RBI/2004-05/423

UBD.DS. Cir.No.44/13.05.00/2004-05

April 15, 2005

The Chief Executive Officers of

All Primary(Urban) Co-operative banks

Dear Sir/Madam,

Maximum Limit on advances-Limits on credit exposure to individuals /Group of borrowers-UCBs

Please refer to our circular UBD. No.DS.PCB.39/13.05.00/1995-96 dated January 16, 1996 read with circular UBD.No.DS.Cir 31/13.05.00/1999-2000 dated April 1, 2000 on captioned subject. At present the prudential exposure ceiling should not exceed 20 percent and 50 percent of the capital funds of the bank in case of individual borrower and group of borrowers respectively. The capital funds comprise of paid up capital and free reserves. Exposure includes both funded and non funded credit limits and underwriting and similar commitments. The sanctioned limits or outstanding whichever is higher is reckoned for arriving at exposure limit. However in respect of non-funded credit limits, only 50 % of such limits or outstanding, whichever is higher is taken for arriving at the exposure ceiling.

2. The matter has been reviewed and it has been decided as under :

i. To fix the prudential exposure limits at 15 percent and 40 percent of the 'Capital Funds' in case of single borrower and group of borrowers respectively.

ii. 'Capital Funds' for the purpose of prudential exposure norm may be fixed in relation to bank's capital funds (both Tier I and Tier II Capital) as defined in the enclosed annexure.

iii. The exposure shall henceforth include both credit exposure and investment exposure (Non SLR) as indicated below:

a) Funded and non funded credit limits and underwriting and similar commitments. The sanctioned limit or outstanding whichever is higher shall be reckoned for arriving at credit exposure limit.

b) In respect of non funded credit limits 100 percent (instead of the existing 50 percent) of such limits or outstanding, whichever is higher, shall be taken into account for this purpose.

c) Non SLR investments indicated in our circular UBD.BPD.PCB 45/16.20.00/2003-04 dated April 14, 2004

3. The banks are advised to compute the revised prudential exposure limits for individual/ group of borrowers w.e.f April 1, 2005.However, in case of the existing borrowers where the outstanding or the sanctioned exposure limit exceed the revised limit, the same be brought down within the revised limits in a maximum period of 2 years, i.e. by March 31, 2007.

4. A fresh directive UBD.No.DS.PCB.DIR.2/13.05.00/04-05 dated April 15 , 2005 issued in this regard is enclosed.

5. All other instruction issued in this regard from time to time remains unchanged.

6. Please acknowledge receipt to the concerned Regional Office of Reserve Bank of India.

Yours faithfully,

sd/-
(K.R Ananda)
Chief General Manager-in-charge.

UBD.No.DS.PCB.DIR. 2 /13.05.00/2004-05

April 15, 2005.

Maximum Limit on Advances

In exercise of the powers conferred under Section 21 and clause (b) of the proviso to clause (b) of the sub-section (1) of Section 20 read with Section 56 of the Banking Regulation Act 1949, the Reserve Bank of India, being satisfied that it is necessary and expedient so to do, hereby directs that with effect from April 1, 2005:

1(a) Ceiling: The exposure ceiling shall be fixed in relation to bank's 'Capital Funds' and it shall not exceed 15 percent of capital funds in case of individual borrower and 40 percent in case of group of borrowers.

'Capital Funds' for the purpose will comprise both Tier I and Tier II Capital of the bank as given in the enclosed annexure.

(b) Exposure shall include funded and non funded credit limits and underwriting and similar commitments. The sanctioned limit or outstanding whichever is higher shall be reckoned for arriving at exposure limit. However in respect of non funded credit limits , 100 percent of such limits or outstanding, whichever is higher, shall be taken into account for this purpose. Exposure to individuals/group of borrowers shall also include investments made by the primary(urban) co-operative banks in Non SLR securities prescribed by Reserve Bank of India. At present Non SLR securities comprise bonds of Public Sector Undertakings (PSUs), Infrastructure bonds floated by the all India Financial Institutions as notified by Reserve Bank of India from time to time, unsecured redeemable bonds floated by the nationalised banks, equity/bonds of all India Financial Institutions and Units of UTI.

2. In the event of any dispute relative to interpretation of any of the provisions of this directive, the decision of Reserve Bank of India thereon, shall be final.

sd/-

(A.V. Sardesai)
Executive Director

Annexure

Enclosure to the directive UBD.No.DS.PCB.DIR.2 /13.05.00/2004-05
dated April 15 , 2005.

<u>Definitions:</u>

<u>Tier I Capital /Core Capital</u>

Tier I Capital would include the following items:

(i) Paid-up share capital collected from regular members of a bank having voting powers.

(ii) Free Reserves as per the audited accounts. Reserves, if any, created out of revaluation of fixed assets or those created to meet outside liabilities should not be included in the Tier I Capital. Free reserves shall exclude all reserves / provisions which are created to meet anticipated loan losses, losses on account of fraud etc., depreciation in investments and other assets and other outside liabilities. While the amounts held under the head "Building Fund" will be eligible to be treated as part of free reserves, "Bad and Doubtful Reserves" shall be excluded.

(iii) Capital Reserve representing surplus arising out of sale proceeds of assets.

(iv) Any surplus (net) in Profit and Loss Account i.e. balance after appropriation towards dividend payable, education fund, other funds whose utilisation is defined, asset loss, if any, etc.

NOTE: Amount of intangible assets, losses in current year and those brought forward from previous periods, deficit in NPA provisions, income wrongly recognized on non performing assets , provision required for liability devolved on bank, etc. will be deducted from Tier I Capital.

<u>Tier II Capital</u>

Undisclosed Reserves

(i) These often have characteristics similar to equity and disclosed reserves. They have the capacity to absorb unexpected losses and can be included in capital, if they represent accumulation of profits and not encumbered by any known liability and should not be routinely used for absorbing normal loss or operating losses.

Revaluation Reserves

(ii) These reserves often serve as a cushion against unexpected losses, but they are less permanent in nature and cannot be considered as 'Core Capital'. Revaluation reserves arise from revaluation of assets that are undervalued in the bank's books. The typical example in this regard is bank premises and marketable securities. The extent to which the revaluation reserves can be relied upon as a cushion for unexpected losses depends mainly upon the level of certainty that can be placed on estimates of the market value of the relevant assets, the subsequent deterioration in values under difficult market conditions or in a forced sale, potential for actual liquidation of those values, tax consequences of revaluation, etc. Therefore, it would be prudent to consider revaluation reserves at a discount of 55 % when determining their value for inclusion in Tier II Capital i.e. only 45% of revaluation reserve should be taken for inclusion in Tier II Capital. Such reserves will have to be reflected on the face of the balance sheet as revaluation reserves.

General Provisions and Loss Reserves

(iii) These will include such provisions of general nature appearing in the books of the bank which are not attributed to any identified potential loss or a diminution in value of an asset or a known liability. Adequate care must be taken to ensure that sufficient provisions have been made to meet all known losses and foreseeable potential losses before considering any amount of general provision as part of Tier II capital as indicated above. To illustrate : excess provision in respect of Bad and Doubtful Debts, general provision for Standard Assets etc. could be considered for inclusion under this category. Such provisions which are considered for inclusion in Tier II capital will be admitted upto 1.25% of total weighted risk assets.

Investment Fluctuation Reserve

(iv) Balance, if any, in the Investment Fluctuation Reserve Fund of the bank.

Hybrid Debt Capital Instruments

(v) Under this category, there are a number of capital instruments, which combine certain characteristics of equity and certain characteristics of debt. Each has a particular feature which can be considered to affect its qualify as capital. Where these instruments have close similarities to equity, in particular, when they are able to support losses on an ongoing basis without triggering liquidation, they may be included in Tier II capital.

Subordinated Debt

(vi) To be eligible for inclusion in Tier II capital, the instrument should be fully paid-up, unsecured, subordinated to the claims of other creditors, free of restrictive clauses and should not be redeemable at the initiative of the holder or without the consent of the bank's supervisory authorities. They often carry a fixed maturity and as they approach maturity, they should be subjected to progressive discount for inclusion in Tier II capital. Instruments with an initial maturity of less than 5 years or with a remaining maturity of one year should not be included as part of Tier II capital. Subordinated debt instruments will be limited to 50 percent of Tier I capital.

NOTE: (a) At present UCBs do not issue instruments of the type indicated at (v) and (vi) above. However, there is no bar on issuing such instruments subject to provisions of respective State Co-operative Societies Act/Multi State Co-operative Societies Act. Issue of such instruments will be subject to prior approval of RBI.

(b) It may be noted that the total of Tier II elements will be limited to a maximum of 100 percent of total Tier I elements for the purpose of compliance with the norms.