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MONETARY AND CREDIT INFORMATION REVIEW

Statement on Monetary Policy

The Reserve Bank in its Statement on Monetary Policy, announced by Dr.Raghuram G Rajan, Governor, on March 4, 2015, decided to:

- reduce the policy repo rate under the liquidity adjustment facility (LAF) by 25 basis points from 7.75 per cent to 7.5 per cent with immediate effect;
- keep the cash reserve ratio (CRR) of scheduled banks unchanged at 4.0 per cent of net demand and time liabilities (NDTL);
- continue to provide liquidity under overnight repos at 0.25 per cent of bank-wise NDTL at the LAF repo rate and liquidity under 7-day and 14-day term repos of up to 0.75 per cent of NDTL of the banking system through auctions; and
- continue with daily variable rate repos and reverse repos to smooth liquidity.

Consequently, the reverse repo rate under the LAF stands adjusted to 6.5 per cent, and the marginal standing facility (MSF) rate and the Bank Rate to 8.5 per cent with immediate effect.

The need to act outside the policy review cycle was prompted by two factors: First, while the next bi-monthly policy statement will be issued on April 7, 2015 the still weak state of certain sectors of the economy as well as the global trend towards easing suggested that any policy action should be anticipatory once sufficient data support the policy stance. Second, with the release of the agreement on the monetary policy framework, it was appropriate for the Reserve Bank to offer guidance on how it would implement the mandate.

Going forward, the Reserve Bank will seek to bring the inflation rate to the mid-point of the band of 4 +/- 2 per cent provided for in the agreement, *i.e.*, to 4 per cent by the end of a two year period starting fiscal year 2016-17.

The guidance on policy action given in the fifth-bi-monthly monetary policy statement of December 2014 is largely unchanged. Further monetary actions will be conditioned by incoming data, especially on the easing of supply constraints, improved availability of key inputs, such as, power, land, minerals and infrastructure, continuing progress on high-quality fiscal consolidation, the pass through of past rate cuts into lending rates, the monsoon out-turn and developments in the international environment.

Banking Regulation

Housing Loans to EWS and LIG Borrowers

With a view to encourage availability of affordable housing to economically weaker sections (EWS) and low income groups (LIG) borrowers, the Reserve Bank has issued instructions on March 5, 2015 that in cases where the cost of the house/dwelling unit does not exceed ₹10 lakh, banks may add stamp duty, registration and other documentation charges to the cost of the house/dwelling unit for the purpose of calculating Loan to Value (LTV) ratio.

On a review, banks are also advised that in cases of projects sponsored by Government/Statutory Authorities, they may disburse the loans as per the payment stages prescribed by such authorities, even where payments sought from house buyers are not linked to the stages of construction, provided such authorities have no past history of non-completion of projects. Earlier, banks could disburse housing loans sanctioned to individuals subject to close linkage to the stages of construction of the housing project/houses and upfront disbursal could not be made in cases of incomplete/under-construction/green field housing projects. (Circular DBR. BP. BC. No.74/ 08.12.015/ 2014-15 dated March 5, 2015)

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KYC Guidelines - Accounts of Proprietary Concerns

To ease the process of opening bank accounts of proprietary concerns, the Reserve Bank, on March 13, 2015, advised the banks to have the discretion to accept only one of the two documents as activity proof while opening accounts of sole proprietary firms in certain cases where the banks are satisfied that it is not possible to furnish any two documents out of the prescribed as activity proof. In such cases, the banks, however, would have to undertake contact point verification, collect such information as would be required to establish the existence of such firm, confirm, clarify and satisfy themselves that the business activity has been verified from the address of the proprietary concern. It is also clarified that the list of registering authorities is only illustrative and therefore includes licence/certificate of practice issued in the name of the proprietary concern by any professional body incorporated under a statute, as one of the documents to prove the activity of the proprietary concern. (DBR.AML.BC.No.77/14.01.001/2014-15 dated March 13, 2015)

Guidelines on Outsourcing of Financial Services

The Reserve Bank, on March 11, 2015, advised banks to meticulously adhere to the guidelines on managing risks as applicable in outsourcing of financial services. The banks also need to take steps to ensure that the service provider employs the same high standard of care in performing the services as would be employed by the banks, if the activities were conducted within the banks and not outsourced. Further, banks should not engage in outsourcing that would result in their internal control, business conduct or reputation being compromised or weakened. The outsourcing of any activity by the bank does not diminish its obligations, and those of its Board and senior management, who have the ultimate responsibility for the outsourced activity.

It is clarified that the Guidelines on Managing Risks and Code of Conduct in Outsourcing of Financial Services by Banks apply to subcontracted activities, as well. Before giving their consent, banks should review the subcontracting arrangements and ensure that these arrangements are compliant with the extant guidelines on outsourcing. Banks should ensure that reconciliation of transactions between the bank and the service provider (and/ or its subcontractor), like outsourcing of cash management, are carried out in a timely manner. An ageing analysis of entries pending reconciliation with outsourced vendors should be placed before the Audit Committee of the Board (ACB) and banks should make efforts to reduce the old outstanding items therein at the earliest. A robust system of internal audit of all outsourced activities should also be put in place and monitored by the ACB of the bank. (DBR.No.BP.BC.76/21.04.158/2014-15 dated March 11, 2015)

Sale of Assets to Securitisation /Reconstruction Company

The Reserve Bank, on March 11, 2015, permitted banks to reverse the excess provision (when the sale of financial Assets to Securitisation / Reconstruction Company (SCs/RCs) is for a value higher than the net book value (NBV) on sale of non-performing assets (NPAs) sold prior to February 26, 2014 to SCs/RCs, to their profit and loss account. Banks can reverse excess provision arising out of sale of NPAs only when the cash received by way of initial consideration and/or redemption of security receipts/pass through certificates is higher than the NBV of the NPAs sold to SCs/RCs. Further, the quantum of excess provision reversed to profit and loss account will be limited to the extent to which cash received exceeds the NBV of the NPAs sold. The quantum of excess provision reversed to the profit and loss account on account of sale of NPAs shall be disclosed in the financial statements of the bank under 'Notes to Accounts'. (DBR.No.BP.BC.75/21.04.048/2014-15 dated March 11, 2015)

Payment Systems

RBI seeks Comments on Draft Circular for Card Payments

The Reserve Bank on March 13, 2015, placed the "Draft Circular for Card Payments - Removal of requirement of Additional Factor of Authentication for small value card present transactions", on its website (www.rbi.org.in) for feedback. As per the draft circular, the Reserve Bank is contemplating to relax the existing instructions relating to the need for additional factor of authentication (AFA) requirements for small value card present transactions only using Near Field Communication (NFC). In this regard, it is advised that -

- Relaxation for AFA requirement is permitted for transactions for a maximum value of ₹ 2,000/- per transaction; banks are free to set lower per transaction limits.
- The contactless cards should necessarily adhere to EMV standards. Suitable velocity checks (daily, monthly, etc) shall be put in place by banks as agreed upon by the customer.
- For transaction value above the threshold limit of ₹ 2000/-, PIN (AFA) will be mandatory.

Further, in the interest of customer protection the banks are also advised:

- to clearly explain to customers about the technology, its use, risks and liability while issuing contact less/ NFC cards.
- to clearly indicate the maximum liability devolving on the customer, if any, at the time of issuance of such cards, along with the responsibility of the customer to report the loss of such cards to the bank immediately through multiple channels made available by the bank.
- to put in place robust mechanisms for seamless reporting of lost/ stolen cards which can be accessed through multiple channels (website, phone banking, SMS, IVR etc.).

However, it may be noted that the above relaxations shall not apply to:

i. ATM transactions irrespective of transaction value.

ii. Card not Present transactions(CNP).

The Reserve Bank has sought comments on the draft circular for feedback. The comments may be emailed to afa@rbi.org.in or sent by post to the Chief General Manager, Department of Payment and Settlement Systems, Reserve Bank of India, Central Office, 14th Floor, Shahid Bhagat Singh Marg, Mumbai-400001 on or before April 4, 2015.

Background

The Reserve Bank of India has been receiving requests from customers and entities in certain niche segments indicating the need to foster innovative payment products / processes and for enhancing the convenience factor in certain use cases / type of transactions without the need for having the mandatory additional factor of authentication (AFA). The requests have been examined from the perspective of the trade-off between security and convenience in card transactions and need for relaxation in extant instructions with suitable safeguards to protect customer interest in light of availability of new technologies. One such technology is that of Near Field Communication (NFC) which is used in contactless cards .The contactless cards are chip card which provides security as well as convenience.

Banking Supervision

Compliance Function in Banks

The Reserve Bank, on March 4, 2015 placed on its website (https://rbi.org.in) a circular on compliance function in banks. In view of the increased focus on compliance review in the supervisory processes, all banks are advised to implement comprehensive compliance plan replete with compliance testing and review structures. (DBS.CO.PPD.10946/11.01.005/2014-15 dated March 04, 2015)

Financial Inclusion

Priority Sector Lending

The Reserve Bank, on March 13, 2015, decided that priority sector loans to persons with disabilities will be eligible for classification under weaker sections category, effective from the date of circular. (FIDD.CO.Plan.BC.51/04.09.01/2014-15 dated March 13, 2015)

The Reserve Bank, on February 25, 2015, decided that overdrafts extended by banks upto ₹ 5,000/- in Pradhan Mantri Jan-DhanYojana (PMJDY) accounts will be eligible for classification under priority sector advances ('others' category) as also weaker sections, provided the borrowers household annual income does not exceed ₹ 60,000/- for rural areas and ₹ 1,20,000/- for non-rural areas. (FIDD.CO.Plan.BC 50 /04.09.01/2014-15 dated February 25, 2015)

Non- Banking Regulation

Designated Director for Compliance with PMLA

The Reserve Bank, on March 16, 2015 advised that non-banking finance companies (NBFCs) can designate a person who holds the position of senior management or equivalent as a "Designated Director" to ensure compliance with the obligations under the Prevention of Money Laundering (Amendment) Act, 2012. However, in no case, the Principal Officer should be nominated as the "Designated Director". Earlier, NBFCs could nominate only a Director on their Boards as "Designated Director". (DNBR. PD. CC. No. 022/ 03.10.042 /2014-15 dated March 16, 2015)

Prior Approval for Change in Shareholding

In order to smoothen the functioning of Securitisation Company / Reconstruction Company (SC / RC), the Reserve Bank on February 24, 2015) decided that, only the following changes in the share holding pattern of the SC/RC will require the Reserve Bank's prior approval:

i. Any transfer of shares by which the transferee becomes a sponsor.

ii. Any transfer of shares by which the transferor ceases to be a sponsor.

iii. An aggregate transfer of ten percent or more of the total paid up share capital of the SC/RC by a sponsor during the period of five years commencing from the date of certificate of registration.

Under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI), 2002, every SC / RC is required to obtain prior approval of the Reserve Bank for any substantial change in its management. For the purpose of this section, the expression "substantial change in management" means the change in the management by way of transfer of shares or amalgamation or transfer of the business of the company. Hence, one of the terms and conditions stipulated to the SC/RCs, while granting them the certificate of registration, states that prior approval of the Reserve Bank will have to be taken by the SC/RCs for any change in their shareholding pattern.(DNBR (PD)CC.No. 01/SCRC/26.03.001/2014-2015 dated February 24, 2015)

Government and Bank Accounts

Sukanya Samriddhi Account

The Reserve Bank advised all banks to bring to the notice of their branches operating Public Provident Fund (PPF), 1968 Scheme that the Sukanya Samriddhi Account Rules, 2014, have come into force with effect from December 2, 2014. Reporting of the SukanyaSamriddhi Account transactions, that is, receipt, payment, penalty, etc., may be directly done through the Government Account at Central Account Section, Reserve Bank of India, Nagpur on daily basis like the transactions of PPF, in order to have uniformity in reporting, reconciliation and accounting.The Agency banks are required to observe the rules and regulations of the Scheme and non-observance of rules and regulations would attract penal action, including de-authorisation of the branch or bank. Pecuniary liabilities, if any, arising from such non-observance shall be borne entirely by the bank. All agency banks may, therefore, approach Central Account Section, Reserve Bank of India, Nagpur for necessary arrangements to report Sukanya Samriddhi Account transactions with immediate effect. These instructions should also be displayed on the notice board. (IDMD (DGBA) CDD .No. 4052/ 15.02.006/ 2014-15 dated March 11, 2015)

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Refund of Overpayment of Pension

Under the extant instructions, whenever any excess payment of government pension is detected, the entire amount should be credited to the government account immediately, presuming an act of omission on the part of the agency bank. On the other hand, if the agency bank is of the view that the excess/wrong payment to the pensioner is due to errors committed by the government, they may take up the matter with full particulars of the cases with respective Government Department for a quick resolution of the matter. In all other cases, where the excess payment has arisen on account of mistakes committed by the bank, the amount paid in excess should be credited back to government account in lump sum immediately.(DGBA.GAD.No.H4054/45.03.001/2014-15 dated March 13, 2015)

Foreign Exchange Management

Prohibition on Acquisition/Transfer of Immovable Property

The Reserve Bank, on March 11, 2015, included citizens of Macau and Hong Kong in the list of countries which are prohibited to acquire/ transfer immovable property in India in terms of FEMA Regulations. Macau and Hong Kong are the two Special Administrative Regions of China notified separately. Under the extant regulations, no person being a citizen of Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal or Bhutan could acquire or transfer immovable property in India, other than lease, not exceeding five years, without prior permission of the Reserve Bank. (A.P. DIR Series Circular No.83 dated March 11, 2015)

ECB Policy — Review of All-in-cost Ceiling

On a review, the Reserve Bank on March 3, 2015 advised Authorised Category-I banks (AD Category-I) that the all-in-cost ceiling of External Commercial borrowing as specified will continue to be applicable till March 31, 2015 and is subject to review thereafter. All other aspects of ECB policy remain unchanged. (A.P. DIR Series Circular No.80 dated March 3, 2015)

Trade Credits for Imports into India — Review

On a review, the Reserve Bank on March 3, 2015 advised Authorised Category-I banks (AD Category-I) that the all-in-cost ceiling of Trade Credits for Imports into India as specified, will continue to be applicable till March 31, 2015 and is subject to review thereafter. All other aspects of Trade Credit policy remain unchanged. (A.P. DIR Series Circular No.81 dated March 3, 2015)

NR Deposits - Discontinuation of Stat 5 and Stat 8

The Reserve Bank, on March 18, 2015, discontinued the submission of Stat 5 and Stat 8 Returns from March 2015 for Non Resident Deposits. Accordingly banks, dealing in foreign exchange may stop sending Stat 5 and Stat 8 Returns (both hard and soft copies) to the Department of Statistics and Information Management, Reserve Bank of India, as banks' submission of NRD-CSR data in XBRL platform has stabilised. (A.P DIR Series Circular No.85 dated March 18, 2015)

Report

Revisiting Existing Priority Sector Lending Guidelines

The Reserve Bank released the Report of the Internal Working Group to Revisit the Existing Priority Sector Lending Guidelines (Chair: Lily Vadera, Chief General Manager, Department of Banking Regulation) on March 2, 2015.

The key recommendations of the Report include:

i) *Overall Priority sector target:* The target for lending to the redefined priority sector is retained uniformly at 40 per cent of Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-Balance Sheet Exposure (CEOBE), whichever is higher, for all scheduled commercial banks. However, foreign banks, which will all now come under the norms, have been given time to comply with the target.

ii) *Agriculture:*Target of 18 per cent of ANBC retained. A sub-target of 8 per cent of ANBC has been recommended for small and marginal farmers to be achieved in a phased manner. More flexibility has been recommended for banks to lend the remaining 10 per cent of the overall agriculture loan target to other farmers, agricultural infrastructure and ancillary activities as defined by the Group. To give a fillip to agri-infrastructure and agri-processing, no caps on loan limits have been stipulated.

iii) *MSME:*In addition to micro and small enterprises, medium enterprises are included within the ambit of priority sector lending. To ensure that the micro enterprises are not crowded out, a sub-target of 7.5 per cent for micro enterprises has been recommended, which is to be achieved in a phased manner.

iv) *OtherSectors:* In addition, loans to sanitation, health care and drinking water facilities and renewable energy will come under the priority sector ambit, as will incremental loans made to exports, with certain ceilings.

v) *Priority Sector Lending Certificates:* The Working Group recommends introduction of priority sector lending certificates (PSLCs) which will enable banks to meet their PSL requirements even while leveraging their comparative advantage in lending.

Suggestions/comments, if any, on the recommendations of the Report, may be sent by post to the Principal Chief General Manager, Reserve Bank of India, Financial Inclusion and Development Department, Central Office Building, 10th Floor, S.B.Marg, Mumbai-400001 or through email (at cgmincfidd@rbi.org.in) on or before March 15, 2015.

Background

The Indian economy has changed since priority sector lending guidelines were conceived. There is a need to reorient guidelines towards today's growth and inclusion agenda. As such, an Internal Working Group was constituted by the Reserve Bank with the objective of revisiting the existing priority sector lending guidelines and suggesting revised guidelines in alignment with the national priorities as well as financial inclusion goals of the country. The objectives also included suggesting ways on how to achieve the priority sector targets in the most effective way as well as measures to be taken in case of under-achievement of the priority sector targets.

The Working Group has focused on channelling credit to segments that get crowded out in the absence of specific targets. These include small and marginal farmers, micro enterprises and the weaker sections while broadening the scope to include other underserved categories of national priority, such as agriculture infrastructure, social infrastructure, renewable energy, exports and medium sized enterprises.

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