

GOVERNMENT OF INDIA

MINISTRY OF FINANCE

RAJYA SABHA

QUESTION NO 02.03.2010

ANSWERED ON

FOREIGN EXCHANGE DERIVATIVE CONTRACTS BY NATIONALIZED BANK

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Shri Sabir Ali

Will the Minister of COAL, HEALTH AND FAMILY WELFARE, INFORMATION AND BROADCASTING AND FINANCE be pleased to state :-

(a) whether it is a fact that some of the Indian Banks including the State Bank of India (SBI) during 2007 and 2008, entered into foreign exchange derivative contracts with certain companies, importers and exporters in violation of Foreign Exchange Management Act (FEMA) resulting in huge losses;

(b) whether inter-departmental group of the Reserve Bank of India (RBI) had identified violation of rules and regulation which are not only serious but also international and deliberate; and

(c) if so, the details thereof?

ANSWER

The Minister of State in the Ministry of Finance

(Shri Namo Narain Meena)

(a) to (c) : The Reserve Bank of India (RBI), as the regulator and supervisor of the banking system, exercises regulatory and supervisory powers under the provisions of Banking Regulation Act, 1949. Accordingly, the prudential guidelines, including the comprehensive guidelines on derivatives, are formulated and issued to the banks by the RBI. The RBI supervises the banks through Annual Financial Inspections (AFIs), need-based scrutinies, off-site surveillance and periodical meetings with the banks.

RBI has constituted an Internal Departmental Group (IDG) during October, 2008 to review the derivative transactions of certain banks, which are active in derivative business. These banks included a few Indian banks. RBI has concluded that this is not a systemic issue. Some of the important irregularities identified by IDG are as under:

?Offering structures that were in violation of extant regulations; ?Offering leveraged structures; ?Not verifying the underlying / insufficient underlying exposures; ?Booking of contracts under past performance basis beyond 50% of eligible limit without obtaining CA certificate; ?Not ensuring adherence to the eligible limit under the past performance route; ?Not carrying out proper due diligence regarding user appropriateness and suitability of the product offered to the customer; ?Undertaking derivative transactions with / selling structured products to customers not having properly documented risk management policy; ?Not obtaining written acknowledgement from clients for understanding risks disclosed; and ?The periodical review reports and annual audit reports were not obtained by the banks from the concerned users.