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MONETARY AND CREDIT
INFORMATION REVIEW

POLICY

Policy for opening Off-Site ATMs relaxed

Scheduled commercial banks can now install off-site automated teller machines (ATMs) at centres/places identified by them, without taking the Reserve Bank's prior permission. This general permission is, however, subject to any direction that the Reserve Bank may issue, including for closure/shifting of any such off-site ATMs. Banks should report full details of the off-site ATMs installed by them to the regional office concerned of the Reserve Bank's Department of Banking Supervision/Department of Banking Operations and Development, Central Office (in respect of off-site ATMs in Maharashtra and Goa) immediately after operationalisation and in any case not later than two weeks in the prescribed format.

Banks providing cash deposit facility to customers at their ATMs, should put in place adequate safeguards/procedures (like access through personal identification number/password etc), to enable identification of the depositor in case the notes deposited are found to be forged/defective.

Banks should continue to report to the Reserve Bank the details of shifting/closure etc., of off-site ATMs immediately after such shifting/closure and in any case, not later than two weeks.

Banks have been further advised that the general permission to open off-site ATMs has being granted subject to the conditions that –

- (i) The business transacted at the off-site ATM is recorded in the books of the respective branch/base branch/centralised data centre.
- (ii) No person other than the security guard is posted at the off-site ATM.
- (iii) Adequate stand-by arrangements are made for meeting the cash requirements of the ATM.
- (iv) Only properly sorted and examined notes are put into circulation through the ATM.
- (v) Third party advertisement, such as, products of other manufacturers/dealers/vendors are not displayed on the ATM screens/network. Banks may, however, utilise the ATM screens for displaying their own products.

The facilities which banks can provide through their off-site ATMs are -

- Deposits/withdrawals
- Personal identification number (PIN) changes
- Requisition for cheque books
- Statement of accounts
- Balance enquiry
- Inter account transfer within the bank between accounts of the same customer or different customers of the bank at the same centre or different centres within the country
- Inter bank funds transfer - transfer of funds between the bank's customers and customers of other banks.
- Mail facility for sending written communication to the bank
- Utility payments like electricity/telephone bill, etc.
- Issue of railway tickets
- Product information

Incidentally, as per the extant instructions, the Reserve Bank's permission is not required for installation of on-site ATMs (ATMs which are located at branches and extension counters for which banks hold authorisations issued by the Reserve Bank under Section 23 of the Banking Regulation Act, 1949).

CONTENTS	PAGE
POLICY	
Policy for opening Off-Site ATMs relaxed	1
Banks' Exposures to CCPs	2
Norms for Closure of Fraud Cases relaxed	2
Issue of Guarantees	2
CO-OPERATIVE BANKING	
Declaration of Dividend	2
Valuation of Properties/Empanelment of Valuers	3
Exposure to Commercial Real Estate	3
Recommendations of the G-20 Working Group on Enhancing Sound Regulation and Strengthening Transparency	4

Banks' Exposures to CCPs

The Reserve Bank has advised all scheduled commercial banks that the revised norms for capital adequacy treatment of banks' various types of credit risk exposures to the central counterparties (CCPs) will be as under:

- (i) The exposures to CCPs on account of derivatives trading and securities financing transactions (e.g. collateralised borrowing and lending obligations, repos) outstanding against them, would be assigned zero exposure value for counterparty credit risk, as it is presumed that the CCPs' exposures to their counterparties are fully collateralised on a daily basis, thereby providing protection for the CCPs' credit risk exposures.
- (ii) The deposits/collaterals kept by banks with the CCPs would attract risk weights appropriate to the nature of the CCP. In the case of the Clearing Corporation of India Limited (CCIL), the risk weight would be 20 per cent and for other CCPs it would be according to the ratings assigned to these entities as per the New Capital Adequacy Framework.

These prescriptions about the adequacy of margin, quality of collateral and risk management systems of the clearing house/CCP would be reviewed after one year.

All existing exposure limits, such as, gap limits for forex exposures, PV01 limits for interest rate risk exposures which are applicable for OTC derivatives exposures of banks would continue to apply for exchange traded transactions as well.

Norms for Closure of Fraud Cases relaxed

Pursuant to receiving representations from banks, the Reserve Bank reviewed its earlier instructions on closure of fraud cases and has decided to allow, for limited statistical/reporting purposes, to close those fraud cases involving amounts up to Rs.25 lakh, where -

- the investigation is on or challan/charge sheet is not filed in the court for more than three years from the date of filing of the first information report (FIR) by the Central Bureau of Investigation (CBI)/police; or
- the trial in the courts, after filing of charge sheet/challan by CBI/police has not started, or is in progress.

All such cases would be eligible for closure subject to the conditions that -

- The examination of staff accountability has been completed.
- The amount of fraud has been recovered or written off.
- Insurance claim, wherever applicable, has been settled.
- The bank has reviewed the systems and procedures, identified the causative factors, plugged the lacunae and the relative facts have been certified by the appropriate authority (Board/Audit Committee of the Board).

In respect of cases now eligible for closure, in view of the revised instructions, banks should submit their proposals for closure, case wise, to the Reserve Bank's regional office under whose jurisdiction their head offices are situated. The cases may be closed after getting the Reserve Bank's approval. Banks should, however, maintain a record of details of such cases in a separate ledger. Even after closure of the fraud cases for limited statistical purposes, banks should vigorously follow up with the investigating agencies (CBI/police) to ensure that the investigation process is taken to its logical conclusion. Similarly, banks should ensure that they are regularly and appropriately represented in the court proceedings as and when required. All the relevant records

pertaining to such cases must be preserved till the cases are finally disposed off by CBI/police or courts, as the case may be.

Banks may, with the approval of their respective Boards, frame their own internal policy for closure of such fraud cases, incorporating the revised norms and other internal procedures/controls as deemed necessary.

Notwithstanding the fact that banks may close cases of fraud even when police/CBI investigation is in progress or cases are pending in the court of law, they should complete, within the prescribed time frame, the process of examination of staff accountability or conclude staff side actions.

In respect of closure of fraud cases involving amounts above Rs.25 lakh, there is no change in the existing instructions.

Issue of Guarantees

Reiterating its earlier instructions, the Reserve Bank has advised banks not to provide guarantees or equivalent commitments for issuance of bonds or debt instruments of any kind.

The Reserve Bank had observed that certain banks have been issuing guarantees on behalf of corporate entities in respect of non-convertible debentures issued by such entities. Guarantees by the banking system for a corporate bond or any debt instrument not only have significant systemic implications but also impede the development of a genuine corporate debt market.

Co-operative Banking

Declaration of Dividend

Consequent on the Reserve Bank introducing a revised system of 'Rating' of primary (urban) co-operative banks (UCBs) based on the CAMELS model from the inspection cycle March 31, 2009, the system of gradation of UCBs has ceased to exist.

UCBs may now declare dividend without the Reserve Bank's prior permission provided -

- i) The capital to risk weighted assets ratio (CRAR) norms, as prescribed by the Reserve Bank, have been complied with.
- ii) The net non-performing assets (NPAs) are less than 10 per cent after making all the necessary provisions as per the assessment made by the Reserve Bank in its last inspection report.
- iii) There is no default in cash reserve ratio (CRR)/statutory liquidity ratio (SLR) during the year for which the dividend is proposed.

Dr. K. C. Chakrabarty takes charge as Deputy Governor

Dr. Kamallesh Chandra Chakrabarty took over charge as Deputy Governor of the Reserve Bank of India from June 15, 2009. The appointment is for a period of three years from the date of his taking charge or until further orders, whichever is earlier.

Dr. Chakrabarty will oversee the Customer Service Department, Department of Administration and Personnel Management, Department of Information Technology, Department of Payment and Settlement Systems, Human Resources Development Department, Rajbhasha Department, Rural Planning & Credit Department, Urban Banks Department and he will be the Alternate Appellate Authority under the Right to Information Act, 2005.

- iv) All the required provisions have been made for NPAs, investments and other assets as per the prudential norms prescribed by the Reserve Bank.
- v) Dividend is paid out of the net profit and after making all statutory provisions and adjustment for accumulated losses in full.

UCBs complying with all the above indicated parameters, except the one at para (ii) above may approach the Reserve Bank's concerned regional office for permission for dividend declaration.

Valuation of Properties/Empanelment of Valuers

Regional rural banks (RRBs) have been advised that while formulating a policy on valuation of properties and appointment of valuers they should follow the guidelines indicated below :

Valuation of Properties

- (i) RRBs should have a Board approved policy in place for valuation of properties including collaterals accepted for their exposures.
- (ii) The valuation should be done by professionally qualified independent valuers i.e., the valuer should not have a direct or indirect interest.
- (iii) RRBs should obtain minimum two independent valuation reports for properties valued at Rs.50 crore or above.

Revaluation of own Properties

In addition to the above, RRBs should keep the following aspects in view while formulating policy for revaluation of their own properties.

- (i) The extant guidelines on capital adequacy permit banks to include revaluation reserves at a discount of 55 per cent as a part of Tier II capital. Such a policy should *inter alia* cover, procedure for identification of assets for revaluation, maintenance of separate set of records for such assets, the frequency of revaluation, depreciation policy for such assets, policy for sale of such revalued assets, etc.
- (ii) As the revaluation should reflect the change in the fair value of the fixed asset, the frequency of revaluation should be determined based on the observed volatility in the prices of the assets in the past. Further, any change in the method of depreciation should reflect the change in the expected pattern of consumption of the future economic benefits of the assets. RRBs should adhere to these principles meticulously while changing the frequency of revaluation/ method of depreciation for a particular class of assets.

Empanelment of Independent Valuers

- (i) RRBs should have a procedure for empanelment of professional valuers and maintain a register of 'approved list of valuers'.
- (ii) RRBs may prescribe a minimum qualification for empanelment of valuers. Different qualifications may be prescribed for different classes of assets (e.g. land and building, plant and machinery, agricultural land, etc.). While prescribing the qualification, RRBs may take into consideration the qualifications prescribed under Section 34AB (Rule 8A) of the Wealth Tax Act, 1957.

RRBs may also be guided by the relevant Accounting Standard issued by the Institute of Chartered Accountants of India.

Exposure to Commercial Real Estate

The Reserve Bank has advised all state and central co-operative banks to desist from financing the commercial real estate sector. As regards the credit facilities already extended to this sector, it should be ensured that such exposures are well secured and adequate provisioning made, wherever required, as per the existing prudential guidelines. It should also be ensured that the credit facilities are not renewed.

Working Group on Benchmark Prime Lending Rate

The Reserve Bank has constituted a Working Group on Benchmark Prime Lending Rate (BPLR) on June 11, 2009. The terms of reference of the Working Group are to:

- (i) review the concept of BPLR and the manner of its computation;
- (ii) examine the extent of sub-BPLR lending and the reasons thereof;
- (iii) examine the wide divergence in BPLRs of major banks;
- (iv) suggest an appropriate loan pricing system for banks based on international best practices;
- (v) review the administered lending rates for small loans up to Rs 2 lakh and for exporters;
- (vi) suggest suitable benchmarks for floating rate loans in the retail segment; and
- (vii) consider any other issue relating to lending rates of banks.

The Working Group is chaired by Shri Deepak Mohanty, Executive Director, Reserve Bank of India and has representations from the concerned departments of the Reserve Bank, Indian Banks' Association, Banking Codes and Standards Board of India, State Bank of India, Punjab National Bank, Canara Bank, ICICI Bank and Citibank. The Group also comprises of external experts. The Working Group is expected to submit its Report by end-August 2009.

The Working Group welcomes comments and suggestions on the issues relating to lending rates of banks including BPLR, which may be forwarded to the Adviser-in-Charge, Monetary Policy Department, Reserve Bank of India, Central Office, Mumbai 400 001.

It may be recalled that the concept of BPLR was introduced in November 2003 for pricing of loans by commercial banks with the objective of enhancing transparency in the pricing of their loan products.

The Annual Policy Statement 2009-10 (Para 87) released in April 2009 noted that, over time, the system of BPLR has evolved in such a manner that it has lost its relevance as a meaningful reference rate as bulk of loans are advanced below BPLR. Furthermore, this impedes the smooth transmission of monetary signals and makes the loan pricing system non-transparent. Accordingly, in order to review the present BPLR system and suggest changes to make credit pricing more transparent, the policy proposed constitution of a Working Group on Benchmark Prime Lending Rate.

Recommendations of the G-20 Working Group on Enhancing Sound Regulation and Strengthening Transparency

(continued from the previous issue)

Recommendation 11

All G-20 members should commit to undertake a Financial Sector Assessment Program (FSAP) report and to publish its conclusions. National authorities may also periodically undertake a self-assessment of their regulatory frameworks based on internationally agreed methodologies and tools.

- India first participated in an FSAP in 2001 conducted by the IMF and the World Bank and also associated with the independent assessment of standards and codes by the Fund/Bank. It also conducted a self-assessment of compliance with international standards and codes in 2002 and its review in 2004 and put these reports in public domain. Since the last FSAP in 2001, India has undertaken a series of ongoing reforms in the financial sector aimed at improving its soundness, resilience and depth. India has completed a comprehensive self-assessment of the financial sector in 2009 under a Committee on Financial Sector Assessment (Chairman: Dr. Rakesh Mohan and Co-Chairman: Shri Ashok Chawla) based on the IMF-WB methodology. The assessment, comprising six volumes, has been published and put in the public domain along with the comments of the internationally acclaimed Peer Reviewers on March 30, 2009. The Reserve Bank will set up a Task Force to take steps for implementation of the recommendations of the two G-20 Working Groups viz., Enhancing Sound Regulations and Strengthening Transparency, and Reinforcing International Co-operation and Promoting Integrity in Financial Markets and will also continuously monitor the implementation. The Task Force will also look into all the issues that have arisen and what follow-up actions relevant to the Reserve Bank need to be taken regarding the recently released report of the Committee on Financial Sector Assessment. The Task Force would suggest an implementation schedule for every quarter on a rolling basis.

Recommendation 12

The FSF and other bodies, particularly the BCBS, should develop and implement supervisory and regulatory approaches to mitigate procyclicality in the financial system by promoting the build-up of capital buffers during the economic expansion and by dampening the adverse interaction between fair valuation, leverage and maturity mismatches in times of stress.

- As against the Basel norm for minimum CRAR of 8 per cent, in India, banks are required to maintain a minimum CRAR of 9 per cent. The overall CRAR of all scheduled commercial banks continued to be strong and it was at 13 per cent at the end-March 2008 and 13.1 per cent at end-December 2008. The Reserve Bank recognises the need for mitigating the element of procyclicality embedded in the

regulatory norms as it may exacerbate cyclical trends. With this objective in view, the Reserve Bank has been employing a menu of macroprudential tools to mitigate the impact of procyclicality.

- FSB and member bodies, BCBS and CGFS have been entrusted with the work of developing regulatory and supervisory approaches to mitigate procyclicality. They are expected to develop a strategic plan by Fall 2009. India will take further action in this regard as per global consensus emerging from the work of international bodies.

Recommendation 13

Accounting standard setters should strengthen accounting recognition of loan loss provisions by considering alternative approaches for recognizing and measuring loan losses that incorporate a broader range of available credit information. They should also examine changes to relevant standards to dampen adverse dynamics associated with fair value accounting, including improvements to valuations when data or modelling is weak. Accounting standards setters and prudential supervisors should work together to identify solutions that are consistent with the complementary objectives of promoting the stability of the financial sector and of providing transparency of economic results in financial reports.

- The Reserve Bank introduced the asset classification and loan provisioning norms in the year 1991-92 which prescribe the minimum provisioning based on classification of assets. Certain areas of difference exist between the requirements of accounting standards in respect of loan loss provisioning (accounting perspective) and the Reserve Bank's present regulatory approach and the Basel II approach of calculating expected loan losses (regulatory perspective). Internationally, there are attempts for a convergence in this regard between the Accounting Task Force (ATF) of the BCBS and the IASB. The Reserve Bank will fine tune its policies in tandem with developments at international level in this regard.
- The Reserve Bank has, over the years, issued guidelines on valuation of various instruments/assets in conformity with the international best practices while keeping India-specific conditions in view. In order to encourage market discipline, the Reserve Bank has developed a set of disclosure requirements which allow the market participants to assess key pieces of information on capital adequacy, risk exposure, risk assessment processes and key business parameters which provide a consistent and understandable disclosure framework that enhances comparability. Banks are also required to comply with the Accounting Standard (AS) on disclosure of accounting policies issued by the Institute of Chartered Accountants of India (ICAI).

(to be continued in the next issue)