B public Deposits

public deposits refer to the unsecured deposits invited by companies from the public mainly to finance working capital needs. A company wishing to invite public deposits makes an advertisement in the newspapers.

Any member of the public can fill up the prescribed form and deposit the money with the company. The company in return issues a deposit receipt. This receipt is an acknowledgement of debt by the company. The terms and conditions of the deposit are printed on the back of the receipt. The rate of interest on public deposits depends on the period of deposit and reputation of the company.

Public deposits of a company cannot exceed 25 per cent of its share capital and free reserves. As these deposits are unsecured, the company having public deposits is required to set aside 10 per cent of deposits maturing by the end of the year. The amount so set aside can be used only for paying such deposits.

Thus, public deposits refer to the deposits received by a company from the public as unsecured debt. Companies prefer public deposits because these deposits are cheaper than bank loans. The public prefers to deposit money with well-established companies because the rate of interest on public deposits is higher than on bank deposits. Now public sector companies also invite public deposits. Public deposits have become a popular source of industrial finance in India.

Merits of Public Deposits:

1. Simplicity:

Public deposits are a very convenient source of business finance. No cumbersome legal formalities are involved. The company raising deposits has to simply give an advertisement and issue a receipt to each depositor.

2. Economy:

Interest paid on public deposits is lower than that paid on debentures and bank loans. Moreover, no underwriting commission, brokerage, etc. has to be paid. Interest paid on public deposits is tax deductible which reduces tax liability. Therefore, public deposits are a cheaper source of finance.

3No Charge on Assets:

Public deposits are unsecured and, therefore, do not create any charge or mortgage on the company's assets. The company can raise loans in future against the security of its assets.

4. Flexibility:

Public deposits can be raised during the season to buy raw materials in bulk and for other short-term needs. They can be returned when the need is over. Therefore, public deposits introduce flexibility in the company's financial structure.

ADVERTISEMENTS:

5. Trading on Equity:

Interest on public deposits is paid at a fixed rate. This enables a company to declare higher rates of dividend to equity shareholders during periods of good earnings.

6. No Dilution of Control:

There is no dilution of shareholders' control because the depositors have no voting rights.

7. Wide Contacts:

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7. Wide Contacts:

Public deposits enable a company to build up contacts with a wider public. These contacts prove helpful in the sale of shares and debentures in future.

Demerits of Public Deposits:

1. Uncertainty:

Public deposits are an uncertain and unreliable source of finance. The depositors may not respond when economic conditions are uncertain. Moreover, they may withdraw their deposits whenever they feel shaky about the financial health of the company.

Depositors are entitled to withdraw their deposits at any time after giving prior notice to the company. During times of financial tightness or distress the depositors may get panicky and wish to withdraw their deposits.

Moreover, if a large number of depositors simultaneously withdraw their deposits during slump, the company may find it difficult to repay a huge sum at once. Therefore, public deposits are described as 'fair weather friends'.

2. Limited Funds:

A limited amount of funds can be raised through public deposits due to legal restrictions.

3. Temporary Finance:

The maturity period of public deposits is short. The company cannot depend upon public deposits for meeting long-term financial needs.

4. Speculation:

As public deposits can be raised easily and quickly, a company may be tempted to raise more funds than it can profitably use. It may keep idle money to meet future contingencies. The management of the company may indulge in over-trading and speculation which exercise harmful effects on the business.

5. Hindrance to Growth of Capital Market:

Public deposits hamper the growth of a healthy capital market in the country. Widespread use of public deposits creates a shortage of industrial securities.

6. Limited Appeal:

Public deposits do not appeal as a mode of investment to bold investors who want capital gains. Conservative investors may also not like these deposits in the absence of proper security.

7. Unsuitable for New Concerns:

New companies lacking in sound credit standing cannot depend upon public deposits. Investors do not like to deposit money with such companies.

What Is Intercorporate Investment?

Intercorporate investment can occur when a company makes any investment in another company. These types of investments can be accounted for in a few different ways depending on the investment.

Generally, the broadest and most comprehensive way to account for these types of investments is by the percentage of ownership stake.

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Understanding Intercorporate Investments
Intercorporate investment occurs when a company makes an investment in another company. Broadly, there can be three categories for classifying an intercorporate investment, which can help to guide and dictate the accounting treatment used. The three categories generally include: minority passive (less than 20% ownership), minority active (20%-50% ownership), and controlling interest (over 50% ownership). These classifications are general divisions, but companies should also consult Accounting Standards Codification (ASC), specifically ASC 805, which details the Generally Accepted Accounting Principles for business combinations.[1] Companies may be able to deviate from the three major classifications depending on participation controls.

here can be a variety of ways a company can choose to make an intercorporate investment. It could be through the purchase of shares of a publicly traded company on a public exchange or a privately negotiated deal for a share of a company that is not publicly traded. The investment may also involve buying the debt of another company, publicly traded or otherwise. The controlling interest of a company will commonly come from a merger or acquisition.
Types of Intercorporate Investments
Below are some additional details on each of the three classifications for intercorporate investments:

Minority passive: Minority passive includes investments that lead to less than 20% ownership in a company. This can cover a broad range of investments, including debt, because ownership and voting rights are not typically offered with debt investments. When a minority passive interest is taken, the investment is basically treated the same as other securities owned by the company for investment purposes.

Minority active: Minority active encompasses investments that lead to 20%-50% of ownership. In this segment companies usually use the equity method. This is an important segment because many companies make a significant ownership investment in another company but may not necessarily want to consolidate the business with consolidated financial statements as is required with a controlling interest. Taking an ownership stake of 20%-50% offers many opportunities for things like joint ventures as well as off-balance sheet reporting.
Controlling interest: Companies that have a 50% or more ownership stake in another company are generally required to use the consolidation method. The consolidation method requires companies to combine their financial reporting and report consolidated financial statements. At the top level, this requires a

comprehensive balance sheet, income statement, and cash flow statement with integrated re

Accounting for Intercorporate Investments

The ownership stake of an intercorporate investment helps to provide general guidance for the methodology used in accounting for the investment on a company's financials. Overall, there are three main methodologies that corresponded with the three broad investment classifications. Keep in mind that debt investments usually don't come with an ownership stake or voting rights.

cost Method

The cost method can be widely used because it encompasses a vast array of investments that are tied to an ownership stake of less than 20%. Intercorporate debt investments are typically accounted for using the cost method because debt does not often come with ownership rights or voting power.

Within the cost method, there can also be some further delineation of investments. Generally, these investments will basically be treated the same as other securities owned by the company for investment purposes. The securities may be designated as held to maturity (bonds), held for trading (bonds and stocks), available for sale (bonds and stocks), or strictly held on the balance sheet at the designated fair value.

Equity Method

In the equity method of accounting, the initial investment in the target company is recorded on the balance sheet. The value of the investment is adjusted based on the percentage of profit or loss for the owner. Dividends are not recorded as income. Rather, dividends increase cash and reduce the value of the investment for the investor.

Goodwill may also be associated with investments when the equity method is used. If the investor pays more than the carrying value of the investment, the target company may recognize goodwill for the difference.

Consolidation

Holding a 50% or more ownership stake in another company generally requires the consolidation method. With the consolidation method, companies must combine their financials into consolidated financial statements. The consolidation method is common after a merger or acquisition.

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Commercial papers [CPs]

A Commercial paper is an unsecured promissory note issued with a fixed Maturity by a Company approved by RBI, negotiable by endorsement and delivery, issued by in bearer from and issued at such discount on the face values as many be determined by the issuing Company.

Participants — Issuers :- All private sector company, public sector units, non-banking Company etc.

Investors :- Individuals, Banks, Corporates and also NRIs. usually banks, large corporate bodies and public sector units with investible funds participate in Cp Market.

Features of commercial paper

1. Short-term money Market instrument :- Commercial paper is a short-term money market instrument comprising usance promissory note with a fixed Maturity
2. Corporate Debt :- It is a Certificate evidencing an unsecured Corporate debt of short term Maturity.
3. Discount to face value :- Commercial paper is issued at a discount to face value basis but it can also be issued in interest bearing form.
4. Promises :- The issuer promises to pay the buyer some fixed amount on some future period but pledges no assets, only his liquidity and established earning

earning power, to guarantee that promise.

5. Issued Directly:- Commercial paper can be issued directly by Company to investors or through banks/Merchant bankers.

Advantages of Commercial paper

(1) Simplicity:- The advantage of commercial paper lies in its simplicity. It involves hardly any documentation between the issuer and investor.

(2) Flexibility:- The issuer can issue commercial paper with the maturities tailored to match the cashflow of the Company.

(3) Diversification:- A well rated Company can diversify its source of finance from banks to short term money markets at some what cheaper cost.

(4) Easy to Raise Long term Capital:-

The companies which are able to raise funds through commercial paper become better ~~than~~ known in the financial world and are thereby placed in a more favourable position for raising such long term capital as they may, from time to time, require. Thus there is an inbuilt incentive for Companies to remain financially strong.

(5) High Returns:- The commercial paper provides investors with higher returns than they could get from the banking system.

Movement of funds :- Commercial paper facilitates securitisation of loans resulting in creation of a secondary market for the paper and efficient movement of funds providing cash surplus to cash deficit entities.

RBI Guidelines on Commercial Paper Issue :-

The important guidelines are :

1. A company can issue commercial paper only if it has:

(i) A tangible net worth of not less than Rs. 10 Crores as per the latest balance sheet

(ii) minimum current ratio of 1.33:1

(iii) A fund based working capital limit of Rs. 25 Crores or more

(iv) a debt servicing ratio closer to 2;

(v) the company is listed on a stock exchange

(vi) subject to CAS discipline

(viii) The issuing company would need to obtain P1 from CRISIL.

2. Commercial paper shall be issued in multiples of Rs. 25 lakhs but the minimum amount to be invested by a single investor shall be Rs. 1 Crore.

3. The commercial paper shall be issued for a minimum Maturity period of 7 days and the maximum period of 6 Months from the date of issue. There will be no grace period on Maturity.

4. The Aggregate amount shall not exceed 20% of the issuers fund based working capital.

MANAGEMENT OF LOANS AND ADVANCES

1. Background

1.1 In the context of rapid growth of primary (urban) co-op. banks (PCBs), qualitative aspects of lending, such as adequacy of lending to meet credit requirements of their borrowers and effective supervision and monitoring of advances have assumed considerable importance.Previously working capital finance provided by the banks to trade and industry was regulated by the Reserve Bank of India through a series of guidelines/instructions issued. There were various quantitative and qualitative restrictions on bank's lending. The banks were also expected to ensure conformity with the basic financial disciplines prescribed by the RBI from time to time under Credit Authorisation Scheme (CAS).

1.2 However, consistent with the policy of liberalisation and financial sector reforms, several indirect measures to regulate bank credit such as exposure norms for lending to individual/group borrowers, prudential norms for income recognition, asset classification and provisioning for advances, capital adequacy ratios, etc. were introduced by RBI and greater operational freedom has been provided to banks in dispensation of credit.

1.3 Banks are now are expected to lay down, through their boards, transparent policies and guidelines for credit dispensation, in respect of each broad category of economic activity, keeping in view the credit exposure norms and various other guidelines issued by the Reserve Bank of India from time to time. Some of the currently applicable guidelines are detailed in the following paragraphs.

2. Working Capital requirements UPTO Rs. 1 crore

2.1 The assessment of working capital requirement of borrowers, other than SSI units, requiring fund based working capital limits upto Rs.1.00 crore and SSI units requiring fund based working capital limits upto to Rs.5.00 crore from the banking system may be made on the basis of their projected annual turn over.

2.2 In accordance with these guidelines, the working capital requirement is to be assessed at 25% of the projected turnover to be shared between the borrower and the bank, viz. borrower contributing 5% of the turnover as net working capital (NWC) and bank providing finance at a minimum of 20% of the turnover.

2.3 The banks may, at their discretion, carryout the assessment based on projected turnover basis or the traditional method. If the credit requirement based on traditional production/processing cycle is higher than the one assessed on projected turnover basis, the same may be sanctioned, as borrower must be financed upto the extent of minimum 20 per cent of their projected annual turnover.

2.4 The banks may satisfy themselves about the reasonableness of the projected annual turnover of the applicants, both for new as well as existing units, on the basis of annual statements of accounts or any other documents such as returns filed with sales-tax/revenue authorities and also ensure that the estimated growth during the year is realistic.

2.5 The borrowers would be required to bring in 5 per cent of their annual turnover as margin money. In other words, 25 per cent of the output value should be computed as working capital requirement, of which at least four-fifth should be provided by the banking sector, the balance one-fifth representing the borrower's contribution towards margin for the working capital. In cases, where output exceeds the projections or where the initial assessment of working capital is found inadequate, suitable enhancement in the working capital limits should be considered by the competent authority as and when deemed necessary. For example, in case, annual turnover of a borrower is projected at Rs. 60.00 lakh, the working capital requirement will be computed at Rs. 15.00 lakh (i.e. 25%) of which Rs. 12 lakh (i.e. 20%) may be provided by the banking system, while Rs. 3.00 lakh (i.e. 5 %) should be borrower's contribution towards margin money.

2.6 Drawals against the limits should, however, be allowed against the usual safeguards so as to ensure that the same are used for the purpose intended. Banks will have to ensure regular and timely submission of monthly statements of stocks, receivables, etc., by the borrowers and also periodical verification of such statements vis-à-vis physical stocks by their officials.

2.7 In regard to the above, few clarifications to some of the issues raised by banks are given in *Annexure* I.

3. Working Capital Requirements ABOVE Rs. 1 crore

3.1 **Method of Assessment**

3.1.1 The revised guidelines in respect of borrowers other than SSI units, requiring working capital limits above Rs.1 crore and for SSI units requiring fund based working capital limits above Rs.5 crore, from the banking system bestow greater level of flexibility to the primary (urban) co-operative banks in their day-to-day operations without diluting the prudential norms for lending as prescribed by Reserve Bank of India.

3.1.2 The earlier prescription regarding Maximum Permissible Bank Finance (MPBF), based on a minimum current ratio of 1.33:1, recommended by Tandon Working Group has been withdrawn. Banks are now free to decide on the minimum current ratio and determine the working capital requirements according to their perception of the borrowers and their credit needs.

3.1.3 Banks may evolve an appropriate system for assessing the working capital credit needs of borrowers whose requirement are above Rs.1 crore. Banks may adopt any of the under-noted methods for arriving at the working capital requirement of such borrowers.

a) The turnover method, as prevalent for small borrowers may be used as a tool of assessment for this segment as well,

b) Since major corporates have adopted cash budgeting as a tool of funds management, banks may follow cash budget system for assessing the working capital finance in respect of large borrowers.

c) The banks may even retain the concept of the MPBF with necessary modifications.

3.2 **Norms for Inventory/Receivables**

3.2.1 In order to provide flexibility in the assessment of credit requirements of borrowers based on a total study of borrowers' business operations, i.e., taking into account the production/processing cycle of the industry as well as the financial and other relevant parameters of the borrower, the banks have also been permitted to decide the levels of holding of each item of inventory as also of receivables, which in their view would represent a reasonable build-up of current assets for being supported by bank finance.

3.2.2 Reserve Bank of India no longer prescribes detailed norms for each item of inventory as also of receivables.

3.3 **Classification of Current Assets and Current Liabilities**

3.3.1 With the withdrawal of MPBF, inventory norms and minimum current ratio, the classification of current assets and current liabilities ceases to be mandatory. The banks may decide on their own as to which items should be included for consideration as current assets or current liabilities.

3.3.2 Banks may also consider evolving suitable internal guidelines for accepting the projections made by their borrowers relating to the item 'Sundry Creditors (Goods)' appearing as an item under 'Other Current Liabilities' in the balance sheet.

3.4 **Bills Discipline**

In respect of borrowers enjoying fund-based working capital credit limits of Rs. 5 crore and more from the banking system, the banks are required to ensure that the book-debt finance does not exceed 75 per cent of the limits sanctioned to borrowers for financing inland credit sales. The remaining 25 per cent of the credit sales may be financed through bills to ensure greater use of bills for financing sales.

3.5 **Grant of Ad hoc Limits**

To meet the contingencies, banks may decide on the quantum and period for granting ad hoc limits to the borrowers based on their commercial judgement and merits of individual cases. While granting the ad hoc limits the banks must ensure that the aggregate credit limits (inclusive of ad hoc limits) do not exceed the prescribed exposure ceiling.

3.6 **Commitment Charge**

The levy of commitment charge is not mandatory and it is left to the discretion of the financing banks/ consortium/syndicate. Accordingly, banks are free to evolve their own guidelines in regard to commitment charge for ensuring credit discipline.

3.7 Consortium Arrangement

The mandatory requirement of formation of consortium for extending working capital finance under multiple banking arrangements has been withdrawn.

3.8 Syndication of Credit

The syndication of loans is an internationally practised model for financing credit requirements. The banks are free to adopt syndication route, irrespective of the quantum of credit involved, if the arrangement suits the borrower and the financing banks.

3.9 Loan System for Delivery of Bank Credit

3.9.1 Background

In order to bring about an element of discipline in the utilisation of bank credit by large borrowers, instill efficiency in funds management, loan system for delivery of bank credit was been introduced for borrowers enjoying working capital credit limits of Rs.10 crore and above from the banking system and the minimum level of loan component for such borrowers was fixed at 80 per cent. These guidelines have been revised by RBI, in the light of current environment of short-term investment opportunities available to both the corporate and the banks. In case any primary (urban) co-operative bank is having borrowers with MPBF of Rs. 10 crore and above where it has participated under consortium/syndication, it should ensure strict compliance with the under-noted guidelines.

3.9.2 Loan Component and Cash Credit Component

(i) Banks may change the composition of working capital by increasing the cash credit component beyond 20 per cent or to increase the loan component beyond 80 per cent, as the case may be, if they so desire.

(ii) Banks are expected to appropriately price each of the two components of working capital finance, taking into account the impact of such decisions on their cash and liquidity management.

(iii) If a borrower so desires, higher loan component can be granted by the bank; this would entail corresponding pro-rata reduction in the cash credit component of the limit.

(iv) In the case of borrowers with working capital (fund based) credit limit of less than Rs. 10 crore, banks may persuade them to go in for the Loan System by offering an incentive in the form of lower rate of interest on the 'loan component' as compared to the 'cash credit component' The actual percentage of 'loan component' in these cases may be settled by the bank with its borrower clients.

(v) In respect of certain business activities which are cyclical and seasonal in nature or have inherent volatility, the strict application of loan system may create difficulties for the borrowers. Banks, may with the approval of their respective Boards, identify such business activities which may be exempt from the loan system of credit delivery.

3.9.3 **Ad hoc Credit Limit**

The ad hoc/additional credit for meeting temporary requirements may be considered by the financing bank only after the borrower has fully utilised/exhausted the existing limit.

3.9.4 **Sharing of Working Capital Finance**

The ground rules for sharing of cash credit and loan components may be laid down by the consortium, wherever formed, subject to the stipulations contained in Para. 3.9.2 above.

The level of individual bank's share shall be governed by the norm for single / group borrowers credit exposure.

3.9.5 **Rate of Interest**

Banks are allowed to fix separate lending rates for 'loan component' and 'cash credit component'.

3.9.6 **Period of Loan**

The minimum period of the loan for working capital purposes may be fixed by banks in consultation with borrowers. Banks may decide to split the loan component according to the need of the borrower with different maturity bases for each segment and allow roll over.

3.9.7 **Security**

In regard to security, sharing of charge, documentation, etc., banks may themselves decide on the requirements, if necessary, in consultation with the other participant banks.

3.9.8 **Export Credit**

Export credit limit would be allowed in the form hitherto granted. The bifurcation of the working capital limit into loan and cash credit components, as stated in paragraph 3.9.2 (i) above, would be effected after excluding the export credit limits (pre-shipment and post-shipment).

3.9.9 **Bills Limit**

Bills limit for inland sales may be fully carved out of the 'loan component'. Bills limit also includes limits for purchase of third party (outstation) cheques/bank drafts. Banks must satisfy themselves that the bills limit is not mis-utilised.

3.9.10 **Renewal/Roll-over of Loan Component**

The loan component , may be renewed/rolled over at the request of the borrower. However, banks may lay down policy guidelines for periodical review of the working capital limit and the same may be scrupulously adhered to.

3.9.11 **Provision for Investing Short Term Surplus Funds of Borrowers**

The banks, at their discretion, may permit the borrowers to invest their short term/temporary surpluses in short-term money market instruments like Commercial Paper (CP), Certificates of Deposit (CDs) and in Term Deposit with banks, etc.

3.9.12 **Applicability**

The loan system would be applicable to borrowal accounts classified as 'standard' or 'sub-standard'.

4 Credit Administration

4.1 **No Objection Certificate**

The primary (urban) co-operative banks should not finance a borrower already availing credit facility from another bank without obtaining a 'No Objection Certificate' from the existing financing bank.

4.2 **Opening of Current Accounts**

Before permitting the parties to open current accounts/sanctioning post-sale limits, the banks should invariably obtain the concurrence of the banks which have sanctioned main limits.

4.3 **Certification of Accounts of Non-Corporate Borrowers by Chartered Accountants**

As per the Income Tax Act, 1961, filing of audited balance sheet and profit & loss account is mandatory for certain types of non-corporate entities. Therefore, the banks must insist on the audited financial statements from the borrowers enjoying large limits; since such borrowers would, in any case, be submitting audit certificate to the income-tax authorities, based on audit of their books of accounts by a Chartered Accountant.

4.4 **Defaults in Payment of Statutory Dues by Borrowers**

4.4.1 It has been observed that many of the borrowers enjoying credit facilities from primary (urban) co-operative banks default in payment of Provident Fund, Employees State Insurance and other statutory dues. Despite this, such borrowers continue to carry on operations with the assistance of bank finance without meeting their statutory, obligations.

4.4.2 In the case of insolvency/winding up of a borrowing employer, under the law, there are certain priorities in regard to the recovery of statutory dues e.g., employees contribution towards provident fund deducted from wages of the employee members for a period of more than six months and not paid to the Commissioner, are a first charge on the assets of borrowers.

4.4.3 In the circumstances, the banks should safeguard their interest vis-à-vis such statutory dues and, therefore, it would be desirable for the banks to ensure that provident funds and similar other dues are paid by the borrowers promptly. For the purpose, the banks should incorporate an appropriate declaration in their application forms for grant/renewal/ enhancement of credit facilities so as to ensure that the position regarding the statutory dues is disclosed therein.

4.4.4 Where warranted, banks should satisfy themselves about genuineness of the party's declaration in this regard. Thus, the sanction/renewal/ enhancement of credit facilities can be utilised by banks as a leverage for enforcing necessary discipline on the part of their borrowers.

4.4.5 In respect of the corporate borrowers and non-corporate borrowers, the amount of statutory dues should normally be reflected in their annual accounts which should be duly certified by the auditors, and hence, the banks should have no difficulty in ascertaining the position of their statutory dues. Nonetheless, in addition to duly audited annual accounts, banks should also obtain a specific certificate from the Chartered Accountant as regards the position of statutory dues, if the audited accounts do not clearly indicate the position.

4.4.6 After ascertaining the quantum of statutory dues, the banks should ensure that these are cleared by the borrowers within a reasonable period and that too through internal generation of funds. The non-payment of statutory dues is one of the symptoms of incipient sickness of an industrial unit. Therefore, it is in the interest of both the lender and borrower to give high priority to the clearance of these dues. Apart from insisting the borrowers to indicate a definite programme for clearance of arrears, banks may consider suitable restrictions on the outflow of funds by way of dividends, repayment of loans from promoters or their friends, relatives or inter-corporate borrowings etc., till the overdue statutory liabilities are cleared.

4.5 Sanction of Advances

4.5.1 Irregularities/ Deficiencies in Credit Sanction

Banks should, take suitable precautions to avoid irregular practices such as sanctioning of advances beyond discretionary powers and/or without proper credit appraisal in order to minimise chances of frauds.

4.5.2 Delegation of Powers

(i) The Board of Directors should delegate specific powers to the Branch Managers and other functionaries at the Head Office level as also to the Chairman in the matter of sanction of advances and expenditure. A system should also be introduced to ensure that powers are exercised within the limits prescribed and any transgressions are immediately reported to Head Office.

(ii) The internal inspectors should examine during the course of inspection of branches whether powers have been exercised properly and any unauthorised exercise of powers should immediately be brought to the notice of Head Office. Similarly, sanctions beyond discretionary powers by the Chairman, Chief Executive Officer and other executives at the Head Office should also be reported to the Board of Directors.

4.5.3 Oral Sanction

The higher authorities at various level should desist from the unhealthy practice of conveying sanction of advances orally or on telephone.

4.5.4 Proper Record of Deviations

(i) Only in exigencies, where sanctions are made on telephone/oral instructions of higher functionaries or sanctions beyond discretionary powers have to be resorted to, the following steps should be taken:

(a) Record of such instructions/sanctions should be maintained by the sanctioning/disbursing authorities explaining the circumstances under which sanctions were made.

(b) Written confirmation of the competent sanctioning authority should be obtained by the disbursing authority / official within a week/fortnight.

(c) Sanctions within discretionary powers should also be reported to Head Office within a stipulated time and Head Office should meticulously follow up receipt of such returns.

(d) Head Office should diligently scrutinise the statements/ returns and should initiate stringent action against erring functionary(ies) if he/they is/are found to have indulged in unauthorised sanctioning.

(ii) Officials should exercise powers delegated to them judiciously and should not exceed their discretionary powers for granting loans and advances. Violation, if any, in this regard should be viewed seriously and the guilty should be punished suitably.

4.6 Monitoring Operations in Loan Accounts

4.6.1 Diversion of Funds

Some of the bank clients are known to be making large cash withdrawals. It is quite possible that such cash withdrawals may be used by the account holders for undesirable or illegal activities. While cash withdrawals cannot be refused, banks should keep a proper vigil over requests of their clients for cash withdrawals from their accounts for large amounts.

4.6.2 Post-Sanction Monitoring

(i) It is the primary responsibility of banks to be vigilant and ensure proper end use of bank funds /monitor the funds flow. It is, therefore, necessary for banks to evolve such arrangements as may be considered necessary to ensure that drawals from cash credit/overdraft accounts are strictly for the purpose for which the credit limits are sanctioned by them. There should be no diversion of working capital finance for acquisition of fixed assets, investments in associate companies/subsidiaries, and acquisition of shares, debentures, units of Unit Trust of India and other mutual funds, and other investments in the capital market. This has to be so, even if there is sufficient drawing power/undrawn limit for the purpose of effecting drawals from the cash credit account.

(ii) Post sanction follow-up of loans and advances should be effective so as to ensure that the security obtained from borrowers by way of hypothecation, pledge, etc. are not tampered with in any manner and are adequate.

(iii) Drawals against clearing cheques should be sanctioned only in respect of first class customers and even in such cases the extent of limits and the need therefor should be subjected to thorough scrutiny and periodical review. Banks should not issue banker's cheques/pay orders/demand drafts against instruments presented for clearing, unless the proceeds thereof are collected and credited to the account of the party. Further, banker's cheques /pay orders/ demand drafts, should not be issued by debit to cash credit /over draft accounts which are already overdrawn or likely to be overdrawn with the issue of such instruments.

(iv) Drawals against clearing instruments should be normally confined to bank drafts and government cheques and only to a limited extent against third party cheques.

(v) Cheques against which drawals are allowed should represent genuine trade transactions and strict vigilance should be observed against assisting kite-flying operations.

(vi) Drawals against cheques of allied /sister concerns should not be permitted and the facility of drawal against clearing cheques should normally be of temporary nature and should not be allowed on a regular basis without proper scrutiny and appraisal.

(vii) Bills of accommodation nature should never be purchased and the officials responsible for purchase of such bills should be punished suitably.

(viii) In case a borrower is found to have diverted finance for the purposes, other than for which it was granted, banks must recall the amounts so diverted. In addition, banks may charge penal interest on the amount diverted.

(ix) Where borrowers fail to repay the amounts diverted from cash credit accounts for uses other than for which the limit was sanctioned, banks should reduce the limits to the extent of amount diverted. The above aspects relating to safe guards are only illustrative in nature and not exhaustive.

4.6.3 **Responsibility**

(i) The primary responsibility for preventing misuse of funds rests with the management of banks. For the purpose, highest standards of integrity and efficiency are imperative in urban banks which are the trustees of public money. The banks should, therefore, take appropriate steps to review and tighten their internal administration and control measures so as to eliminate the scope for misuse/diversion of funds and malpractices.

(ii) Banks should take serious view of instances of misuse of power, corruption and other malpractices indulged by the members of staff and erring staff members should be given punishments befitting the seriousness of the irregularity. Light punishments such as issue of warning, stoppage of increments, transfer, etc. may not prove a deterrent in all cases. Quick disposal of enquiries by the banks and award of deterrent punishment would be necessary in all such cases, The Board should take more active interest in these matters.

4.7 Annual Review of Advances

For an effective monitoring of the advances, it is imperative for the banks to undertake an exercise for review of the advances on a regular basis. Apart from the usual objective of such a review of assessing the quality of operation, safety of funds, etc. the review should specifically attempt to make an assessment of the working capital requirements of the borrower based on the latest data available, whether limits continue to be within the need-based requirements and according to the bank's prescribed lending norms.

5. Other Guidelines

5.1 Relief Measures to Persons Affected by Natural Calamities

5.1.1 The primary (urban) co-operative banks are expected to provide relief and rehabilitation assistance, in their area of operation to people affected by natural calamities such as droughts, floods, cyclones, etc.

5.1.2 The Government of India has evolved, in consultation with the RBI and the IBA, a set of broad guidelines (Standing Guidelines) indicating the steps to be taken by the banks in calamity affected areas. The Standing Guidelines, duly modified, are given in Annexure II.

5.1.3 In order to avoid delay in taking relief measures on the occurrence of natural calamity, banks should evolve a suitable policy framework with the approval of the Board of Directors. An element of flexibility may be provided in the measures so as to synchronise the same with the measures which could be appropriate in a given situation in a particular State or District and parameters, in this regard, may be decided in consultation with SLBC/DCC, as the case may be.

5.1.4 Banks should get the documentation settled as per revised guidelines in consultation with their legal departments, taking into account the relevant provisions of the Contract Act and the Limitations Act and may issue appropriate instructions to their offices in respect of documentation in relation to cases covered by these guidelines.

5.1.5 Whenever required, RBI advises the banks to follow these guidelines in respect of persons affected by riots and disturbances.

5.2 Disclosure of Information on Defaulting Borrowers of Banks and Financial Institutions

5.2.1 The Reserve Bank of India has been collecting information regarding defaulting borrowers and suit filed accounts of scheduled commercial banks and financial institutions for circulation among banks and financial institutions to put them on guard against such defaulters.

5.2.2 Similar information has also to be collected from scheduled primary (urban) co-operative banks. These banks are, therefore, required to submit to the Reserve Bank of India as at the end of September and March every year, the details of the borrowal accounts which have been classified as doubtful, loss or suit filed with outstanding (both under funded and non-funded limits) aggregating Rs. 1 crore and above as per the format given in *Annexure* III.

5.2.3 The Reserve Bank of India is circulating to the banks and financial institutions the information on the defaulters (i.e., advances classified as doubtful and loss). The banks and financial institutions may make use of the information while considering the merits of the requests for new or additional credit limits by existing and new constituents.

5.2.4 The Reserve Bank of India has also been publishing a list of borrowal accounts against which Banks and Financial Institutions have filed suits for recovery of advances (outstanding aggregating Rs.1.00 crore and above) based on information furnished by scheduled commercial banks and financial institutions. Such list published as on 31 March each year in Compact Disc (CD) form and updated on quarterly basis is available with RBI, Publications Division at the following address:

Section
Sales Review and Publications
Division of Reports, of India
Reserve Bank Ground Floor
Amar Building, P.B. No. 1036
P.B. Road,
Fort, Mumbai 400 001.

The said list and its quarterly up dates are also placed on RBI's Website (www.rbi.org.in)

5.2.5 It is likely that some of the borrowers named in the list of suit filed accounts may approach the scheduled primary (urban) co-operative banks for their credit requirements. The information available in the above mentioned CD will be of immense use to scheduled primary (urban) co-operative banks, while considering requests for fresh/additional credit limits. The banks can verify the list to ensure that the defaulting borrowing units as also their proprietors/partners/ directors etc. named in the published list of suit-filed accounts, either in their own names or in the names of other units with which they are associated, are not extended further credit facilities.

5.2.6 The banks may make enquiry, if any, about the defaulters from the reporting bank/ financial institution.

6 MONITORING OF WILFUL DEFAULTERS

6.1 Collection and dissemination of information on cases of wilful default of Rs. 25.00 lakh and above

6.1.1 Pursuant to the instructions of the Central Vigilance Commission for collection of information on wilful defaulters by RBI and dissemination to the reporting banks and financial institutions, a scheme has been framed under which the banks and financial institutions will be required to submit the details of the wilful defaulters. The scheduled primary (urban) co-operative banks have also been brought within the ambit of the scheme.

6.1.2 The details of the scheme are given below:

(i) The scheme has come into force with effect from 1st April 1999. Accordingly, scheduled primary (urban) co-operative banks are required to report on a quarterly basis, all cases of wilful defaults which occurred, or are detected after 31st March 1999 in the proforma given in Annexure IV.

(ii) The scheme covers all non-performing borrowal accounts with outstanding (funded facilities and such non-funded facilities which are converted into funded facilities) aggregating to Rs. 25.00 lakh and above.

6.2 Wilful Default

'A wilful default would be deemed to have occurred, if :

(a) The unit has defaulted in meeting its payment / repayment obligations to the lender even when it has the capacity to honour the said obligations.

OR

The unit has defaulted in meeting its payment / repayment obligations to the lender and has not utilised the finance from the lender for the specific purposes for which finance was availed of but has diverted the funds for other purposes.

OR

(c) The unit has defaulted in meeting its payment / repayment obligations to the lender and has siphoned off the funds so that the funds have not been utilised for the specific purpose for which finance was availed of, nor the funds are available with the unit in the form of other assets.

6.3 Diversion and siphoning of funds

6.3.1 Diversion of funds would be construed to include any one of the under-noted occurrences:

(a) utilisation of short-term working capital funds for long-term purposes not in conformity with the terms of sanctions;

(b) deploying borrowed funds for purposes / activities or creation of assets other than those for which the loan was sanctioned;

(c) transferring funds to the subsidiaries / group companies or other corporates by whatever modalities;

(d) routing of funds through any bank other than the lender bank or members of consortium without prior permission of the lender;

(e) investment in other companies by way of acquiring equities / debt instruments without approval of lenders;

(f) short fall in deployment of funds vis-à-vis the amounts disbursed / drawn and the difference not being accounted for.

6.3.2 Siphoning of funds should be construed to have occur if any funds borrowed are utilised for purposes unrelated to the operations of the borrower, to the detriment of the financial health of the entity or of the lender. The decision as to whether a particular instance amounts to siphoning of funds would have to be a judgement of the lenders based on objective facts and circumstances of the case.

6.4 Cut-off limits

While the penal measures normally be attracted by all the borrowers identified as wilful defaulters or the promoters involved in diversion / siphoning of funds, keeping in view the present limit of Rs.25 lakh fixed by the Central Vigilance Commission for reporting of cases of wilful default by scheduled banks to RBI, any wilful defaulter with an outstanding balance of Rs.25 lakh or more would attract the penal measure stipulated at para 6.6 below. The limit of Rs.25 lakh may also be applied for the purpose of taking congnisance of the instances of `siphoning '/ `diversion' of funds.

6.5 End-use of Funds

In cases of project financing, banks should seek to ensure end use of funds by, inter alia, obtaining certification from the Chartered Accountants for the purpose. In case of short-term corporate / clean loans, such an approach ought to be supplemented by `due diligence' on the part of lenders themselves, and to the extent possible, such loans should be limited to only those borrowers whose integrity and reliability were above board. Scheduled pcbs, therefore, should not depend entirely on the certificates issued by the Chartered Accountants but strengthen their internal controls and the credit risk management system to enhance the quality of their loan portfolio. Needless to say, ensuring end-use of funds by banks should form a part of their loan policy document for which appropriate measures should be put in place.

6.5.1 The following are the illustrative measures that could be taken by the lenders for monitoring and ensuring end-use of funds :

(a) Meaningful scrutiny of quarterly progress reports / operating statements / balance sheets of the borrowers;

(b) Regular inspection of borrowers' assets charged to the lenders as security;

(c) Periodical scrutiny of borrowers' books of accounts and the no-lien accounts maintained with other banks;

(d) Periodical visits to the assisted units;

(e) System of periodical stock audit, in case of working capital finance;

(f) Periodical comprehensive management audit of the 'Credit' function of the lenders, so as to identify the systemic weaknesses in the credit-administration.

6.6 Penal measures

In order to prevent the access to the capital markets by the wilful defaulters, a copy of the list of wilful defaulters is forwarded by RBI to SEBI as well. It has also been decided that the following measures should be initiated by schedule pcbs against the wilful defaulters

(i) No additional facilities be granted to the listed wilful defaulters. In addition, the entrepreneurs / promoters of companies where banks have identified siphoning / diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions should be debarred from institutional finance for floating new ventures for a period of 5 years from the date the name of the wilful defaulter is published in the list of wilful defaulters by the RBI.

(ii) The legal process, where warranted, against the borrowers/guarantors and foreclosure of loans should be initiated expeditiously. The lenders may also initiate criminal proceedings against wilful defaulters, wherever necessary.

(iii) Wherever possible, the banks should adopt a proactive approach for a change of management of the wilfully defaulting borrower unit. It would be imperative on the part of the banks to put in place a transparent mechanism for the entire process so that the penal provisions are not misused and the scope of such discretionary powers is kept to the barest minimum. It should be ensured that a solitary or isolated instance is not made the basis for imposing the penal action.

6.7 Treatment of Group

While dealing with wilful default of a single borrowing company in a group, the banks should consider the track record of the individual company, with reference to its repayment performance to its lenders. However, in cases where a letter of comfort and/or the guarantees furnished by the companies within the group on behalf of the wilfully defaulting units are not honoured when invoked by scheduled banks, such group companies should also be reckoned as wilful defaulters.

6.8 Role of Auditors

6.8.1 In case any falsification of accounts on the part of the borrowers is observed by banks, they should lodge a formal complaint against the auditors of the borrowers, with Institute of Chartered Accountant of India (ICAI) if it is observed that the auditors were negligent or deficient in conducting the audit to enable the ICAI to examine and fix accountability of the auditors.

6.8.2 With a view to monitoring the end-use of funds, if the lenders desire a specific certification from borrowers' auditors regarding diversion / siphoning of funds by the borrower, the lender should award a separate mandate to the auditors for the purpose. To facilitate such certification by the auditors scheduled pcbs will also need to ensure that appropriate covenants in the loan agreements are incorporated to enable award of such a mandate by the lenders to the borrowers / auditors.

6.9 Filing of Suits to Recover Dues from Wilful Defaulters

6.9.1 There are few cases where the amount outstanding is substantial but the banks have not initiated any legal action against the defaulting borrowers. It may be noted that the cases of wilful defaults have an element of fraud and cheating and therefore, should be viewed differently.

6.9.2 Scheduled pcbs should examine all cases of wilful defaults of Rs. 1.00 crore and above and file suits in such cases, if not already done. Banks should also examine whether in such cases of wilful defaults, there are instances of cheating/fraud by the defaulting borrowers and if so, they should also file criminal cases against those borrowers. In other cases involving amounts below Rs. 1.00 crore, banks should take appropriate action, including legal action, against the defaulting borrowers.

7. GUIDELINES FOR REHABILITATION OF SICK SMALL SCALE INDUSTRIAL UNITS

The Reserve Bank of India, had constituted a Working Group on Rehabilitation of Sick SSI units, under the Chairmanship of Shri S. S. Kohli, to review the existing guidelines in regard to rehabilitation of sick small scale units and to recommend the revision of the guidelines for rehabilitation of currently sick and potentially viable SSI units, making them transparent and non-discretionary. The revised guidelines are detailed in Annexure V. Reserve Bank of India has accepted all the major recommendations of the Group.

(ii) The emphasis of the rehabilitation effort in case of SSI units is on early detection of signs of incipien sickness, adequate and intensive relief measures and their speedy application rather than giving a long spa of time to the units for rehabilitation.

(iii) The banks should take a sympathetic attitude and strive for rehabilitation, in respect of units in the SSI sector, particularly wherever the sickness is on account of circumstances beyond the control of the entrepreneurs. Banks are also advised to take a pro-active stance in providing timely assistance for rehabilitation of small scale units, which are affected by the industrial down turn and delays in payments against supplies made by them to large scale and other units.

(iv) In the case of units which are not applicable of revival, banks should try for a settlement and \or resort to other recovery measures expeditiously.

(v) It may be noted that the enclosed guidelines are applicable to industrial units which were being financed by the bank before they turned into sick units. Primary (urban) co-operative banks are not expected to take over financing of sick industrial units, particularly, those financed by commercial banks earlier, in view of the risks involved.

8. SPECIFIC LENDING ACTIVITIES

8.1 Bridge Loans/Interim Finance

8.1.1 The grant of bridge loan/interim finance by pcbs to any company (including finance companies) is totally prohibited.

8.1.2 The ban on sanction of bridge loans/interim finance is also applicable in respect of Euro issues.

8.1.3 The banks should not circumvent these instructions by purport and/or intent by sanction of credit under a different nomenclature like unsecured negotiable notes, floating rate interest bonds, etc. as also short-term loans, the repayment of which is proposed/expected to be made out of funds to be or likely to be mobilised from external/other sources and not out of the surplus generated by the use of the asset(s).

8.1.4 If any bank has sanctioned and disbursed any bridge loan/interim finance, it should report the same to the concerned Regional Office of the Urban Banks Department with full particulars and certifying that the loans are utilised strictly for the purpose for which the public issue and/or market borrowing was intended. Thereafter, the concerned banks should immediately take steps to ensure timely repayment of such bridge loans/interim finance already sanctioned and disbursed and under no circumstances, should the banks allow extension of time for repayment of existing bridge loans/interim finance.

8.1.5 These instructions are issued by the Reserve Bank of India in exercise of powers conferred by th Sections 21 and 35A read with section 56 of the Banking Regulation Act, 1949.

.2 Advances to Builders/Contractors

8.2.1 The builders/contractors, who generally require, huge funds, take advance payments from the prospective buyers or from those on whose behalf construction is undertaken and, therefore, may not normally require bank finance for the purpose. Any financial assistance extended to them by banks may result in dual financing. The banks should, therefore, normally refrain from sanctioning loans and advances to this category of borrowers.

8.2.2 However, where contractors undertake comparatively small construction work on their own, (i.e. when no advance payments are received by them for the purpose), the banks may consider extending financial assistance to them against the hypothecation of construction materials, provided such loans and advances are in accordance with the by-laws of the bank.

8.2.3 The banks should frame comprehensive prudential norms relating to the ceiling on the total amount of real estate loans, single/aggregate exposure limit for such loans, margins, security, repayment schedule and availability of supplementary finance taking into account guidelines issued by RBI and the policy should be approved by the bank's Board.

8.2.4 Banks should undertake a proper scrutiny of the relevant loan applications, and satisfy themselves, among other things, about the genuineness of the purpose, the quantum of financial assistance required, creditworthiness of the borrower, his repayment capacity, etc. and also observe the usual safeguards, such as, obtaining periodical stock statements, carrying out periodical inspections, determining drawing power strictly on the basis of the stock held, maintaining a margin of not less than 40 to 50 percent, etc. They should also ensure that materials used up in the construction work are not included in the stock statements for the purpose of determining the drawing power.

8.2.5 The banks may also take collateral security, wherever available. As the construction work progresses the contractors will get paid and such payments should be applied to reduce the balance in the borrowal accounts. If possible, the banks, could perhaps enter into a tripartite agreement-with the borrower and his clients, particularly when no collateral securities are available for such advances. Thus, the banks should ensure that bank credit is used for productive construction activity and not for activity connected with speculation in real estate.

8.3 Financing of Leasing/Hire Purchase Companies

9.3.1 Enrolment of Financial Companies as Members

(i) Primary (urban) co-operative banks are normally not expected to enroll non-banking financial institutions like investment and financial companies as their members since it would be in contravention of the State Co-operative Societies Act concerned and will also not be in conformity with the provisions of model by-law No.9 recommended for adoption, by all banks.

(ii) Therefore, the primary (urban) co-operative banks are not permitted to finance such type of non-banking financial companies (NBFCs).

8.3.2 Norms for financing Leasing/Hire Purchases Companies

(i) As in the case of finance and investment companies, admission of non-banking financial companies which are not engaged exclusively in leasing/hire purchase business as members may be contrary to the provisions contained in the state co-operative societies act concerned and model bye-law No.9 referred to above. It will, therefore, be necessary for banks to obtain prior approval of the concerned Registrar of Co-operative Societies before admitting them as members.

(ii) Even financing the leasing/hire purchase companies by primary (urban) co-operative banks on a large scale is not favoured by the Reserve Bank of India, since the banks are basically required to cater to the credit needs of the people of small means.

(iii) Presently banks with working capital funds aggregating to Rs. 25 crore and above, only are permitted take up the financing of leasing/hire purchase companies that too only in consortium with other scheduled commercial banks. The banks should observe the following norms, while financing such companies :

(a) The level of finance to leasing/hire purchase companies depends on the net owned funds of the companies, subject to the overall ceiling on their borrowings upto ten times of their owned funds.

(b) Bank credit to companies exclusively engaged in equipment leasing and hire purchases and such leasing/hire purchase companies which are predominantly engaged in equipment leasing/hire purchase business (i.e., at least 75 per cent of assets are in equipment leasing/hire purchase and 75 per cent of their gross income is derived from these two types of activities as per their last audited balance sheet) may be extended within the ceiling of three times of the net owned funds within the overall ceiling of their borrowings upto ten times of net owned funds.

(c) In the case of other equipment leasing/hire purchases companies (i.e. companies whose assets in equipment leasing/hire purchase business are less than 75 per cent and whose gross income derived from these two types of activities as per the last audited balance sheet is less than 75 per cent of its gross income), the credit limit has to be within two times of their net owned funds from the present level of four times.

8.4 Working Capital Finance to Information Technology (IT) and Software Industry

8.4.1 Banks are permitted to decide on their own the loan policy and the manner of estimating the working capital finance based on MPBF method or any other method to be approved by their Board of Directors. The stance of Reserve Bank policy towards operational freedom to banks remains unchanged. At the same time, Reserve Bank recognises the fact that the banks are not comfortable with extending aggressive credit support to a relatively new area of software industry unlike other traditional industries, due to several factors which make the assessment of credit needs and follow up thereof difficult, if not insurmountable.

8.4.2 In order to bring about uniformity in approach, the Reserve Bank has formulated guidelines for information of banks, on various aspects of lending to information technology and software industry to facilitate free flow of credit. The same were enclosed to our circular DS.SUB.No.4/13.05.00/98-99 dated 5 October 1998, addressed to scheduled PCBs. Banks are, however, free to modify the guidelines based on their own experience without reference to Reserve Bank to achieve the purpose of the guidelines in letter and spirit.

8.4.3 These guidelines have been framed based on the recommendations made by the study group appointed by Reserve Bank to study the modalities of credit extension to software industry as also taking into account the suggestions made by the industry associations.

8.4.4 This being a relatively new area of credit deployment, primary (urban) co-operative banks may take adequate steps to develop expertise in this area. Besides other measures which banks might take, the need for training staff for developing them in acquiring skills of project appraisal in this new area of activity need not be over-emphasised. It has to be ensured that the concerned staff is well aware of the requirements of the industry and remain in tune with the latest developments so that the higher standards of project appraisal can be maintained before extending the working capital finance to Information Technology and software industries.

9. DISCOUNTING / REDISCOUNTING OF BILLS BY BANKS

Banks may adhere to the following guidelines while purchasing / discounting / negotiating / rediscounting of genuine commercial / trade bills:

i. Since banks have already been given freedom to decide their own guidelines for assessing / sanctioning working capital limits of borrowers, they may sanction working capital limit as also bills limit to borrowers after proper appraisal of their credit needs and in accordance with the loan policy as approved by their Board of Directors.

ii. Banks should clearly lay down a bills discounting policy approved by their Board of Directors, which should be consistent with their policy of sanctioning of working capital limits. In this case, the procedure for Boar approval should include banks' core operating process from the time the bills are tendered till these ar realised. Banks may review their core operating processes and simplify the procedure in respect of bi financing. In order to address the oft-cited problem of delay in realisation of bills, banks may take advantage of improved computer / communication network like Structured Financial Messaging System (SFMS), wherever available, and adopt the system of 'value dating' of their clients' accounts.

iii. Banks should open letters of credit (LCs) and purchase / discount / negotiate bills under LCs only in respect of genuine commercial and trade transactions of their borrower constituents who have been sanctioned regular credit facilities by the banks. Banks should not, therefore, extend fund based (including bills financing) or non-fund based facilities like opening of LCs, providing guarantees and acceptances to non-constituent borrower or / and non-constituent member of a consortium / multiple banking arrangement.

iv. For the purpose of credit exposure, bills purchased / discounted / negotiated under LCs or otherwise should be reckoned on the bank's borrower constituent. Accordingly, the exposure should attract a risk weight appropriate to the borrower constituent (viz, 100% for firms, individuals, corporate etc.) for capital adequacy purposes.

v. While purchasing / discounting / negotiating bills under LCs or otherwise, banks should establish genuineness of underlying transactions / documents.

vi. Banks should ensure that blank LC forms are kept in safe custody as in case of security items like blank cheques, demand drafts etc. and verified / balanced on daily basis. LC forms should be issued to customers under joint signatures of the bank's authorised officials.

vii. The practice of drawing bills of exchange claused 'without recourse' and issuing letters of credit bearing the legend 'without recourse' should be discouraged because such notations deprive the negotiating bank of the right of recourse it has against the drawer under the Negotiable Instruments Act. Banks should not, therefore, open LCs and purchase / discount / negotiate bills bearing the 'without recourse' clause.

viii. Accommodation bills should not be purchased / discounted / negotiated by banks. The underlying trade transactions should be clearly identified and a proper record thereof maintained at the branches conducting the bills business.

ix. Banks should be circumspect while discounting bills drawn by front finance companies set up by larg industrial groups on other group companies.

x. Bills rediscounts should be restricted to usance bills held by other banks. Banks should not rediscount b earlier discounted by non-bank financial companies (NBFCs) except in respect of bills arising from sal light commercial vehicles and two / three wheelers.

xi. Banks may exercise their commercial judgment in discounting of bills of services sector. However, discounting such bills, banks should ensure that actual services are rendered and accommodation bil not discounted. ***Services sector bills should not be eligible for rediscounting.*** Further, providing finance against discounting of services sector bills may be treated as unsecured advance and therefore, should be within the limits prescribed by UBD for sanction of unsecured advances.

xii. In order to promote payment discipline which would to a certain extent encourage acceptance of bills, all corporate and other constituent borrowers having turnover above threshold level as fixed by the bank's Board of Directors should be mandated to disclose 'aging schedule' of their overdue payables in their periodical returns submitted to banks.

xiii. Banks should not enter into Repo transactions using bills discounted / rediscounted as collateral.