

## Developments in Co-operative Banking

### Introduction

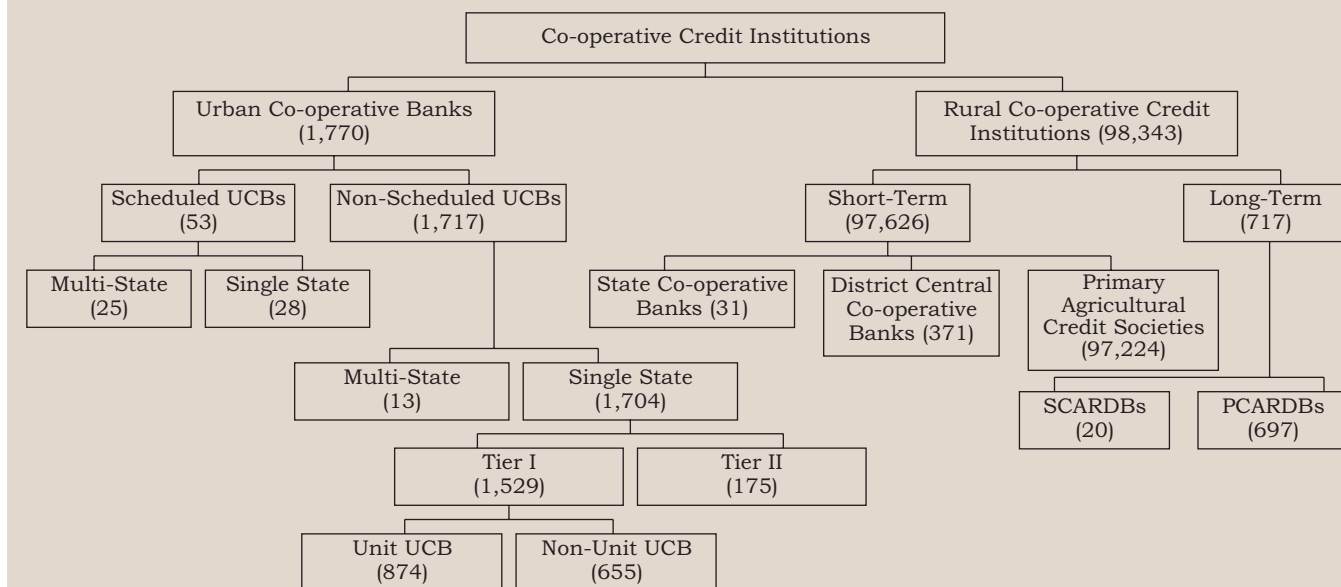
4.1 The co-operative banking sector, with its more than a century old existence, plays an important role in enlarging the reach of institutional credit both from geographic and socio-economic perspective. Though it supplements the efforts of the commercial banks in credit delivery and deposit mobilisation, its extensive branch networks with reach even in remote areas, makes it an important instrument for achieving greater financial inclusion. However, the financial health of most of the co-operative banks has been a cause for concern and has so far proved to be a serious handicap in reaching out to the larger population. Thus, the focus of recent policy measures is on revitalising and strengthening the co-operative banking sector in India. The ongoing task of revitalising the rural co-operative sector is progressing on the lines of the recommendations of the Task Force to review the problems of rural co-operative sector and for the UCBs, based on Vision Document, 2005.

4.2 The structure of the co-operative banking sector in India is complex. Credit needs of diverse sections of the population, both in terms of location and tenor, are addressed by different segments of the co-operative banking sector. While the urban areas are served by the urban co-operative banks with a single tier structure, the rural areas are largely served by two distinct sets of institutions extending short-term and long-term credit. The short-term co-operative credit institutions have a three-tier structure comprising State co-operative banks (StCBs) at the apex level, district central co-operative banks (DCCBs) at the intermediate level and

primary agricultural credit societies (PACS) at the base level. The long-term co-operative credit institutions have, generally, a two-tier structure comprising the State co-operative agriculture and rural development banks (SCARDBs) at the State level and the primary co-operative agriculture and rural development banks (PCARDBs) at the district or block level. Long-term co-operative credit institutions have a unitary structure in some States with State level banks operating through their own branches, while in other States they have a mixed structure with the existence of both unitary and two-tier systems. The States which do not have long-term co-operative credit entities are served by State co-operative banks (Chart IV.1).

4.3 Recognising the importance of urban co-operative banks in providing banking services to the middle and lower income group of people, the Reserve Bank in March 2005 drafted a Vision Document for UCBs pointing out the problem of dual control as a restrictive mechanism inhibiting its ability to handle the weaknesses of the entities within the sector. As per the terms of the document, so far 23 State Governments and Central Government (in case of multi-State UCBs) have signed the Memoranda of Understanding (MoUs) with the Reserve Bank covering 98.6 per cent of the total number of the UCBs representing 99.2 per cent of deposits of the sector. As a part of the MoU, the State level Task Force for Co-operative Urban Banks (TAFUCBs) have been set up to identify the potentially viable and non-viable UCBs in the State and to chart out the revival path and non-disruptive exit route for the two sets of banks, respectively. These measures instilled public confidence in the

**Chart IV.1: Structure of Co-operative Credit Institutions in India**



SCARDBs : State Co-operative Agriculture and Rural Development Banks.  
PCARDBs : Primary Co-operative Agriculture and Rural Development Banks.

**Note :** Figures in parentheses indicate the number of institutions at end-March 2008 for UCBs and at end- March 2007 for rural co-operative credit institutions.

sector which is evident from the increase in deposits for three successive years, *i.e.*, from 2005-06 to 2007-08.

4.4 During 2007-08, the Reserve Bank continued with its policy of encouraging States to sign MoUs to establish a co-ordinated supervisory/regulatory structure, by further incentivising the scheme in the form of additional business opportunities, opening of new ATMs and conversion of exchange counters into branches, among others. The process of consolidation through mergers of UCBs progressed further during the year with a total of 61 mergers being effected upon the issue of statutory orders by the Central Registrar of Co-operative Societies/Registrar of Co-operative Societies (CRCS/RCS) concerned. Further, as on March 31, 2008, 268 UCBs were under various stages of liquidation. All these measures appeared to have positive impact on the performance of the UCBs as a whole. Their businesses expanded

at an impressive rate and operating profit increased during the year.

4.5 The process of implementation of the recommendations of the Task Force on revival of short-term rural co-operative credit structure (Chairman: Prof. A. Vaidyanathan) started with the announcement of a package by the Government of India. Twenty five States have signed MoUs with the Government of India and NABARD. At end-March 2008, 59,294 PACS completed the required special audit. Until end-August 2008, eight States had amended their respective Co-operative Societies Acts. Common Accounting System (CAS) and management information system (MIS) were introduced along with several human resources development (HRD) initiatives. Recapitalisation of eligible PACS has been initiated. The Central Government also reached an agreement with the State Governments regarding the contents of the package to implement the Vaidyanathan Committee report on revival of long-term co-operative credit structure.

4.6 Balance sheets of all segments of the rural co-operative banking sector, except for SCARDBs, expanded during 2006-07. Continuing with the trend witnessed in the last year, the upper tier of both short-term and long-term rural co-operative credit institutions made profits during 2006-07 also, while the lower tier (*viz.*, PACS and PCARDBs) incurred losses. However, the profits made by the upper tier were lower during 2006-07, while the losses incurred by the lower tier were higher as compared with 2005-06. As a result, at the aggregate level, the financial performance of the rural co-operative banking sector on the whole deteriorated further during 2006-07. Asset quality in terms of NPAs to loan ratio improved at the aggregate level as well as at disaggregated level for all segments of rural credit structure, barring PCARDBs (in case of PCARDBs the ratio remained unchanged during 2006-07). The recovery performance improved this year for DCCBs, PACS and PCARDBs, while it worsened for StCBs and SCARDBs.

4.7 The chapter is organised into five sections. Section 2 details the policy developments, business operations and performance of urban co-operative banks, while Section 3 focuses on the policy developments and performance of rural co-operative banks. Section 4 delineates the role of NABARD in the rural co-operative sector and the initiatives taken during the year to improve the performance of the rural co-operative banking sector. Section 5 reviews the progress made in the implementation of the Vaidyanathan Committee's recommendations on revival of the rural co-operative banking sector.

## 2. Urban Co-operative Banks

### Policy Developments

4.8 The consultative mechanism adopted by the Reserve Bank for regulation and supervision of UCBs in line with the

framework suggested in the Vision Document (2005) through signing of MoUs helped strengthen the sector. Furthermore, the Reserve Bank guidelines on merger/amalgamation of UCBs, just prior to commencement of the MoU process, helped phase out non-viable banks through a non-disruptive exit route. Both of these mechanisms progressed well during 2007-08 and helped the UCB sector to strengthen further. Besides, the Reserve Bank continued with its policy of relaxed regulatory norms for Tier I UCBs, *i.e.*, smaller UCBs with deposit base of less than Rs.100 crore and having branches limited to a single district. Moreover, the Reserve Bank also made available a number of facilities to UCBs in those States that have signed MoU with the Reserve Bank.

### Structural Initiatives

#### *Vision Document*

4.9 A significant proposal of the Vision Document was to address the problem of dual control of UCBs by signing of MoU between the Reserve Bank and the respective State Governments, and establishing a consultative forum for supervision of the banks. Accordingly, the Reserve Bank approached the States having a large network of UCBs for signing MoUs. Since June 2005, MoUs have been signed with 23 State Governments (upto October 20, 2008) and with the Central Government in respect of multi-State UCBs and TAFCUBs have been constituted in all such States. The mechanism of TAFCUBs has been able to restore the confidence in the UCB sector (Box.IV.1).

#### *Two Tier Regulatory Structures - Definition Amended*

4.10 The definition of Tier I bank was amended with effect from March 7, 2008. Banks falling under the following categories are classified as Tier I banks: (i) unit banks, *i.e.*, banks having a single branch/head office

**Box IV.1: MoU and TAFUCBs - Impact and Progress**

In order to ensure greater convergence of regulatory and supervisory policies between the two regulators in the urban co-operative banking sector, viz., State Governments (Central Government in case of Multi-State UCBs) and the Reserve Bank, the latter pursued a policy of encouraging the State Governments to sign a Memorandum of Understanding (MoU) in this regard. Pursuant to this policy, as on October 20, 2008, 23 States, viz., Gujarat, Andhra Pradesh, Karnataka, Madhya Pradesh, Uttarakhand, Rajasthan, Chhattisgarh, Goa, Maharashtra, Haryana, National Capital Territory of Delhi, West Bengal, Assam, Tripura, Punjab, U.P., Manipur, Meghalaya, Himachal Pradesh, Kerala, Mizoram, Tamil Nadu and Sikkim have signed MoUs with the Reserve Bank. MoU has also been signed with central Government in respect of multi state UCBs. As on October 20, 2008, the MoU has covered 1,746 UCBs out of 1,770 which accounts for 98.6 per cent of total number of UCBs and 99.2 per cent of total deposits as well as advances of the sector. As per the arrangements under MoU, the Reserve Bank constitutes State level Task Force for Co-operative Urban Banks (TAFUCB) comprising representatives of the Reserve Bank, the State Government and the UCB sector. Accordingly, TAFUCBs have been constituted in all States that have signed MoUs. A Central TAFUCB has also been constituted for the multi-state UCBs. TAFUCBs identify potentially viable and non-viable UCBs in

States and suggest revival path for the viable and non-disruptive exit route for the non-viable ones. The exit of non-viable banks could be through merger/amalgamation with stronger banks, conversion of them into societies or liquidation, as the last option.

TAFUCBs, since its inception, have examined the position of 949 UCBs (Including cases of banks reviewed more than once) and taken decision on finalising merger with respect to 14 banks. Orders of directions by the Reserve Bank were imposed on 37 banks and licenses were cancelled for 40 banks.

The impact of the consultative process is assessed in respect of UCBs in states that signed MoUs before December 2006. As at end-March 2008, number of UCBs in Grade IV declined from what it was at end-March 2006 in all of these states, except in Rajasthan and Maharashtra/Goa. In case of UCBs in Grade III, their number declined in all these states as at end-March 2008 over the same three year period. However, in Uttarakhand the number remained same as it was at end-March 2007 (Table I).

Total number of Grade I and II banks increased over the 3 year period from 2006 to 2008 in all these states except Maharashtra/Goa which witnessed a decline in number. In Uttarakhand the number of Grade I and II remained unchanged in 2007 and 2008. Grade III and IV banks declined in all the States over the mentioned three year reference period (Table 2).

**Table 1: Comparison of Grades in the Last Three Years in First Nine States that signed MoU before December 2006**  
(As at end-March 2008)

States	End March	Grade I	Grade II	Grade III	Grade IV	Total
1. Andhra Pradesh	2008	72	26	7	10	115
	2007	65	33	7	11	116
	2006	48	43	18	15	124
2. Gujarat	2008	110	99	27	35	271
	2007	114	88	42	40	284
	2006	136	50	67	43	296
3. Karnataka	2008	118	75	54	33	280
	2007	99	92	55	42	288
	2006	90	76	85	46	297
4. Madhya Pradesh/ Chhattisgarh	2008	18	27	16	9	70
	2007	17	29	15	13	74
	2006	16	28	17	14	75
5. Maharashtra/Goa	2008	201	191	101	116	609
	2007	134	254	115	119	622
	2006	226	173	127	104	630
6. Rajasthan	2008	23	13	1	2	39
	2007	24	13	1	1	39
	2006	25	10	3	1	39
7. Uttarakhand	2008	4		1	1	6
	2007	4		1	2	7
	2006					
<b>Total</b>	<b>2008</b>	<b>546</b>	<b>431</b>	<b>207</b>	<b>206</b>	<b>1,390</b>
	<b>2007</b>	<b>457</b>	<b>509</b>	<b>236</b>	<b>228</b>	<b>1,430</b>
	<b>2006</b>	<b>541</b>	<b>380</b>	<b>317</b>	<b>223</b>	<b>1,461</b>

**Table 2: Number of UCBs in Grades 'I & II' and in Grades 'III & IV' and their Percentage to Total Number of UCBs in First Nine TAFUCB States that Signed MoU before December 2006.**  
(As at end-March 2008)

States		No. of Banks		Percentage to Total	
		Grades I & II	Grades III & IV	Grades I & II	Grades III & IV
1. Andhra Pradesh	2008	98	17	85	15
	2007	98	18	84	16
	2006	91	33	73	27
2. Gujarat	2008	209	62	77	23
	2007	202	82	71	29
	2006	186	110	63	37
3. Karnataka	2008	193	87	69	31
	2007	191	97	66	34
	2006	166	131	56	44
4. Madhya Pradesh/ Chhattisgarh	2008	45	25	64	36
	2007	46	28	62	38
	2006	44	31	59	41
5. Maharashtra/Goa	2008	392	217	64	36
	2007	388	234	62	38
	2006	399	231	63	37
7. Rajasthan	2008	36	3	92	8
	2007	37	2	95	5
	2006	35	4	90	10
8. Uttarakhand	2008	4	2	67	33
	2007	4	3	57	43
	2006				
<b>Total</b>	<b>2008</b>	<b>977</b>	<b>413</b>	<b>70</b>	<b>30</b>
	<b>2007</b>	<b>966</b>	<b>464</b>	<b>68</b>	<b>32</b>
	<b>2006</b>	<b>921</b>	<b>540</b>	<b>63</b>	<b>37</b>

**Note :** 1. Sound UCBs with no supervisory concern are classified as Grade I. The remaining three grades would indicate existence of supervisory concerns in increasing degree as per their positions on capital adequacy, net loss, NPA level, default in maintenance of CRR/SLR etc.  
2. Data related to Uttarakhand for the year 2006 are not available.

and banks with deposits below Rs.100 crore, whose branches are located in a single district; (ii) banks with deposits below Rs.100 crore having branches in more than one district, provided the branches are in contiguous districts, and deposits and advances of branches in one district separately constitute at least 95 per cent of the total deposits and advances, respectively, of the bank; (iii) banks with deposits below Rs.100 crore, whose branches were originally in a single district but subsequently, became multi-district due to reorganisation of the district. The deposit base of Rs.100 crore would be determined on the basis of average of fortnightly net demand and time liabilities (NDTL) in the financial year concerned and that of advances on the basis of fortnightly average in the financial year concerned. Rest of the UCBs are categorised as Tier II banks.

#### *Merger/Amalgamation and Exit of Unviable Entities*

4.11 The consolidation of the UCB sector through the process of merger of weak entities with stronger ones was set in motion by providing transparent and objective guidelines for granting 'no-objection' to merger proposals (Box IV.2).

#### *Financial Restructuring of UCBs having Negative Net Worth*

4.12 Apart from the non-disruptive exit route through mergers/amalgamations, the Reserve Bank also considered financial restructuring proposals for problem banks with large negative net-worth and with large number of deposit erosion. The financial restructuring proposals had to fulfill the following conditions: (i) interest of small depositors should be protected in full; (ii) a portion of deposit of individual depositors above Rs.1 lakh would be converted into equity. A portion of deposit of institutional depositors would be converted into innovative perpetual debt instrument (IPDI), which would

be eligible for inclusion as Tier I capital, subject to certain terms and conditions; (iii) the proportion of deposits converted into equity/IPDI should be such that the net worth of the bank after reconstruction becomes positive; (iv) the bank would have to maintain CRR/SLR on the restructured regular deposits; (v) after restructuring, the management of the bank should be in the hands of a board of administrators consisting of representatives of individual depositors, institutional depositors as well as professional bankers to ensure proper implementation of the reconstruction scheme, including recovery of NPAs.

#### *Working Group on Umbrella Organisations and Constitution of Revival Fund for the UCB Sector*

4.13 A Working Group on Umbrella Organisations and creation of Revival Fund for the UCB Sector was constituted by the Reserve Bank (Chairman: Shri V.S Das) on July 23, 2008: (i) to study the regulatory and supervisory structure of umbrella organisations of financial co-operative institutions/banks as prevalent in other parts of the world, especially in relation to raising of capital and intra co-operative group support system; (ii) to study the existing structure and legal framework for UCBs in India and to examine the need and scope for a federated structure/umbrella organisation for UCBs at the State level; (iii) to suggest appropriate supervisory and regulatory framework to facilitate emergence of such umbrella organisation(s) for UCBs, taking into consideration the international systems and experiences; and (iv) to study and suggest modalities for setting up an appropriate mutual assistance/revival fund for urban co-operative banks and the nature of support that could be provided by such fund. The Working Group, which comprises members from the Central Government, the State Governments, the UCB sector and the Reserve Bank have held three meetings so far.

**Box IV.2: Merger and Amalgamation of UCBs**

Merger and amalgamation provides an inorganic route for expansion, facilitating in the process consolidation, and emergence of strong entities and also paving the way for non-disruptive exit of weak/unviable entities. In view of these merits, the Reserve Bank provided transparent and objective guidelines for granting no-objection to merger proposals. The Reserve Bank looks into the financial aspects of the merger only with a view to protecting the interests of depositors and financial stability. Almost invariably, banks voluntarily approach the Reserve Bank to obtain no objection for their merger proposal. The guidelines on mergers are intended to facilitate the process by delineating the pre-requisites and steps to be taken for merger between banks.

The process of merger and amalgamation is elaborate. The application for merger giving the proposed scheme has to be submitted by the acquirer bank to the Registrar of Co-operative Societies (RCS)/Central Registrar of Co-operative

Societies (CRCS) and a copy of the proposal is simultaneously forwarded to the Reserve Bank along with certain specified information. The Reserve Bank examines the proposals and places the same before an expert group for screening and recommendations. On evaluation, if the proposal is found to be suitable, the Reserve Bank issues no objection certificate (NOC) to the RCS/CRCS and the banks concerned. RCS/CRCS, being the authorities vested with the responsibility of administering the Co-operative Societies Act, then issues the order of amalgamation of the target UCB in compliance with the provisions of the Act under which the bank is registered.

Pursuant to the issue of guidelines on merger of UCBs, since February 2005, Reserve Bank received 107 proposals for merger in respect of 92 banks. The Reserve Bank has issued NOC in 68 cases (Table 1 and 2). Of these, 61 mergers became effective upon the issue of statutory orders by the RCS/CRCS concerned. Twenty

**Table 1: State-wise Break-up of Acquirer Banks**  
(As on November 7, 2008)

Sr. Act Under No. Which Registered	No. of Acquirer Banks	No. of Proposals Submitted	No. of NOC Issued	No. of Proposals Rejected	No. of Proposals Withdrawn	Proposals Under Process
1	2	3	4	5	6	7
1. Multi-State	13	56	40	9	3	4
2. Maharashtra	14	22	11	8	Nil	3
3. Gujarat	6	9	7	1	1	Nil
4. Andhra Pradesh	6	7	5	Nil	Nil	2
5. Karnataka	3	4	2	1	Nil	1
6. Rajasthan	2	2	Nil	1	Nil	1
7. Punjab	1	1	1	Nil	Nil	Nil
8. Uttarakhand	2	3	2	Nil	1	Nil
9. Madhya Pradesh	2	2	Nil	Nil	Nil	2
10. Chattisgarh	1	1	Nil	Nil	Nil	1
<b>Total (1 to 10)</b>	<b>50</b>	<b>107</b>	<b>68</b>	<b>20</b>	<b>5</b>	<b>14</b>

**Table 2: State-wise Break-up of Target Banks**  
(As on November 7, 2008)

Sr. Act Under No. Which Registered	No. of Target Banks	No. of Proposals Submitted	No. of NOC Issued	No. of banks Merged	No. of Proposals Withdrawn	Proposals Rejected	Proposals Under process
1	2	3	4	5	6	7	8
1. Multi-State	1	1	1	1	NIL	NIL	NIL
2. Maharashtra	36	45	24	22	2	12	5
3. Gujarat	25	27	22	19	2	2	1
4. Andhra Pradesh	11	11	9	8	NIL	NIL	2
5. Karnataka	6	8	5	4	NIL	2	1
6. Goa	1	1	1	1	NIL	NIL	NIL
7. Rajasthan	1	1	NIL	NIL	NIL	1	NIL
8. Delhi	1	1	NIL	NIL	NIL	1	NIL
9. Punjab	1	1	1	1	NIL	NIL	NIL
10. Madhya Pradesh	6	7	3	4	NIL	2	2
11. Uttarakhand	2	3	2	1	1	NIL	NIL
12. Chattisgarh	1	1	NIL	NIL	NIL	NIL	1
<b>Total (1 to 12)</b>	<b>92</b>	<b>107</b>	<b>68</b>	<b>61</b>	<b>5</b>	<b>20</b>	<b>12</b>

**Table 3: Grade-wise Distribution of Merged Banks**

Grade	Number of Banks
I	8
II	4
III	8
IV	41
<b>Total</b>	<b>61</b>

*Memo item:* Out of 41 Grade IV banks, 35 banks had negative net worth.

proposals for merger were rejected by the Reserve Bank, five proposals were withdrawn by the banks and the remaining 14 are under consideration. Out of the 68 target banks for which NOC for merger was issued, 61 banks were merged and 35 of them were having negative net worth (Table 3). The profit-making banks were also permitted to merge with the aim of consolidation and strengthening the sector.

## Statutory Pre-emptions

### Policy on CRR

4.14 The cash reserve ratio (CRR) for scheduled primary urban co-operative banks was reduced to 5.50 per cent with effect from the fortnight beginning November 8, 2008 (Table IV.1).

### Policy on SLR

4.15 As per the provisions of Section 24 of the Banking Regulation Act, 1949 (AACS), deposits placed by UCBs with the higher financing agencies in the co-operative sector, viz., DCCBs/StCBs would be reckoned as SLR assets to the extent they are not encumbered. However, instances have come to light where some UCBs availed loans from the DCCB/StCB concerned without specifically earmarking their liability against their deposits. Though technically the entire deposits were being treated as eligible SLR asset, the deposits as such may not be available to the UCBs to meet their liquidity needs. Moreover, the lender bank (DCCB/StCB) in such cases can exercise its lien over the deposits of UCBs which have availed of loans in case of defaults. It was, therefore, decided that when a UCB avails of a loan from a DCCB/StCB with which it is maintaining deposits, for the purpose of computation of SLR, the amount of loan availed from the DCCB/StCB, would be deducted from the deposits, irrespective of whether lien has been marked on such deposits or not. UCBs have

been given a certain period to comply with the SLR requirements in the case of shortfall, if any, arising from the above instructions.

4.16 The issue of valuation of special securities, viz., those that do not qualify for the purpose of complying with the SLR requirements of banks, was examined. It was decided that for the limited purpose of valuation, all special securities issued by the Government of India directly to the beneficiary entities and which do not carry SLR status, may be valued at a spread of 25 basis points above the corresponding yield on Government of India securities. This amendment would come into force from the financial year 2008-09. Presently, such special securities comprise oil bonds, fertiliser bonds, bonds issued to the State Bank of India (during the recent rights issue), the *erstwhile* Unit Trust of India, Industrial Finance Corporation of India Ltd., Food Corporation of India, Industrial Investment Bank of India Ltd., the *erstwhile* Industrial Development Bank of India and the *erstwhile* Shipping Development Finance Corporation.

4.17 It was further clarified on July 11, 2008 that the balance maintained by UCBs in current account with IDBI Bank Ltd. would not be eligible for being reckoned as 'net balance' in current account for the purpose of CRR/SLR under sections 18 and 24 of Banking Regulation Act, 1949 (AACS) since IDBI Bank Ltd. is not reckoned for maintaining current accounts that will be treated as cash for the purpose of CRR/SLR by co-operative banks. UCBs, maintaining current account balances with IDBI Bank and presently reporting the same as CRR/SLR, were advised to intimate the position as on June 2008 to respective regional offices of the Reserve Bank.

**Table IV.1: Changes in CRR**

Sr.No.	Effective date*	CRR (As percentage of NDTL)
1	2	3
1.	April 14, 2007	6.25
2.	April 28, 2007	6.50
3.	August 4, 2007	7.00
4.	November 10, 2007	7.50
5.	April 26, 2008	7.75
6.	May 10, 2008	8.00
7.	May 24, 2008	8.25
8.	July 5, 2008	8.50
9.	July 19, 2008	8.75
10.	August 30, 2008	9.00
11.	October 11, 2008	6.50
12.	October 25, 2008	6.00
13.	November 8, 2008	5.50

\*: From the fortnight beginning.

## Regulatory Initiatives

### Asset Classification and Provisioning Norms

4.18 The asset classification and provisioning norms for Tier I UCBs would

continue to be different from Tier II UCBs as follows: (i) the 180 day loan delinquency norm for NPAs was extended by one year, i.e., up to March 31, 2009; (ii) the 12-month period for classification of a 'sub-standard' asset in 'doubtful' category by Tier I UCBs would be made effective from April 1, 2009 instead of April 1, 2008; (iii) these banks would be required to provide 100 per cent on the secured portion of D-III advances ('doubtful' for more than 3 years) as on or after April 1, 2010; and (iv) for the outstanding stock of D-III advances as on March 31, 2010, banks would be required to provide: (a) 50 per cent as on March 31, 2010; (b) 60 per cent as on March 31, 2011; (c) 75 per cent as on March 31, 2012; and (d) 100 per cent as on March 31, 2013.

4.19 For Tier II banks, 100 per cent provisioning norms for advances classified as D-III would be applicable on or after April 1, 2007 instead of those so classified on or after April 1, 2006. Consequently, for the outstanding stock of D-III assets as on March 31, 2007, banks are required to provide: (a) 50 per cent up to March 31, 2007; (b) 60 per cent as on March 31, 2008; (c) 75 per cent as on March 31, 2009; (d) 100 per cent as on March 31, 2010.

4.20 Keeping in view the nature of membership and loan profile of the salary earners' banks (SEBs), it was decided that the SEBs in Tier II may provide for standard assets in respect of personal loans at the rate of 0.4 per cent instead of the existing level of 2 per cent. Provisioning requirement in respect of loans and advances qualifying as capital market exposure, commercial real estate loans and loans and advances to systemically important NBFCs (non-deposit taking companies) would, however, continue to be 2 per cent for such banks. Tier I banks are already subject to a provisioning requirement of 0.25 per cent on their standard advances.

4.21 UCBs were required to provide at the rate of 10 per cent and 20 per cent per annum,

respectively, on their exposure to DCCBs, StCBs facing financial problems. In view of the absence of adequate avenues for raising of capital by these banks and the adverse impact of the revised provisioning norms on the profitability of UCBs, it was decided to defer the implementation of the revised provisioning norms by one year, i.e., to March 31, 2009.

#### *Risk Weights for Capital Adequacy*

4.22 According to the announcement made in the Annual Policy Statement for the year 2007-08, risk weight on loans up to Rs.1 lakh against gold and silver ornaments was reduced to 50 per cent from the prevailing level of 125 per cent. Further, risk weight for capital adequacy purpose on housing loans to individuals was reduced from the prevailing level of 75 per cent to 50 per cent as a temporary measure. This dispensation is applicable for loans up to Rs.20 lakh and would be reviewed after one year, keeping in view the default experience and other relevant factors. Moreover, as announced in the Annual Policy Statement 2008-09, the limit in respect of bank loans for housing in terms of applicability of risk weights for capital adequacy purposes was enhanced from Rs.20 lakh to Rs.30 lakh and such loans would carry a risk weight of 50 per cent. Education loans were earlier classified as a part of 'consumer credit' for the purpose of capital adequacy and attracted risk weight of 125 per cent. After a review, UCBs were advised not to classify education loans as 'consumer credit' for the purpose of capital adequacy norms. Accordingly the risk weight applicable to education loans would be 100 per cent as against 125 per cent.

#### *Asset-Liability Management*

4.23 Scheduled UCBs were advised to submit the structural liquidity statement and interest rate sensitivity statement through the asset-liability management (ALM) module provided in the off-site surveillance software



(OSS). The statement of structural liquidity was to be prepared at fortnightly intervals starting with the last reporting friday of June 2007, *i.e.*, June 22, 2007 and that of interest rate sensitivity on a monthly basis starting with the last reporting friday of the month of June, 2007. ALM guidelines have been prescribed for non-scheduled UCBs also and would be effective from the quarter ending December 2008. Basic liquidity risk management guidelines have been prescribed for Tier I banks as well which would also come into effect from the quarter ending December 2008.

4.24 UCBs were earlier advised not to consider any proposal for granting advances against shares/debentures for trading or for granting advances to share or stock brokers. It was further clarified to UCBs that they were prohibited from extending any fund based or non-fund based credit facilities, whether secured or unsecured, to stockbrokers. The prohibition would thus cover in addition to shares and debentures, loans and advances against other securities such as fixed deposits and LIC policies, among others. They were also advised not to extend any facility to commodity brokers. This includes issue of guarantees on behalf of the commodity brokers. Advances against units of mutual funds could be extended only to individuals as in the case of advances against the security of shares, debentures and bonds. UCBs were advised that any credit facility presently in force, but not in consonance with the above instructions should be withdrawn/closed without any delay.

4.25 Despite various safeguards being in place pertaining to the post sanction monitoring of advances, instances of diversion of funds and non-credit of sale proceeds to borrowal accounts continue to come to light and are observed to be important factor contributing to the perpetration of frauds/the account turning NPAs. UCBs were, therefore, advised on September 13, 2007 to adopt more

stringent safeguards, especially where accounts showed signs of turning into NPAs, *e.g.*, resorting to more frequent inspections of borrower's godowns, ensuring that the sale proceeds were routed through the borrower's accounts maintained with the bank and insisting on pledge of the stock instead of hypothecation. Whenever stock under hypothecation to cash credit and other loan accounts are found to have been sold but proceeds thereof have not been credited to the loan account, such action should normally be treated as a fraud and banks should take immediate steps to secure the remaining stock so as to prevent further erosion in the value of the available security.

#### *Frauds and Suspicious Transactions*

4.26 It was communicated to UCBs that as a part of transaction monitoring mechanism, they are required to put in place an appropriate software application that alerts them when the transactions are inconsistent with risk categorisation and updated profile of customers. They were also advised to initiate urgent steps to ensure electronic filing of cash transaction report (CTR) and suspicious transaction report (STR) to Financial Intelligence Unit - India (FIU-IND). Further, in view of reports by FIU-IND that many banks are yet to file electronic reports, UCBs were advised to arrange for filing the data of non-computerised branches into an electronic file with the help of the editable electronic utilities of CTR/STR as made available by FIU-IND on their website (<http://fiuindia.gov.in>). It was further clarified that cash transaction reporting by branches to their principal officer should be submitted on a monthly basis and not on a fortnightly basis and the principal officer, in turn, should ensure to submit CTR for every month to FIU-IND within the prescribed time schedule, *i.e.*, by 15 th of the succeeding month. It was reiterated that the cut-off limit of Rs.10 lakh for reporting in CTR should be applicable to integrally connected cash transactions also.

4.27 UCBs were advised on December 15, 2004 that they should pay special attention to all complex, unusual/large transactions and all unusual patterns of transactions which had no apparent economic or visible lawful purpose. It was further advised that the background papers/documents of such transactions should be examined and properly recorded to make it available to auditors and also to the Reserve Bank/other relevant authorities.

4.28 UCBs were also advised that the customers should not be tipped off on the STRs filed by them with FIU-IND. Banks should report all such attempted transactions in STRs, even if not completed by customers, irrespective of the amounts of transaction. 'Suspicious Transactions' are defined in Rule 2(g) of Rules notified under the Prevention of Money Laundering Act, 2002. Banks should submit STRs, if they have reasonable grounds to believe that the transaction involves proceeds of crime, generally, irrespective of the amount of transaction and/or threshold limit envisaged for predicate offences in part B of schedule of the PMLA, 2002. UCBs were advised to create awareness about KYC/AML among their staff and for generating alerts for suspicious transactions, they may consider the indicative list of suspicious activities contained in Annex E of the Indian Bank Association (IBA's) Guidance Note for Banks, 2005. UCBs were advised that these guidelines were issued under section 35A of the Banking Regulation Act, 1949(AACS) and any contravention of the said guidelines might attract penalties under the relevant provisions of the Act.

4.29 As wire transfer is an instantaneous and the most preferred route for transfer of funds across the globe, there is a need for preventing terrorists and other criminals from having unfettered access to it for moving their funds and for detecting any misuse when it occurs. UCBs were, therefore, advised to

invariably ensure certain specified information about all wire transfers. An ordering bank, where the wire transfer originates, must ensure that qualifying wire transfer contains complete originator information and intermediary bank should ensure that the same is retained with the transfer. The record of such information should be preserved for a period of 10 years. A beneficiary bank should have effective risk-based procedures in place to identify wire transfers lacking complete originator information. The lack of complete originator information may be considered as a factor in assessing whether a wire transfer or related transactions are suspicious and whether they should be reported to the FIU-IND.

## **Credit Delivery and Financial Inclusion**

### *Priority Sector Lending*

4.30 In view of significant changes in the regulatory framework for UCBs, which has become more or less comparable with that of commercial banks and the exemptions hitherto enjoyed by UCBs from the payment of income tax having been withdrawn, the priority sector lending target for UCBs was brought down to 40 per cent of the adjusted bank credit (ABC) (total loans and advances plus investments made by UCBs in non-SLR bonds) or credit equivalent amount of off-balance sheet exposure (OBE), whichever is higher, as on March 31 of the previous year and thus brought at par with the target applicable to commercial banks. The revised target came into effect from April 1, 2008.

4.31 UCBs were required to submit data annually on priority sector lending within a month from the end of the reference period, i.e., March 31 every year and credit flow to minority communities every half year as on March 31 and September 30 in the prescribed format. The existing reporting formats and periodicity were reviewed and revised on June 30, 2008. Sectors that qualify for inclusion as

priority sector were revised in August 2007 and areas that qualify for inclusion as priority sector now include: (i) total agricultural credit (direct and indirect); (ii) total credit to small enterprises (direct and indirect); (iii) retail trade; (iv) micro credit; (v) State sponsored organisations for SC/ST; (vi) education; and (vii) housing. UCBs were advised to submit the first set of revised returns by April 15, 2009 to the concerned Regional Offices of the Reserve Bank.

4.32 The definitions of micro, small and medium enterprises were modified on August 30, 2007. The modified definitions of micro, small and medium enterprises engaged in manufacturing or production and in providing or rendering services are as under—(i) enterprises engaged in the manufacture or production, processing or preservation of goods: (a) where investment in plant and machinery does not exceed Rs.25 lakh is a micro enterprise; (b) where the investment in plant and machinery is more than Rs.25 lakh, but does not exceed Rs.5 crore is a small enterprise; (c) where the investment in plant and machinery is more than Rs.5 crore, but does not exceed Rs.10 crore is a medium enterprise; and (ii) enterprises engaged in providing or rendering services: (a) where the investment in equipments does not exceed Rs.10 lakh is a micro enterprise; (b) where the investment in equipment is more than Rs.10 lakh, but does not exceed Rs.2 crore is a small enterprise; (c) where the investment in equipment is more than Rs.2 crore, but does not exceed Rs.5 crore is a medium enterprise. Bank's lending to medium enterprises would not be included for the purpose of reckoning under the priority sector.

*Agricultural Debt Waiver and Debt Relief Scheme, 2008*

4.33 In the budget speech for 2008-09, the Hon'ble Union Finance Minister announced a Debt Waiver and Debt Relief Scheme for

farmers, which was subsequently notified by the Government. The detailed scheme along with necessary explanations was forwarded to UCBs and they were advised to take necessary action for implementing the scheme.

*Guidelines for Relief Measures by Banks to Poultry Industry, 2008*

4.34 In view of the instances of outbreak of Avian Influenza (bird flu) in some parts of the country and consequent loss of income on account of culling of birds for poultry units financed by the banks, UCBs were advised on February 19, 2008 to consider extending certain facilities to them as under: (i) principal and interest due on working capital loans as also instalments and interest on term loans which had fallen due for payment on or after the onset of bird flu, i.e., December 31, 2007 and remaining unpaid amount may be converted into term loans—the converted loans may be recovered in instalments based on projected future inflows over a period up to three years with an initial moratorium of up to one year (the first year of repayment may be fixed after the expiry of moratorium period); (ii) the remaining portion of term loans may be rescheduled similarly with a moratorium period up to one year depending upon the cash flow generating capacity of the unit; (iii) the rescheduling/conversion may be completed on or before April 30, 2008; (iv) the rescheduled/converted loans may be treated as current dues; (v) after conversion as above, the borrower will be eligible for fresh need-based finance; (vi) the relief measures as above may be extended to all accounts of poultry industry, which were classified as standard accounts as on December 31, 2007.

*KYC norms*

4.35 In order to ensure that the customer acceptance policy and its implementation does not result in denial of banking services to general public, especially to those who are financially or socially disadvantaged, UCBs were advised to review their extant internal instructions in this regard so that a section of

public may not be denied access to banking services. It was clarified to UCBs that 'permanent correct address' referred to in the existing instructions, means the address at which person normally resides and can be taken as the address as mentioned in a utility bill or any other document accepted by the bank for verification of the address of the customer. Banks should keep in mind the spirit of instructions issued by the Reserve Bank and avoid undue hardships to individuals who are otherwise classified as low risk customers. Banks were further advised that the review of risk categorisation of customers should be carried out not less than once in six months. Banks should also introduce a system of periodical updating of customer identification data after the account was opened. The periodicity of such updation should not be less than once in five years in case of low risk category customers and not less than once in two years in case of high and medium risk categories of customers.

### **Customer Services**

4.36 UCBs were advised on May 18, 2007 to lay down appropriate internal principles and procedures so that usurious interest, including processing and other charges are not levied by them on loans and advances. In laying down such principles and procedures in respect of small value loans, particularly, personal loans and such other loans of similar nature, banks were advised to take into account certain broad guidelines. Banks were further advised to put in place such principles and procedures within a period of three months from the date of notification.

4.37 UCBs were advised that all transactions, including payment of interest on deposits/charging of interest on advances, should be rounded off to the nearest rupee (fraction of 50 paise and above to be rounded off to the next higher rupee and that of less than 50 paise to be ignored). Banks were,

however, advised that cheques issued by their clients for amounts containing fraction of rupee should not be rejected or dishonoured. Banks were also advised to ensure that the concerned staffs are well versed with these instructions so that general public does not suffer. They should also ensure that appropriate action is taken against members of their staff who are found to have refused to accept cheques/drafts containing fraction of a rupee. Banks were also advised to note that violation of aforesaid instructions would be liable to be penalised under the provisions of the Banking Regulation Act, 1949 (AACS).

4.38 UCBs were advised to generally insist that a person opening a deposit account makes a nomination. The bank should explain the advantages of nomination facility to the depositor and if the person still does not want to nominate, the bank should ask him to give a specific letter to the effect that he does not want to make nomination. In case the person declines to give such a letter, the bank should record the fact on the account opening form and proceed with opening of the account, if otherwise found eligible. Under no circumstances, though, should a bank refuse to open an account solely on the ground that the person opening the account has refused to nominate. UCBs were also advised to follow the procedure outlined above in respect of deposit accounts in the name of sole proprietary concerns.

4.39 Some schemes with lock-in periods and other restrictive features floated by some banks were not in conformity with the Reserve Bank's instructions. Banks, which have floated such deposit schemes, were advised to discontinue the schemes with immediate effect and report compliance to concerned regional offices of the Reserve Bank.

4.40 Scheduled UCBs were advised to formulate a comprehensive and transparent policy covering the following three aspects,

taking into account their technological capabilities, systems and processes adopted for clearing arrangements and other internal arrangements for collection through correspondents: (a) immediate credit of local/outstation cheques; (b) timeframe for collection of local/outstation instruments; and (c) interest payment for delayed collection. They were also advised to review their existing arrangements and capabilities and work out a scheme for reduction in collection period. Adequate care should be taken to ensure that the interests of the small depositors were fully protected. The policy should clearly lay down the liability of the banks by way of interest payments due to delay for non-compliance with the standards set by the banks themselves and should be integrated with the deposit policy formulation by the bank in line with the IBA's noted policy. Scheduled UCBs were advised to place the policy before the board and obtain their specific approval thereon. They were advised to send a copy of cheque collection policy, after the board's approval, to the Reserve Bank for its confirmation before implementation.

4.41 To increase the usage of ATMs as a delivery channel, banks entered into bilateral or multi-lateral arrangements with other banks to have inter-bank ATM networks. The charges levied on the customers vary from bank to bank, according to the ATM network that is used for the transaction. The ideal situation is that a customer should be able to

access any ATM installed in the country free of charge through an equitable co-operative initiative by banks. Based on the feedback report on an approach paper placed on the website of the Reserve Bank, a framework of service charges for implementation by all banks was decided (Table IV.2).

4.42 For the services at (i) and (ii) in Table IV.2, the customer would not be levied any charge under any other head and for services at (iii), the charge of Rs.20 would be all inclusive and no other charges would be levied under any other head, irrespective of the amount of withdrawal. The service charges for the following types of cash withdrawal transactions may be determined by the banks themselves: (a) cash withdrawal with the use of credit cards; and (b) cash withdrawal in an ATM located abroad.

*Other Measures*

4.43 The Committee on Procedures and Performance Audit on Public Services (CPPAPS) had made some recommendations for easy operation of lockers. on June 21, 2007, UCBs were also advised accordingly. UCBs were also permitted to lay down policies with the approval of their boards for sanction of gold loans with bullet repayment option, subject to the guidelines issued by the Reserve Bank.

4.44 Since visually challenged persons are legally competent to contract, banking facilities including cheque book facility/

**Table IV.2: ATM Charges**

Sr. No.	Service	Charges
1	2	3
(i)	For use of own ATMs for any purpose	Free (with effect from March 12, 2008)
(ii)	For use of other bank ATMs for balance enquiries	Free (with effect from March 12, 2008)
(iii)	For use of other bank ATMs for cash withdrawals	<ul style="list-style-type: none"> <li>• No bank shall increase the charges prevailing as on December 23, 2007 (i.e., the date of release of Approach Paper on RBI website)</li> <li>• Banks which are charging more than Rs.20 per transaction shall reduce the charges to a maximum of Rs.20 per transaction by March 31, 2008</li> <li>• Free with effect from April 1, 2009</li> </ul>

operation of ATM/locker, etc., cannot be denied to them. It was brought to the notice of the Reserve Bank that visually challenged persons were facing problems in availing of banking facilities. UCBs were, therefore, advised on June 4, 2008 to ensure that all banking facilities such as cheque book facility, including third party cheques, ATM facility, net banking facility, locker facility, retail loans and credit cards, among others, should invariably be offered to the visually challenged without any discrimination.

### **Other Policy Initiatives**

#### *Investments in Non-SLR Securities by UCBs*

4.45 To allow UCBs greater flexibility in making non-SLR investments, the instructions on the subject were reviewed and significant changes in the guidelines were made. First, UCBs can now invest in 'A' or equivalent rated commercial papers (CPs), debentures and bonds that are redeemable in nature which were not permitted earlier. Second, they can also invest in units of debt mutual funds and money market mutual funds. Earlier, only investment in units of UTI were permitted and not in other mutual funds. This distinction was done away with, though no investment in equity linked mutual funds is permitted. Third, fresh investments in shares of all-India financial institutions (AIFIs) would also not be permitted unlike hitherto. Fourth, balances held in deposit accounts with commercial banks and in permitted scheduled UCBs and investments in certificate of deposits issued by commercial banks would be outside the limit of 10 per cent of total deposit prescribed for non-SLR investments. Fifth, a cap of 10 per cent of NDTL has been placed on the total amount of funds that can be placed as inter-bank deposits (for all purposes including clearing, remittance, etc). The prudential inter-bank exposure limit of 10 per cent of the NDTL would be all-inclusive and not limited to inter-bank call and notice money. The only exception is made for Tier I UCBs, which may place deposits up to 15 per cent of their NDTL with public sector banks

over and above the said prudential limit of 10 per cent of NDTL. Sixth, exposure to any single bank should not exceed 2 per cent of the depositing bank's DTL as on March 31 of the previous year, inclusive of its total non-SLR investments and deposits placed with that bank. Deposits, if any, placed for availing CSGL facility, currency chest facility and non-fund based facilities like bank guarantee (BG), letter of credit (LC) would be excluded to determine the single bank's exposure limit for this purpose.

#### *Instruments for Augmenting Capital Funds*

4.46 In order to facilitate raising of capital funds, UCBs were permitted on July 15, 2008 to issue preference shares, viz., (i) perpetual non-cumulative preference shares (PNCPS); (ii) perpetual cumulative preference shares (PCPS); (iii) redeemable non-cumulative preference shares (RNCPS); and (iv) redeemable cumulative preference shares (RCPS). Further, UCBs were also permitted to raise term deposits for a minimum period of not less than 5 years, which would be eligible to be treated as Tier II capital. The important features of the instruments for augmenting capital funds are: first, the extant share linking norm would not be applicable to a member who was already holding 5 per cent of the total paid-up share capital of an UCB; Second, Tier II capital has been further divided into upper and lower tiers. PCPS, RNCPS and RCPS 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. Long-term deposit should not exceed 50 per cent of Tier II capital and that total Tier II should not exceed Tier I capital; Third, as per extant instructions, elements of Tier II capital were reckoned as capital funds up to a maximum of 100 per cent of Tier I capital. In the case of banks that are having CRAR less than 9 per cent, it was decided that the above restriction should be kept in abeyance for five years, i.e., up to March 31, 2013 in order to give time to the banks to raise Tier I capital. In other words,

Tier II capital would be reckoned as capital funds for capital adequacy purpose even if a bank does not have Tier I capital. However, during this period, 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.

*Implementation of Recommendations of the Working Group on Access Criteria to Payment Systems*

4.47 According to the announcement made in the Annual Policy Statement 2007-08, a Working Group was constituted for prescribing guidelines for access to various payment systems. The Working Group recommended that membership to clearing houses at MICR centres be confined to licenced banks meeting the following financial criteria: (i) CRAR of 9 per cent; (ii) net NPA of less than 10 per cent; (iii) no default in maintenance of CRR and SLR during the past one year; and (iv) net profit in at least one of the two preceding years. Further, the Working Group recommended that the entities which are presently members of clearing houses at MICR centres but ineligible to be members as per the proposed access criteria, would have to conform to the prescribed norms within one year, failing which membership would be downgraded to that of a sub-member. The Working Group has also recommended that such banks may be barred with immediate effect, from sponsoring any sub-member.

*INFINET Membership for UCBs*

4.48 On the basis of the recommendations of the Working Group for 'Access to Payment Systems' constituted for preparation of comprehensive guidelines setting out the minimum eligibility criteria for membership of clearing houses/payment systems, regional offices of the Reserve Bank were advised to extend INFINET membership to all UCBs, provided they had the requisite infrastructure in place for the same. The applicant bank should be advised to submit details of infrastructure available with it for

participation in the INFINET, together with a board resolution for seeking the membership. Subject to the above parameters, unlicensed UCBs could also be permitted to avail of INFINET membership so long as their application for license has not been rejected by the Reserve Bank. Regional offices of the Reserve Bank were further advised to make it clear to these banks that the membership would not in any way entitle them to claim a banking license at a later date and their application for license would be examined independently on its merits.

4.49 The efforts to increase the spread of technology in the UCB sector attracted greater attention with the setting up of a Working Group to examine the areas relating to IT support to UCBs (Box IV.3).

*Rationalisation of Returns Submitted by UCBs*

4.50 In view of a large number of returns that the UCBs were required to submit, as directed by the Board for Financial Supervision (BFS), an exercise for rationalisation of returns to be submitted by UCBs was undertaken. The returns submitted by UCBs were examined from the point of view of reducing the volume of data to be submitted by banks without compromising on the breadth and depth of information being obtained from them. The rationalisation of the returns was done and the maximum number of returns was reduced to 29 as against a maximum of 36 returns required to be submitted by the scheduled UCBs earlier.

*Insurance Business*

4.51 According to the Annual Policy Statement for the year 2007-08, UCBs registered in States that had entered into MoU with the Reserve Bank or those registered under Multi-State Co-operative Societies Act, 2002 were allowed to undertake insurance agency business as corporate agents without risk participation, subject to compliance with the following eligibility norms: first, UCB should have a minimum net worth of Rs.10 crore; second, it should not have been

### Box IV.3: Working Group on IT support to UCBs

The Mid-term Review of the Annual Policy Statement for the year 2007-08 announced the constitution of a Working Group comprising representatives of the Reserve Bank, State Governments and the UCBs sector to examine the various areas where IT support could be provided to the UCBs by the Reserve Bank. Accordingly a Working Group on IT support to UCBs (Chairman: Shri R. Gandhi) was constituted.

The Group, while acknowledging the increasing importance of IT in UCBs, observed that there was a wide variance among them with regard to the usage of IT. In fact, the lack of uniformity in the levels of computerisation and inadequate awareness about the efficacy of computers in enhancing competitiveness prompted the Group to articulate the following minimum IT infrastructure which should exist in each UCB regardless of its size, location or profitability: (i) computerised front-end, *i.e.*, customer interface; (ii) automatic back-end accounting (through software); (iii) computerised MIS reporting; and (iv) automated regulatory reporting.

The Group felt that in order to implement the minimum level of IT infrastructure by the UCBs, core banking solution (CBS) would be required to be adopted by them. The model of CBS may vary according to the size and spread of the UCBs.

The Group suggested two methods for acquiring the IT infrastructure, *viz.*, (i) application service provider; and (ii) outright purchase. The former is suitable for small banks, particularly the unit banks because the problems of software development and maintenance, training and retention of IT professionals, installation and maintenance of complex and costly hardware and other logistics like data centres, would be addressed by the service provider without need for much initiative or involvement of the UCBs. An agency like Institute for Development and Research in Banking Technology (IDRBT) could short-list/select one/a few vendors and be the conduit and service quality assurer to the UCBs. On the other hand, the method of outright purchase of the CBS, including data centre may be preferable to a few large banks.

The Group also deliberated on delivery mechanism and felt that support could be routed through IDRBT and if required, IDRBT might develop an area of expertise within itself to cater to the IT needs of small banks, including UCBs. National and State Federation of co-operatives might also think of creating such IT facilities for UCBs in the long run for the benefit of the sector. The recommendations of the Group are being examined by the Reserve Bank.

classified as Grade III or IV. The minimum net worth criteria earlier applicable was dispensed with for such banks on May 15, 2008.

#### *Norms for Maintaining NRE/NRO Accounts*

4.52 UCBs registered in States that had entered into a MoU with the Reserve Bank for supervisory and regulatory co-ordination and those registered under the Multi State Co-operative Societies Act, 2002 were permitted to open NRE account subject to compliance with the following eligibility norms: (i) minimum net worth of Rs.25 crore; (ii) CRAR of not less than 9 per cent; (iii) net NPAs to be less than 10 per cent; (iv) compliance with CRR/SLR requirements; (v) net profit during the preceding three years without any accumulated losses; (vi) sound internal control systems; (vii) satisfactory compliance with KYC/AML guidelines; and (viii) presence of at least two professional directors on the board.

4.53 UCBs are not permitted to accept NRO deposits and are required to close these accounts within a given time frame. It was decided on June 4, 2007 that banks may maintain NRO accounts, arising from their re-

designation as such, upon the account holders becoming non-resident. Opening of fresh NRO accounts was not permitted. Furthermore, no fresh credit, barring periodical credit of interest, was allowed in these accounts. However, these restrictions were not applicable to UCBs holding AD Category-I licence.

#### *Relaxation in Branch Authorisation Policy for UCBs*

4.54 In terms of the Annual Policy Statement 2007-08, UCBs were allowed to open new branches/extension counters. The eligibility criteria prescribed for new branches/extension counters were as under: (i) the bank should be registered under the Cooperative Societies Act of the States that had signed MoU with the Reserve Bank or under the Multi-State Cooperative Societies Act, 2002; (ii) the bank should be licensed and have an elected board of directors with at least two professionals; (iii) the bank should comply with the following mutually exclusive, performance/financial parameters – (a) CRAR should not be less than 9 per cent; (b) net NPA should be below 10 per cent; (c) there should



have been no default in maintenance of CRR/SLR in the preceding financial year; (d) the bank should have net profit in the preceding financial year; (e) the net worth should not be less than Rs.10 crore; and (f) the average net worth per branch/extension counter, including the additional centres for which licenses are sought, should not be less than Rs.2 crore per branch in A and B centres with population more than 5 lakh and Rs.1 crore in C and D centres with population less than 5 lakh. UCBs satisfying the above mentioned conditions are eligible for additional branches/extension counters not exceeding 10 per cent of their existing branch network, over a period of two years. All UCBs are required to obtain prior authorisation for opening of extension counters.

4.55 Further, in terms of the Annual Policy Statement 2008-09, approvals for branch expansion including off-site ATMs in respect of well managed and financially sound UCBs in the States that have signed MoUs and those registered under the Multi-State Co-operative Societies Act, 2002, are now considered, based on their annual business plans, subject to: (i) maintenance of a minimum CRAR of 10 per cent on a continuous basis with minimum owned funds commensurate with entry point capital norms for the centre where the branch is proposed; (ii) net NPAs should be less than 10 per cent; (iii) no default in maintenance of CRR/SLR during the preceding financial year; (iv) net profit in the immediate preceding financial year; and (v) regulatory comfort based on its track record of compliance.

4.56 The Annual Policy Statement for the Year 2008-09 liberalised the eligibility norms for opening of on-site ATMs. Accordingly, w.e.f. May 26, 2008, UCBs that are registered in States that have signed MoUs with the Reserve Bank or under Multi-State Co-operative Societies Act, 2002 and classified in Grades other than Grade III and IV, are allowed to set up on-site ATMs without prior approval of the Reserve Bank.

4.57 The powers for grant of branch authorisation for Tier I banks registered under

the State Co-operative Societies Acts in States that had signed MoUs with the Reserve Bank were delegated to its regional offices. On receipt of annual business plans, regional offices of the Reserve Bank were advised to scrutinise whether UCBs satisfied the norms prescribed and any other requirements identified in consultation with TAFCUB.

#### *Shifting of Offices*

4.58 In relaxation of the existing guidelines, UCBs were permitted on August 28, 2007 to shift their branches from one city to another in their area of operation within the same State, subject to the following conditions: (a) the new centre should be located in an area with same or lower population compared to the existing centre; (b) a branch located in under-banked district can be shifted to another centre in under-banked district only; and (c) the shifting should be beneficial to the bank in terms of cost and business. UCBs were further advised to submit their applications in this regard to the regional office of Urban Co-operative Bank Department of the Reserve Bank in whose jurisdiction the head office of the bank was situated.

#### *Mahila Urban Co-operative Banks – Membership*

4.59 Membership of *Mahila* UCBs was exclusively confined to women except as nominal members for the purpose of standing as sureties for the borrowers from the bank. Taking into account the representations made by the banks and their federations and the findings of case studies carried out by the Reserve Bank in this regard, existing *Mahila* UCBs which conform to the extant entry point norms for general category banks, were permitted to enroll male members up to a limit of 25 per cent of their total regular membership, subject to compliance by the banks with their respective bye-laws. Registrar of Co-operative Societies of Central and all State Governments were requested to convey their approval to UCBs wherever applicable, for induction of male borrowers up to a limit of 25 per cent of their total regular membership.