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POLICY

Guidelines on Note Authentication and Fitness Sorting

The Reserve Bank has laid down the guidelines on "Note Authentication and Fitness Sorting Parameters" which prescribe the standards/parameters to be followed by banks while processing banknotes. Some of the main highlights of the guidelines are:

- The parameters provided in the guidelines form the minimum standards for cash handling machines used by banks. All the fitness parameters laid down in the guidelines are to be evaluated individually. A note must pass all the fitness parameters to be considered fit for recycling. A fit note is a note that is genuine, sufficiently clean to allow its denomination to be readily ascertained and thus suitable for recycling. An unfit note is a note that is not suitable for recycling because of its physical condition or belongs to a series that has been phased out by the Reserve Bank.
- Authenticity check is a prerequisite for fitness sorting. Notes can only be recycled/reissued if they are evaluated as genuine. Fitness sorting can be done only in case of genuine notes. The machines should be able to identify and separate suspected counterfeits and notes which are unfit for circulation in a reliable and consistent fashion.
- The Reserve Bank phases out certain series (issue) of notes from circulation from time to time. These notes, though considered legal tender unless otherwise specified, are unfit for recycling. As and when the Reserve Bank decides to phase out a specific series (issue) of a specific denomination of notes, the machines should sort all the phased out notes as unfit, irrespective of their physical condition.
- The parameters provided in the guidelines are applicable to machines operated by banks, either directly by their staff or indirectly by their agents. These machines can be those which-
 - i. check the authenticity and fitness of notes, i.e., note processing machines/note sorting machines, or;
 - ii. check only the authenticity of notes, i.e., note authentication machines.

- The machines should perform authenticity check with reference to the features of genuine notes as disclosed by the Reserve Bank from time to time. Any note which is not found to be having all the features of a genuine note should be classified by the machines as suspect.
- As a part of fitness sorting, notes with any visual or physical defects are to be sorted as unfit as per the criteria set out in the guidelines. The criteria of fitness sorting in brief are:

Soiling: Soiling refers to the general distribution of dirt across the entire note or in some patterns. It is a measure of the loss of reflectivity from the unprinted areas due to dirt, ageing (yellowing), wear and extraneous markings and includes decolouration due to ageing, excessive folding wear and other wearing. Soiling increases the optical density and decreases the reflectance of the notes. Notes exceeding the soiling levels set out in the guidelines should be sorted as unfit. Both the obverse and the reverse of the note should be checked for soiling.

Limpness: Limpness relates to structural deterioration or wear resulting in a marked lack of stiffness in the note

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paper. Notes with a very low stiffness should be sorted as unfit. Notes with very low stiffness of paper, i.e., with paper which is worn out in circulation or mechanically mutilated should be sorted out as unfit. Detectors for paper quality should be adapted to the same level as for soiling.

Dog-Ears: Notes with dog-ears with an area of more than 130 mm² and a minimum length of the smaller edge greater than 10 mm should be sorted as unfit. Chipped notes should also be sorted as unfit.

Tears: Notes exhibiting at least one tear at the edge should be classified as those having tears. Notes with tears larger than those indicated in the guidelines should be sorted as unfit.

Holes: This refers to notes with at least one visible hole. Notes with holes with area exceeding 10 mm² should be sorted as unfit.

Stains: Stains are visible markings which are not part of the feature of a note. Notes should be detected as unfit if localised - i.e., with limited extension - stain can be recognised on its surface. In case the total area covered by stains exceeds 500 mm², the note should be sorted as unfit. A note with a single stain covering an area of more than 200 mm² should be sorted as unfit. Both the obverse and the reverse of the note should be checked for stains.

Graffiti: Graffiti refers to deliberate graphic alteration of the note with, for example, figures or letters. Fitness sorting criteria in case of graffiti should be the same as those for stains. Both the obverse and the reverse of the note should be checked for graffiti.

Crumples/Folds: Crumpled/folded notes should be sorted as unfit if the folds result in reduction of the original note in length or width greater than 5 mm.

Decolouration: Notes affected by decolouration should be sorted as unfit if the ink is partially or wholly missing from its surface. Both the obverse and the reverse of the note should be checked for decolouration.

Repair: A repaired note is created by joining parts of the same note together, for example, by using extraneous matter such as tape, paper or glue. Notes with the types of repairs, as detailed in the guidelines should be sorted as unfit.

- Mutilated, imperfect and mismatched notes should be classified as unfit. A mutilated note is a note, of which a portion is missing or which is composed of more than two pieces. An imperfect note is a note, which is wholly or partially, obliterated, shrunk, washed, altered or indecipherable but does not include a mutilated note. A mismatched note is a note, which has been formed by joining a half note of any one note to a half note of another note.

It may be recalled that earlier, the Reserve Bank had placed the draft guidelines on its website for seeking comments/views and after taking into account the comments received from various stakeholders including banks, equipment manufacturers

and members of public, the guidelines on "Note Authentication and Fitness Sorting Parameters" have been issued.

Statutory Liquidity Ratio

At present, banks obtain liquidity from the Reserve Bank under the liquidity adjustment facility (LAF) against the collateral of eligible securities that are in excess of their prescribed statutory liquidity ratio (SLR). The Reserve Bank has decided that, in addition, purely as a temporary measure, scheduled commercial banks may avail additional liquidity support under the LAF to the extent of up to 0.5 per cent of their net demand and time liabilities. The additional liquidity support will be available from the LAF auctions of May 28, 2010 to July 2, 2010. The Reserve Bank has advised that for any shortfall in maintenance of SLR arising out of availment of this additional liquidity support under LAF, banks may apply to the Reserve Bank in writing with a request not to demand payment of the penal interest thereon.

Imposition of Penalties on PDs

In order to maintain transparency with regard to imposition of penalties and in conformity with the best practices in disclosure of penalties imposed by the regulator, the Reserve Bank has decided that the details of the penalty levied on a primary dealer (PD) should be placed in the public domain. A press release will be issued by the Reserve Bank giving details of the circumstances under which the penalty is imposed on the PD along with the communication on the imposition of penalty being placed in the public domain. The penalty should also be disclosed in the "Notes on Accounts" to the balance sheet of the primary dealer in the next annual report.

Credit Flow to Agriculture

On the basis of representations received seeking enhancement of limits, the Reserve Bank has decided that banks may waive margin/security requirements for agricultural loans from the existing level of Rs.50,000/- to Rs.1,00,000/- with immediate effect. Banks have also been requested to give adequate publicity to this change while instructing their controlling offices/branches for immediate implementation.

UCBs

Real Estate and Commercial Real Estate

In terms of the extant norms, the total exposure of urban co-operative banks (UCBs) to real estate, including individual housing loans and commercial real estate (CRE) is restricted to 15 per cent of total deposit resources of banks. In this regard, the Reserve Bank has clarified that finance extended to the eligible category of borrowers will be categorised as housing finance. While the purpose of the loan should determine whether the loans granted against the security of immovable property need to be classified as real estate loans, the source of repayment will determine whether the exposure is against commercial real estate. The ceiling of 15 per cent may be reckoned on the total deposits of a bank based on the audited balance sheet as on March 31 of the previous financial

year. The exposure for the purpose of computing the prescribed limit of 15 per cent should take into account both fund based and non fund based facilities. UCBs may utilise up to 15 per cent of their total deposit resources to provide housing, real estate and CRE loans. Working capital loans against hypothecation of construction materials provided to the contractors, who undertake comparatively small construction on their own without receiving advance payments, are exempted from the prescribed limit of 15 per cent.

Placement of Deposits with other Banks

The Reserve Bank has advised non-scheduled UCBs, which have exposures to other non-scheduled UCBs on account of clearing arrangements, to review their exposures to such banks periodically based on their published balance sheet and profit and loss account statements. It was observed that the smaller non-scheduled UCBs were keeping current account/minimum required balance for clearing purpose with relatively larger non-scheduled bank for sub member clearing arrangements. It was felt that the financial position of the non-scheduled UCB, with whom such deposits were kept, could take a hit due to unexpected downturn in its business and which could also affect the financial position of the depositing bank and its business. As per the extant provisions, the prudential interbank (gross) exposure limit and inter-bank counter party limit for placing deposits with other banks by UCBs for all purposes including for availing clearing facility has been prescribed. UCBs are required to formulate a policy taking into account their funds position, liquidity and other needs for placement of deposits with other banks, the cost of funds, expected rate of return and interest margin on such deposits, the counter party risk, etc., and place it before their board of directors which should review the position at least at half yearly intervals.

FEMA

Fictitious Lottery Schemes

The Reserve Bank has advised authorised dealer Category-I banks (AD Category-I banks) to be extra vigilant in view of the large number of fictitious lottery offers and offers of cheap funds from abroad being received by the public. As per the extant provisions, remittances in any form towards participation in lottery schemes are prohibited under the Foreign Exchange Management Act, 1999 (FEMA). Further, these restrictions are also applicable to remittances for participation in lottery like schemes existing under different names like money circulation scheme or remittances for the purpose of securing prize money/awards, etc. In recent times there has been a spate of fictitious offers of cheap funds from the fraudsters through letters, e-mails, mobile phones, SMS, etc. Communications on fake letterheads of the Reserve Bank and purportedly signed by its top executives/senior officials are also being sent to targeted people. Many residents have been victims of such teasing offers and lost huge money in the process. The Reserve Bank has already alerted the public on several occasions about such fictitious schemes/offers, through the print and the electronic media and more such

public education campaigns are being planned. It has also been brought to the notice of the Reserve Bank that fraudsters are seeking money from the gullible people, under different heads, such as, processing fees/transaction fees/tax clearance charges/conversion charges, clearing fees, etc. The victims of the fraud have also been persuaded to deposit the amount in accounts with banks in India, and such amounts have been withdrawn immediately. It is also observed that multiple accounts are being opened in the name of individuals or proprietary concerns, at different bank branches for collecting the transaction charges, etc. In view of the aforesaid, the Reserve Bank has advised AD Category-I banks to exercise due caution while opening or allowing transactions in such accounts. The Reserve Bank has also clarified that any person resident in India collecting and effecting/remitting such payments directly/indirectly outside India would make himself/herself liable to be proceeded against with, for contravention of FEMA besides being liable for violation of regulations relating to know your customer (KYC) norms/anti-money laundering (AML) standards. AD Category-I banks have also been advised to bring the contents of the extant provisions to the notice of their constituents and customers concerned besides giving wide publicity to the press releases issued by the Reserve Bank on fictitious offers/lottery winnings/cheap fund offers.

INFORMATION

Payment and Settlement Systems

The Reserve Bank, as the central bank of the country has played a catalytic role, over the years, in creating an institutional framework for development of a safe, secure, sound and efficient payment system in the country. A major milestone was achieved when the Payment and Settlement Systems Act, 2007 (the PSS Act) was enacted empowering the Reserve Bank to regulate and supervise the payment and settlement systems, lay down policies to this effect and provide a legal basis for multilateral netting and settlement finality. Accordingly, the Reserve Bank framed and notified the 'Board for Regulation and Supervision of Payment and Settlement Systems Regulations, 2008' and 'Payment and Settlement Systems Regulations, 2008' for operationalisation of the PSS Act.

The PSS Act and the two regulations have come into effect from August 12, 2008. The PSS Act stipulates that no person other than the Reserve Bank should commence or operate a payment system, except under and in accordance with an authorisation issued by the Reserve Bank as per the provisions of the PSS Act. All persons operating a payment system or desirous of setting up a payment system as defined in the PSS Act, need to apply for authorisation to the Reserve Bank, unless specifically exempted in terms of the PSS Act, in the form and manner as stipulated in the regulations. The stock exchanges and the clearing corporations of the stock exchanges have been exempted from the provisions of the PSS Act.

Since the PSS Act became effective, the Reserve Bank has received applications for authorisation from operators/proposed operators of prepaid and other cards, payment gateways,

money transfers, mobile payments, automated teller machine (ATM) network, etc. The banks providing mobile payment services in accordance with the "Mobile Banking Transactions in India- Operative Guidelines for Banks" issued on October 8, 2008 under Section 18 of the PSS Act, are required to obtain approval from the Reserve Bank.

The Reserve Bank, as the supervisor and regulator of the payment and settlement systems, strives to ensure development of efficient and smooth systems matching the needs and growing sophistication of the financial sector. The rapid advancements in the field of information technology (IT) have contributed to emergence of new products as well as methods of payment and settlement. Emergence of new modes of payments and increasing complexity of transactions, however, also pose challenges in terms of formulating appropriate regulatory and supervisory frameworks.

Source: RBI Annual Report 2008-09

Penalty for Forged Notes

The Reserve Bank imposes penalty for the forged notes detected in soiled note remittances or in chest balances of the currency chest of any bank. The penalty would be an amount equal to the notional 'value' of the counterfeit note in addition to the loss. During the period from July, 2009 to February, 2010 penalty amounting to Rs.1,08,23,219/- was recovered from public sector banks on account of forged notes detected in soiled note remittances or in chest balances.

The Reserve Bank also lodges first information reports (FIRs) against banks in whose remittances and chest balances forged notes are detected. During the period from July, 2009 to February, 2010, 4894 cases were registered with the police authorities against the banks on account of forged notes detected.

Source: Parliament Questions

Steps for Financial Inclusion

The Reserve Bank has taken the following steps recently to address the issue of financial inclusion:

- All public and private sector banks were advised in January 2010 to come up with specific board approved financial inclusion plans (FIPs) by March 2010 incorporating some basic minimum qualitative features, and quantitative indicators with a view to rolling them out over the next three years. Such board approved FIPs will be an integral part of their business plans and will also include criteria on financial inclusion to be used in the performance evaluation of their field staff.
- To improve banking penetration in the north-east, the Reserve Bank has asked the state governments and banks to identify centres where there is a need for setting up either full-fledged branches or those offering forex

facilities, handling government business or for meeting currency requirements. It has also offered to fund the capital and running costs for five years provided the state government concerned is willing to make available the premises and appropriate security arrangements.

- In November 2009, banks were advised to draw up a roadmap by March 2010 to provide banking services through a banking outlet in every village having a population of over 2,000 by March 2011 which will result in extending financial inclusion to more than one lakh villages. Such banking services may not necessarily be extended through a brick and mortar branch but can be provided through any of the various forms of ICT- based models, including through business correspondents (BCs).

Source: Parliament Questions

Equity Capital of Public Sector Banks

Equity Capital of Public Sector Banks as on March 31, 2010:

Sl. No	Name of the Bank	Total Paid-up Equity Capital (in Rs.crore)	Government Shareholding %age	Amount (in Rs.crore)
1	Allahabad Bank	446.70	55.23	246.70
2	Andhra bank	485.00	51.55	250.00
3	Bank of Baroda	364.27	53.81	196.00
4	Bank of India	525.18	64.47	338.58
5	Bank of Maharashtra	430.52	76.77	330.52
6	Canara Bank	410.00	73.17	300.00
7	Central Bank of India	404.14	80.20	324.14
8	Corporation Bank	143.44	57.17	82.00
9	Dena Bank	286.82	51.19	146.82
10	Indian Bank	429.77	80.00	343.82
11	Indian Overseas Bank	544.80	61.23	333.60
12	Oriental Bank of Commerce	250.54	51.09	128.00
13	Punjab & Sind Bank	183.06	100.00	183.06
14	Punjab National Bank	315.30	57.80	182.24
15	Syndicate Bank	521.97	66.47	346.95
16	UCO Bank	549.36	63.59	349.36
17	Union Bank of India	505.12	55.43	280.00
18	United Bank of India	316.43	84.20	266.43
19	Vijaya Bank	433.52	53.87	233.52
20	State Bank of India	634.88	59.41	377.21
21	IDBI Ltd	724.78	52.67	381.78
TOTAL		8905.60		5620.73

Source: Parliament Questions