of crop loan disbursed from the date of disbursement/drawal up to the date of payment or up to the date beyond which the outstanding loan becomes overdue i.e. March 31, 2009 for kharif and June 30, 2009 for rabi, respectively, whichever is earlier. This subvention would be available to public sector banks on the condition that they make available short-term credit at ground level at 7 per cent per annum.

Public sector banks have been advised to immediately submit their estimates of short-term production credit to farmers up to Rs.3 lakh for kharif and rabi 2008-09 (separately) to the Reserve Bank to enable it to provide the Government with an estimate of the likely amount of subvention. The estimates should be realistic in nature.

Banks have also been advised that -

- To enable the Government to provide subvention, banks should submit their claims on a half-yearly basis as at September 30, 2008 and March 31, 2009 and on a quarterly basis as at June 30, 2009 (for rabi), within one month from the respective dates.
- The claims for the half-year ending March 31, 2009 and quarter ending June 30, 2009 (for rabi) should be accompanied by a statutory auditor's certificate certifying that the claims for subvention for the entire year ended March 31, 2009 and quarter ending June 30, 2009 (as the case may be) are true and correct. Final settlement of the claims would be done only on receipt of this certificate.
- Claims should be submitted to the Reserve Bank's Rural Planning and Credit Department, Central Office, Mumbai.

In case of regional rural banks (RRBs) and co-operatives, a separate circular would be issued by the National Bank for Agriculture and Rural Development (NABARD).

CRR increased

On a review of the current global and domestic macroeconomic and financial developments, the cash reserve ratio (CRR) of scheduled banks has been increased by 50 basis points to 8.75 per cent of their net demand and time liabilities in two stages, effective from the fortnights as indicated below:

Effective date (i.e., the fortnight beginning from)	CRR on net demand and time liabilities (in per cent)
July 5, 2008	8.50
July 19, 2008	8.75

Mobile Payments in India

The Reserve Bank has advised banks to keep on hold their mobile payment services till it issues the final guidelines. It has also advised banks to dissociate themselves from any mobile based money transfer service which has not received the Reserve Bank's explicit approval or is not covered by any of its guidelines.

It may be recalled that the Reserve Bank had on June 12, 2008, placed on its website, draft guidelines for banks on mobile payments for feedback. It is currently in the process of

CONTENTS

PAGE

POLICY

Interest Subvention for Short-term Crop Loans	1
CRR increased	1
Mobile Payments in India	1

UCBs

Instruments for Augmenting Capital Funds	2
Wilful Defaulters	2
Balances held with IDBI Bank Limited	3

FEMA

Security for External Commercial Borrowings	3
Overseas Direct Investment by Registered Trust/Society	4

CUSTOMER SERVICE

Credit Card Operations	4
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finalising the operative guidelines on mobile banking for banks after evaluating the feedback received.

While the Reserve Bank has no objection to banks using the mobile channel for providing basic services, such as, mobile alerts for credit/debit entry, balance enquiry etc., which are in the nature of providing information, due care needs to be taken for permitting the channel to customers for initiating payment instructions. Considering, however, that there are a number of attendant issues, it has advised banks to keep on hold their mobile payment services till it issues the final guidelines.

UCBs

Instruments for Augmenting Capital Funds

The Reserve Bank had constituted a working group (Chairman: Shri N.S.Vishwanathan) to examine the issues concerning raising of capital by urban co-operative banks (UCBs) and identifying alternate instruments/avenues for augmenting their capital funds. Based on the recommendations of the working group and in order to facilitate UCBs in raising capital funds (Tier I and Tier II) for complying with the prescribed capital adequacy norms, the Reserve Bank has permitted them to issue financial instruments. The financial instruments are:

Preference Shares

Preference shares of the following types:

- i) Perpetual non-cumulative preference shares (PNCPS).
- ii) Perpetual cumulative preference shares (PCPS).
- iii) Redeemable non-cumulative preference shares (RNCPS).
- iv) Redeemable cumulative preference shares (RCPS).

While perpetual non-cumulative preference shares would be eligible to be treated as Tier I capital, perpetual cumulative preference shares, redeemable non-cumulative preference shares and redeemable cumulative preference shares would be eligible to be treated as Tier II capital. UCBs, however, are not permitted to subscribe to the preference shares of other UCBs.

Long Term Deposits

UCBs may raise term deposits for a minimum period of not less than 5 years, which would be eligible to be treated as Tier II capital.

Share Linkage Norms

As per the current regulatory prescriptions, borrowings from UCBs are linked to shareholdings of the borrowing members. At present, the shareholding requirement is 2.5 per cent for secured borrowings and 5 per cent for unsecured borrowings. Taking into account the recommendation of the working group and the feedback received in this regard, it has been decided that the extant share linking norm may be applicable for member's shareholdings up to the limit of 5 per cent of the total paid up share capital of the bank. Where a member is already holding 5 per cent of the total paid up share capital of an UCB, it would not be necessary for him to subscribe to any

additional share capital on account of the application of the extant share linking norms. In other words, a borrowing member may be required to hold shares for an amount that may be computed as per the extant share linking norms or for an amount that is 5 per cent of the total paid up share capital of the bank, whichever is lower.

Classification of Capital Funds

As per the extant instructions, capital funds are divided into Tier I capital and Tier II capital. Elements of Tier II capital are reckoned as capital funds up to a maximum of 100 per cent of Tier I capital. It has now been decided to further divide Tier II capital into upper and lower tiers. Perpetual cumulative preference shares, redeemable non-cumulative preference shares and redeemable cumulative preference shares would be treated as upper Tier II capital. Long term deposits would be treated as lower Tier II capital. PNCPS should not exceed 20 per cent of Tier I capital (excluding PNCPS). Long term deposit should not exceed 50 per cent of Tier I capital and the total Tier II capital should not exceed Tier I capital.

The elements of Tier II capital are reckoned as capital funds up to a maximum of 100 per cent of Tier I capital. This restriction has now been kept in abeyance for a period of five years, i.e. up to March 31, 2013 for UCBs that are having capital to risk weighted assets ratio (CRAR) of less than 9 per cent in order to give them time to raise Tier I capital. In other words, Tier II capital would be reckoned as capital funds for capital adequacy purpose even if a UCB does not have Tier I capital. During this period, however, for the purpose of capital adequacy requirement, lower Tier II capital alone would be restricted to 50 per cent of the prescribed CRAR and the progressive discount in respect of Tier II capital would be applicable.

UCBs may issue preference shares and long term deposits subject to compliance with their bye-laws/provisions of the Co-operative Societies Act under which they are registered and with the approval of the concerned Registrar of Co-operative Societies/Central Registrar of Co-operative Societies, wherever applicable, and the Reserve Bank. The central/state governments are being requested separately to make necessary amendments to the Multi-State Cooperative Societies Act/Co-operative Societies Acts/Rules, wherever necessary.

Wilful Defaulters

In supersession of the definition/illustrations contained in the Reserve Bank's circular of August 1, 2002, the term "wilful default" has been redefined as follows:

A wilful default would be deemed to have occurred if any of the following events are noted:

- A unit has defaulted in meeting its payment/repayment obligations to the lender even when it has the capacity to honour the obligation.
- A unit has defaulted in meeting its payment/repayment obligation to the lender and has not utilised the finance from the lender for the specific purposes for which the finance was availed of but has diverted the funds for other purposes.

- A unit has defaulted in meeting its payment/repayment obligations to the lender and has siphoned off the funds, as a result, the funds have not been utilised for the specific purpose for which the finance was availed of nor are the funds available with the unit in the form of other assets.
- The unit has defaulted in meeting its payment/repayment obligation to the lender and has also disposed off/removed the movable fixed assets or immovable property given by it for the purpose of securing a term loan, without the knowledge of the bank/lender.

Further, it is reiterated that no additional facilities should be granted by any scheduled urban co-operative bank to the listed wilful defaulters. In addition, entrepreneurs/promoters of companies which have been identified for siphoning/diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions should be debarred from institutional finance for floating new ventures for a period of five years from the date the name of the wilful defaulter is published in the Reserve Bank's wilful defaulters' list.

Balances held with IDBI Bank Limited

The Reserve Bank has advised all UCBs that the balance maintained by them in current account with IDBI Bank Limited would not be eligible for being reckoned as 'net balance in current account' for the purpose of cash reserve ratio (CRR)/statutory liquidity ratio (SLR) under Section 18 and 24 of the Banking Regulation Act, 1949 (AACS).

UCBs maintaining current account balances with IDBI Bank Limited and presently reporting them under CRR/SLR, have been advised to intimate the position as on June 30, 2008 to the Reserve Bank's respective regional office.

In terms of Section 18(1) (c) and 24(2) (a) of the Banking Regulation Act, 1949 (AACS), net balance maintained in current account by co-operative banks with the following banks are treated as cash for the purpose of CRR/SLR:

- State Bank of India
- a subsidiary bank, and
- a corresponding new bank.

As IDBI Bank Limited is not one of these banks, these instructions have been issued.

FEMA

Security for External Commercial Borrowings

As a measure of rationalisation of the existing procedures, AD Category - I banks have been allowed to convey 'no objection' under the Foreign Exchange Management Act (FEMA), 1999 for creation of charge on immovable assets, financial securities and issue of corporate or personal guarantees in favour of overseas lender/security trustee, to secure external commercial borrowings (ECBs) to be raised by borrowers.

Prior to according 'no objection' under FEMA, 1999, AD Category - I banks should ensure and satisfy themselves that (i) the underlying ECB is strictly in compliance with the extant ECB guidelines, (ii) the loan agreement contains a security clause which requires the borrower to create charge on

immovable assets/financial securities/furnish corporate or personal guarantee, (iii) the loan agreement has been signed by both the lender and the borrower, and (iv) the borrower has obtained loan registration number (LRN) from the Reserve Bank.

Creation of Charge on Immovable Assets

AD Category - I banks may convey their 'no objection' under FEMA, 1999 for creation of charge on immovable assets either in favour of the lender or the security trustee, subject to the conditions that:

- The 'no objection' is granted only to a resident ECB borrower.
- The period of such charge on immovable assets is co-terminus with the maturity of the underlying ECB.
- Such 'no objection' is not to be construed as permission to acquire immovable asset (property) in India, by the overseas lender/security trustee.
- If the charge is enforced/invoked, the immovable asset (property) would have to be sold only to a person resident in India and the sale proceeds should be repatriated to liquidate the outstanding ECB.

Creation of Charge over Financial Securities

AD Category - I banks may convey their 'no objection' under FEMA, 1999 to the resident ECB borrower for pledge of shares of the borrowing company held by promoters as well as in domestic associate companies of the borrower to secure the ECB subject to the conditions that :

- The period of such pledge is co-terminus with the maturity of the underlying ECB.
- If the pledge is invoked, the transfer shall be in accordance with the extant foreign direct investment (FDI) policy.
- A certificate is obtained from the company's statutory auditor that the ECB proceeds have been/will be utilised for the permitted end-use/s.

Issue of Corporate/Personal Guarantee

The 'no objection' to the resident ECB borrower for issue of corporate or personal guarantee under FEMA, 1999 may be conveyed after -

- Obtaining board resolution for issue of corporate guarantee from the company issuing such guarantees, specifying the names of the officials authorised to execute such guarantees on behalf of the company or in individual capacity.
- Obtaining specific requests from individuals to issue personal guarantee indicating details of the ECB.
- Ensuring that the period of the corporate or personal guarantee is co-terminus with the maturity of the underlying ECB.

AD Category - I banks may invariably specify that the 'no objection' is issued from the foreign exchange angle under the provisions of FEMA, 1999 and should not be construed as an approval by any other statutory authority or government under any other laws/regulations. If further approval or permission is required from any other regulatory/statutory authority or government under the relevant laws/regulations, the applicant should take the approval of the authority concerned before undertaking the transaction. Further, the 'no objection' should not be construed as regularising or validating any irregularities,

contravention or other lapses, if any, under the provisions of FEMA or any other laws or regulations.

These amendments to the ECB guidelines have come into force from July 11, 2008.

Overseas Direct Investment by Registered Trust/Society

With a view to further liberalising the policy on overseas investments, registered trusts and societies engaged in manufacturing/educational sector have now been allowed to make investment in the same sector(s) in a joint venture or wholly owned subsidiary outside India, with the Reserve Bank's prior approval. Registered trusts/societies which satisfy the below indicated criteria are eligible to apply for overseas investment :

Criteria

Trust

- i) The Trust should be registered under the Indian Trust Act, 1882.
- ii) The Trust deed should permit the proposed investment overseas.
- iii) The proposed investment should be approved by the trustee/s.
- iv) The authorised dealer bank should be satisfied that the trust is 'know your customer' (KYC) compliant and is engaged in a bonafide activity.
- v) The Trust should have been in existence at least for a period of three years.
- vi) The Trust should not have come under the adverse notice of any regulatory/enforcement agency like the Directorate of Enforcement, Central Bureau of Investigation (CBI) etc.

Society

- i) The Society should be registered under the Societies Registration Act, 1860.
- ii) The Memorandum of Association and rules and regulations should permit the Society to make the proposed investment which should also be approved by the governing body/council or a managing/executive committee.
- iii) The authorised dealer bank should be satisfied that the Society is KYC compliant and is engaged in a bonafide activity.
- iv) The Society should have been in existence at least for a period of three years.
- v) The Society should not have come under the adverse notice of any regulatory/enforcement agency like the Directorate of Enforcement, CBI etc.

AD Category – I banks should ensure that in addition to the registration, special license/permission has been obtained by the applicant for activities which require special license/

permission either from the Ministry of Home Affairs, Government of India or from the relevant local authority, as the case may be.

Trusts/societies satisfying the above eligibility criteria may submit their application/s in Form ODI-Part I, through their AD Category - I bank/s. The AD Category – I bank, after ensuring that the applicant satisfies the prescribed criteria, may forward the application/s with their comments/recommendations, to the Reserve Bank's Foreign Exchange Department at Mumbai for consideration.

CUSTOMER SERVICE

Credit Card Operations

Based on the complaints received by the Reserve Bank as also by the offices of the Banking Ombudsmen, a study was undertaken on the credit card operations of banks. The gist of the recommendations of the study together with existing RBI instructions, if any, and the action required to be taken by banks in this regard are placed on the RBI website www.rbi.org.in

Unsolicited Cards

Reiterating its earlier instructions, the Reserve Bank has advised banks that they should not issue unsolicited credit cards. In case an unsolicited card is issued and activated without the consent of the recipient and the latter is billed for the same, the card issuing bank should not only reverse the charges forthwith, but also pay a penalty without demur to the recipient amounting to twice the value of the charges reversed.

The person in whose name the card has been issued can also approach the Banking Ombudsman who would determine the amount of compensation payable to him by the bank as per the provisions of the Banking Ombudsman Scheme, 2006 i.e., for loss of the complainant's time, expenses incurred, harassment and mental anguish suffered by him. Further, there have been instances where unsolicited credit cards issued have been misused before reaching the person in whose name the card is issued. It is clarified that any loss arising out of misuse of such unsolicited cards would be the responsibility of the card issuing bank only and the person in whose name the card has been issued cannot be held responsible for the same.

Insurance Cover

Where insurance cover is offered to credit card holders in tie-up with insurance companies, banks should obtain in writing from the credit card holder, the details of nominee/s for the insurance cover in respect of accidental death and disablement benefits. Banks should ensure that the relevant nomination details are recorded by the insurance company. Banks should also issue a letter to the credit card holder indicating the name, address and telephone number of the insurance company.

Banks have been advised to scrupulously adhere to these instructions and any violation/s would be viewed seriously by the Reserve Bank.