

# REPORT OF THE BOARD OF DIRECTORS ON THE WORKING OF THE DEPOSIT INSURANCE AND CREDIT GUARANTEE CORPORATION FOR THE YEAR ENDED 31<sup>st</sup> MARCH 2005 SUBMITTED IN TERMS OF SECTION 32(1) OF THE DEPOSIT INSURANCE AND CREDIT GUARANTEE CORPORATION ACT, 1961

## PART I - BANKING SECTOR SCENARIO

There has been significant improvement in the asset quality and profitability of the commercial banking sector due to continuing focus on risk management systems, recovery management and corporate governance practices. The capital-to-risk weighted assets ratio showed continuing improvements across various commercial banks. However, despite several years of operational experience, financial performance of a number of co-operative banks is still below their potential. Deteriorating asset quality has led to increasing incidence of financial weakness in the co-operative banking sector.

## PART II - ISSUES RELATING TO DEPOSIT INSURANCE IN INDIA

2.1 Deposit Insurance plays a key role in maintenance of financial stability by sustaining public confidence in the banking system in India through protection of depositors, especially small and less sophisticated depositors, against loss of deposit to a significant extent. One of the issues of deposit insurance is to maintain a target fund ratio or range (i.e. insurance fund as a percentage of insured deposits). In principle, the target fund ratio should be sufficient to reduce the probability of the fund's insolvency to an acceptable minimum, although estimating probabilities of the loss is very complicated in practice. Many countries find it useful to set a target level for the fund. The FDIC has stipulated such fund ratio at 1.25%. No target fund ratio has been prescribed in India.

Though the fund ratio has improved in the past few years and currently stands at 0.79 % as on 31st March 2005, it is necessary to further strengthen the fund and raise the fund ratio well above 1% over a well-defined time-frame.

2.2. The second issue relates to fixation of priority in sharing of realizations of assets of failed banks. Although in terms of the provisions of the DICGC Act, 1961 and the DICGC General Regulations, 1961, the liquidators of insured banks are required to pay back out of realization of assets of such banks to DICGC after making provisions for expenses and ensuring that the balances left with them are sufficient to declare a dividend of not less than one paise in the rupee to each depositor, it is observed that orders on priorities in sharing of realization of assets issued by some state governments to liquidators of insured banks are not in consonance with the relevant provisions of the DICGC Act and the DICGC General Regulations resulting in a very miniscule recovery of such amounts for the Corporation and thereby adversely affecting its funds position. While the aggregate amount of claims paid and provided for in respect of 27 commercial banks and 108 co-operative banks, since the inception of the Scheme amounted to **Rs. 1484.57** crore, repayment received out of the recoveries etc., amounted to **Rs. 103.98** crore. The recoveries accounted for 7.00 per cent of the total claims paid. It is essential that the respective state authorities issue orders on priorities in sharing of recovery of assets in accordance with the provisions of the DICGC Act and the DICGC General Regulations.

2.3 The third issue relates to the compulsory obligation on the part of the Corporation to register all banks as insured. In India different segments of the banking sector are subjected to different regulatory and supervisory regimes with varying degrees of stringency and enforceability of supervisory action. As such, access to deposit insurance for all banks is likely to impose losses on the fund. Granting authority to DICGC to admit / exclude banks from the coverage of deposit insurance to reduce the problem of moral hazard is a possible solution for effective management of the financial risk of the Corporation.

2.4. The fourth issue is desirability of introduction of risk-based premium (RBP). Though the primary advantage of a flat-rate premium system is the relative ease with which premium can be calculated and administered, in such a system, low risk banks effectively pay for part of the deposit insurance benefit received by high-risk banks. Further, as premium is paid at a flat rate by all insured banks to the Corporation, which is mandatorily required to register all banks as insured, irrespective of the risk profiles of their assets, there is an acute problem of moral hazard in as much as banks can go for riskier lending beyond prudential limits knowing fully well that the interest of depositors is taken care of by DICGC. As against this, RBP encourages more prudent risk-management practices and thereby contributes to maintenance of financial stability.

### **PART III - THE WORKING AND OPERATIONS OF DEPOSIT INSURANCE AND CREDIT GUARANTEE CORPORATION**

#### **3.1 Jurisdiction**

##### **A. Geographical coverage**

The deposit insurance scheme in India

at present covers commercial banks including local area banks and regional rural banks in all the States & Union Territories. While the deposit insurance scheme also covers co-operative banks in 25 States and three Union Territories, the position of their coverage in the 4 States viz., **Meghalaya, Mizoram, Nagaland and Arunachal Pradesh, 3 Union Territories of Lakshadweep, Chandigarh, and Dadra & Nagar Haveli** is as under:

- (i) Government of India Ministry of Finance, Department of Economic Affairs New Delhi have been requested to issue necessary notification to extend the Deposit Insurance Scheme to the Co-operative banks in the State of Arunachal Pradesh. The matter regarding the extension of the Scheme to the co-operative banks in the states of **Mizoram, Meghalaya and Nagaland** and two Union Territories viz., **Lakshadweep and Dadra & Nagar Haveli** continues to be pending with the concerned Governments for carrying out the necessary amendments to their Co-operative Societies Acts to the satisfaction of the Corporation.
- (ii) With regard to the Union Territory of **Chandigarh**, Government of India, Legislative Department, Chandigarh Administration have been advised to confirm that a notification has been issued by the Central Government giving effect to Section 2 of Punjab Co-op. Societies (Amendment) Act, 1981 & 1994 validly adopting the said Act for the Union Territory of Chandigarh. The reply from the Government is awaited. The matter is being pursued.

##### **B.1. Co-operative Banks registered under Karnataka Souhadra Sahakari Act, 1997 and similar state enactments**

The banks that have opted to register as 'Co-operative Societies' under the Karnataka Souharda Sahakari Act, 1997(KSS Act) could not be termed as co-operative banks as defined under Section 2 (1) of the NABARD Act 1981 and would, therefore, be outside the purview (of Section 56) of BR Act, 1949 and consequentially out of the purview of the DICGC Act, 1961 (vide Section 2 (dd), 2( r )and 13 A ibid).

Government of Karnataka had since amended the KSS Act, 1997 and on examination it was observed that the banks registered under the amended KSS Act can be considered as eligible co-operative banks without further amendments to KSS (Amendment) Act 2004. The deposit insurance cover has been extended to the co-operative banks registered under the KSS Act, 1997.

### **B.2. Co-operative Banks registered under the Multi-State Co-operative Societies Act, 2002**

Government of India, Ministry of Law and Justice, Legislative Department , New Delhi vide their notification No 32 of 2004 dated 24th September 2004 amended the provisions of BR Act, 1949 and the DICGC Act, 1961. As a result of this amendment all the banks registered under Multi State Co-op Societies Act (MSCS Act) have been considered as "eligible co-operative banks" for extension of deposit insurance cover. Accordingly deposit insurance cover has been restored to the banks registered under the MSCS Act, 2002.

### **3.2 Registration/De-registration of Insured Banks**

Year-wise and category-wise particulars showing the number of banks registered by the Corporation since inception of the scheme in 1962 are furnished in **Annexure I and I-A**. During the year, 1 Commercial Bank and 2 Co-operative Banks were registered as insured banks and 1 commercial bank,

2 foreign banks, 1 Local Area Bank and 47 co-operative banks were de-registered, the details of which are furnished in **Annexure II**.

### **3.3 Coverage of deposit insurance**

The ceiling amount of insurance cover for deposits with an insured bank continued to be Rs.1,00,000 per depositor per bank **in the same right and capacity**. The number of accounts and the amount of deposits insured with the Corporation as also the extent of protection afforded to depositors at the end of June 2003 and September 2004 are furnished in Table 1.

**Table 1: Insured Deposits**

Particulars (Account in lakhs and amount in Rupees crore)	June 2003	September 2004
1 Total No of Accounts.	5440	6495
2 Fully protected accounts	5189	6195
3 Percentage of 2 to 1	95.39	95.38
4 Assessable deposits	13,18,268	16,19,815
5 Insured deposits	8,70,940	9,91,365
6 Percentage of 5 to 4	66.07	61.20

The year-wise details for last ten years are furnished in Annexures III and IV.

### **3.4 DEPOSIT INSURANCE PREMIUM**

The deposit insurance premium was enhanced in two phases from 5 paise per Rs. 100 of assessable deposit to 8 paise per Rs. 100 of assessable deposit from the financial year 2004-05 and 10 paise per Rs. 100 of assessable deposit from the financial year 2005-06. The category-wise break-up of premium (including interest on overdue premium) collected from insured banks during 2003-04 and 2004-05 are furnished in Table 2.

**Table 2 : Premium received**

(Rupees in Crore)			
Year	Commercial Banks including LABs & RRBs	Co-operative Banks	Total
2003-04	684.28	86.35	770.63
2004-05	1211.84	142.94	1354.78

#### 4. SETTLEMENT OF DEPOSIT INSURANCE CLAIMS

During the year 2004-2005, the Corporation has settled aggregate claims for Rs. 440.25 crore in respect of 14 co-operative banks as detailed in Table 3.

**Table 3 : Claims settled**

(Rupees)			
Sr. No.	Name of the Bank	No. of Depositors	Amount of Claims (Rs.)
1	The Nayaka Mercantile Co-op Bank, Gujarat	2317	2,55,31,199.77
2	The Charminar Co-op Bank Ltd, Hyderabad. A.P	99673	23,15,66,626.00
3	The General Co-op Bank Ltd. Gujarat	59082	70,25,56,502.48
4	The Praja Co-op Bank Ltd., A.P.	1	58,193.97
5	Charotar Nagarik Sahakari Bank Ltd., Gujarat	175128	2,00,39,26,863.61
6	Shri Adinath Sahakari Co-op Bank Ltd., Maharashtra	1	43,208.00
7	Trimoorathi Sahakari Bank Ltd, Maharashtra	1	37,368.44
8	Western Co-op Bank Ltd, Maharashtra	2328	3,45,42,787.00
9	Pratibha Mahila Sahakari Bank Ltd., Maharashtra.	14174	3,38,33,810.60

10	Visnagar Nagarik Sah. Bank Ltd., Gujarat	227956	1,34,86,68,264.78
11	Theni Co-op Urban Bank Ltd., Tamil Nadu.	1	10,000.00
12	Narsarraopet Co-op Urban Bank Ltd., A.P.	397	17,94,449.97
13	Bhanjanagar CUBL, Orissa.	2209	97,99,510.00
14	Sai Co-op Bank Ltd., A.P.	1480	1,01,70,178.97
<b>Total</b>			<b>4,40,25,38,963.59</b>

\* Additional admitted during the year.

Further, a provision of Rs 1788.52 crore has been made towards the likely claim liabilities in respect of depositors of 113 banks which are under liquidation or whose licence / application for licence to carry on banking business has been cancelled / rejected by Reserve Bank of India.

#### 4.1 Position of Claims settled/Repayments received

As on 31st March 2005, the aggregate amount (cumulative) of claims paid and provided for since the inception of the Scheme, in respect of 27 commercial banks was Rs. 290.18 crore. Repayment received from liquidators/amalgamated banks upto 31st March 2005 aggregated Rs. 84.40 crore contributing 29.09 per cent of claims paid (including Rs.4.77 crore received during the year). The total amount of claims paid/provided for in respect of 108 co-operative banks, since the inception of the Scheme till 31st March 2005 was Rs. 1194.39 crore. (including Rs. 440.25 crore paid during the year). Repayments received from the liquidators/ amalgamated banks upto 31st March 2005 aggregated Rs. 19.43 crore contributing 1.63 per cent of claims paid (including Rs 6.33 crore received during the year). The particulars of banks in respect of which claims have been paid, written off, provided for and repayments received till 31st March 2005 are furnished in **Annexure V**.

## 5. CREDIT GUARANTEE SCHEMES

As on 31<sup>st</sup> March 2005 no credit institution was participating in any of the Credit Guarantee Schemes of the Corporation and, as such no claim was received during the year 2004-05 under any of the credit guarantee schemes of the Corporation.

The details of guarantee fees received, guarantee claims received and claims paid during the period 1991-92 to 2004-05 are given in Table 4.

The scheme-wise break-up of guarantee fee received since 1991-92 is given in **ANNEXURE VI**.

### 5.1 Small Borrowers' Credit Guarantee Schemes

- (i) Small Loans Guarantee Scheme, 1971 (SLGS 1971)
- (ii) Small Loans (Co-operative Banks) Guarantee Scheme, 1984 (SLCBGS 1984)

Upto the year ended March 2005, the Corporation had settled 3,74,23,627 claims for

Rs.10,043.06 crore under the schemes. The year-wise details of receipt and disposal of claims under the Corporation's credit guarantee schemes relating to small borrowers are given in **Annexure VII**.

Recoveries received under the Schemes during the year by virtue of Corporation's subrogation rights aggregated Rs.14.04 crore as against Rs.18.85 crore received during the previous year. The cumulative amount of recoveries received since the inception of the Schemes aggregated to Rs.2004.58 crore forming 28.89 per cent of claims paid at Rs.6938.84 crore.

### 5.2 Small Loans (SSI) Guarantee Scheme, 1981

The details of claims received and disposed of year-wise, from 1st April 1981 onwards are given in **Annexure VIII**.

Recoveries made under the Scheme during the year by virtue of the Corporation's right of subrogation amounted to Rs. 1.61 crore as compared to Rs 2.16 crore received during the previous year. Cumulative recoveries since 1981 aggregated Rs.264.23 crore as on 31st March 2005 forming 26.39 per cent of the

**Table 4 : Guarantee fees / Claims received and claims paid**

(Amount in Rs. Crores)					
Year	Guarantee fee receipts	Guarantee claims receipts	Claims paid	Gap (2)-(3)	Gap (2)-(4)
1.	2.	3.	4.	5.	6.
1991-92	565.87	627.23	462.29	(-) 61.35	(+) 103.58
1992-93	702.78	1143.27	643.55	(-) 440.49	(+)69.23
1993-94	846.09	1490.76	889.99	(-) 644.67	(-)43.90
1994-95	829.13	1726.82	1179.01	(-) 897.69	(-) 349.88
1995-96	704.64	2365.23	1042.27	(-) 1660.59	(-) 337.63
1996-97	564.02	2112.37	378.64	(-) 1548.35	(+) 185.38
1997-98	164.91	497.26	371.40	(-) 332.35	(-) 206.49
1998-99	123.23	252.19	601.91	(-) 128.96	(-) 478.68
1999-00	21.99	245.49	403.13	(-) 223.50	(-) 381.14
2000-01	0.07	36.06	47.34	(-) 35.99	(-) 47.27
2001-02	0.02	1.24	1.33	(-) 1.22	(-) 1.31
2002-03	0.21	0.26	0.14	(-)0.05	(-) 0.07
2003-04	0.02 *	-	-	-	-
2004-05	-	-	-	-	-

\* Guarantee Fee received after stipulated period was refunded to bank during the year 2003-04 .

total amount of claims paid at Rs.1001.13 crore under the Credit Guarantee Scheme for Small Scale Industries.

### 5.3 Credit Guarantee Scheme for Small Scale Industries, Government's Credit Guarantee Scheme (since cancelled)

The Corporation continues to act as an agent of the Government of India, to pursue with the credit institutions for recoveries in claim paid accounts under the erstwhile Government Scheme. Out of the total amount of Rs 1.35 lakh representing the recoveries received in claim paid accounts during the year ended 31st March 2005 under the Scheme, the Corporation remitted a sum of Rs.1.21 lakh to the Government after retaining an amount of Rs. 0.14 lakh towards administrative expenditure incurred by it.

## 6. INVESTMENTS

In accordance with the provisions of the Deposit Insurance and Credit Guarantee Corporation Act, 1961, the amounts, which were not required for the time being, were invested in Central Government Securities including Treasury Bills. The investments in terms of book value (cost) aggregate Rs. 9363.18 crore, 433.46 crore and Rs.93.35 crore respectively in Deposit Insurance Fund (DIF), Credit Guarantee Fund (CGF) and General Fund (GF) as on 31st March 2005. The diminution in the value of the investments of all the three Funds has been fully provided for to the satisfaction of Statutory Auditors. Diminution in the value of investments consequent upon rising interest rates in the year under review has adversely impacted the surplus available in various funds of the Corporation for meeting liabilities in future and is, therefore, a cause for serious concern. The Corporation has initiated a suitable corrective action by way of putting in place an Risk Management Framework appropriate to its balance sheet structure.

## 7. ORGANISATION MATTERS

### 7.1 Board of Directors

The general superintendence, direction and the management of the affairs and business of the Corporation vest in a Board of Directors which may exercise all powers and does all acts and things which may be exercised or done by the Corporation.

**7.1.1** In terms of Regulation 6 of the DICGC General Regulations, 1961, the Board of Directors of the Corporation is required to meet ordinarily once in a quarter each year. During the year ended 31st March 2005, four meetings of the Board were held.

### 7.2 Audit Committee of the Board

The Audit Committee of the Board was constituted in June 2003 with the following members:

Shri Mukund M. Chitale	Chairman
Shri Sudesh Kumar	Member
Shri S. Doreswamy	Member
Shri M.G. Bhide	Member

Since the formation of the Audit Committee, eight meetings were held (the last meeting was held on 28th May, 2005).

### 7.3 Management

Smt. K.J. Udeshi is the Chairperson of the Corporation. Shri A.V. Sardesai, Executive Director, RBI was appointed as RBI's Nominee Director on the Board of the Corporation on 11th November, 2004 vice Smt. Shyamala Gopinath, Executive Director, RBI. Shri S.S.Gangopadhyay has taken over as CGM-in-Charge of the Corporation vice Shri Anand Sinha w.e.f March 24, 2005.



#### **7.4 Budgetary Control**

The Corporation has devised various control returns under its Management Information System (MIS) for submission by the participating entities for monitoring receipt of premium and guarantee fees and to exercise budgetary control over revenue and expenditure under its three Funds viz., Deposit Insurance Fund, Credit Guarantee Fund and General Fund.

#### **7.5 Inspection and Management Audit by RBI**

Inspection department of Reserve Bank of India conducted Management Audit and Systems Inspection- 2003 in the month of June / July 2003.

#### **7.6 Training and Skill Enhancement**

During the year, 64 employees including 14 officers, 43 Class III and 7 Class IV staff were deputed for various training programmes conducted by Reserve Bank of India at various training Colleges and Zonal Training Centres (ZTC). Apart from outside trainings, an in-house training was arranged in ZTC, Navi Mumbai, for the staff of Deposit Insurance Department. 5 officers and 13 class III employees of the department participated in the training. The Corporation has also taken initiatives in spreading awareness about deposit insurance. To start with the Corporation has requested RBI to include sessions on DICGC, in the training programmes conducted by various training institutions of Reserve Bank of India. College of Agricultural Banking, Pune and ZTC, Navi Mumbai have already accepted our proposals and have included sessions on DICGC in the curriculum of their existing programmes. The Corporation has started providing faculty support to these institutions.

#### **7.7 Foreign Training/Visits**

During 2004-05, 5 officers were deputed by the Corporation to participate in training programmes,

seminars and conferences organised by International Association of Deposit Insurers (IADI), BIS, Korea Deposit Insurance Corporation and Deposit Insurance Corporation of Japan. Areas of training covered included, inter alia, deposit insurance and insolvency resolution, insolvency issues and role of deposit insurers, dealing with bank failures, guidance on bank resolutions banking supervision and limitations of management responsibility of failed financial institutions.

The Deputy Governor, Mr. Hajime Shinohara, Deposit Insurance Corporation of Japan (DICJ) visited the Corporation on February 17, 2005 and met the Chairperson and the Officers of the Corporation.

#### **7.8 Membership of IADI**

The Corporation has become Member of International Association of Deposit Insurers (IADI) which is an umbrella organisation for deposit insurers the world over. The BIS and the Financial Stability Forum (FSF) also associate with the IADI. Its objectives are to contribute to the stability of financial systems by promoting international cooperation in the field of deposit insurance and to encourage exchange of views and experience, conducting research, undertaking training, and developing deposit insurance guidance.

#### **7.9 Progressive use of Hindi**

The Corporation ensures compliance of Section 3(3) of the Official Languages Implementation Act. The Head Office of the Corporation has been notified under Rule 1Q(4) of the Official Languages Rules, 1976. The Corporation prepares quarterly progress reports of use of Hindi. The Official Languages Implementation Committee meets regularly once a quarter to monitor as well as to promote the use of Hindi in the day-to-day functioning of the Corporation.

### 7.10 Auditors

In terms of Section 29(1) of the Deposit Insurance and Credit Guarantee Corporation Act, 1961, M/s Chajjed & Doshi, Chartered Accountants, Mumbai were re-appointed, (with the approval of the Reserve Bank of India), as auditors of the Corporation for the year ended 31st March 2005.

## 8. ANNUAL ACCOUNTS

### Balance Sheet and Revenue Account

8.1 Revenue accounts for the year ended 31<sup>st</sup> March 2005 and Balance Sheet as on 31<sup>st</sup> March 2005 showing the position of the three Funds of the Corporation viz. Deposit Insurance Fund (DIF), Credit Guarantee Fund (CGF) and General Fund (GF), together with Statutory Auditors' Report are attached.

8.2 The Revenue Accounts are prepared after making provisions for the incremental liabilities as per actuarial valuations in respect of DIF (there being no incremental liabilities in CGF) and for other outstanding liabilities to the satisfaction of Statutory Auditors. The Revenue Surpluses (before tax) in DIF, CGF, and GF during the year 2004-05 were Rs.883.73 crore, Rs.132.72 crore and Rs.2.66 crore as against previous year's surpluses of Rs.566.52

crore, Rs.196.20 crore and Rs.2.85 crore respectively. As approved by the Board of Directors, the accumulated surpluses in the CGF as on 31-3-2005, save Rs.250 crore, amounting to Rs.1,344.81 crore were transferred from CGF to DIF in terms of Section 25 A (b) of Deposit Insurance and Credit Guarantee Corporation Act, 1961. The accumulated surpluses (after tax) in the DIF, CGF and GF as on 31st March 2005 stood at Rs.6942.51 crore, Rs.250.00 crore, and Rs.25.77 crore respectively.

The Board appreciates the dedicated efforts put in by the staff of the Corporation for maintaining the operational efficiency.

For and on behalf of the  
Board of Directors

**DEPOSIT INSURANCE  
AND CREDIT GUARANTEE  
CORPORATION  
MUMBAI - 400 008**

(K.J. Udeshi)  
Chairperson

Dated: 28th May, 2005