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MONETARY AND CREDIT
INFORMATION REVIEW

POLICY

Stripping/Reconstitution of Government Securities

The Reserve Bank has decided to introduce separate trading of registered interest and principal of securities (STRIPS) in government securities as part of the efforts to develop the government securities market. Detailed guidelines outlining the process of stripping/reconstitution and other operational procedures regarding transactions in STRIPS have been provided. STRIPS in government securities will ensure availability of sovereign zero coupon bonds, which will lead to the development of a market determined zero coupon yield curve (ZCYC). STRIPS will also provide institutional investors with an additional instrument for their asset-liability management. Further, as STRIPS have zero reinvestment risk (discounted instruments with no periodic interest payment thereby obviating the need for reinvestment of intermediate cash flows arising out of the investment), they can be attractive to retail/non-institutional investors.

Investment Portfolio of Primary Dealers

The Reserve Bank, while reviewing the guidelines in respect to categorisation of government securities for the standalone primary dealers (PDs), has decided to permit the standalone PDs to hold government securities in the held-to maturity (HTM) category to the extent of their audited net owned funds (NOFs) as at the March end of the preceding financial year. The NOFs will be computed in terms of the explanatory note to section 45-IA of chapter III-B of the Reserve Bank of India Act, 1934. As per earlier provisions, the standalone PDs were allowed to categorise government securities up to 100 per cent of their paid up capital in the HTM category, subject to certain conditions. Banks undertaking PD activities departmentally would continue to follow the extant guidelines applicable to banks in regard to the classification and valuation of the investment portfolio issued by the Reserve Bank.

Educational Loan Scheme

The Reserve Bank has directed all scheduled commercial banks to ensure meticulous compliance of its directives regarding educational loan scheme which requires that no security may be insisted upon for loans upto Rs.4.00 lakh. The

Reserve Bank have been receiving representations from various quarters that banks were demanding collateral security even for loans upto Rs.4.00 lakh. Keeping this in view, banks have been asked to issue suitable instructions to their branches/controlling offices in this regard.

Clearing-related Overdraft

As per the extant provisions, for unauthorised overdrafts on account of adverse clearing position, defaulting banks are required to pay penal interest at the rate applicable to clean overdrafts plus 2 per cent from the following working day till the position is regularised. The Reserve Bank has been receiving a number of references regarding exorbitant interest being levied by some clearing house managing banks for extending clearing-related overdrafts in member bank settlement accounts and also some member banks

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routinely demanding overdraft free of interest from settlement banks to meet clearing-related shortfalls during the day. A meeting of major clearing house managing banks was conducted where the issue was discussed and, for the sake of uniformity in levy of interest for clearing-related overdrafts, it has been decided as under:

- a. To benchmark the applicable interest rate for clearing-related overdrafts to the Reserve Bank liquidity adjustment facility (LAF) repo rate.
- b. For intra-day overdraft (the day when the overdraft is extended, irrespective of the time period for which the overdraft facility is enjoyed), interest shall be charged at relevant LAF repo rate + 100 basis points.
- c. If the overdraft extends to the following day (overnight and beyond), interest shall be charged at relevant LAF repo rate + 300 basis points.
- d. The cushion of 100 and 300 basis points over the relevant LAF repo rate is provided as the clearing-related overdraft is non-collateralised whereas repo is collateralised in nature.
- e. In instances where settlement accounts of member banks (with the settlement bank at the concerned clearing location) are not credited in time and the settlement bank has levied overdraft charges, though funds have already been remitted and credited to the settlement bank's account at Mumbai (or any other central location - through RTGS or otherwise), the overdraft charges shall be refunded, on member banks proving that the funds were received in time by the settlement bank.

Micro and Small Enterprises (MSEs)

Accepting the recommendations of a working group to review the credit guarantee scheme (CGS) of the credit guarantee fund trust for micro and small enterprises (CGTMSE), the Reserve Bank has directed all scheduled commercial banks including regional rural banks and local area banks to not to accept collateral security in the case of loans upto Rs.10 lakh extended to units in the MSE sector. Banks have also been asked to strongly encourage their branch level functionaries to avail of the CGS cover, including making performance in this regard a criterion in the evaluation of their field staff. It may be recalled that the report of the working group to review CGS containing several recommendations was released on March 06, 2010.

Non-SLR Investments

As per prudential norms for classification, valuation and operation of investment portfolio by banks, bank's investment in unlisted non-SLR securities should not exceed 10 per cent of its total investment in non-SLR securities as on March 31, of the previous year. Further, banks have been allowed to invest in unrated bonds of companies engaged in infrastructure activities within the ceiling of 10 per cent of unlisted non-SLR securities. Since there is a time lag between issuance and listing of securities, which are proposed to be listed but not listed at the time of subscription, banks may not be able to

participate in primary issues of non-SLR securities. In view of the above the Reserve Bank has now decided that investment in non-SLR debt securities (both primary and secondary market) by banks where the security is proposed to be listed on the exchange(s) may be considered as investment in listed security at the time of making investment. However, if such security is not listed within the period specified, the same will be reckoned for the 10 per cent limit specified for unlisted non-SLR securities. In case such investments included under unlisted non-SLR securities lead to a breach of the 10 per cent limit, the bank would not be allowed to make further investment in non-SLR securities (both primary and secondary market) as also in unrated bonds issued by companies engaged in infrastructure activities till such time bank's investment in unlisted non-SLR securities comes within the limit of 10 per cent.

Priority Sector Lending

The Reserve Bank has clarified that loans granted by banks for agricultural and allied activities are eligible for classification under priority sector, irrespective of whether borrowing entity is engaged in export or otherwise. The export credit granted for agricultural and allied activities may be reported separately under heading: "export credit to agriculture sector". Some of the banks had sought clarification in respect of classification of working capital limits granted to borrowers engaged in agricultural and allied activities and to food and agro-based processing units by way of export credit, under priority sector.

Business Correspondents

The Reserve Bank has permitted banks to engage any individual, including those operating common service centres (CSCs) as business correspondents (BCs), subject to banks' comfort level and their carrying out suitable due diligence as also instituting additional safeguards as may be considered appropriate to minimise the agency risks. The policy in this regard was announced earlier as a part of the annual policy statement for the year 2010-11 of the Reserve Bank.

FEMA

Current Account Transactions – Liberalisation

As per the extant provisions, prior approval of the ministry of commerce and industry, Government of India, is required for drawing foreign exchange for remittances under technical collaboration agreements where payment of royalty exceeds 5 per cent on local sales and 8 per cent on exports and lump-sum payment exceeds USD 2 million. While reviewing the extant policy in regard to foreign technology agreements, the government has decided to omit the aforesaid provision as a measure of further liberalisation. Accordingly, authorised dealer Category-I banks (AD Category-I banks) may permit drawal of foreign exchange by persons for payment of royalty and lump-sum payment under technical collaboration agreements without the approval of ministry of commerce and industry, Government of India.

External Commercial Borrowings (ECB) Policy

On a review of the policy, the Reserve Bank has decided to modify the extant ECB policy in respect of the infrastructure finance companies (IFCs) i.e. non-banking finance companies (NBFCs) categorised as IFCs by the Reserve Bank. As per the extant norms, IFCs have been permitted to avail of ECBs for on-lending to the infrastructure sector, as defined in the extant ECB policy, under the approval route. As a measure of liberalisation of the existing procedures, it has been decided to permit the IFCs to avail of ECBs, including the outstanding ECBs, up to 50 per cent of their owned funds under the automatic route, subject to their compliance with the prudential guidelines already in place. ECBs by IFCs above 50 per cent of their owned funds would require the approval of the Reserve Bank and will, therefore, be considered under the approval route. Designated authorised dealer banks have been directed to ensure compliance with the extant norms while certifying the ECB application both under the automatic and approval routes. All the other aspects of ECB policy such as USD 500 million limit per company per financial year under the automatic route, eligible borrower, recognised lender, end-use, average maturity period, prepayment, refinancing of existing ECB and reporting arrangements remain unchanged.

Foreign Direct Investment (FDI)

The Reserve Bank, in consultation with the Government of India, has reviewed the extant guidelines applicable to issue of equity instruments to a person resident outside India under the foreign direct investment (FDI) policy. As per the extant policy, an Indian company may issue equity shares, compulsorily convertible preference shares and compulsorily convertible debentures (equity instruments) to a person resident outside India under the FDI policy, subject to inter-alia, compliance with the pricing guidelines. Further, a general permission is available for transfer of equity instruments, by way of sale, from residents to non-residents (including transfer of subscriber's shares) of an Indian company in sectors other than financial services sector (i.e. banks, NBFCs, insurance, asset reconstruction companies, infrastructure companies in securities market namely, stock exchanges, depositories and clearing corporations, credit information companies and commodity exchanges) from residents to non-residents and vice-versa. The extant guidelines have been reviewed and accordingly the pricing guidelines in respect of issue of shares including preferential allotment have been revised. The main highlights of the revised instructions applicable to transfer of shares of an Indian company are as follows:

- I. Transfer by resident to non-resident (i.e. to foreign national, non-resident Indian, foreign institutional investor and incorporated non-resident entity other than erstwhile overseas corporate body)-
 - (a) Where shares of an Indian company are listed on a recognised stock exchange in India, the price of shares transferred by way of sale shall not be less than the price at which a preferential allotment of shares can be made under the Securities and Exchange Board of India (SEBI) guidelines, as

applicable, provided that the same is determined for such duration as specified therein, preceding the relevant date, which shall be the date of purchase or sale of shares.

- (b) Where the shares of an Indian company are not listed on a recognised stock exchange in India, the transfer of shares shall be at a price not less than the fair value to be determined by a SEBI registered Category-I merchant banker or a chartered accountant as per the discounted free cash flow method. The price per share arrived at should be certified by a SEBI registered Category-I merchant banker/chartered accountant.

II. Transfer by Non-resident to resident-

- (a) Price of shares transferred by way of sale, by non-resident to resident shall not be more than the minimum price at which the transfer of shares can be made from a resident to a non-resident as given above.

Foreign Exchange for Visits Abroad

In terms of the extant provisions, authorised dealers and full fledged money changers are permitted to sell foreign exchange in the form of foreign currency notes and coins, up to USD 2,000 or its equivalent, to the travellers proceeding to countries other than Iraq, Libya, Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States. The existing limits have been reviewed and the Reserve Bank has decided to increase this ceiling, with immediate effect, to USD 3,000 to the travellers without the prior permission from the Reserve Bank. Authorised dealers and full fledged money changers may, as hitherto, continue to sell foreign exchange in the form of foreign currency notes and coins up to USD 5,000 or its equivalent to the travellers proceeding to Iraq or Libya, out of the overall foreign exchange released and full foreign exchange may be released in the form of foreign currency notes and coins to the travellers proceeding to the Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States.

NBFCs

Finance for Housing Projects

The Reserve Bank has directed that while granting finance to housing/development projects, non-banking finance companies (NBFCs) should stipulate as a part of the terms and conditions that:

- (i) the builder/developer/owner/company would disclose in the pamphlets/brochures/advertisements etc., the name(s) of the entity to which the property is mortgaged.
- (ii) the builder/developer/owner/company should indicate in the pamphlets/brochures, that they would provide no objection certificate (NOC)/permission of the mortgagee entity for sale of flats/property, if required.

It may be recalled that earlier in a case which had come up before the Hon'ble High Court of Judicature at Bombay, the Hon'ble Court had observed that the bank granting finance in housing should insist on disclosure of the charge or any other liability on the plot in question or development project being duly made in the brochure or pamphlet etc., which may be published by developer/owner inviting public at large to purchase flats and properties. The Court had also added that this obviously would be part of the terms and conditions on which the loan may be sanctioned by the bank. Keeping in view the observations made by the Hon'ble court, the Reserve Bank has advised NBFCs also to ensure compliance with the above stipulations so that funds are not released unless the builder/developer/owner/company fulfils the above requirements.

Overseas Investment by NBFCs

The Reserve Bank has emphasised that all NBFCs desirous of making any overseas investment must obtain 'No Objection Certificate' (NoC) from the Reserve Bank before making such investment. Applications in this regard shall clearly state the activities intended to be undertaken by the overseas entity. NBFCs are not permitted to make direct investment in a foreign entity engaged in activities not approved under FEMA. As per the extant regulations, an Indian party requires prior approval of the concerned regulatory authorities both in India and abroad, to make an investment in an entity outside India engaged in financial services activities. Regulated entities in the financial sector making investments in any activity overseas are required to comply with the above regulation. Any investment made by NBFCs without regulatory clearance would be treated as a violation of FEMA and would attract penal provisions.

URBAN CO-OPERATIVE BANKS

Opening of Off-site ATMs

The Reserve Bank has decided to allow well managed urban co-operative banks (UCBs) to set up off-site ATMs without seeking approval through the annual business plans subject to UCBs meeting the following conditions:

- 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 off-site ATM is proposed/where the bank is registered.
- ii) Net NPAs being less than 5 per cent.
- iii) No default in the maintenance of CRR/SLR during the preceding financial year.
- iv) Continuous net profit for the last three years.
- v) Sound internal control system with at least two professional directors on the board.

- vi) Regulatory comfort based on inter-alia, track record of compliance.

UCBs, satisfying the above mentioned norms may prepare an application for opening off-site ATMs, as per their requirement, in their existing area of operation, with the approval of their board of directors. All other instructions on functional facilities provided at off-site ATMs, inter-account transfer, telephone connection between the 'stand alone' ATMs with branch ATMs and shared payment network system, posting of person other than security guard, sharing/interlinking of ATMs etc., remain unchanged

INFORMATION

Better Facilities for Pensioners

Providing better facilities to pensioners has always been a top priority of the government as well as the Reserve Bank. The steps taken in this regard inter-alia include:

- i. The scheme for payment of pension to central civil pensioners by authorised banks provides that, if a pensioner is unable to obtain a life certificate from an authorised bank official on account of serious illness/incapacitation etc., the officer-in-charge of the paying branch may nominate an officer to visit the pensioner at his/her residence/hospital for the purpose of recording the life certificate.
- ii. Banking Codes and Standards Board of India (BCSBI) has included pension as payment services for application of 'Code of Commitment by Banks to Customers'. Accordingly, banks are committed to extend the banking services under the adopted code. The BCSBI sets minimum standards of banking services.
- iii. The Reserve Bank has advised the banks to implement promptly the government orders increasing the dearness allowance to pensioners.
- iv. No disbursement or delay in disbursement of pension (to the extent the grievance can be attributed to the action on part of the bank concerned, but not with regard to its employees) is one of the grounds of complaints prescribed under Banking Ombudsman Scheme, 2006. The complaints received at the banking ombudsman offices are also redressed promptly by taking up the matter with concerned banks as per the provisions of the scheme.
- v. Indian Banks' Association has also advised banks to frame guidelines to ensure that customers, especially senior citizens are not put to inconvenience in transacting the business.
- vi. Further, directions have also been issued by the government to all public sector banks to ensure establishment of central pension processing centres, in terms of RBI guidelines dated October 01, 2008.

Source: Parliament Questions