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RESERVE BANK OF INDIA

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No. 2004/ 118
DBOD No. BP.BC. 29 / 21.04.048/ 2004-05 August 13, 2004

All Commercial Banks
(excluding RRBs)

Dear Sir,

Prudential norms – State Government guaranteed exposures

Please refer to our circular DBOD No. BP.BC.103/ 21.00.002/ 98 dated October 31, 1998, which contained, among others, prudential norms regarding State Government guaranteed advances. Presently, asset classification and provisioning requirements in respect of State Government guaranteed exposures are linked to invocation of the State Government guarantee.

2. The prudential norms pertaining to State Government guaranteed exposures have been reviewed and it has been decided to delink the requirement of invocation of State Government guarantee for deciding the asset classification and provisioning requirements and prescribe revised norms in respect of the following exposures, which are backed by State Government guarantee:

(a) Loans and advances; and
(b) Investments.

The existing and the revised prudential norms applicable to exposures backed by State Government guarantees are furnished in the Annex.

3. With a view to enabling banks to have a smooth transition to the revised norms, it has been decided that the revised prudential norms in respect of State Government guaranteed exposures may be implemented in a phased manner as under:

(a) For the year ending March 31, 2005, State Government guaranteed advance and investment in State Government guaranteed securities would attract asset classification and provisioning norms, if interest and/or principal or any other amount due to the bank remains overdue for more than 180 days.

(b) With effect from the year ending March 31, 2006, State Government guaranteed advance and investment in State Government guaranteed securities would attract asset classification and provisioning norms, if interest and/or instalment of principal or any other amount due to the bank remains overdue for more than 90 days.

Yours faithfully,

(C.R.Muralidharan)
Chief General Manager-in-Charge

Encls: as above

ANNEX

Prudential norms for State Government guaranteed exposures

1. Loans and advances

Sr. No.	Existing Prudential norms	Revised Prudential norms
(a)	**Income recognition**	
	A State Government guaranteed advance, where interest and/or instalment of principal/ or any other amount due to the bank remains overdue for a period more than 90 days shall become a non performing advance. The interest due on such advances should not be taken to income account, unless it has been realised.	A State Government guaranteed advance, where interest and/or instalment of principal/ or any other amount due to the bank remains overdue for a period more than 90 days shall become a **non performing advance**. The interest due on such advances should not be taken to income account, unless it has been realised. **(No change)**
(b)	**Asset Classification and Provisioning**	
	A State Government guaranteed advance where interest and/or instalment of principal/ or any other amount due to the bank remains overdue for a period of more than 90 days after invocation of the State Government guarantee shall be subjected to appropriate asset classification and provisioning norms.	**For the year ending March 31, 2005**, a State Government guaranteed advance shall be classified as 'substandard' or 'doubtful' or 'loss', if interest and/or principal or any other amount due to the bank **remains overdue for more than 180 days** and attract appropriate provisioning norms. **With effect from the year ending March 31, 2006**, a State Government guaranteed advance shall be classified as 'substandard' or 'doubtful' or 'loss', if interest and/or instalment of principal or any other amount due to the bank **remains overdue for more than 90 days and** attract appropriate provisioning norms**.**
(c)	**Risk Weights**	
	(i) A State Government guaranteed advance attracts zero per cent risk weight.	A State Government guaranteed advance will attract zero per cent risk weight. **(No change)**.

	(ii) A State Government guaranteed advance where guarantee has been invoked and the concerned State Government has remained in default for a period of more than 90 days, will attract a risk weight of 100 per cent.	A State Government guaranteed advance which has become a non performing advance will attract a risk weight of 100 per cent.

2. Investments

Sr. No.	Existing Prudential norms	Revised Prudential norms
(a)	**Income recognition**	
	Investment in securities where payment of interest or repayment of principal is guaranteed by State Governments will become a non-performing investment if interest/ instalment (including maturity proceeds) is due and remains unpaid for more than 90 days. Banks should not take income on non-performing investments to income account unless it has been realised.	Investment in securities where payment of interest or repayment of principal is guaranteed by State Government will become a **non-performing investment** if interest/ instalment (including maturity proceeds) or any other amount due to the bank remains unpaid for more than 90 days. Banks should not take income on non-performing investments to income account unless it has been realised.
(b)	**Asset Classification and Provisioning**	
	i) Investment in the nature of deemed advance Investments in State Government guaranteed securities, which are in the nature of 'deemed advance', will attract appropriate asset classification and provisioning norms **as in the case of advances** when interest and/or instalment of principal or any other amount due to the bank remains overdue for a period of more than 90 days after invocation of the state government guarantee.	**For the year ending March 31, 2005**, investment in State Government guaranteed securities, which are in the nature of 'deemed advance', will attract appropriate asset classification and provisioning norms **as in the case of advances** when interest and/or instalment of principal or any other amount due to the bank **remains overdue for more than 180 days**. **With effect from the year ending March 31, 2006,** investment in State Government guaranteed securities, which are in the nature of 'deemed advance', will attract appropriate asset classification and provisioning norms **as in the case of advances** when the

		interest and/or installment of principal or any other amount due to the bank **remains overdue for a period of more than 90 days.**
	ii) Other Investments which are not in the nature of deemed advance Investments in State Government guaranteed securities, which are ***not*** in the nature of 'deemed advance', will attract appropriate asset classification and provisioning norms, when interest and/or instalment of principal (including maturity proceeds) or any other amount is due to the bank and remains overdue for a period more than 90 days after invocation of the state government guarantee. The provisioning norms would be as under: *a) Quoted securities* Banks should mark to market these securities with reference to their market value and make appropriate provisions for the depreciation in the value of the investment. Banks should not set-off the depreciation requirement in respect of these non-performing securities against the appreciation in respect of other performing securities. *b) Unquoted securities* Banks should make provisions for the debentures as in the case of debentures/ bonds treated as advances. The depreciation/ provision requirement towards debentures where the interest is in arrears or principal is not paid as per due date, shall not be allowed to be set-off against appreciation against other debentures/ bonds.	Investment in State Government guaranteed securities, which are **not** in the nature of 'deemed advance', will attract appropriate asset classification and provisioning norms when interest/ instalment of principal (including maturity proceeds) or any other amount due to the bank remains unpaid as under : (i) for more than 180 days for the year ending March 31, 2005 and (ii) for more than 90 days with effect from the year ending March 31, 2006. The provisioning norm would be as under : *a) Quoted securities* Banks should mark to market these securities with reference to their market value and make appropriate provisions for the depreciation in the value of the investment. Banks should not set-off the depreciation requirement in respect of these non-performing securities against the appreciation in respect of other performing securities. *b) Unquoted securities* Banks should make provisions for the unquoted securities as in the case of investments in the nature of deemed advances. Banks should not set-off the depreciation/ provision requirement in respect of these non-performing securities against the appreciation in respect of other performing securities.
(c)	**Risk Weights**	

	Investment in State Government guaranteed securities of Government undertakings which form part of the approved market borrowing programme attracts an aggregate risk weight of 2.5 per cent (zero per cent for credit risk and 2.5 per cent for market risk). Investment in State Government guaranteed securities of Government undertakings which **do not** form part of the approved market borrowing programme attract an aggregate risk weight of 22.5 per cent (20 per cent for credit risk + 2.5 per cent for market risk) Investment in State Government guaranteed securities attract a risk weight of 102.5 per cent if the guarantee is invoked and concerned State Government has remained in default.	Investment in State Government guaranteed securities of Government undertakings which form part of the approved market borrowing programme attracts a zero per cent risk weight for credit risk. Investment in State Government guaranteed securities of Government undertakings which **do not** form part of the approved market borrowing programme attracts a 20 per cent risk weight for credit risk. Investment in securities where payment of interest or repayment of principal is guaranteed by State Government, which has become a non performing investment, will attract a 100 per cent risk weight for credit risk. The above securities will attract an additional risk weight of 2.5 per cent for market risk. The additional risk weight of 2.5 per cent for market risk would not be required with effect from March 31, 2005 on the investment included under Held for Trading category. The additional risk weight of 2.5 per cent towards market risk would not be required with effect from March 31, 2006 on the investment included under Available for Sale and Held to Maturity categories.